The Growing Economic Presence of Gulf Countries in the Mediterranean Region

Abdullah Baabood
Director
Gulf Research Centre, University of Cambridge

Fuelled by a historic record increase in oil prices, the Gulf Cooperation Council (GCC) states' (Bahrain, Kuwait, Qatar, Oman and Saudi Arabia) economies and their financial surpluses continued to grow at an unprecedented rate. Oil wealth has transformed these backwater traditional and conservative states to the forefront of international politics and finance, and Gulf foreign investments have been on the increase over the years. Although the bulk of GCC investments were channelled into the traditional economies of the developed countries of the US and Europe as well as the rising Asian economies of China and India, a growing proportion of GCC investments stayed in the region, including the neighbouring Mediterranean. Indeed, over the past few years, partly because of the geopolitical ramifications following the events of September 11, 2001, GCC investments have started to pour into the Mediterranean region, spurring its economic development.

In 2008, Gulf investments and economic presence in the neighbouring Mediterranean region continued to grow, albeit at a slower pace, due to the recent global economic and financial crisis, which precipitated a fall in the oil price and reduced GCC states' revenues and financial surpluses.

The Global Economic Crisis Slows Down the Process but Does Not Halt It

By 2008, the global financial crisis profoundly changed the global business environment, and the accompanying uncertainty has impacted on the growing trend of global foreign direct investment (FDI). World FDI flows, which, according to the United Nations Conference on Trade and Development (UNCTAD), rose by 30% in 2007 –well above the previous all-time high set in 2000 and reaching a historic record of 1.833 billion dollars, were estimated to have fallen by 21% in 2008 to an estimated 1.4 billion dollars.

Over the period of 2002-2006, the Mediterranean region managed to capture its fair share of this global inflow, receiving world FDI corresponding to its demographic importance of 4%, but began to slow down in 2007 due to the crisis. In 2008, the Med share of global FDI began to decrease only slightly below the global trend (-17%) and below the bar of 4%, helped by the strength of their economic performance and the resiliency of North Africa (-5.2%) and particularly Egypt (10.9 billion dollars against 11.6 billion dollars in 2007). (See Table 5 and Chart 17)

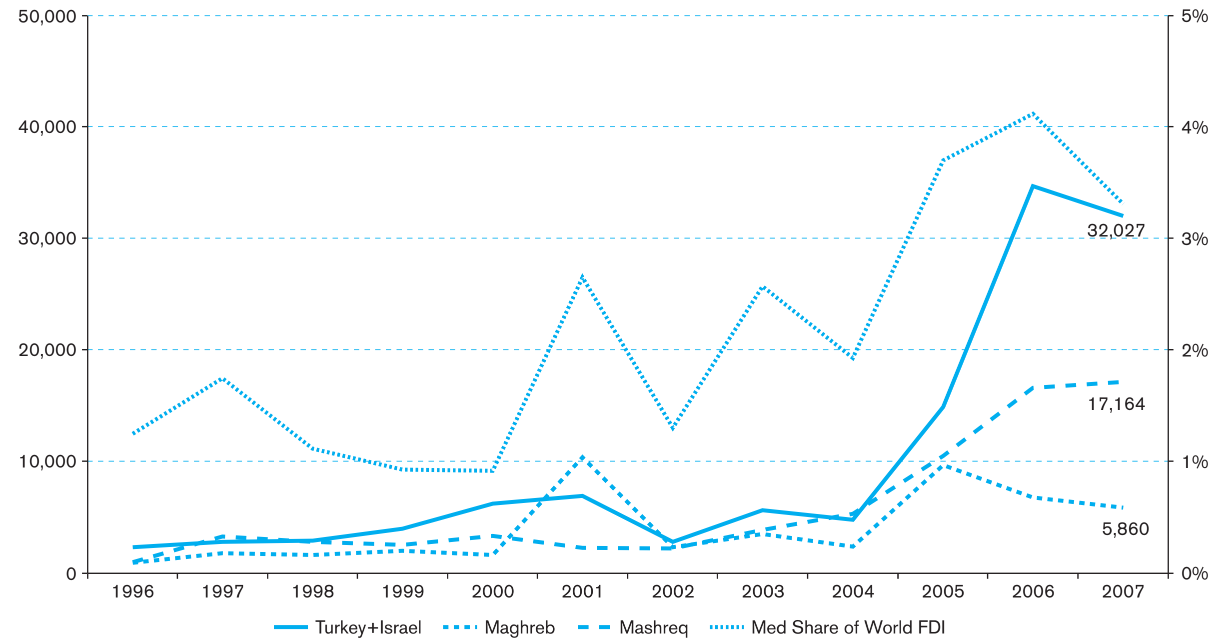
The 13 countries that border the Mediterranean (Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, the Palestine Authority, Syria, Tunisia, plus Turkey, Libya, Malta and Cyprus) received direct foreign investment totalling 68 billion euros in 2006 and 61 billion euros in 2007. In 2008, the Mediterranean region started to be affected by the world economic and financial crisis with an overall drop in FDI of a little less than 40 billion euros in 2008 (-35%).

The Gulf States have not been entirely immune from this global crisis. It precipitated a fall in energy demand and a dip in oil price from their historic record levels, causing a drop in government revenues and a loss in confidence. Petrodollars from the oil and gas industries and sovereign wealth funds (SWFs), which had shielded many Middle Eastern economies from the global meltdown and delayed its impact, began to dry up as global liquidity became tight. The increasingly adventurous Gulf investors, who had shown a strong appetite to invest in the Mediterranean region,

TABLE 5	Evolution of FDI Inflows by Sub-Region of Destination (annualised flows, in million euros, 2003-2008)						
Destination	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**Total**
Mashreq	1,861	1,658	11,615	28,558	27,285	7,280	78,257
Maghreb	6,013	7,251	7,381	11,821	15,830	8,018	56,314
Other Med	1,937	871	20,474	28,608	18,261	24,693	94,844
Total	9,810	12,780	39,471	68,987	61,376	39,991	232,415

Source: ANIMA-MIPO.

CHART 17 **FDI Inflows for Med Regions and Med Share of World FDI (in million dollars)**



Source: United Nations Conference on Trade and Development –*World Investment Report* (UNCTAD-WIR).

slowed or deferred some of their decisions as they began to weigh up the effect of the global financial crisis.

The Gulf Economic Growth as a Source of Investment

Despite the global turmoil, GCC economic growth remained strong in 2008, pushing the GCC's combined nominal GDP up to 1 trillion dollars. The region's economy continued to expand vigorously, especially in the first half of 2008 (about 7%), before it began to decelerate in the latter half due to the secondary effect of the global economic crisis and averaged 5.7%.

High oil prices with a higher volume of exports between 2002 and the autumn of 2008 strengthened the key macroeconomic indicators in the six GCC countries, and the region achieved record budget surpluses over the seven years before the global financial crisis caused prices to collapse and economic growth to stall. (See Table 6)

With average oil prices 45% higher in 2008 than in 2007 and coupled with incremental additions to export volumes, this gave another boost to the GCC's cumulative export earnings, which reached about 2.2 trillion dollars over the period. Such was the ascent of oil prices that the current account surplus swelled dramatically from around 50 billion dollars in 2003-04 (year ending June) to almost 400 billion dollars in 2007-08, equivalent to over 30% of GDP. In aggregate, the current account registered a cumulative surplus of 912 billion dollars over the period (Table 7, Charts 18 and 19).

The GCC as an Investment Powerhouse

Like most oil-exporting countries, the GCC states started transforming oil windfall into financial wealth after the 2002 surge in oil prices by setting up ded-

TABLE 6 **GCC: Main Economic Indicators**

	2006	2007	2008f	2009f
Nominal GDP ($bn)	731	821	1,098	1,036
Hydrocarbon, GDP ($ bn)[1]	368	409	613	479
Non-hydrocarbon GDP ($ bn)	363	412	485	557
Real GDP (% change)	5.8	5.2	5.7	4.2
Hydrocarbon	1.8	1.1	4.0	1.0
Non-hydrocarbon	8.1	7.5	6.4	5.4
Inflation (average)	4.8	6.8	11.8	8.5
Current account bal. ($ bn)	211	206	342	155
% GDP	29	25	31	15
External debt (% GDP)	20	27	38	31
Foreign Assets ($ bn)	933	1,244	1,467	1,605
% GDP	128	152	134	155
Fiscal balance (% GDP)	22	19	23	13
Oil price (Brent; $/barrel)	66.3	72.6	105.3	75.5
Oil production (mbd)	15.9	15.4	16	15.7
Gas production (mboe/d)	3.8	4.0	4.4	4.8

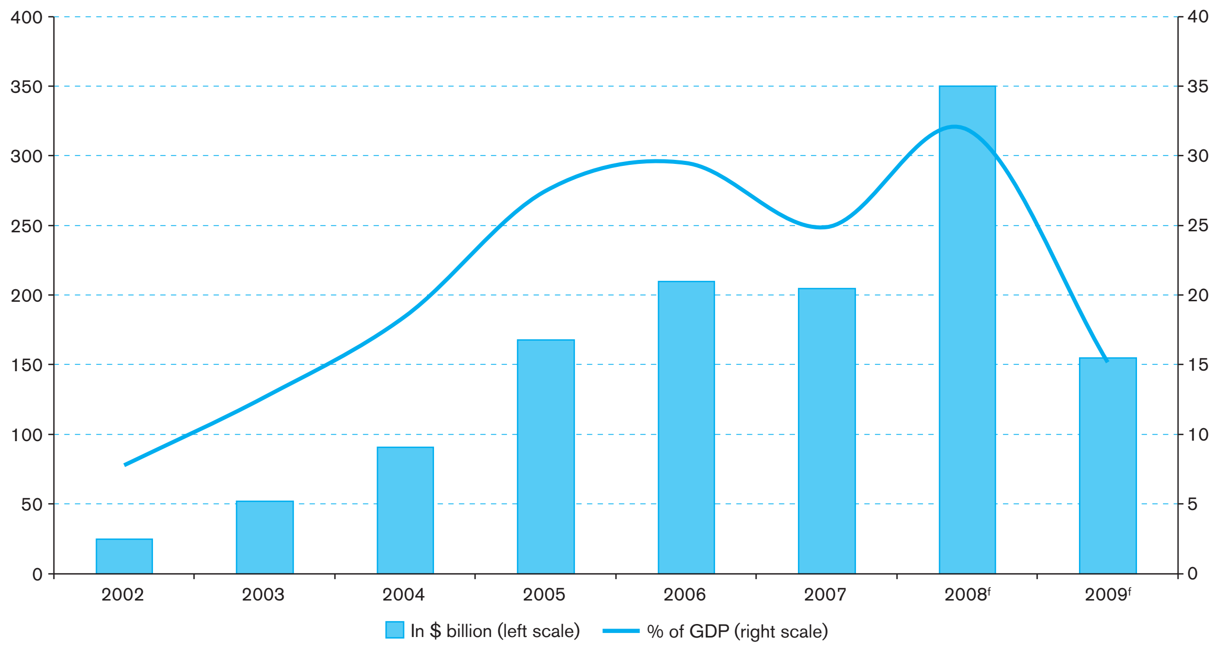
Source: The Institute of International Finance (IIF), 2008.
f = forecast; [1] Refers to crude oil and arid natural gas, mbd = millions of barrels a day, mboe/d = millions of barrels of oil equivalent a days.

TABLE 7 **GCC Current Account Surplus (in billion dollars)**

	2006	2007	2008f	2009f
Trade Balance	284	299	465	286
Exports	485	563	792	642
Hydrocarbon	372	421	825	458
Oil	352	398	584	425
Gas	20	23	41	33
Non-Hydrocarbon	112	142	167	184
Imports	-201	-264	-327	-356
Services, net	-57	-72	-91	-104
Incomes, net	20	19	15	26
Transfers, net	-35	-40	-46	-52
Current account balance	211	206	342	155
% GDP	29	25	31	15
Memoranda:				
Oil production (mbd)	15.9	15.4	15.9	15.6
Brent oil price ($/bl. av.)	66.3	72.6	105.3	75.6

Source: IIF, Nov. 6, 2008.
f = forecast; mbd = million barrels a day.

CHART 18 **Current Account Surpluses Remain Strong**

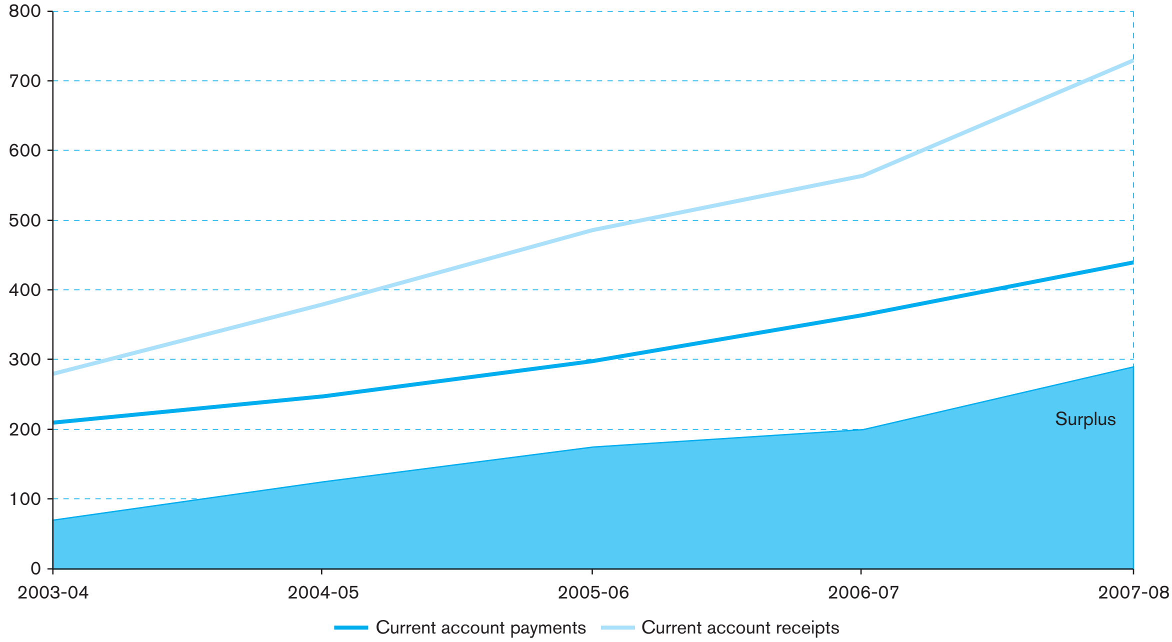


Source: Institute of International Finance IIF, 2008. f = forecast;

icated investment funds exclusively for the oil surplus they had earned. In fact, the funds of the GCC alone accounted for around half the assets held by sovereign wealth funds globally (Chart 20).

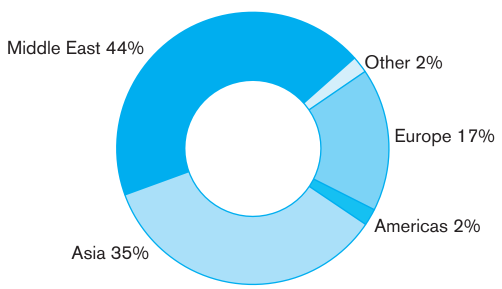
Whereas in the beginning of 2000, the funds of the GCC did not constitute more than 350 billion dollars and investments were predominantly concentrated in US assets, this trend began to change after September 11, so by the end of 2008, where foreign assets of state institutions and the banking sector were reported to rise to nearly 900-1.5 trillion dollars (not taking into account possible recent declines in asset values), the pattern of investments changed from low-risk portfolios to high-risk ones, such as equity and alternative investments, especially in the emerging economies of Asia and the

CHART 19 **GCC Current Account (billion dollars)**



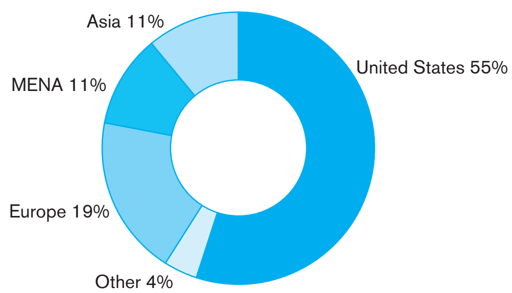
Source: Samba, December 2008.

CHART 20 **Sovereign Wealth Funds by Region**



Source: The Sovereign Wealth Funds Institute.

CHART 21 **Distribution of Capital Outflows from Countries of the Gulf Cooperation Council, 2002-2006**



Source: Institute of International Finance, 2008.

Mediterranean. Nearly one quarter of Gulf foreign investments since 2002 were in Asia and the Middle East/North Africa (Table 8 and Chart 21).

TABLE 8 **Estimated Geographical Distribution of GCC Capital Outflows, June 2003-June 2008 (billions of dollars)**

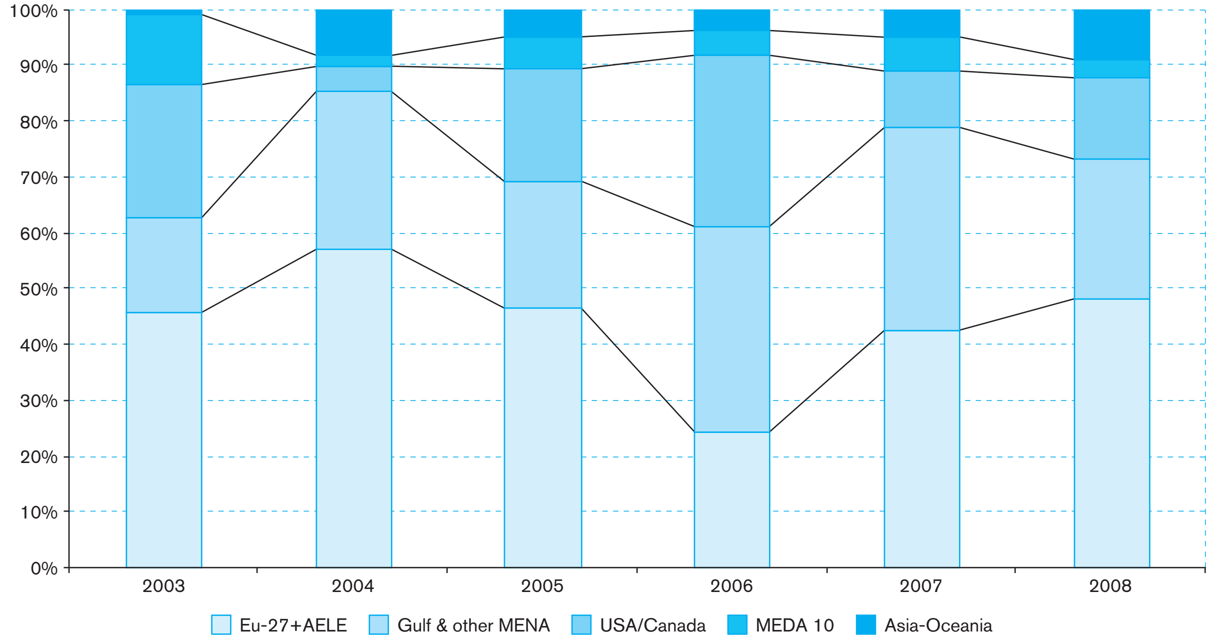
MENA	120
Europe	200
US	450
Asia	120
Other	22
Total	912

Source Samba, December 2008.

The Appeal of the Mediterranean

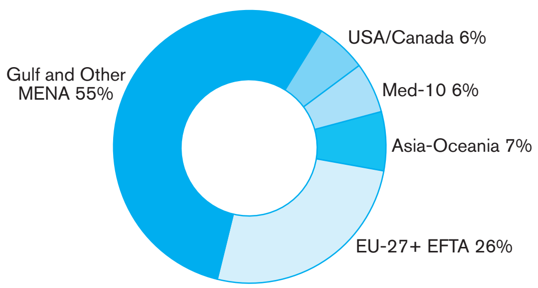
Besides a geographical proximity, and cultural and linguistic affinity, the Mediterranean region offered the Gulf States an attractive alternative outlet for the diversification of their investments and for recycling their financial surpluses. For the Gulf States, investment in the Mediterranean is viewed as an extension of the home market and safer and closer to home, especially after the events of September 11, 2001. Moreover, the Mediterranean region's economic base, as well as economic reform, although patchy, offers high return and an enormous potential given the prospects of further Euro-Mediterranean integration following the Barcelona Process and the Union for the Mediterranean with the envisaged Euromed Free Trade Area

CHART 22 **Relative Contribution of the Main FDI Emitting Regions into the Med Region (Med 13, in % of annualised declared amounts)**



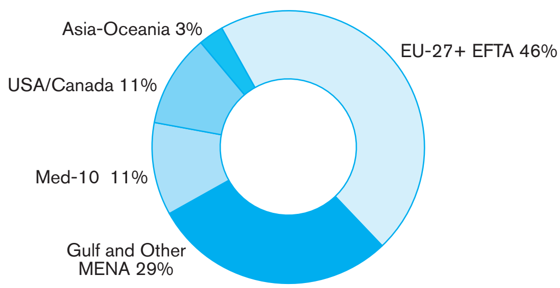
Source: ANIMA-MIPO (2003-2008).

CHART 23 **Main FDI-Emitting Regions towards the Mashreq since 2003 (in % of annualised declared amounts, 2003-08)**



Source: Anima-MIPO.

CHART 24 **Main FDI-Emitting Regions towards the Maghreb since 2003 (in % of annualised declared amounts, 2003-08)**



Source: Anima-MIPO.

in 2010.
Largely due to this, global FDI, especially from the Gulf States, but also from Europe and the US, began to pour into the Mediterranean economies. (See Chart 22)

Gulf Investment in the Mediterranean Is Enduring

Given the Gulf States' financial surpluses and the appeal of the Mediterranean, investment from the GCC into the Mediterranean has been growing over the last five boom years. According to Anima, Gulf investments in the Mediterranean constituted around 30% of total amounts and 18% of announced projects. However, as financial surpluses began to dry up, Gulf investments decreased and recorded only 8.5 billion euros in 2008, against 22 billion in 2007. The Gulf, however, remained one of the main pillars of investments in the Mediterranean, with concentration in the Mashreq (Charts 23 and 24), alongside European investments, which concentrate especially in Turkey, the Maghreb and Egypt.
The United Arab Emirates (UAE) heads the pack with an investment of 30.6 billion euros between 2003 and 2007 (see Table 9), which is more than half of the GCC total, and taking 183 of the projects. In

TABLE 9	Origin-Destination Cross Table 2003-08 (foreign share in gross budgets as announced)												
	Destination	Maghreb				Mashreq					Other Med		Total
Origin	In € mln	Algeria	Morocco	Tunisia	Libya	Egypt	Jordan	Lebanon	Palestine	Syria	Israel	Turkey	
Gulf	Saudi Arabia	736	439	80	12	2,993	1,345	493	53	1,250		3,667	11,066
	Bahrain	143	592	132	0	229	1497	0		452		66	3,110
	UAE	1,939	2,110	4,795	564	17,848	2,313	1,218	0	1,111		3,852	35,751
	Kuwait	2,081	730	296	55	3,009	1,513	1,257	0	1,533		1,148	11,693
	Qatar		54	403	223	1,503	762		339	669		230	4,182
	Oth. MENA	298	217	0	164	1	69	173	0	396	225	823	2,366

Source: ANIMA-MIPO.

2008, the UAE announced a further 66 projects with a cumulative gross value of 17 billion euros, equivalent to 4.7 billion euros in 2008, constituting around 12% of all FDI emitters in the Med region in that year, the majority of which has been in the real estate sector. Three long-term real estate megaprojects –Abu Dhabi Investment Authority (ADIA) and Gulf Investment House (GIH) at Porta Moda in Tunisia (10 years), Al Maabar at Aqaba in Jordon (seven years) and Emirates International Investment Company (EIIC) Dounya Parc (five billion dollars over five years)– alone represent two thirds of this amount. Kuwait and Saudi Arabia follow the UAE with slightly more than 11 billion euros each and more than 100 projects by 2007. In 2008 Kuwait announced a further 34 projects, mainly in Egypt and Jordan, while investment projects of Saudi Arabia fell in 2008 to 22 following 43 projects in 2007, mainly in Egypt and Algeria. The main concentration has been in the real estate sector. In 2008 the Gulf States invested 4.2 billion euros in this sector, which constituted around 50% of the FDI in the region, principally in the Mashreq.

Bahrain and Qatar follow the rank with about 2.3 and 2.9 billion euros respectively and about 20 projects each, while Oman does not appear in Table 9 for lack of projects. Bahrain showed more interest in Jordan and Morocco (Batelco owns Umniah Telecom in Jordan, and real estate and tourism projects by Gulf Finance House in these two countries). UAE-, Kuwait- and Qatar-based investors show a strong preference for Egypt as the main destination of their investments, while investors from Saudi Arabia tend to prefer Turkey, followed by Egypt. Saudi Arabia announced eight significant projects in Turkey in 2007: massive investments by Oger in telecom and banking and acquisition of banks and food-processing industries.

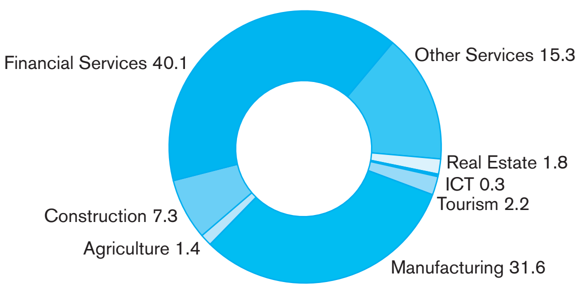
Changing Pattern of Gulf Investments

As well as the size and volume, the pattern of Gulf investments and their diversification in the neighbouring economies has also changed since the 1970s and 1980s earlier oil boom periods. At that time Gulf investments were more concentrated in the traditional sectors of real estate development and activities associated with the hydrocarbon sector. This time round, there seems to be more appetite for diversification, but Gulf investments in the Mediterranean still represent an unbalanced sectoral profile. Construction and transport sectors took 52% of the amounts (and 26 of the projects), while the tourism sector made up 19% and telecom was 10% over 2003-2008. Energy, heavy chemical industry, cement and metallurgy account for 13% of the total. There is also a growing investment in the banking and finance sector. This sectoral mix reflects the model of unbalanced development of the economies of the Gulf, in which consumer goods industries and light industries are not very present.

However, through partnerships with companies based in industrial countries and their accumulated cooperative experience in GCC countries, Gulf investments have increasingly become more diversified and more enterprising. Gulf presence in Egypt, for example, has expanded beyond their traditional areas to include manufacturing, organic farming, communication and information technology, financial services, and logistics (see Chart 25).

The new Gulf leadership in charge of investment decisions has proved to be more bullish than its forefathers. This new generation has had the benefit of a wider business and finance education as well as international exposure and training. International expertise has also been employed to support their investment activities. Gulf investors showed great panache for launching large budgets and ambitious *greenfield*

CHART 25 **Non-Oil Sector Direct Foreign Investments in Egypt 2007-08 (percent of total)**



Source: Balance of Payments Statistics, the Central Bank of Egypt Quarterly Reports (FY2007-8).

projects (the creation of new facilities) in comparison to their European and American counterparts. Over 2003-2007, Gulf investments in *greenfield* projects in the Mediterranean made up 40% of the projects and 53% of the amount invested. External growth (acquisition, including privatisation), or *brownfield* projects, accounted for 23% of the projects and 30% of investment flows.

Conclusions

Despite the global financial crisis, which caught up with the region a little later than elsewhere, the Gulf economies have managed to achieve high growth rates in 2008. Although with the onset of the crisis in 2009 they are expected to slow down, their financial surpluses are estimated to rise even with a worst-case oil price scenario. Recycling their oil wealth is a strategic tool, given their low absorption capacity, particularly for the benefit of the next generation. Foreign investment income is part of a strategy to prepare for a Gulf economy beyond oil.

The attraction to diversify their investment in the neighbouring Mediterranean region beyond traditional markets is more appealing given the high return on their investments and the potential growth of the Mediterranean countries given the partial liberalisation and reform that some of these countries are undergoing. Besides its geographical proximity and cultural and linguistic affinity, the economic base of the Mediterranean countries and the looming Euro-Med space adds a further dimension.

Gulf presence in the Mediterranean, which has been growing over the past few years despite the global financial crisis, which has slowed the pace but not altered the trend, is expected to grow further as Gulf investors start to build up momentum and develop valuable business networks in the region. The scale and nature of the Gulf presence, which has predominantly been in the real estate and tourism sectors, has begun to change and Gulf investments have increasingly become more daring than their US and European counterparts.

Regional dynamics including stability and a successful completion of the Middle East Peace process, as well as further inter- and intra-regional integration, especially between the Mediterranean and the Gulf through, for example, the Greater Arab Free Trade Area (GAFTA) are bound to increase this relationship. In addition, the possibility of linking the EU-GCC track with the Union of the Mediterranean will provide the needed institutional framework under which greater exchange of trade and investment is bound to flourish. The institutional support for the combination of European know-how and technology with Gulf financial muscle will help to invigorate the very necessary and long-awaited development process in the Mediterranean region.

References

Abdelkrim, S.; Henry, P. (eds.). “Foreign Direct Investment Towards the Med Countries in 2008: Facing the Crisis.” *Anima Investment Network Study*, No. 3, March 2009.

Institute of International Finance (IIF). *Summary Gulf Cooperation Council Countries*. Appraisal, 6 November 2008

IIF. *Update*. Gulf Cooperation Council Countries, 4 December 2008,

Joffé, E.G.H. “Investment in the South Mediterranean” in *The Euro-Mediterranean Dialogue: Prospects for an Area of Prosperity and Security*. Rome: Foundation for European Progressive Studies/ Fondazione Italianieuropei, 2009.

VV.AA. *The Coming Oil Windfall in the Gulf*. McKinsey Global Institute, January 2008.

VV.AA. “Tracking GCC Foreign Investments: How the Strategies are Changing with Markets in Turmoil.” *Report Series*, Samba Financial Group, December 2008.