GCC Countries as “Rentier States” Revisited

Review Article by Robert Springborg


Resources Blessed: Diversification and the Gulf Development Model (Vol. 1), ed. by Giacomo Luciani.

National Employment, Migration and Education in the GCC (Vol. 2), ed. by Steffen Hertog.


The GCC in the Global Economy (Vol. 4), ed. by Richard Youngs.

Giacomo Luciani, the senior editor of this four volume set, along with Hazem Beblawi laid the conceptual foundations for Arab rentier states a quarter of a century ago. He and his team of some 40 researchers have now revisited this concept as part of a broader effort to describe and analyze the political economies of the Gulf Cooperation Council (GCC) states. The very title of the flagship volume edited by Luciani, Resources Blessed: Diversification and the Gulf Development Model, suggests revision to the prevailing, Luciani-influenced orthodoxy that the resource curse and its attendant rentierism are inherently inconsistent with economic diversification and development. Revisionism implied by the title is indeed borne out as the editor and authors present a largely positive account of the economic accomplishments and future of the GCC states, distancing themselves, sometimes explicitly, not only from negative prognostications for rentier states, but even from the present applicability of the concept itself to the “mothers” of all rentier states, those that comprise the GCC.

Such a corrective effort is long overdue, if only because the inevitable stretching of what was originally a useful concept may have rendered it too general and amorphous to provide useful analytical insight and unambiguous causal explanations. Moreover, a literature of corrections and qualifications to the concept has gradually emerged over the past decade or so, suggesting the need and timeliness of returning to the original empirical base for its formulation. If its applicability even in the Gulf is now in doubt, it is clearly time for rentierism to be reconsidered, revised, or possibly even rejected as a useful notion.

The original argument rested on the proposition that abundant hydrocarbon rents accruing to governments would inevitably lead to authoritarian states focused on allocation rather than extraction and production. Having no need for taxation they would not be com-

pelled to grant representation. Having little need for revenue from non-hydrocarbon based direct and indirect taxes, they would neglect development of a productive economy that could generate taxable earnings. States organized around allocation would not have reason to create market incentives for development. They would also structure relationships with society vertically through chains of patronage dependence. Societies and labor forces would in turn be segmented, unable to form horizontal linkages, such as those reflected in working and middle classes, labor unions and political parties, necessary for both political and economic development. State domination of the economy, as reflected in monopolies granted to state-owned enterprises (SOEs) in the most profitable sectors, key of which is that of hydrocarbon extraction, processing, and export, would impede both private development and improved performance of the SOEs themselves. The portrait painted of the rentier political economy was, at least in the concept’s early years, one of stagnating stability based on a social contract, the mutual obligations of which would perpetuate the separation of state and society and render democratization unlikely, even irrelevant.

Initial disaffection with the concept resulted from observation of the uneven impact of the alleged resource curse. Indeed, in some settings, with Norway being that most frequently cited, oil seemed more blessing than curse. Democracy remained intact in those countries where it had previously been established. While some evidence of Dutch disease did seem ubiquitous in “oil curse” economies, many countries were able if not to completely contain it, at least to develop other sectors of their economies. In the meantime, large-scale quantitative comparative studies began to suggest qualifications to the basic correlation between oil rents and authoritarianism and to cast doubt on alleged relationships with other hypothesized dependent variables as well.

The so-called “new institutionalists” also joined the fray, at least indirectly, with macro-historical studies of national economic performance. Their conclusion is that economic failure results not from an abundance of rents, but from defective political institutions. If politics are not inclusive, economic institutions will inevitably also be exclusive, designed to

---


extract wealth from society not for the general good, but for the benefit of elites. By contrast, inclusive economic institutions are those with laws and practices that motivate production by protecting property rights, enforcing contracts and providing opportunities to invest and multiply capital. The recent book by Daron Acemoglu and James Robinson, for example, Why Nations Fail: The Origins of Power, Prosperity, and Poverty, deploys this institutional argument to explain what they see as the economic failure of the Ottoman Empire. Others have argued the case for a broad Middle Eastern historical path dependency, in which postcolonial states essentially replicated the extractive institutions first established by their Ottoman and colonialist predecessors, leaving open the question of whether post-colonial states will break this path dependency.

These institutional arguments, however, may not fully fit the historical facts of the Ottoman Empire or accurately depict the political economies of contemporary Middle Eastern rentier states. As regards the latter, the recently released Paying Taxes 2013 Report of the World Bank, the International Finance Corporation, and PricewaterhouseCoopers, for example, demonstrates unambiguously that the Middle East and North Africa (MENA) is the region of the world with the least extractive governments as measured by total taxes as a percentage of gross domestic product (GDP). The term extraction, to the extent it is intended as synonymous with taxation, is misleading. In any case, the malady of contemporary rentier states seems not to be the malignancy of excessive extraction, from which Ottoman and European precursors supposedly suffered, but the benign neglect inherent in allocation. Indeed, one sub-school of institutionalists indebted to Charles Tilly makes the case that because taxation requires real and effective penetration of society and economy, it historically is the motor force of institutional development. By contrast, allocation neither compels state development nor forces state and society into an embrace that fosters growth and accountable governance.

As the oil curse/rentier state debate was globalizing from its origins in the MENA and being subject to more careful empirical and theoretical scrutiny, scholars of the region began to reconsider whether the rentier concept remained as applicable as it once seemed to be. Tim Niblock’s careful chronicling of the maturation of Saudi state institutions was among the first to contend that they were not inherently stagnant even in the mother of all rentier states and that just as for the Norwegians, oil could be a blessing for Saudi insti-

9. For the argument that Acemoglu and Robinson have their facts wrong about the Ottoman Empire, see Sübidey Togan, review of Why Nations Fail, by Acemoglu and Robinson, Newsletter of the Economic Research Forum, Vol. 19, No. 2 (Autumn 2012), pp. 16–19.
tutional development. Marcel’s similarly detailed comparative assessment of the capacities and performances of Middle Eastern national oil companies graphically illustrated this point with regard to ARAMCO, which she ranked at the top of such firms and virtually the equivalent of leading multinationals such as Exxon and BP.

And it was not just the alleged incompatibility of institutional growth and rentierism that drew the attention of scholars of the region. Similarly investigated was the assumption that rents were consumables unable to be accumulated into fixed capital that would ultimately provide structural power for the beneficiaries of those rents. Giacamo Luciani himself was among the first to identify and seek to quantify the emergence of a Gulf bourgeoisie, while subsequent work, including that by Steffen Hertog, one of the editors of the set under review, focused on private fixed capital formation resulting from rents. Yet another relevant area of investigation focused on the rent to population ratio and its implications for strategies of rule. According to one empirical study, the higher the proportion of rents to citizens, the more likely rulers would rely upon allocation in the form of public employment rather than repression to contain their populations. The Arab Spring seemed in fact to bear out this hypothesized relationship. Arab states with relatively low rent to population ratios, such as Yemen, Syria, and Egypt, did indeed rely principally on repression, whereas those with high rent to population ratios, such as Kuwait, Saudi Arabia, and the United Arab Emirates (UAE), sought to hose down potential discontent by increasing allocations.

The rentier state concept and its closely connected “oil curse” hypothesis have, in sum, already given rise to a plethora of empirical and theoretical scholarship. Some such work, including variants of the new institutionalism and cross-national aggregate data studies, have at least called some deterministic versions of rentierism and the oil curse into question, if not altogether dismissed the utility of the concept. By comparison, research focused on MENA rentier states, and especially those of the GCC, has generally sought to qualify rather than dismiss rentierism and its consequences. Some research has postulated that the concept was time limited, applicable only or primarily during the first great oil boom in the mid to late 1970s when governments cascaded rents into the citizenry and public goods because private sector alternatives were simply not available. Other research, including

17. For rents per capita in selected Arab countries, see Ali and Elbadawi, “The Political Economy of Public Sector Employment,” p. 23.
that under review here, contends that the concept remains relevant, but needs to be modified in light of changed circumstances, including that of the steady transformation of rents into private fixed capital, accompanied by the development of state institutions able to perform more functions than simply allocating rents. According to this last view, rentier states contained the seeds of their own, possibly beneficial, destruction. Differences in interpretation in this end of rentierism scholarship turn on the rates of state decay and what replaces defunct rentier states. The rent to population ratio dictum prophesizes that rentier states are heading toward the dustbins of history as their hydrocarbon revenues stagnate in real terms and their populations mushroom. They will be replaced by republics of some variant, possibly Islamist, as the colonial dialectic, long delayed by virtue of small and backward populations as well as by oil rents, finally plays out even in the MENA’s former backwater. Alternatively, rentier states will not collapse suddenly, if at all. Instead, the process of reform in which they are presently engaged will be accelerated, propelled by the growing structural power of capital deployed by non-royal upper and middle classes.

This four-volume set provides not only further commentary on important conceptual issues of rentierism, but empirical grist for these theoretical mills. Luciani sets the tone in the introduction to his edited, lead off volume when he states that “the distinguishing characteristic of the GCC states and ruling elites has been their strong commitment to the transformation of their economies” (p. 9). He goes on to argue that a “significant share of the rent has been used to buy political consensus — just as a good share of taxation revenue is used for obtaining consensus in all democracies … (but) what matters is that nevertheless enough of the rent from resources is still invested in diversification” (p. 9). As for the resource curse, he denies that reliance on oil exports inevitably forestalls industrialization and diversification, claiming instead that good public policies, which he characterizes as those supportive of infrastructural growth, can overcome the allegedly fatal Dutch disease side effect of the curse (pp. 10–12). He further contends that particularities of GCC oil dependent economies render standard measurements of growth and diversification inappropriate, systematically understating both (pp. 12–16). GCC policy makers, in his view, have wisely cherry picked from among the recommendations inherent in the Washington Consensus of neoliberal reforms, most importantly by supporting more state intervention than recommended by neoliberal orthodoxy, especially by direct ownership of and subsidies to industry. He concludes by declaring the book’s aim as “demonstrating that indeed resources can be a blessing rather than a curse,” and that the GCC states are achieving diversification (p. 27).

The four-volume set is not very sharply focused on this objective, no doubt owing to the large number of contributors with different backgrounds and interests. But much of the empirical material is at least indirectly relevant to the Luciani proposition that GCC rentier states are successfully diversifying, hence escaping the resource curse thanks to having formulated and applied an appropriate development model. And virtually all of the chapters are of interest to committed students of GCC political economies, written as they have been by leading scholars and accomplished specialists.

Sifting through the more than 1,100 pages in search of evidence that might pertain directly to the proposition that at least in the GCC states rentierism can or indeed has evolved into more sophisticated, self-sustaining political economies, yields mixed results. The overall impression conveyed by data presented in the four volumes is that the diversification hypothesis is confirmed, but only if interpreted narrowly. Industrialization based on adding value to hydrocarbons and exploiting comparative advantage in energy intensive processing has proceeded apace as numerous chapters, especially those in the first volume, attest. The GCC share of global refining and petrochemical production is steadily rising.

19. This theme is developed, for example, in Giacomo Luciani, ed., Constitutional Reform and Political Participation in the Gulf (Dubai: Gulf Research Center, 2006).
the former for example having almost doubled to 8.6% over the 30 years ending in 2010 (p. 186). Its global market share of petrochemicals has increased even more dramatically, so much so that Luciani concludes that “by 2015, the Gulf producers will have become so important that further increasing their market share may become progressively more difficult” (p. 206). But, he goes on to note, GCC producers and especially those in Saudi Arabia are increasingly relying on joint ventures with Asian and Western firms in order not only to obtain access to technology, but to overcome international resistance to their expanding market share. Similarly, the GCC is forecast to account for 10% of global aluminum production by 2015 and will surely continue to rise after that date given “expansion of existing facilities coming on stream” (p. 231). As for features of the GCC industrial model, a key one is that of the continuing lead role of the state, similar or even more profound than that of the East Asian “tigers.” Steffen Hertog’s incisive analysis of the role of GCC state-owned enterprises (SOEs) reveals them as playing positive and leading roles in industrial and even other sectors, thus countering the commonplace assumption that SOEs, especially in rentier economies, are inherently inefficient and non-competitive (pp. 115–138). He attributes their relative success in the GCC to the fact that this region has largely escaped the economically vitiating effects of the colonial dialectic: “The absence of a populist ideology has arguably allowed GCC regimes to keep specific parts of the public sector lean, de-politicized, and oriented towards clear managerial (as opposed to political) targets” (p. 137). On first glance, then, the state-led GCC development model appears successful, at least within the industrial sector.

As for the other two legs of the GCC “three-legged” development model consisting of 1) hydrocarbon value added and energy intensive processing, 2) logistics/services, and 3) financial investments/services, the picture is somewhat more mixed. Many of the authors stress the vital importance to the overall economies of the GCC’s successful physical infrastructure development. The first volume contains a chapter by Eckart Woertz on logistical infrastructure which chronicles its rapid expansion and argues for its centrality to the GCC diversification strategy. As for financial investments and services, Eckart Woertz’s edited volume in the set, *GCC Financial Markets: The World’s New Money Centers*, is given over entirely to these matters, providing a somewhat skeptical view of accomplishments. Lack ing in the four-volume set is equivalent attention to service industries such as air travel, tourism, real estate, and freight handling, which form the backbone of the “Dubai, Inc.” variant of the model. Although these services are described and analyzed in various chapters, especially in the Woertz volume just mentioned, a systematic analysis of the viability of its subcomponents and of this leg of the three-legged model would have been useful.

As for a broader evaluation of the GCC model, a key issue is that of linkages, or more accurately, the relative lack thereof. While it is true that GCC manufacturing focused on hydrocarbons and energy intensive mineral processing has been profitable and globally competitive, its horizontal linkages into other sectors of manufacturing are weak, as are its linkages with the domestic labor force. Hans-Georg Mueller, for example, in his overview of industrial development in the GCC, notes that “most of the manufacturing sub-sectors not related to oil and gas fall into the low and medium-low technology industries … Overall, GCC industries are characterized by the scarcity of technology-intensive and capital goods industries other than petrochemical industries … (B)ackward and forward linkages of GCC manufacturing industries are still weak …” He concludes by noting that the low rankings of GCC states in UNIDO’s Competitive Industrial Performance Index results primarily from their inadequate technological capabilities (p. 149).

This deficiency is closely related to the other “missing link” in at least the industrial component of the triangular development model, which is that of labor force participation and skill development. Steffen Hertog’s volume in the set, *National Employment, Migration and Education in the GCC*, focuses on this weakness, with careful examinations of various ways and means to overcome segmentation in the labor force between public and private, national and expatriate. Labor market upgrading and nationalization, to say nothing
of increasing the ratio of the labor force to the population and stimulating greater participation of women in that labor force, are challenges that the GCC development model is not well-equipped to meet. Quick fixes such as imposing minimum wages in the private sector to induce employers to hire nationals (see Eberhard Feess in Hertog, pp. 7–64) are analyzed but rejected as unworkable and ineffective. The magnitude of the problem of underutilization and misallocation of national human resources is graphically illustrated by Hertog, who notes that presently only 800,000 Saudis are employed in the private sector, while some 400,000 are reaching working age annually (p. 61); that only 51,000 Saudi women are employed in the private sector (p. 73); and that of 1.8 million Saudi civil servants, fully half a million are employed in the Ministry of Interior (p. 68). Hardly surprising then are stagnating labor productivity, in part because private employers have little or no incentive to upgrade skills of expatriates, and the associated decline of Total Factor Productivity (TFP) (p. 75). The one bright spot in the labor market picture is a slight increase of mid-level Saudi private sector employees, but that is offset by the further bifurcation of the public sector labor force into a small elite with high skills and a mass of low skilled civil servants (p. 78).

The economics of the labor force are similarly disturbing. The GCC contributes more to labor remittances than any other region in the world — 21% of $283 billion (p. 177) — thus depriving its economies of a potentially high wage driven GDP multiplier. A related drain is that of what Hertog terms “the price of informal labor markets,” which includes the selling of work visas through the kafala system, creation of fake companies and employees to skirt nationalization laws, and various other “workarounds” that drain tens of billions of dollars from the productive sectors (pp. 95–97). A case study by Hasan Tariq Alhasan of attempts to reform the kafala system in Bahrain and that country’s overall labor market is indicative of the profound degree to which problems of segmentation of the labor force are both deleterious to GCC economies and embedded within existing power structures, thus causing one to wonder if this is a problem inherent in the Gulf development model, or is susceptible to resolution through appropriate, politically possible public policies. Moreover, the labor force constitutes only one dimension of the broader problem of incorporating GCC populations into their national political economies. A thoughtful chapter by Philippe Fargues and Imco Bouwer illustrates the contradictions of GCC policies, which for all intents and purposes deny citizenship to expatriate employees and their families, whose annual growth rate is 6.5%, compared to that of 3% for GCC nationals. The GCC already has the world’s highest proportion of migrants in its overall population, 39% compared to about half that for Australia and Canada, and of course given the higher growth rate of non-nationals, that proportion continues to grow (p. 234). An ever larger number of second- and even third-generation expatriate residents denied citizenship highlights the need for GCC states to develop naturalization policies and to treat those immigrants “as an opportunity, not a threat” (p. 257).

The third leg of the GCC development model, financial services and investments, is dealt with in Eckart Woertz, ed., GCC Financial Markets: The World’s New Money Centers. Its theme is that despite possessing a substantial share of the world’s investment capital, the Gulf’s financial sector, overly dependent upon banks, remains surprisingly poorly developed overall. Bond markets as described by Michael P. Grifferty remain primitive, equivalent to only 13% of GDP in the GCC as compared to 42% in emerging markets and 159% globally (p. 68). Moreover, governments account for fully 70% of GCC bonds, the private sector being conspicuous in its hesitancy to issue bonds (pp. 111–113). Stock markets are somewhat more developed, but characterized by their thinness and volatility. Only half of the 712 firms listed on GCC markets issue traded shares and those shares typically account for as little as 5% of their firms’ total share capital, the remainder held closely by family owners. Share ownership tends to be concentrated in the hands of wealthy families, with 58% of all shares in Qatar, for example, owned by members of ten families. The 20 largest companies in the GCC are not listed on any GCC exchange, while the ten largest listed companies make up 50–80% of total GCC stock market capitalization. In her thorough
review of these markets, Randa Alami concludes that none of the GCC states are accurately described as an emerging market because of the narrowness of investment opportunities and low rates of foreign participation (pp. 31–66).

So, despite possessing relatively more surplus capital than any other emerging market, the GCC has yet to develop the financial infrastructure effectively to manage it. Other chapters in the Woertz volume further illustrate the shortcomings. Large pension liabilities remain essentially unfunded and overall management of pension funds is inadequate (p. 73). Islamic banking, as described by leading authority Rodney Wilson in chapter nine, is the one area in which the GCC has taken the global lead, accounting for 22% of all banking in the GCC, compared to 1% globally. Half of the world’s Islamic banks and 40% of sukuk (Islamic bonds) are in the GCC. Although Islamic banking has clearly mobilized substantial capital in the Gulf, questions remain about its operations and possibly even sustainability.

Only two GCC states, Kuwait and the UAE, have legislation governing Islamic finance. It was in the latter, in fact, where the crisis arose in the wake of the 2008 global economic recession over the issue as to whether sukuk are “asset based or asset backed,” i.e., whether or not the fixed assets of the real estate projects financed by the sukuk should be considered as collateral, hence open to seizure by the “creditors” holding those Islamic bonds, an issue taken up by Woertz in his chapter on the “Repercussions of Dubai’s Debt Crisis” (pp. 137–164). Not surprising in light of this and some other ambiguities in Islamic finance, it declined more in 2009 than other GCC-based financial institutions (pp. 91–92). Woertz also raises the pregnant if paradoxical question of whether the GCC is in fact over-banked even as its financial sector is underdeveloped. Competition between the GCC member states to attract financial institutions, such as that between Qatar and the UAE in their respective financial centers, may have led to the GCC economy, whose total GDP is less than that of Holland’s, to have too many, undifferentiated institutions competing for too little business.

The fourth volume of the set, edited by Richard Youngs, is The GCC in the Global Economy. Its chapters also raise some doubt about the ultimate success of the Gulf development model. What is undeniably true is that GCC-Asian links, well described by Youngs as well as by John Sasuya in this volume, are being expanded and solidified. Such ties to the world’s most dynamic region imply that in the coming years GCC growth will be further propelled by servicing Asian markets, with the GCC in turn being the recipient of Asian technology, capital, labor, and goods. So as long as Asian demand for oil and gas continues to expand more rapidly than elsewhere, the die seems cast for stronger, mutually beneficial economic relationships to be forged, although security issues briefly described in the volume could complicate the commercial pivot toward Asia. Additionally, although the Asian connection holds out great promise, it begs the question of the GCC-MENA relationship. Might Asia simply replace the West as the center in the long established hub-and-spoke system that tied the GCC to Europe and the US, thereby obstructing greater GCC-MENA economic integration? The volume presents some evidence to that effect, including the decline of Arabs in the GCC expatriate labor force from 72% in 1975 to 32% in 2004; to the increase of Lebanese among Arab expatriates in the GCC to a full half; to the fact that the bulk of admittedly large GCC investment in the Arab world is in tourism and real estate rather than in sectors producing tradable goods (pp. 33–36); and to the fact that GCC trade with Asia, so heavily concentrated in hydrocarbons, could paradoxically discourage rather than encourage diversification.

It borders on the impudent to even ask what is missing in a collaborative research project that resulted in more than 1,100 pages of published text. Indeed, the answer would be nothing vital if the query is limited to the economics of the GCC. The 40-some authors have provided a remarkably comprehensive account of national GCC economies and of relations between them, the region and the world. Their contributions in turn feed into broader theoretical debates about rentierism and the resource curse. If, however, it is also relevant to ask about the sustainability and ultimate success of the model, then its political underpinnings and implications are relevant, although not directly addressed in the volume.
While some of the authors at least obliquely address political matters, the politics of the Gulf development model are not systematically treated. Those politics seem especially relevant in light of the Arab Spring, which has witnessed popular mobilizations of varying degrees and types in virtually all of the GCC states. In response, those states have returned to rentierism of old, seeking to temper protest with allocation and, when that fails, with more severe repression. This knee-jerk, royal reaction casts some doubt on the hope implied in the purported GCC model that these monarchies will evolve from ruling to reining ones, giving way gradually in the face of growing structural power of autonomous capital and the civil society it in turn finances. It also raises the fundamental questions of whether the population to rent ratio can be sustained at a sufficient level to mollify the population and, even if it is, might political mobilization nevertheless undermine the utility of resource allocation? Can we safely assume that the colonial dialectic will never play out in the GCC, where monarchs dependent upon Western-sourced security and Eastern markets for their oil and gas, fail to gainfully employ their ever younger citizenry, continue to deny expatriates basic rights, and provide only very limited voice and accountability? This seems a risky assumption, but it is one upon which the purported Gulf development model nevertheless rests, whatever industrial, service, and financial diversification it delivers. Hopefully, the very talented editors who have done us readers a service by producing this set of volumes that casts light not only on GCC economies, but on resource curses and rentierism, will in future turn their attention to the model’s downstream politics. Whether they will remain placid enough to keep the GCC states and their development model afloat, or will cause them to capsize by their turbulence, is a query worthy of another set of volumes.

Professor Robert Springborg, Naval Postgraduate School, Monterey, California
List of GCC countries, nations, or member states - Bahrain, Kuwait, Oman, Qatar, Saudi Arabia (KSA), UAE. Yemen and Iran are Muslim countries but not GCC members. Also called the Arab Gulf Cooperation Council (AGCC). Population statistics, foreign expat resident percentages, currency, land area, other figures and data. Yemen and Iran are Muslim countries but not GCC members. Population statistics, foreign expat resident percentages, currency, land area, other figures and data. GCC countries are ‘rentier states’. This term describes a distributive societal contract on which the government’s legitimacy depends. Very cheap and subsidized energy is an integral part of the wealth transfer to the domestic population from oil and natural gas generated revenues. The states provide free medical care, education, low-income housing, and high-paying public service jobs in exchange for the population’s compliance to the rule of the royal family. The GCC regimes think they have no responsibility for responding to any of the population’s pressure because the population pays (alm Evidence from GCC Countries. @inproceedings{AlMawali2015DoNR, title={Do Natural Resources of Rentier States Promote Military Expenditures? Evidence from GCC Countries}, author={Nasser Al-Mawali}, year={2015} }. Nasser Al-Mawali. Published 2015. Economics. This study aims to explore the effect of natural resources of rentier states on military expenditure using the panel data from GCC countries. The principle findings suggest that types of natural resources matter and that the rent from oil only appeared to fuel the military expenditure of GCC, other natural resources such as gas and minerals a... The long-run causal relationship between military spending and economic growth in China: revisited, Defence and Peace Economics. O. Dimitraki, F. Menla Ali. 2013.