GCC brand, cohesion and a move to a common currency

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The Gulf Co-operation Council ("GCC") was created on May 25, 1981, and comprises the Gulf States of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. A unified economic agreement between the members (often referred to as Gulf Cooperative Countries) was signed in Riyadh on November 11, 1981. The GCC has many objectives and purposes, an overview of which will be discussed below.

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The basic objectives of the GCC are to effect co-ordination, integration and inter-connection between member states in all fields, strengthening ties between their peoples, formulating similar regulations in various fields such as economy, finance, trade, customs, tourism, legislation, administration, as well as fostering scientific and technical progress in industry, mining, agriculture, water and animal resources, establishing scientific research centres, setting up joint ventures, and encouraging co-operation of the private sector. Articles 8 and 9 of the Unified Economic Agreement between the GCC countries allows free movement of capital and individuals across GCC countries and the freedom to exercise economic activities, and the principles established by the agreement are being made concrete in many ways.

The past 10 years in particular has seen phenomenal growth in the economies of the member states, partly enabled by increased revenue from the high oil prices but also through diversification into other industries (in order to reduce high oil dependence) and de-regulation to encourage privatisation and competition. The UAE (particularly Dubai) has through the use of free zones, strongly diversified into other sectors such as banking and financial services, real estate, telecommunications, media, hospitality, tourism and regional services. All these sectors are also being pursued in the other countries, with Saudi Arabia actively encouraging non-oil industries and manufacturing, Qatar developing as the major global Liquified Natural Gas player, and Bahrain becoming a strong regional financial centre. There have been various regulatory and fiscal reforms in the member states to liberalise trade and boost the domestic business environment. With their rapid economic growth, the member states are together and individually boosting the image of the GCC as a very important zone in the global market place for investments and for conducting business internationally. The GCC "brand", which has been very successful in promoting the visibility and image of the region, is being actively pursued to further enhance market power and credibility.

The launch of a GCC common market in January 1, 2008 marked an important step in its economic integration. It moved beyond the free movement of goods and services that has been agreed upon in the GCC customs union to include labour and capital flows as well, representing a milestone in the GCC's history since its inception in 1981. The main goal of the

common currency is to facilitate economic growth and prosperity among the member states and foster economic integration. In the long run, the creation of a single currency may boost intra-regional trade and investment and may help, over time, to reduce country differences and achieve convergence with respect to economic policy. But there are some challenges.

1. The fulfilment of the common market long-term objectives relies on common and similar features and characteristics of the GCC countries. Despite the fact that the member states had agreed to peg their currencies to the dollar in preparation for the introduction of a GCC single currency, the timetable for the monetary union has been in doubt. Although the convergence criteria have yet to be established, there is concern that countries will not want to give up control of fiscal policy, especially as some governments use fiscal means to boost growth and reduce risk in times of low oil prices. Oman announced in 2007 that it would skip the 2010 deadline over concerns that spending targets could constrain economic growth. Similarly, the UAE Central Bank governor indicated that the GCC was unlikely to have a single currency by 2015. Kuwait also appeared to have broken ranks when it abandoned its peg to the US dollar, as the rising cost of imports in non-dollar denominations was driving up inflation. The current global financial turmoil may increase these tensions, and it would be important to co-ordinate government policy shifts in order to ensure cohesion and avoid weakening the GCC brand.

2. GCC countries still impose restrictions on ownership and the type of activities that non-nationals can exercise.

3. Also, labour market regulation and institutions are not very similar, and preclude labour from moving across GCC countries. Unemployment rates are not even across the countries. Oman's unemployment rate, for example, is estimated to be 18 percent, which appears similar to Bahrain and Saudi Arabia. In contrast, the UAE, Kuwait and Qatar benefit from much lower unemployment rates in the range of three to five percent.

4. On average oil still represents overall more than 80 percent of export receipts and budget revenues, and as a result the economies of the GCC countries remain heavily vulnerable to the fluctuation of oil on the international stage. Even the non-oil sector in GCC is perceived as dependent to a large extent on the performance of the oil sector. Oman for example has substantially less oil reserves than the other GCC countries, with only Bahrain appearing to be in a similar situation. A high share of the non-oil aggregate value added originates mainly from trade and business services.

These issues as well as the challenges of equalising the fiscal deficits of the various GCC countries, standardising interest rate levels and co-ordinating taxation policies, make macroeconomic cohesion and the political and economic planning of a common currency a most formidable task.

Notwithstanding the obstacles, GCC leaders have shown a strong commitment to the regional grouping. This commitment stems from the many common traits shared by GCC countries notably the similarity in their political, social, demographic and cultural structures. Even if integration is moving at a much slower pace than is generally hoped, GCC countries are often praised for taking a pragmatic approach consisting of progressively reinforcing commonalities rather than hastily imposing unrealistic conditions to achieve such integration, holding the view that the complete integration of product markets requires the elimination of the transaction costs and uncertainties associated with the existence of separate currencies.

Relative to the European Community, the GCC is still at an early phase but has made much quicker progress within a short time. The EC has been important in the development of trade and economy of its member states. With a longer-term perspective, a similar trend could result from efforts of the GCC governments to diversify their economies, whilst pursuing economic cohesion. If these lead to a strengthening of the domestic, non-energy sectors, they could pave the way for stronger economic and monetary integration of the GCC. A strong GCC brand could significantly enhance these, and provide more options in widening the global market place.

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The Cragus Group is a leading independent tax advisory firm based in Dubai with special focus on the Middle East and Africa.