



SUSTAINABLE INTRA GCC TRADE-TOO LITTLE TO ANALYSE OR ARE WE MISSING SOMETHING?

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ABSTRACT

Purpose: This paper analyses trade patterns between Gulf Corporation Council (GCC) states, and diversification within these in order to explore the success of a potential single currency union.

Design/Methodology/Approach: This empirical research quantitatively analyses patterns of merchandise trade between the GCC states during 2005–15, with specific focus on concentration, diversification and similarity of trade (export and import) as well diversification within GCC economies.

Findings: The paper concludes that while Bahrain exports show dissimilarity when compared with other GCC states, its imports appear very similar. The other five GCC states show similarity among themselves in both exports and imports. Diversification can help in sustainable trade between GCC states in the medium to long-term.

Originality/Value: The results of the paper will be of value to GCC policymakers to provide a clear rationale for boosting trade and diversification with the long-term goal of a single currency economic union.

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INTRODUCTION

The Gulf Cooperation Council (GCC) was set up in 1981 between Bahrain, Oman, Qatar, Saudi Arabia, United Arab Emirates and Kuwait to strengthen cooperation and economic development in the region. The GCC has made strides towards economic consolidation by forming a customs union and a common market. The long-term vision is to create an Economic and Monetary Union (EMU) with a single currency. Progress towards the EMU has been slow, and the recent oil price plunge has led to concerns regarding member countries' sustainable growth due to their significant dependence on oil and their lack of diversification (Ganguli, 2016). The GCC economies, although similar, do not meet all the convergence criteria that were met by the **European Union** (EU) accession countries during the 1990s prior to joining the Economic and Monetary Union (EMU). Therefore, the GCC economies are not considered ready for a sustainable single currency zone without further diversification and integration (Ganguli, 2016).

Since 2001, GCC economies have formed a common market and forged a customs union. Dr Khalid Shams Abdulqader (2015) stated that:

“Perhaps the GCC’s greatest achievement to date has been its success in invigorating trade among its member states, via the customs union and the joint market. Merely getting this far was sure to have a positive impact on mutual trade . . . almost \$100 billion in trade took place between member states in 2013. This is seven times greater than it was in 2000, before the launch of the customs union. Despite this dramatic growth, however, mutual trade still represents a mere 7.1 per cent of the aggregate foreign trade conducted by the six member states.”

In contrast, in 2013 just over 62% of the total value of goods (intra-EU and extra-EU trade combined) exported from EU Member States was directed to other Member States (Eurostat database, 2016). One of the reasons for slow trade is the lack of a good transportation network among GCC states. Some of the GCC states, for example, Bahrain, UAE and Qatar, have become important aviation hubs; this has helped in integrating the region through air transport. The role of the private sector has remained weak and the government sector has loomed large with heavy expenditure and high employment levels.

DIVERSIFICATION IN THE GCC

Each GCC country has launched a diversification strategy to overcome the hurdles imposed by fluctuations in oil prices under a heavy dependence on oil. The Bahrain 2030 economic vision aims to provide a robust and vibrant private sector that employs Bahrainis; these employees will be able to access proper healthcare, education and a sound and secure



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environment. Its national development strategy aims at developing a sound business environment aimed at doubling the income of Bahrainis through a competitive economy, boosted by a growing private sector. Bahrain aims to build a knowledge-based economy.

Kuwait would like to diversify into trade and finance led by a competitive private sector. It aims at a strong legal system. In addition, the government targets a strong fiscal system for a strong private sector growth. The six pillars of reforms include private sector reforms, labour market reforms, institutional and fiscal reforms, among others. Attracting foreign investment is another goal for the government, together with improving the business climate, diversification and Public Private Partnerships (PPPs).

Oman identified sectors such as logistics, manufacturing, fisheries and mining for further development as part of an aggressive strategy for diversification. Oman's 9th development plan aims to reduce dependence on oil through boosting the Small and Medium Enterprise (SME) sector, providing training and education for absorbing more Omanis into the private sector by reducing expatriate employment and creating PPPs.

Qatar's diversification strategy is built on improvement in education, culture, responsible use of natural gas, sports, finance and transportation, among others. Fiscal restructuring is also planned for the future, together with efforts for improving the health and education system, improved participation of Qataris in the labour force, environmental development, among others.

Saudi Arabia follows similar diversification strategies, including higher participation of Saudi nationals in the labour force, diversification of the national economy and increased privatisation as the main goals. The National Transformation Program (NTP) aims to increase the share of the private sector from 40% to 65% by 2020, as well as increasing the contribution of the SME sector from 20% to 35%. PPP schemes are envisaged for increased private sector participation and fiscal restructuring has been implemented for combatting higher budget deficits due to low oil prices.

The UAE has been the most diversified among all the GCC states, and aims to become a knowledge-based economy with sustainable development goals for environmental protection and management.

Literature Survey

Ravi (2013) pointed out that the intra GCC trade is at a very modest level, and an integrated GCC has not achieved a significant GCC trade level. Moreover, the trade is heavily influenced by oil prices. Boughanmi (2008) suggested that although intra GCC trade is small, it is not insignificant compared to the predictions of the gravity trade model that was used in his paper. Askari et al. (2003) indicated that the lack of diversification and complementarity led to low intra GCC trade. Gani (2011) discussed that the lack of a business environment has led to low trade within the GCC. He used various business environment indicators that showed a significant impact on trade in the GCC, and called for major reforms in such areas for boosting trade within the region. Hossain and Naser (2008) discussed the improvement in trade in the GCC since



the implementation of the customs union, which was also followed by higher levels of Foreign Direct Investment (FDI), joint ventures and technology diffusion in the region.

Abdmoulah (2011) suggested that intra GCC trade can be enhanced using the diversification of the export strategy away from oil, and opening markets for GCC exports through the ratification of more regional trade agreements. Facilitation of further trade through the opening of more transport and communication networks within the region, and free movement of labour, capital and resources within the same should be enhanced.

Wolde and Bhattacharya (2010) concluded that delays in customs clearance and lack of infrastructure, such as transport facilities, explain why trade in the Middle East and North Africa region (MENA) is low compared to the predictions of the gravity trade model. Dennis (2006) showed that GCC trade with the EU will lead to higher benefits than the integration of the GCC itself. Mundell (1961), in his Optimum Currency Area (OCA) analysis, concludes that countries benefit from using a single currency in a region due to microeconomic gains arising from easier transactions owing to price transparency, reduced exchange rate risks, higher trade and investment due to loss of risks, higher capital and labour mobility for ease of doing business.

This paper addresses diversification efforts in the GCC, and studies the nature of intra GCC trade to examine if intra GCC trade and diversification activities pay off with complementarity.

Achievements of Diversification Efforts in the GCC

Callen et al. (2014) mentioned:

“Growth in GCC non-oil output averaged 6.8 percent during 2000-13, and the share of the non-oil sector in total real GDP rose by 12 percentage points to 70 percent, driven mainly by Saudi Arabia and the United Arab Emirates.”

Most of the growth in non-oil output has been linked to the growth in oil prices after 2000. A total of seven million jobs have been created in the GCC during 2000-2010. Of these, 88% of the private sector jobs were offered to expatriates, while nationals filled 70% of the public sector jobs. Although there has been non-oil exports growth in goods, the growth has not been uniform across the GCC states. Most of the growth in non-oil manufacturing exports has originated from Saudi Arabia, Dubai and Oman. In its true sense of diversification, Dubai has fared well among the GCC states through the strengthening of sectors such as aluminium (Dubai Aluminium (DUBAL), now part of Emirates Global Aluminium), transportation (Emirates Airlines and two large airports), trade (Jebel Ali Port), finance (Dubai International Financial Center), and tourism (more than 500 hotels) (Callen et al., 2014).

Outside the Middle East, the GCC has entered into discussions with India, the EU and others to sign free trade agreements. Three of the GCC states have signed free trade agreements with the USA, and a GCC-Singapore free trade agreement was ratified in 2013. Export promotion and diversification strategies are being focussed on



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the establishment of the Export Development Authority in Saudi Arabia and an Export Development Center in Bahrain.

As part of its diversification initiatives in the GCC, Bahrain has attracted offshore financial institutions to create a financial hub. Bahrain's financial sector contributes 17.2% towards its GDP (http://www.cbb.gov.bh/page-p-financial_sector_fact_sheet.htm). Training and development and possibilities of career progression had a positive impact on Bahraini rates in the financial sector of Bahrain (Ganguli and Matar, 2016). Medical tourism represents a particularly rich opportunity for Bahrain to further diversify its tourism strategy, allowing its travel and hotel sectors to prosper, intensifying competition for higher quality medical services, and allowing hotels and hospitals to optimise their performance (Ganguli and Ebrahim, 2017). The UAE and Qatar have developed airlines and logistics; Saudi Arabia is developing industrial clusters around oil and its technology; Kuwait is focussing on the oil industry, and Qatar on natural gas and energy related sectors.

International Trade and the GCC states

The literature has mentioned that GCC states have little or no trade between themselves, and there has been little improvement in the volume of trade in the aftermath of the integration in the GCC with efforts such as free trade agreements, common market and customs union. This paper studies the nature of merchandise trade within the GCC to identify any trend in changes in the composition of the trade items in the recent years. Table 1 shows the concentration and diversification indices of the merchandise export items of the GCC states for the years 1995 and 2005 respectively. The concentration index shows if the country's export and import goods are concentrated on a few products or are well diversified across the basket of tradable goods.

Table 1 Merchandise Export Product Concentration and Diversification Indices of the GCC States at the three Digit Standard International Trade Classification (SITC) level

Economy	1995			2015		
	Items	Concentration Index	Diversification Index	Items	Concentration Index	Diversification Index
Bahrain	180	0.40	0.76	217	0.31	0.67
Kuwait	186	0.61	0.84	218	0.60	0.79
Oman	151	0.75	0.76	219	0.45	0.72
Qatar	112	0.63	0.83	211	0.51	0.80
Saudi Arabia	241	0.68	0.83	247	0.53	0.76
UAE	250	0.06	0.35	258	0.24	0.48

Source: UNCTAD Stats

As evident from the economic diversification initiatives of the GCC states discussed above, there has been a slight improvement in the export concentration indices for merchandise products between 1995 and 2015, with all countries having reduced these

values. This indicates that the exports of the GCC economies are less concentrated on their hydrocarbon and hydrocarbon-related products, although by a small margin. The diversification index, which shows values closer to 1 for all the GCC states in 1995 (due to the high concentration of hydrocarbon-related exports in their share of total exports to the rest of the world), indicates a slight decrease in 2015 from the 1995 values; this implies lesser divergence from the world patterns of exports, although marginal. Both the indices point to similar patterns of more diversity or lesser concentration of items from oil and oil-related products in the export basket. This change in pattern does not necessarily relate to the recent oil price decline since the indices are calculated on the basis of total exports/imports of commodities. The only exception in the above trend of the values is the reversal of the export concentration and diversification indices for the UAE from a lower to marginally higher levels; however, it remains significantly less than the other GCC countries. The relatively more diversified nature of the UAE economy is evident from the above values, despite their marginal increase from 1995 to 2013. Cherif and Hasanov (2014) mention that compared to the rest of the GCC, the UAE has increased its non-oil exports substantially.

Table 2 Merchandise Import Product Concentration and Diversification Indices of the GCC States During 1995 and 2015

Economy	1995			2015		
	Items	Concentration Index	Diversification Index	Items	Concentration Index	Diversification Index
Bahrain	230	0.27	0.46	240	0.11	0.44
Kuwait	205	0.10	0.39	243	0.10	0.37
Oman	225	0.09	0.44	245	0.09	0.38
Qatar	212	0.11	0.46	246	0.09	0.42
Saudi Arabia	251	0.06	0.37	245	0.09	0.33
UAE	250	0.06	0.35	259	0.10	0.33

Source: UNCTAD Stats

Table 2 shows the merchandise import product concentration and diversification indices of the GCC states during 1995 and 2015.

The GCC economies exhibit a very low concentration and similarly low diversification indices, indicating that the imports are widely diversified; they are also similar to world patterns in 1995 and 2015 respectively. This is natural since most of the GCC countries have to import all essential commodities. The number of import items has increased for all the GCC economies over the years, but the concentration index has either declined or remained steady for all the GCC states; this is clearly a redeeming feature. The diversification index has declined for all and therefore corroborates the findings regarding more diversification efforts of the economies. The only exception is, again, the UAE, although by a small margin.

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Similarity of Trade between the GCC States

Similarity index¹, as initially provided by Grubel and Lloyd (1975), shows the degree to which two economies trade similar products. Higher values of the index (>0.5) show high similarities of trade between countries and low values indicate lower similarity. Table 3 shows the similarity index between Bahrain and each of the GCC states in 1995 and 2013. The table shows that exports between Bahrain and each of the GCC states were very similar in nature in 1995. However, the same is not true between Bahrain and the rest of the GCC in 2013: Bahrain's exports show marked dissimilarity from those of the other GCC states. This is possibly a reflection of Bahrain's diversification efforts launched earlier than most GCC states. Table 3 also shows Bahrain's similarity index in terms of imports with the rest of the GCC states. It shows that Bahrain's diversification efforts have not been able to sustain self-sufficiency in imports as its imports are very similar in nature to the imports of the rest of the GCC states. These similarity indices have either remained the same or have increased marginally in 2013 from 1995 values.

Table 3 Bahrain's Similarity Index with GCC countries

	Bahrain's Similarity Index			
	Exports		Imports	
	1995	2013	1995	2013
Bahrain	1.00	1.00	1.00	1.00
Kuwait	0.57	0.23	0.70	0.74
Oman	0.55	0.24	0.51	0.59
Qatar	0.49	0.16	0.65	0.63
Saudi Arabia	0.51	0.15	0.50	0.72
United Arab Emirates	0.53	0.28	0.54	0.56

Source: UNCTAD Stats

¹The index is calculated at the three-digit level of the SITC Revision 3 and ranges from 0 to 1. Value closer to 1 reveals the greater similarity of the trade structure between two countries or two groups of countries. The indicator is computed as follows:

$$S_{jk} = 1 - \frac{1}{2} \sum_i |h_{ij} - h_{ik}|$$

where

S_{jk} = Indicator of similarity in merchandise trade structures

h_{ij} = Share in total merchandise exports or imports of product i of country or country group j

h_{ik} = Share in total merchandise exports or imports of product i in country or country group k

<http://unctadstat.unctad.org/wds/TableViewer/summary.aspx>

Table 4 Kuwait's Similarity Index with GCC Countries

	Kuwait's Similarity Index			
	Exports		Imports	
	1995	2013	1995	2013
Bahrain	0.57	0.23	0.70	0.74
Kuwait	1.00	1.00	1.00	1.00
Oman	0.68	0.66	0.68	0.64
Qatar	0.77	0.50	0.58	0.71
Saudi Arabia	0.75	0.86	0.71	0.75
United Arab Emirates	0.78	0.61	0.67	0.60

Source: UNCTAD Stats

Kuwait's exports and imports with rest of the GCC are very similar, both in 1995 and 2013. This indicates a dependence on oil for exports and less diversification due to import requirements remaining similar to all GCC countries. The same trend is noticed among all GCC states, except Bahrain as mentioned in Table 3.

Table 5 Oman's Similarity Index with GCC Countries

	Oman's Similarity Index			
	Exports		Imports	
	1995	2013	1995	2013
Bahrain	0.55	0.24	0.51	0.59
Kuwait	0.68	0.66	0.68	0.64
Oman	1.00	1.00	1.00	1.00
Qatar	0.76	0.59	0.60	0.62
Saudi Arabia	0.79	0.62	0.67	0.67
United Arab Emirates	0.76	0.63	0.64	0.56

Source: UNCTAD Stats

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Table 6 Qatar's Similarity Index with GCC Countries

	Qatar's Similarity Index			
	Exports		Imports	
	1995	2013	1995	2013
Bahrain	0.49	0.16	0.65	0.63
Kuwait	0.77	0.50	0.58	0.71
Oman	0.76	0.59	0.60	0.62
Qatar	1.00	1.00	1.00	1.00
Saudi Arabia	0.85	0.46	0.58	0.68
United Arab Emirates	0.78	0.50	0.57	0.59

Source: UNCTAD Stats

Table 7 Saudi Arabia's Similarity Index with GCC Countries

	Saudi Arabia's Similarity Index			
	Exports		Imports	
	1995	2013	1995	2013
Bahrain	0.51	0.15	0.50	0.72
Kuwait	0.75	0.86	0.71	0.75
Oman	0.79	0.62	0.67	0.67
Qatar	0.85	0.46	0.58	0.68
Saudi Arabia	1.00	1.00	1.00	1.00
United Arab Emirates	0.77	0.58	0.67	0.65

Source: UNCTAD Stats

Table 8 UAE's Similarity Index with GCC Countries

	United Arab Emirates' Similarity Index			
	Exports		Imports	
	1995	2013	1995	2013
Bahrain	0.53	0.28	0.54	0.56
Kuwait	0.58	0.61	0.67	0.60
Oman	0.76	0.63	0.64	0.56
Qatar	0.78	0.50	0.57	0.59
Saudi Arabia	0.77	0.58	0.67	0.65
United Arab Emirates	1.00	1.00	1.00	1.00

Source: UNCTAD stats

CONCLUSIONS

This paper has studied diversification efforts in the GCC in the recent times, and examined GCC economies from their trade concentration, diversification and similarity indices for the years 1995 and 2013. The literature mentions that the GCC economies exhibit low intra GCC trade. It has identified various reasons for this, such as low infrastructure, lack of transportation, inadequate business environment, lack of diversification and trade complementarity for low intra GCC trade. The paper examined the concentration, diversification and similarity indices of the GCC countries and concludes that economic diversification initiatives of the GCC states seem to have resulted in a slight improvement in the export concentration indices for merchandise products between 1995 and 2015 for GCC countries. The only exception in the above trend is the reversal of the export concentration and diversification indices for the UAE from lower to marginally higher levels during 1995 to 2013; however, they remain significantly less than the other GCC counterparts. The relatively more diversified nature of the UAE economy is evident from the low values of all indices despite the marginal increases in the indices during 1995 to 2013.

The diversification indices show a similar pattern to the concentration indices as they are two sides of the same coin; they verify the findings from the examination of the concentration indices. Bahrain's exports show a marked dissimilarity from those of the other GCC countries from examination of the similarity index. This is possibly a reflection of Bahrain's diversification efforts that were launched earlier than most GCC states. The rest of the GCC countries show high similarity indices in 1995 and 2013, both in imports and exports with minor exceptions. This indicates that results of diversification initiatives are yet to kick off and spill over to the international trade sector, and, at present, GCC economies, with the exception of Bahrain, exhibit very similar trade in products and a low degree of diversification.

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