



Workers in Kuwait's public oil sector went on strike for three days in April 2016 in opposition to government plans to reduce state spending by cutting employee benefits.

Meaningful Change or False Dawn: Policymaking in an Age of Austerity *by Kristian Coates Ulrichsen*

A new generation is taking office in the Gulf as a cadre of ambitious, young ruling family members and technocrats have emerged in Qatar, Saudi Arabia, and the United Arab Emirates (UAE). Both the Emir and the newly-appointed Foreign Minister of Qatar are 35 years old, while the most talked-about figure in Saudi Arabia, Deputy Crown Prince Mohammad bin Salman, is 30 years old. Their rise to power is reminiscent of the early years of the Gulf states' existence as independent sovereign countries, and the generation of 'nation-builders' such as Sheikh Zayed in the UAE. However, while that generation was tasked with overseeing the entrance of the GCC states into the oil era and cushioning the transformative impact of social and economic change, the task facing this generation is far harder and made more urgent by the recent collapse in world oil prices.

The speed with which budget surpluses have turned into deficits since 2014 has illustrated the scale of the economic volatility in GCC economies and their continuing vulnerability to oil price swings, notwithstanding the heavy emphasis on economic diversification since the early 2000s. The

International Monetary Fund has projected that lower oil prices cost Arab oil exporters some \$360 billion in lost revenues in 2015 and predicted that the six GCC states will face a cumulative fiscal deficit of as much as \$1 trillion over the next five years.¹ The situation is most acute in comparatively resource-poorer Bahrain, which was stripped of its investment grade credit rating by S&P in February 2016, and Oman, where GDP is estimated to have contracted by between fourteen and seventeen percent in 2015.² However, even in wealthier Abu Dhabi, nominal GDP is set to be 24 percent lower in 2016 than the peak year of 2014, while Saudi Arabia ran a budget deficit of \$98 billion and burned through more than \$100 billion in reserves in 2015.³

Financial countermeasures

A raft of measures has been taken under consideration in response to these rising fiscal pressures—including spending cuts and culling jobs, raising debt, drawing down on savings, and selling assets, with reported sell-offs by multiple Gulf-based sovereign wealth funds in recent months. Among the most contentious policy responses has been the long overdue reform of subsidy programs that—in energy alone—were estimated to have cost Saudi Arabia \$107 billion in 2015.⁴ All GCC states bar Kuwait have taken action to scale back fuel subsidies, with the UAE being the first to do so in August 2015. Prices for gasoline have risen by as much as 56 percent in Bahrain and 50 percent in Saudi Arabia with double digit rises also in Qatar and Oman, albeit from very low starting points.⁵ Bahrain has also removed subsidies on meat prices, expressed its intent to phase out power and water subsidies, and has raised industrial gas use prices, as has Oman.⁶

And yet, Moody's Investors Service has forecast that the spate of fuel price rises will only lead to savings equivalent to about one percent of GDP and, as such, do little more than dent the overall size of the fiscal deficits facing the GCC states.⁷ Moreover, the broader political sensitivity of tampering with one of the key mechanisms of wealth redistribution from the state to its citizenry has been evident most strongly in Kuwait and Bahrain, the two Gulf states with the most vocal and activist parliamentary bodies. It will not be easy for GCC officials to make further and deeper cuts that really begin to impact on Gulf nationals rather than expatriates; Bahrain, for instance, softened the blow of the meat price rises by compensating citizens for the additional cost involved. In addition, the demographic imbalance in Gulf labor markets, where up to 80 percent of some labor forces consist of migrant workers, has enabled state-owned firms to lay off considerable numbers of higher-skilled foreigners in initial rounds of cost-cutting, particularly in Qatar. However, sooner or later, nationals will inevitably start to feel the pain, too.

The wider issue

The real challenge for officials in the Gulf is how to reformulate a ruling 'bargain' that has underpinned sociopolitical stability for decades but is no longer economically sustainable. Until 2014, the prevailing hope in the region was that

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this 'moment of truth' was more of a medium-term issue rather than an urgent short-term one, and that politically sensitive reductions in current spending could be avoided or minimized by cutbacks in capital expenditure instead. Moreover, the regional political upheaval of the past five years illustrat-

II. Analysis

ed how the instinctive response of many governments in the GCC was to intensify populist short-term measures intended to blunt or pre-empt the social and economic roots of potential or actual political tension. Such policies succeeded in preserving political structures and stability (for the most part) in 2011 but had the unintended consequence of, as Steffen Hertog has noted, creating “a ratchet effect that demands ever larger outlays during every political crisis” because “expectations are easy to raise but difficult to curb.”⁸

Whereas current spending on wages and subsidies largely tracked the increase in oil prices during the decade after 2003, it will be much harder, if not outright impossible, to cut public expenditure by anything that remotely matches the decline in oil revenues over the past eighteen months. There is, to be sure, a much more open political and even public acceptance of the realization that change must happen and that the status quo simply cannot continue, and such sentiments have clearly been articulated by figures such as Prince Mohammad bin Salman in Saudi Arabia and in the recent government reshuffle undertaken by Sheikhs Mohammed bin Zayed and Mohammed bin Rashid in the UAE. In addition, the years of plenty perhaps have dulled memories of previous downturns, but Gulf states have faced similarly difficult situations in the past and survived intact; most GCC states ran budget deficits for most of the 1980s and 1990s—Saudi debt reached nearly 100 percent of GDP in 1998 compared with about two percent today.⁹

Periods of change inevitably involve tradeoffs, and while recent months have seen senior public figures in the Gulf talk about the bigger picture and think creatively and outside of the box, the true test of their ‘Thatcherite’ tendencies will be whether they can push through and implement successfully major reforms in the face of opposition from vested political or economic interests. Recent announcements of further policy reform in Saudi Arabia and Kuwait have been noticeably short on actual detail, and the delay in announcing Saudi Arabia’s National Transformation Program, without which the expansive Saudi Vision 2030 cannot properly be assessed (or implemented), may turn out to be a harbinger of things to come.

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¹ Simeon Kerr, “IMF Warns on Gulf States Growth amid Oil Price Fall and Conflict,” *Financial Times*, 21 October 2015.

² Archane Narayanan, “Bahrain Cancels \$750 Mln Bond Sale after S&P Downgrade,” *Reuters*, 18 February 2016; “Oman’s Nominal GDP Falls by 14.2% in First Half of 2015,” *Oman Times*, 13 January 2016.

³ “Abu Dhabi: Low Oil Prices Take their Toll on Economy,” *Gulf States News*, Volume 40, Issue 1010, 18 February 2016; Vivian Nereim and Glen Carey, “Saudi 2015 Budget Deficit is \$98 Billion as Revenue Drops,” *Bloomberg Business*, 28 December 2015.

⁴ Simeon Kerr, “Saudi Arabia Looks to Reform Energy Subsidy Program,” *Financial Times*, 12 November 2015.

⁵ Tim Boersma and Steve Griffiths, *Reforming Energy Subsidies: Initial Lessons from the United Arab Emirates*, (Energy, Security and Climate Initiative, Brookings: January 2016), 6.

⁶ Ibid.

⁷ “Fuel Subsidy Reforms to Make Only a Modest Dent in GCC Deficits,” *Gulf States News*, Volume 40, Issue 1010, 18 February 2010.

⁸ Steffen Hertog, “The Costs of Counter-Revolution in the Gulf,” *Foreign Policy*, 31 May 2011.

⁹ Thomas Lippman, “New Saudi Budget: the Good, the Bad, and the Potentially Ugly,” *Lobe Log*, 29 December 2015.