GCC Single Market Failure: Problems And Solutions

*By-Omar al-Ubaydli**

In 2008, the Gulf Cooperation Council (GCC) launched its own version of the European Union's (EU) hugely successful single market. Goods, labor, and capital were all supposedly permitted to flow across the GCC's internal borders unencumbered by fees or legal restrictions. A Kuwaiti should be free to relocate to Oman, secure employment with an Omani pension, find local schools for his children, spend his summers in his Bahraini apartment, and live off his Saudi share dividends.

Almost six years on, as my co-authors Mahmood Abdulghaffar and Omar Mahmood and I discuss in a recent paper published in Middle Eastern Finance and Economics, it is safe to say that this vision is some way from being realized. The Federation of GCC Chambers of Commerce has documented a litany of single-market malfunctions spanning the entire spectrum of economic activity: jobs are advertised explicitly favoring nationals over other GCC citizens, GCC trucks face long waits and fees when crossing borders, GCC banks are unable to open GCC branches, GCC citizens cannot purchase GCC shares or real estate outside their home country, and many other examples.

This is not merely a problem of foregone potential gains. Spurred on by the recent improvement in Western-Iranian relations, the GCC has accelerated toward monetary union (MEES, 13 December 2013). For the single currency to work properly, a precondition is a correctly functioning single market, and so the GCC is at risk of putting the cart before the horse. Fortunately for policymakers, comparing the GCC to the EU helps us diagnose and fix the problems.

SINGLE MARKETS: WHAT AND WHY?

You go into a supermarket and purchase chocolate. You don't feel like eating it immediately, so you put it in your pocket and drive home. When hunger strikes, you consume the bar. Thankfully, despite choosing to eat it at home rather than its point of purchase, there are no extra fees to pay or any forms to complete. If there were, you would probably not bother buying a chocolate. And if moving goods around town meant having to pay fees and fill out lots of paperwork, your wages' real value would be a lot smaller, and so you probably wouldn't work as hard either. People would have to find ways to produce the goods and services they want in their own home, and if this was too inefficient, they would simply go without.

A single market involves eliminating all the barriers to geographically relocating goods and factors of production. The simple chocolate example illustrates the potentially huge benefits of integrating markets. Single markets facilitate the flow of resources to their most valuable uses: efficient producers drive out inefficient ones who would otherwise be propped up by tariffs or legal protections; entrepreneurs face a much stronger incentive to innovate since they can deploy their invention on a much larger scale; consumers with peculiar tastes are much more likely to find a company that can cater to them because the market is big enough to support diversity; workers with a skill from a country that is suffering from an oversupply of the skill can move to a country that has a shortage; and so on.

In principle, the GCC stands to gain much more from a single market than the EU due to its cultural and linguistic homogeneity. Greek nurses looking to move to Finland to solve a shortage of Finnish nurses have to worry about learning Finnish, different cultural customs, a radically different climate, and being quite far from home. These barriers impair the single market's ability to transfer resources to their most efficient use. In contrast, a Qatari banker thinking of moving to the UAE already speaks Arabic, has grown up with almost identical customs, is used to the searing heat, and knows that his relatives are no more than an hour away by plane (in fact he is likely to have many members of his extended family living in the UAE). So if anything, the GCC single market should be more desirable than its EU counterpart and easier to implement.

THE GCC SINGLE MARKET

Several years after its 2008 activation, various GCC General Secretariat statistics point to some success in the GCC single market project. In 2011: 13mn GCC citizens traveled within the GCC; 41,000 GCC citizens worked in another GCC country; 16,000 GCC citizens owned real estate in another GCC country; 35,000 licenses for economic activity were granted to GCC citizens outside their home country; 456,000 GCC citizens owned shares in joint stock companies listed in another GCC country; and intra-GCC trade was $85bn.

However according to the same data source, certain figures point toward a seriously malfunctioning GCC single market (the following are purely illustrative and are not meant to highlight any particular offenders):

- 32 non-Omani GCC citizens worked in the Omani private sector.
- 18 non-Saudi GCC citizens were enrolled in Saudi retirement plans.
- Two Omani citizens owned real estate in Qatar, compared to 966 Omanis in the UAE.
- One non-Qatari GCC bank operated in Qatar.
- Three loans were given by the Kuwaiti government to non-Kuwaiti GCC industrial projects.

By way of comparison, a few years after its 1992 inception, the EU single market was already flourishing, and scholars were able to produce evidence of the economic benefits. Why has the GCC project progressed so slowly compared to the EU despite the obvious advantages that the GCC has over its European counterpart?

The problem is essentially an issue of enforcement: the relevant GCC institutions have passed the laws which nominally constitute a single market, but thousands of public and private institutions in the member states are failing to fully comply with the laws and are not being held accountable. The non-adherence is due to a combination of procedural ignorance, institutional inertia, and willful non-compliance, and there is no GCC institution that has the power to rectify the situation.

GCC: STRUCTURAL MALFUNCTION

The GCC is composed of five main bodies complemented by a range of committees. The only body that has substantial executive powers is its highest authority, the Supreme Council, which is made up of six heads of state (the other bodies are consultative and administrative). The Supreme Council meets annually, and while some decisions require only a majority, important decisions require unanimity. Critically, it is not conceived to represent the GCC's holistic interests. The prevalence of veto power for each country means that the GCC is better described as an intergovernmental forum than a union.

The GCC is not structured in a manner that permits the sort of systematic and wide-ranging enforcement needed for the

Continued on – p21

Continued from – p20

correct functioning of a single market. For example, suppose that a Bahraini businesswoman applies for a license to operate a business in Saudi Arabia and she is refused on the grounds that she does not have Saudi citizenship. There is no GCC body to whom she can complain: if she goes to the Secretariat General, they will correctly point out that there is nothing that they can do, and that her complaint must be forwarded to the Saudi government. If the Saudi government decides to willingly violate the single market rules (possibly in defense of its own citizens' narrow interests), then the complainant is out of options. In principle, the Secretariat General could schedule a discussion of the Bahraini businesswoman's complaint in the Supreme Council's next annual meeting, and the Supreme Council could then issue a decree, but that is clearly an inefficient use of the Council's time.

Put shortly, enforcing a single market requires a dedicated institution which has substantial resources and considerable executive powers. No such institution exists in the GCC. What about the EU?

TOWARD A SOLUTION: EU MODEL

The EU successfully enforces its single market by depending on the efforts of a well-resourced, powerful institution that is constitutionally mandated to pursue the EU's holistic interests: the European Commission (EC). Its nominal independence from the EU's 28 member states means that it will seek to punish countries that violate single market rules in their own interest against the collective interests of the EU, and its 33,000 employees and constitutional powers ensure that it has the means to do so (in comparison, the GCC Secretariat General has around 500 employees, which is a sixth of the EC's workforce on a per capita basis).

Despite its considerable resources, the EC cannot directly police the EU's 500 million citizens, and so it works in partnership with the member governments. If an EU company is failing to comply with a single market rule, the national government responsible must act. Upon detecting a violation, the EC will formally remind the national government of its responsibility. If the government persists in its failure to enforce, the EC will initiate legal proceedings, including fines, against it under the supervision of the European Court of Justice.

For example consider the case of Commission V Greece C-387/97 regarding the illegal Kourroupitos landfill in Greece. The case arose due to an alleged failure to apply the Waste Framework Directive and Hazardous Waste Directive, which concern the closure and cleanup of illegal landfills. The EC requested a daily penalty of 24,600 ECUs (the Euro's predecessor). The Court of Justice awarded a 20,000 ECU fine.

THE DISTANT FUTURE: FEDERATION?

The EU's superiority in enforcing a single market is due in large part to the maturity of its institutions: the process of European economic integration commenced in the immediate postwar era, compared to the 1980s in the case of the GCC. However the EC still has to rely on the help of the member governments in enforcing EU law.

Federations such as the USA and Australia, which represent a higher level of political and economic integration than the EU, boast centralized institutions that are powerful enough to enforce laws directly without the need for assistance from constituent governments. The Federal government in the US commands a much larger budget and workforce than the EU's centralized institutions on a per capita basis.

For example in the US, the Environmental Protection Agency is a Federal institution that is charged with regulating the environment. If it detects a violating firm in, say, the state of California, it will initiate legal proceedings against the company directly rather than holding the California State government accountable. It can do this because the federal governmental architecture provides it with the necessary financial resources and executive authority. However this technique of enforcing a single market is not an option for the GCC as many intermediate steps of economic and non-economic integration must first be completed.

WHAT SHOULD THE GCC DO?

Despite centuries of murderous conflict and cultural heterogeneity, the EU has been far more successful in establishing a single market than the peacefully coexisting and culturally homogenous members of the GCC. While it is unclear if the EU system is appropriate for the GCC, it is clear that the current GCC structure is not working. If it genuinely wants to create a single market, the GCC needs to reform its institutions. The first step is for the six member states to agree to cede some more power to the centralized GCC institutions, and for them to acknowledge that maintaining a discretionary veto option on a wide range of GCC laws is incompatible with a functioning single market.

A departure point worth considering would be to grant the GCC Secretariat General more power, as this would limit the need to undertake a massive overhaul of the GCC's structure. Whatever path the GCC chooses, it should take note of the UAE Central Bank's reminder that a sound single market is a precondition for a single currency rather than a parallel project. ◆◆

***Omar al-Ubaydli is a Senior Fellow at the Bahrain Center for Strategic, International and Energy Studies.**

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