The Private Sector and Social Divide in the GCC

by Rola Dashti

Successful economic reform depends on citizen buy-in

Since the dramatic fall of oil prices began in mid-2014, policymakers in the Gulf Cooperation Council (GCC) states have come to realize amid shrinking fiscal balances that maintaining a rentier state approach is not conducive to sustainable development. GCC states have thus reaffirmed their political commitment to fiscal reform, reducing oil dependence and diversifying toward a knowledge-based economy. In particular, recent economic development plans have focused on reform policies that increase the private sector's growth and expand its role within the region's economy. But despite these efforts, the private sector's contribution to the knowledge economy, research and innovation remains negligible.

Today, the private sector contributes about 35 percent of the Gulf states' GDP, generating about $120 billion in inter-trade within the GCC and employing about 80 percent of the workforce. Yet most of this employment has been filled by low-paid and low-productivity migrant work. For the most part, the private sector still provides little quality employment that would be acceptable to nationals—particularly in the wealthier Gulf states of Kuwait, Qatar and the UAE.

The GCC private sector's wealth has surpassed $2 trillion, and the majority of it is in the hands of family businesses. Given the limited investment opportunities within the region's vital productive economic sectors, most of the private sector's funds are redirected and invested outside of the region. Locally, Gulf businesses mostly function as agents or intermediaries for international firms that provide the bulk of the region's goods and services. Moreover, both the size and growth of the private sector in the GCC economies is highly dependent on government expenditures.

The success of diversification policies relies, from each government's perspective, on initiating reform measures and addressing structural barriers to diversification. Specific focus areas include improving the education system, enhancing the efficiency of the labor market, reducing regulatory barriers to competition, developing effective government institutions and constructing market-friendly administrative and regulatory laws.

Businesses vs the citizenry

But policymakers must be cognizant of the arising conflict between the business community and citizens. At the moment, both compete for state resources and rely heavily on government spending while contributing little to fiscal budgets. The private sector employs relatively few Gulf nationals and concentrates business opportunities in the hands of few families that generate minimal productive investment and entrepreneurship opportunities for the region's growing and well-educated citizenry. Part of transforming economic activities and expanding the private sector's role should include the privatization of government assets (including utilities, transportation services, oil and gas related activities, infrastructure, health and education) and public-private partnership (PPP) projects. Doing so will attract both local investment and foreign direct investment

(FDI), increase job creation and reduce state expenditures. Only then will the government's role in the various Gulf states shift away from being the main investor, provider of services and employer toward becoming merely a facilitator, regulator, enabler and driver of business.

Yet adopting privatization and PPP policies will be seen by citizens as a transfer of wealth from the state to the business community. In the absence of policies that will safeguard citizens from the negative effects of privatization, public support for these reforms will be negligible. This will likely lead to public outcry, discontent and social unrest in the long run.

But a balance can be struck. Kuwait's parliament has ameliorated this concern in their privatization and PPP laws. These laws have stated that any privatized entity will be 50 percent owned by citizens through an initial public offering (IPO) at par value per share, 24 percent owned by the state and 26 percent owned by the private sector. The operation and management of these companies will be carried out by a strategic investor, and 70 percent of these companies' workforce must be nationals. In addition, the Kuwaiti parliament passed a foreign investment law that encourages FDI and increases the transfer of technical knowhow and administrative capacities from foreign companies to domestic businesses. All of this has led many nationals to acknowledge the benefits of privatization and PPP since it has provided them a with a stake in the reform program.

Challenges within the private sector

For the private sector to succeed as GCC governments have envisaged, several internal and external factors must also be addressed. Internally, the private sector needs to adopt plans that will reduce its dependence on government spending, address the issue of business separation of ownership and management, improve corporate governance and deal with uncertainty over business succession (only 17 percent of GCC family businesses have put in place effective succession plans).

Externally, the private sector must strike a balance between the economic gains resulting from

> The success of diversification policies relies, from each government's perspective, on initiating reform measures and addressing structural barriers to diversification.

a more diversified economy on the one hand and increased societal interdependence and corporate social responsibility on the other. Increasing societal linkages can be achieved by supporting entrepreneurial ventures and opportunities, providing employment to citizens and developing internship and apprenticeship programs with universities and vocational training institutes. These efforts will help ensure a successful private sector in the Gulf.

Dr. Rola Dashti is a former MP and Minister of Planning and Development in Kuwait.