

# Gulf States Newsletter

Bahrain, Iran, Iraq, Kuwait, Oman, Qatar, Saudi Arabia, UAE, Yemen

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## GSN

### Companies & People

#### **Bahrain Assembly Hits Government Where It Hurts**

Bahrain's new House of Deputies has demonstrated an unexpected independence by refusing to give immediate approval to the government's \$500m international bond programme signed with **BNP Paribas, Salomon Brothers International** and **Schroeder, Salomon, Smith Barney**. With the Shia **Al-Wefaq National Islamic Alliance** and the main secular opposition having boycotted last October's general election, the Assembly is dominated by Sunni Islamists – who were expected to take a solidly pro-government line, save on issues such as the sale of alcohol. But the new deputies, with **Al-Assalah Society** leader **Sheikh Adel Al-Mowdah** in the vanguard, want detailed explanations of how the money will be used.

In a sign of the times, the Islamists are also angry that the government did not try to raise the funds from Islamic institutions before turning to the international markets. The bond is intended to finance \$130m of the \$1.7bn **Aluminium Bahrain (Alba)** expansion, the **Bahrain Petroleum Company (Bapco)** refinery upgrade

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**Foreigners dominate the workforce in many Gulf states: how to manage this reliance is a fundamental issue, but relatively little is known about key groups of migrant workers. A recent study from Kerala throws some light on this trend, but key questions remain: can Gulf economies be as competitive if they employ nationals rather than cheaper expatriates?** PAGE 9

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### GSN's Analysis

**Stung by their apparent impotence in the face of a US-led confrontation with Iraq, Arab governments have rearranged their planned Bahrain summit. It will now be held in Cairo in early March to help regain momentum. The initiative comes amid signs of life in Pan-Arab policy, with Amr Moussa trying to beef up the Arab League.** PAGE 3

**Egyptian President Hosni Mubarak has to wrestle with internal problems while balancing a parlous geopolitical situation. GSN reports from Cairo on Egypt's role in the region's conflicts. We assess the weight with which a traditional Arab giant now punches.** PAGE 4

**Intelligence is king in the "war against terrorism", but its use in defining global conflicts is contentious, with US and UK troops building up for an assault on Iraq. Colin Powell's best moment at the UN on 5 February came when signals and human intelligence met via telephone intercepts of Iraqi generals. Powell sounded least convincing when trying to make the Al-Qaeda/Iraq link. Intelligence agents are protesting at being "politicised" over this issue in a dispute that is obscuring the USA's arguable – but not conclusive – case for tackling Iraq almost immediately.** GSN VIEW, PAGE 2

**The Kurdistan Regional Government could provide a model for a post-Saddam Iraq. GSN analyses the KRG.** MIDDLE EAST INSIDER, PAGE 13

**Qatar's leaders remain apparently relaxed in the face of rising regional tensions, preferring to focus on the potential of gas projects rather than any political downside. GSN rates Qatar B/2+.** RISK MANAGEMENT REPORT, PAGE 16

**Elements of the Saudi leadership tend to deny there are any domestic tensions, but Crown Prince Abdallah's Charter implies major change is necessary, so the Al-Sauds can evolve to survive. There are legitimate political risk and payments fears in GSN's C/2- Risk Grade.** RISK MANAGEMENT REPORT, PAGE 17

**Ten years ago incoming US President Bill Clinton promised to "focus like a laser" on the economy, but real challenges loomed in Iraq, Somalia and Bosnia.** PERSPECTIVE, PAGE 2

There could not be a better time for Prince Turki Bin Faisal Al-Saud to be appointed Saudi Ambassador to the UK. Prime Minister Tony Blair's London is at the centre of the US-led diplomatic offensive to force Iraq to disarm and President Saddam Hussein to go. Jetting into London on 5-6 February, Iranian Foreign Minister Kamal Kharazi said his sole aim was to discuss Iraq with Blair and Foreign Secretary Jack Straw, just back from watching Colin Powell's magisterial personal display at the UN Security Council.

Prince Turki is especially well qualified to interpret contemporary Western politics for a Saudi government in which he holds ministerial status. With the late Kamal Adham, he fathered the Saudi intelligence service – and in Blair's London, as in President George W Bush's Washington, intelligence is king. It is satellite intelligence that Powell used to try to convince the world on 5 February that now was the time to strike against Iraq. The US Secretary of State's best moment, perhaps, was when technology met human intelligence via telephone intercepts of Iraqi generals apparently discussing concealment from the UN weapons inspectors. But intelligence is a difficult business, as any professional would admit. US signals intelligence monitored hundreds of thousands of conversations; they found the fag ends of a smoking gun, but no cigar.

Powell sounded least convincing when trying once more to make the Al-Qaeda/Iraq link. As predicted, he cited Ansar Al-Islam in northern Iraq and the presence in Baghdad of alleged Al-Qaeda toxins expert (and possibly hit man in Jordan) Abu Musab Al-Zarqawi. As GSN put it last time: "A 'Smoking Gun' May Rise Out Of The Underworld" (GSN 702/3). But despite claiming as much by presenting 'new evidence' of an Al-Qaeda cell organising in the last eight months out of Baghdad, the US case – previously rehearsed by Blair – for a Bin

Laden/Saddam link looked thin.

So thin, indeed, that intelligence agents have protested at being "politicised" over the issue. Central Intelligence Agency (CIA) and British security operatives have complained unusually loudly about their political bosses pressuring them to produce intelligence that 'proves' an Al-Qaeda link. This would place Iraq more firmly in a 9/11 context than Bush has been able to do since inventing the 'Axis of Evil' one year ago. Anglo-Saxon politicians believe that lining up the elusive Bin Laden with Saddam would convert a sceptical majority in the West to accepting that a military solution is inevitable to finish off the work of the last Gulf war.

The BBC was leaked a 12 January UK Defence Intelligence Staff briefing on Iraq/Al-Qaeda – embarrassingly unveiled by defence correspondent Andrew Gilligan on 5 February – that reported contacts, but said that "any fledgling relationship foundered" between two antagonistic ideologies. In response, and only hours before going in to bat after Powell at the UN, Foreign Secretary Straw argued weakly that: "The Iraqi regime seems to be allowing a permissive environment... What we don't know is the extent of those links." No wonder Blair sounded less convinced of his facts in Parliament on 5 February than he had a week before when quoting 'intelligence' on the Al-Qaeda link.

Outside a domestic US context, these manoeuvres are baffling when the rest of Powell's presentation is taken into account. It built up an arguable – but not conclusive – case for tackling Iraq now. If the USA's new pre-emptive doctrine of international relations is to be followed, it should lead to military conflict. The problem for the Bush Administration and its few real friends (who include Blair but not most of his party) is that the Arabs and Europeans see war only as a last resort – and for them the jury could be out for a very long time.

## Perspective: Ten Years Ago

The Western missile and air strikes against Iraq added a harshly discordant note to President Bill Clinton's otherwise upbeat and festive inauguration in Washington; a baleful underlining of the foreign policy dilemma he faces. Clinton had vowed over and over to "focus like a laser" on the nation's economy, but when he was sworn in as the 42nd chief executive of the USA, he faced even more pressing concerns.

"Challenges abound and we all know them", Clinton declared in one of his campaign speeches. He listed the crises in Iraq, Somalia and Bosnia by name. But to know the problems is not necessarily to be able to solve them – a distinction which will now be disagreeably obvious to the incumbent in the White House. Of all the crises, Iraq clearly presents the most immediate – and the most difficult – challenge to the new US President.

Missiles and air strikes forced Saddam Hussein to back down from his attempt to defy United Nations rulings on Iraq and reaffirmed the conspicuous inadequacy of Iraq's

military capacity. But the confrontation also confirmed the seemingly unbridgeable gap between Baghdad and a majority of other countries about just what Iraq is or is not permitted to do under the Gulf War ceasefire resolutions...

It is a measure of Saddam's political adroitness that by constantly frustrating and thwarting the consensus in the UN about Iraq he has managed to divert that consensus into questioning the validity of its own policies. Yet a vast majority of countries continue to condemn Saddam's rule and expect the USA, largely, to be the instrument of that condemnation. Even the Arab states, except for Sudan and Yemen, continue to insist on Iraq's compliance on all the Security Council resolutions... There is no doubt at all in the minds of the Gulf Arab governments that as long as Saddam Hussein lives and holds power, Iraq remains a continuing and constant threat to regional peace.

*Gulf States Newsletter, Vol. 18, No. 454, February 1993*

### Arab Leaders Manoeuvre Ahead Of Talks About Action

**S**tung by their impotence in the face of the US-led confrontation with Iraq, Arab governments have moved forward their summit, scheduled for 24 March in Bahrain, to Cairo earlier in the month. While the summit promised much from an Arab policy perspective, the timetable established by an apparently impatient President George W Bush, meant war may have been declared by then

League of Arab States officials said the meeting had been transferred to Egypt at Bahrain's request.

The date will be announced when foreign ministers convene in Cairo on 16 February.

Once again, Arab leaders are being forced to react to geopolitical events, rather than setting the agenda. In terms of Arab politics, Bahrain was to be a big deal. Saudi Arabia's Crown Prince Abdallah Bin Abdelaziz (CPA) is not the only regional leader to have begun circulating reform proposals for discussion there. Qatar, Sudan, Bahrain, Tunisia and Egypt had also put forward ideas – although none seemed likely to match the impact of CPA's bluntly worded call for better governance and accountability across the Arab world (GSN 702/8).

This flurry of activity is partly in response to Colonel Muammar Qadhafi of Libya's threat last autumn to withdraw from the Arab League in apparent protest at the failure of member countries to promote a coherent and effective common front.

Other governments might not share the Libyan policy agenda, but Qadhafi's complaint has highlighted Arab governments' wider frustration at their own failure to coherently present a clear message. Libya was particularly concerned to see a common and tougher line presented on the Israel/Palestine issue. But this has led other leaders to start looking more generally at questions of Arab collective work and solidarity in a world where their voice is increasingly marginalised.

The democratisation hinted at by CPA is being promoted in the Kingdom by reformists like Riyadh lawyer Abdelaziz Al-Gasim, who on 22 January personally presented a petition to the Crown Prince from some 100 signatories drawn from a cross-section of male Saudi society. But for now, many officials in Gulf states prefer to focus on CPA's themes of inter-governmental collaboration, rather than his warnings about the decayed state of domestic rule and accountability in Arab countries.

There is a growing awareness that governance issues will not go away, but a reluctance to face up to what that might imply in political terms. "This is a conceptual issue – there is no right or wrong," one policymaker told GSN, retreating into generalities. "There is a challenge to develop ideas on how to

deal with the changes facing the Arab world."

The Arab League Secretariat has been reinvigorated by the activist leadership of former Egyptian foreign minister Amr Moussa, and now has ambitions for a central role in the development of more effective co-operation. Iraq has provided an early opportunity to signal these hopes, according to GSN's soundings in Cairo.

Moussa has persuaded 18 of the 22 member governments to send their foreign ministers to a crisis meeting on Iraq, to be held in Cairo in a few days' time ["mid-February"]. Given the dominant role played by the United Nations Security Council, and the USA's determination to bring the confrontation with Iraq to a head, the Arab League will struggle to have any significant influence on the crisis. But officials say that at least member states are not quitting the field of play prematurely.

#### MOUSSA BREATHES LIFE INTO THE ARAB LEAGUE

For Moussa it is important to show the League is still a grouping that has some meaning. His prime goal has been to focus international efforts on the implementation of Security Council Resolution 1441, which provided for the current round of inspections. He is resigned to the fact that any eventual lifting of sanctions – provided for under Resolution 1284 – has slipped right off the agenda for now and is not worth raising at this stage.

League sources believe there is a clear improvement in the level of co-operation displayed by Baghdad on this occasion. The Secretariat is reluctant to admit, even to itself, the likelihood of war, feeling bound to press the case for ongoing inspections. Understandably, it cannot be seen to acquiesce, even tacitly, in speculation about regime change in Iraq, a member state.

Even if there is war the Iraq crisis will have allowed Moussa to revive the League's profile as a significant diplomatic player, largely thanks to the intermediary role he played in last year's talks to persuade President Saddam Hussein to resume co-operation with the UN.

The League has invested considerable capital in trying to break down the hostility between Iraq and Kuwait. Officials believe there was a notable softening of Iraqi attitudes at last March's Beirut summit, compared with its pugnacious stance at Amman in 2001. Moussa helped to persuade Baghdad to work within the tripartite commission (with Kuwait and Saudi Arabia) on prisoners.

This diplomatic activity has been paralleled by a more institutional effort to enhance inter-Arab co-operation. Moussa has overhauled the League Secretariat's structure and invested in information

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technology; and he has strengthened the common bodies through which Arab governments cooperate. He suggested that prime ministers participate in the Economic and Social Council.

The League now has specialist commissions examining issues of civil society and Arabs living outside the region.

Moussa is trying to sharpen up the work of the roughly 25 specialised Arab agencies and the 22 inter-ministerial councils. Through the *Arab*

*Labour Organisation*, work continues on efforts to set common basic standards for the treatment of Arab migrant workers.

But although Iraq has provided a chance for Arab states to parade a largely coherent common foreign policy position on the key issue of the day, co-operation on a permanent basis is still well short of the *European Union* model. The League is a long way from creating an EU-style institutional core – and Moussa is openly aware of that fact.

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## Egypt Adapts To A Diminished International Role

Six weeks leaves scant time for the diplomats of the Arab world to pull off the improbable. But if war is to be avoided in the apparently last-gasp interval accorded by US President **George W Bush** for **Iraq** to become the Middle East's most transparent military power and abandon any secret hope of retaining weapons of mass destruction (WMD), then **Saddam Hussein's** regional neighbours have to induce him to adopt a degree of openness about security and scientific structures that would be utterly out of character and could weaken his regime's long-term hold on power.

Up until the last minute, Arab governments will hope that somehow Saddam can be won around. In this situation Egypt, the historic regional leader, finds itself in an uncomfortable situation.

President **Hosni Mubarak** has to wrestle with his own internal problems of governance and reform. In late January, his government successfully floated the Egyptian pound, which will please business but may add to the cost of subsidising basic living standards for the poor. As Prime Minister **Atef Ebeid** hinted to *GSN*, the government has to reckon with the risk of a slump in tourism and investment as westerners shy away from the Middle East (*GSN* 703/1).

The handling of the Iraq crisis poses diplomatic difficulties, related to probably doomed attempts at averting an attack on Iraq and to wider questions about Egypt's role as an international player.

For all Cairo's frenetic bustle, it is not at the centre of the diplomatic action. **United Nations** weapons inspectors have their back up base in **Cyprus**, while the political traffic is largely passing directly between the UN in New York and key Western capitals.

Western governments and military commanders are stepping up their efforts to placate the Gulf states. Egypt may be one of the region's main powers – and the second largest recipient of US aid – but it is not a key focus. The Western media presence is now minimal given Egypt's traditional status as the Arab world's epicentre.

Mubarak is a leading Arab head of state, but in the present situation that does not count for a lot – and the Egyptian government knows it.

Officially, the government is committed to the *League of Arab States* view that war should be avoided and any residual Iraqi WMD threat can be contained through inspections and the counterbalancing military strength of other countries.

Egypt and other Middle Eastern governments regard **Israeli Prime Minister Ariel Sharon's** hard-line stance as a far greater threat to regional stability, because of the desperation this provokes among **Palestinians** and the anti-Western anger it generates in their populations – shown by a growing wave of protests in Cairo. Such despair is a breeding ground for the extremism the USA professes to be so worried about.

Interviewed by the **UAE** daily *Al-Ittihad*, Mubarak saw a need to “deal with the Israeli Prime Minister in a new way” during Sharon's second term, won last month. He subsequently invited the Arabs' ultimate *bête noire* to visit Egypt for talks, in what would be Sharon's first meeting as Prime Minister with an Arab head of state.

### WASHINGTON'S RELUCTANT ALLY

Mubarak can still count on a friendly and polite hearing in Washington, but he has little room to pressure the Bush Administration for a shift in priorities. Hugely dependent on US financial aid, Egypt cannot afford to fall out with Washington.

Well-placed analysts canvassed by *GSN* in Cairo believe that while Mubarak will continue to consult other regional leaders and visiting westerners, and while his diplomats will tour other Arab capitals, the will or capacity to exert leverage is absent.

Egypt will not participate in the war – but nor is it expected to abandon military co-operation and common exercises with the USA or even lead moves to oppose Bush's policy at the UN. Foreign Minister **Ahmed Maher** told the Paris daily *Le Monde* that Egypt would maintain international rights of passage through the Suez Canal – and thus not block coalition warships headed for the Gulf.

There is a lot of criticism of the USA, but there is also a realisation of the need to keep relations with Washington on an even keel. A top-level delegation was to be dispatched to Washington in late January comprising the sort of Egyptians any US administration can understand – Mubarak's chief

political adviser **Osama Al-Baz**, Economy Minister **Youssef Boutros Ghali** and fast-rising presidential son **Gamal Mubarak**.

The Egyptian leadership has been careful not to expose itself through over-ambitious frontline diplomacy. Palestinian talks have been brokered by intelligence chief **Omar Sulaiman**, while Ebeid concentrates on economics and maintaining social peace at home.

Following talks between the foreign ministers of **Egypt, Iran, Jordan, Saudi Arabia, Syria** and **Turkey** in Istanbul aimed at fashioning a regional response to the Iraq crisis, Mubarak visited several Gulf states. In the UAE he met President **Sheikh Zayed Bin Sultan Al-Nahayan** and **Abu Dhabi** Crown Prince **Sheikh Khalifa Bin Zayed in Al-Ain**. In **Kuwait**, he was met at the airport by a clearly infirm Emir **Sheikh Jaber Al-Ahmed Al-Sabah**, and held talks with Acting Prime Minister **Sheikh Sabah Al-Ahmed Al-Sabah**.

Mubarak has consulted Gulf leaders, but he has not risked his prestige on a potentially vain attempt at shuttle talks between Washington and Baghdad.

Egypt prefers to invest diplomatic capital in attempts to unblock the Israel/Palestinian logjam – through discussions with Palestinian factions over ways to reform and create a more coherent and credible entity that would be harder for Israel to spurn. These talks are not going smoothly.

Palestinian reform is an agenda shared by the USA and UK. They welcomed Mubarak's surprise move to invite Sharon for talks. Egypt has been pushing for **Amram Mitzna's** defeated **Labor Party** to join a coalition, to avoid a further shift to the right in Israel – which says much for Cairo's pragmatic world view, but will not go down well with many Arab governments, including Egypt's rival for regional leadership, **Crown Prince Abdallah's** Saudi Arabia.

#### **SADDAM MUST GO**

"Deep at heart, everybody wants to get rid of Saddam Hussein," noted one analyst.

Fundamentally, the Cairo government distrusts and dislikes Iraq's President, whose bellicose rhetoric makes it harder for the likes of Egypt and Jordan to steer a middle course, maintaining good relations with both Arab neighbours and the West.

Egypt recently cancelled the visit of an Iraqi envoy to Cairo when Saddam opted to send his cousin, alleged war criminal **Ali Hassan Al-Majid**. "We are willing to receive an Iraqi envoy, but you would accept that the person chosen was not the best," and official told *GSN*. "The personality of the messenger could have harmed the message."

For Egypt's leaders, the greatest concern about the likely American overthrow of Saddam is the potential impact of a war on the national economy, and on internal stability.

Opinions among Cairene commentators and planners are divided over whether the crisis will alter Egypt's long-term relationships and sympathy

towards Western countries. In January, **France's** President **Jacques Chirac** was flavour of the month among both policy-makers and tea-drinkers in the souk. But if Chirac eventually opts to throw French troops into the fray, he could end up more disliked than the UK's **Tony Blair**, whose close partnership with Washington provokes perplexity (*GSN* 703/9).

Much will depend on how matters play out in the UN. If Saddam is seen to take a confrontational and obstructive approach, that will widen understanding of a Security Council decision to use force, even if Egypt is still opposed to the idea.

But if Iraq appears to be relatively co-operative and is still attacked, then attitudes in Arab capitals will be much angrier. The same will be true if the war does not go according to plan and drags on for months, with heavy casualties.

Egypt remains deeply concerned that the USA has taken far too narrow a view of security and is neglecting the danger that a post-war Iraq could be divided and unstable – and that Muslim anger at US intervention could simply foster more terrorism.

Even those senior Cairo commentators who are broadly sympathetic to Washington and believe Franco-German objections to war are shallow and unreliable, regard US talk of rebuilding Iraq as a beacon of democratic good governance in the Middle East as simplistic and naïve. They do not think it sensible to draw parallels with the recreation of German democracy after **Hitler's** defeat or with the post-Communist transformation of central Europe. "Americans see Iraq as Germany. We see it as something between **Afghanistan** and **Yugoslavia**," commented one analyst. Dismissing the Iraqi opposition in exile as on a par with the **Cuban** émigrés of the Bay of Pigs fiasco, he suggested post-war Iraq could be condemned to instability on a **Lebanese** civil war scale, or worse.

#### **DAMAGE LIMITATION**

Despite protestations to the contrary Egypt is becoming resigned to the notion that its main role will be to help in damage limitation after a war, trying to rebuild a measure of regional stability and secure progress on Israel/Palestine – which it sees as the real danger to peace.

Maher actually stated that: "A day will come when [UN inspection chiefs **Hans**] **Blix** and [Egyptian **Mohammed**] **Al-Baradei** will say 'enough, it's enough; we think we can advance no further and that things are going badly'." The Security Council would then have to decide if what had been achieved was sufficient and whether it should take the measures it judged necessary. "We should not sacrifice a possibility of peace for the sake of going fast."

This sounds very much like a government preparing the ground for the public acceptance of a UN decision in favour of using force. Once again the region's traditional big power has found itself outpunched by genuine geopolitical heavyweights.

### Cooler Heads Prevail As Anti-American Tensions Rise

Recent events in **Kuwait** and **Bahrain** have sent shockwaves through their security establishments, forcing the cooler heads in both governments to keep a tight rein on security mandarins while US troops deploy.

Anti-Americanism has heavily impacted on the security of both states. In Kuwait, resentment is not broad-based but has been marked by a spate of serious violent incidents against US citizens whenever it has unpredictably surfaced.

Bahrain is the opposite, involving broad-based dissatisfaction with US regional policy that has not yet spilled over into serious violence, despite New Year rioting. In these states – and to a lesser extent in **Oman**, **Qatar** and the **UAE** – public disorder incidents look likely to rise as long as the open-ended **Iraq** and **Palestinian** crises persist.

#### SECURITY ISSUES IN KUWAIT

Recent gun attacks on US military personnel and contractors pose a difficult challenge for Kuwait's security services. The first occurred last October, with the fatal shooting of a US serviceman on Failaka Island; the second came a month later, when two US servicemen were seriously wounded on a main road (*GSN 698/3*). On 21 January two US contractors were attacked; one died (*GSN 702/16*).

The authorities said 25-year-old **Al-Qaeda** supporter **Sami Mohammed Marzook Al-Mutairi** subsequently confessed to the attack. It is not clear whether he was part of a group, although three other men were held over allegations of supplying Mutairi with weapons. Another radical group, **Daawa wal Jihad**, also claimed responsibility for the attack and close links to **Al-Qaeda**.

The three attacks were not apparently connected and involved US citizens in transit or otherwise away from defended locales. This form of non-networked, semi-spontaneous attack is difficult to predict – and therefore to foil – through early warning. Like many **GCC** states, a significant proportion of Kuwait's security apparatus – notably the 5,000-strong **National Guard** – focuses on keypoint defence of fixed infrastructure; it is not configured to protect mobile, dispersed targets such as personnel in transit.

Although unconnected to President **Saddam Hussein's** December call to Kuwaitis to rise up against the US presence in their country, Baghdad's message and the January attack have spurred a low-profile heightening of security efforts. Americans are now recommended, and US government employees are required, to travel in groups of at least four people, split between two or more vehicles.

Kuwait's police and Interior Ministry security forces were placed on full alert, though the latter have maintained a low profile. The **Kuwaiti State Security (KSS)** and **Criminal Investigation Department (CID)** organisations have stepped up surveillance on the 70-120 Kuwaiti "**Afghanis**" – Kuwaiti citizens who served in **Afghanistan** during the Soviet occupation. According to US Ambassador **Richard Jones**, numerous Kuwaitis who have received training from **Al-Qaeda** and the **Taliban** remain at large.

In a move that is likely to provoke a backlash from Islamist legislators and thus general deadlock and delays in legislative matters, Education Minister **Musaed Rashed Al-Haroun** announced that the government was setting up a committee under a member of the royal family to vet the national curriculum for texts encouraging a radical or confrontational view of Islam.

#### BIG STICK APPROACH

The prospect of more widespread civil disorder was raised by Acting Prime Minister **Sheikh Sabah Al-Ahmed Al-Sabah**, who summed up saying: "My concern is not what will happen outside Kuwait, but how to control matters inside."

The monarchy seems well-equipped to deal with broader, as its previous muscular treatment of dissent has shown. Kuwait is the only **GCC** state to have experienced a prolonged period of martial law in its recent history; over 115 convictions were brought in military courts during the four months of military rule that followed the Gulf War in 1991.

The two State Security Courts that sit at other times are barely more lenient. Critics say they lack due process and sit in closed session during their vital early sessions.

Kuwait has dealt swiftly with general dissent from its immigrant communities, detaining 5,800 non-Kuwaitis in the aftermath of the Gulf War and summarily deporting 370,000 of the 400,000 resident Palestinians. Kuwait's ability to isolate large numbers of detainees and displace large populations remains intact, despite a decade of relative calm. In October 1999, following rioting in **Egyptian** ghettos, 3,000 workers were rounded up and relocated to desert internment camps.

The Emiri Guard – mounted in 70 **General Dynamics/Steyr-Daimler-Puch Spezialfahrzeug AV Technology Corporation** Pandur light armoured vehicles – provides a final fallback.

#### BAHRAIN'S POLICING CHALLENGE

In contrast to Kuwait and the other **GCC** states, Bahrain is used to coping with large-scale violent

incidents, and is instead readjusting to meet the challenge of policing broad-based protest activity that has so far remained non-violent.

During the mid-1990s a spiralling security crisis saw street violence, the barricading of Shiite ghettos and arson against infrastructure. The security forces – comprising the 11,000-strong *Public Security Force* and the small *Security and Intelligence Service (SIS)* – were regularly called on to enter ‘no-go’ areas, breach barricades, and employ riot police tactics. In 1995-96, the *Bahrain Defence Force* was almost activated to render military assistance to the civil power, backed by the *Royal Saudi Land Forces*.

Until their repeal in February 2001, the *State Security Law* and State Security Court (SSC) had underpinned the security state for 26 years. **King Hamad Bin Isa Al-Khalifa** has sought to liberalise Bahrain with some success, but many conservatives – often identified with the King’s uncle Prime Minister **Sheikh Khalifa Bin Salman Al-Khalifa** – seized on January’s riots as evidence that political violence was again on the rise.

Veteran Interior Minister **Sheikh Mohammed Bin Khalifa Al-Khalifa** described the riots as a threat to national security. Information Minister **Nabeel Al-Hamer** suggested that far from being spontaneous outbursts of socio-economically driven hooliganism, the riots were “premeditated political actions” linked to the Shiite opposition; he labelled the rioters “terrorists” and “saboteurs”.

Although stopping short of calling for the return of the *State Security Law* and SSC, conservative legislators and National Security chief **Sheikh Abdelaziz Bin Atteyattolah Al-Khalifa** demanded tougher action, citing the “loss of credibility and authority of the police and security forces in the eyes of the youth”.

Despite making 55 arrests at the riot and issuing generous rewards for information leading to further arrests, police forces were roundly condemned for failing to crack enough heads.

#### CIVIL SOCIETY RESPONSE

The wind was largely removed from the hardliners’ sails when the main opposition *Al-Wefaq National Islamic Alliance* issued uncompromising condemnation of the riot, and by calming words from King Hamad, who gently doused speculation that it had any links to either opposition politics or rising anti-Americanism (*GSN 701/4*).

Anti-American rhetoric has been growing at street level for over the year, reflecting growing anger at US policy on both the **Israel-Palestine** conflict and **Iraq**. This is reflected in a consumer boycott charted by *GSN*.

An April 2002 protest outside the US Embassy in Manama was broken up, causing the death of a demonstrator. An early January demonstration at the US Fifth Fleet headquarters went off peacefully but signalled growing public unease with King Hamad’s strong support for US regional policy.

More marches are scheduled, and the King is squeezed between two pressures: while popular attitudes are likely to continue to harden towards US policy and deployments, conservative deputies who underpin government control in Parliament will demand tougher responses, arguing that the intense levels of violence experienced in Bahrain in the mid-1990s also started as isolated incidents.

## KUWAIT: Sticking Plaster Government

The resignation of Finance Minister **Youssef Al-Ibrahim** has finally been accepted, after a period when it was unclear whether First Deputy (and Acting) Premier **Sheikh Sabah Al-Ahmed Al-Sabah**, patron of the cabinet’s shrunken modernising wing, would make one last effort to persuade him to stay on (*GSN 702/15*).

The Planning and Finance portfolio has been assumed on a caretaker basis by the suave and affable Deputy Foreign Minister **Sheikh Mohammed Sabah Al-Salim Al-Sabah**. After months of pressure from parliamentary opponents, Ibrahim escaped for a quiet break abroad.

Fluent in idiomatic English, Sheikh Mohammed is well able to present of Kuwait’s financial image. But he already has an over-full agenda – a fact that highlights the temporary nature of present cabinet job allocations in the run-up to this year’s parliamentary election.

The Ministry of Oil is also in the hands of another very capable but over-worked caretaker – **Sheikh Ahmed Al-Fahad Al-Ahmed Al-Sabah**.

After the election, both posts will need full-time occupants if the government is to make further headway on a challenging economic reform programme, including the participation of foreign oil majors to develop the northern oilfields near the Iraq border, on territory for now to be a military zone.

#### CONTINUED FROM PAGE 1

(\$85m), the much-anticipated Formula 1 racetrack (\$200m) and a coastal resort in Bandar Al-Seef (\$80m).

The bond issue has been oversubscribed. Final implementation may not be delayed if the nominated upper house – dominated by pro-government appointees – votes in favour of approving the borrowing. A joint session of both houses, chaired by the upper house speaker, would then make a final decision on whether to approve the bond on the current basis. This, and the expected subsequent row, will give a good idea of the real balance of power in Bahrain.

#### IRAN: Alternative Society Wedding

With his troops doing **Saddam Hussein**’s bidding, manoeuvring along **Iraq**’s Iranian border, *Mojaheddin-e Khalq Organisation (MKO)* leader **Massoud Rajavi** has reportedly married MKO Military Commander **Zohreh Atrianfar**. Iranian press reports say she is *Executives of Construction Party* member and *Hamshahri* editor Mohammad Atrianfar’s sister.

## Bush's Very Special Envoy: The Rise Of Zalmay Khalilzad

WASHINGTON—Zalmay Khalilzad, leader of the US team shaping a post-Saddam Iraq, is a star in the ascendant, who has served his time in the backrooms off the corridors of power and among the universities and think-tanks when the Reagan and Bush administrations who raised him to prominence were interrupted by the eight-year Clinton era.

Although only formally appointed to his current position in December, Khalilzad has been a key player in the team supervising the Bush Administration's response to 9/11. In May 2001, the Afghan/American was appointed Special Assistant to the President and Senior Director for Gulf, South-west Asia and other regional issues in the *National Security Council (NSC)* – a position he retained when he became point man for Bush's efforts to develop Afghanistan's first post-Taliban government.

Now he's doing the same for Iraq. In December, Khalilzad led a strong team of NSC, Pentagon and State Department to a conference in London intended to weld disparate Iraqi groups into an effective coalition. Khalilzad boldly declared: "Together, we foresee an Iraq committed to the rule of law, human rights and democracy... in which all Iraqis will enjoy civil and political rights." Khalilzad has been forthright in setting out a vision for post-Saddam Iraq. Asked about Kurdish separatism – and possible Shiite separatism in the South – he said that any intervention coalition "will reunify Iraq" and would preserve its territorial integrity, as if forgetting that Iraq's division stems from the US-led coalition's intervention in northern Iraq in 1991. For Khalilzad: "Our objective is a broad-based and representative government [that will] give all religious and ethnic groups a voice." Specific measures to be undertaken by the occupation authorities would include "a judicial process" to deal with suspected Iraqi war criminals and a "major reconstruction programme that will put Iraq on the path to prosperity" – to be largely financed from oil revenues.

### A REPUBLICAN AFGHAN

An Afghan who came to the USA some time before the Russian invasion of 1979, Khalilzad has been a policy adviser for the *Republicans* for almost 18 years, working on Middle East and South Asian issues in general and Afghanistan in particular. Although the Russian invasion and subsequent resistance and internal civil strife prompted many Afghans to flee to the USA, few rose to prominence. So it was no conspiracy that both Khalilzad and Hamid Karzai, now Afghanistan's head of government, should have been retained as consultants in the 1990s by the US *Unocal* oil company when it was planning to construct a gas pipeline across Afghanistan from Central Asia to Pakistan. The \$2bn scheme was the biggest potential project involving the war-ravaged country and that meant that somehow the Taliban would have to be squared. So Khalilzad, who in 2001 was to head the Bush Administration's team to ensure the Taliban's downfall in Afghanistan, found himself in December 1997 a member of a select group of policy experts called upon to meet a delegation of Taliban ministers when they visited to the USA to see Unocal's Sugarland, Texas base and to hold brief talks with the State Department.

Khalilzad is a Pushtun born in Mazar-I-Sharif in or around 1951. He studied at the *American University of Beirut*, and in 1979 secured his PhD from the *University of Chicago*; he then taught at New York's *Columbia University*. Married, with two children, Khalilzad became an American citizen in 1984 and the following year moved to the State Department, serving for the next four years as special advisor on the Iran-Iraq War and Afghanistan.

When the first Bush era opened in 1989, Khalilzad moved to California, initially to work at *Rand Corporation* and teaching political science at the *University of California*, San Diego. He was founding head of Rand's Center for Middle Eastern Studies. He returned to Washington in 1991 as assistant deputy under secretary of defence for policy planning, working under Paul Wolfowitz – now deputy to Defence Secretary Donald Rumsfeld. In 1998, Wolfowitz and Khalilzad were among a number of conservative signatories to a letter sent to President Clinton calling on the US to overthrow Saddam.

Khalilzad may come from a hard-line policy background, but he phrases his words carefully. Interviewed during the London conference, he declared: "We don't want war with Iraq. We want Saddam to comply with UN resolutions and [we want] freedom and liberty for the Iraqi people. We hope war will be avoided. The ball is in Mr Hussein's court." However, in a major policy speech delivered in October, Khalilzad said that if war comes: "This will be a liberation, not a conquest or an occupation." Khalilzad told the *Washington Institute for Near East Policy* that the US plan for post-Saddam Iraq would involve running the country until a democratic Iraqi government was deemed ready. It is not clear if this is still the case, with Washington sources indicating that many of Bush's senior officials now favour a rapid in-and-out-again approach to US intervention.

### A CONTROVERSIAL APPOINTMENT

Khalilzad's background as an oil company adviser raised concerns when he was handling Afghanistan and still does so with regard to Iraq. The influential *Friedrich-Ebert-Stiftung (FES)*, which has strong ties to the *German Social Democratic Party (SPD)*, commented recently that regardless of whether there was any accuracy to the various conspiracy theories regarding the future of Iraqi oil, "Islamic fundamentalists will play their trump card – Islamic oil and Western exploitation – to rally political support. And they will find this support – particularly in the streets." The FES commentary added: "The appointment of Zalmay Khalilzad, who at present is also the special envoy of the US in charge of Afghanistan and who was previously employed in the American oil industry, as the special envoy of the US government for post-Saddam Iraq naturally supports this (mis-)perception."

### Cbi Buys African Energy and Middle East Energy

A version of this article was published in the February issue of the monthly *Middle East Energy*.

The authoritative monthly *African Energy* and its *Middle East Energy* supplement were purchased by GSN's publisher, *Cross-border Information Ltd (Cbi)* on 31 January 2003, from Platts, a division of The McGraw-Hill Companies.

Cbi is led by *African Energy's* founding editor Jon Marks, who will continue to shape the publication backed by his existing editorial team. *African Energy* was created by Marks in April 1998 and joined Platts' other newsletters in 2001.

From 28 February 2003 *African Energy* will be hosted on a new website: [www.africa-energy.com](http://www.africa-energy.com)

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# Problems Of Competitiveness Emerge For Employers As Gulf Workforces Nationalise

Foreigners account for much of the workforce in *Gulf Co-operation Council* states, and in several are a clear majority of the population. How to manage this reliance is one of the most fundamental issues facing GCC governments at a time when the gradual liberalisation of global trade is exposing workers' treatment to increased scrutiny. Gulf rulers have to balance their concern for economic competitiveness, continued growth and affordable services – for which cheap labour is a key ingredient – against their populations' desire to conserve local cultural patterns while opening up job opportunities for their children.

Moves towards democratisation have raised the visibility of these dilemmas, because they call attention to the demands of national residents, expose migrant workers' conditions to increased media scrutiny and force the publication of more population data.

The controversy over the inclusion of new passport holders on **Bahrain's** electoral roll for last year's elections provided a sharp reminder of how delicate these issues can be. Disputes over the failure to pay foreign construction workers that would in the past have attracted little public notice are now out in the realm of public discussion and government action in some countries. **Qatar** has been setting up a new body to take care of migrant workers' rights.

Reliable, comprehensive data remains in short supply on the flow of migrants to the Gulf, and the underlying economic and social patterns. Although the region's dramatic transformation and development has depended heavily on the inflow of skilled and unskilled workers, surprisingly little is known about their role. But the Gulf's competitiveness is hugely reliant on its access to a large pool of relatively inexpensive workers. Labour-intensive businesses that rely mainly on local workers – such as **Bahrain's** textile factories – are rarities.

As Gulf governments attempt to promote their workforces' nationalisation they face a fundamental challenge of competitiveness. Can they persuade locals to take up middle and lower ranking posts at levels of pay that maintain these jobs' commercial viability? Professional specialists from the West, the Arab world and Asia tend to hold senior and middle ranking positions, in which they are being slowly replaced by Gulf nationals. The mass workforce is dominated by South Asians.

There are many positions that for the foreseeable future will continue to be carried out almost

entirely by foreigners, however successful programmes of "Emiratisation", "Omanisation" or "Saudi-isation" prove to be.

### Kerala Study Shows Migration Trend

A study published by the Thiruvananthapuram-based *Centre for Development Studies (CDS)* has shed some rigorous academic light on links between Kerala, south-west **India**, and Gulf states, particularly the **UAE**\*

Keralites are found throughout much of the GCC and the thread of air routes that now link their state to the Gulf bears witness to the vast movement of workers back and forth. Their near ubiquitous presence is largely explained by the paradoxical conditions at home: a big population concentrated in a narrow coastal strip of land, with land and jobs in short supply, but a strong tradition of primary education which ensures that almost everyone is literate and thus able to seek employment abroad in a region where English is one of the principle working languages.

The CDS researchers estimate that 1.3m-1.5m Keralites who maintain a household address in the state live outside India. However, the large-scale movement of workers abroad began only three decades ago, stimulated by the newly rich Arabia's need for cheap foreign workers to build oil-funded infrastructure and staff emerging service activities. The Middle East's pull was overwhelming, accounting for 95% of all Keralite emigrants; the **USA** ranks next, with just 2.2% of the total.

Almost 40% of those in the Gulf are in **Saudi Arabia**, with the **UAE** ranking next. **Oman** is also popular, not least due to its geographical proximity and strong ties with the Indian sub-continent.

The largest source of emigrants from Kerala is the Malappuram Thrissur area, a relatively poor and largely Muslim area in the north of the state.

### Kerala Immigrants, 1998

	Number of migrants	% of total
Saudi Arabia	519,000	38.1
UAE	405,000	29.7
Oman	142,000	10.4
Bahrain	77,000	5.7
Kuwait	69,000	5.1
Qatar	64,000	4.7
USA	30,000	2.2
Other countries	57,000	4.2

Source: KC Zachariah, ET Mathew and S Irudaya Rajan (1999).

## Migrants In The UAE Economy

Keralites are probably the most significant migrant group in UAE, where they dominate the **Indian** presence. Data from **UAE Exchange Centre**, the country's largest currency exchange firm, suggests that in 2000 almost 58% of the Rs71.87bn (\$1.5bn) in remittances sent home from the UAE to India went to Kerala. The only other states to weigh substantially in the cashflow were Tamil Nadu, Punjab and Maharashtra.

Keralites must be seen in the context of a much larger migrant workforce. In 1995, there were almost 1.4m migrant workers in the UAE, of whom 1.2m were from Asia, with only 175,000 Arabs and 21,000 Europeans. Some 585,000 Indians were the largest group; perhaps half of these were Keralites. There were 293,000 **Pakistanis**, 105,000 **Bangladeshis**, 87,000 **Singhalese**, 70,000 **Filipinos** and 35,000 **Iranians**.

In some cases, traditional patterns of contact, recruitment and business sponsorship have evolved with particular locations. Pakistanis from North West Frontier region dominate taxi driving in **Abu Dhabi** (whereas they are not so predominant in the Northern Emirates). Wage levels span the full income scale. But the heaviest concentration is at the lower end, in Dh750-2,000/month range. Most workers cannot save large sums of money: 36% manage to put aside less than Dh500/month, and another 34% less than Dh1,000.

One-third of all migrants and almost 70% of the contract workers live in special camps, with four to eight people usually sharing a room. About one-quarter of the camps lack a full range of basic amenities – water, electricity, air-conditioning and cooking facilities. The camps, such as those in **Dubai** at Sonapur, 15km from downtown, and at the Al-Quoz and Jebel Ali free zones, are maintained by employers who bus their staff into work each day.

About one-fifth of the workers – usually those vulnerable to exploitation because they failed to enter the UAE on proper work visas – do not receive the pay and benefits specified in their contracts. But it is administrative and managerial staff, rather than unskilled personnel, who most often find themselves forced out of a job without receiving all due pay.

### NO GAIN WITHOUT PAIN

Migrants pay dearly for the privilege of securing employment in the Gulf – which goes some way towards explaining why so many choose to remain there long-term, rather than just doing two- or three-year stints. On average, CDS found, a Keralite spends Rs44,000 to go abroad, to pay for tickets, visa fees and agent's commission.

Their reward is a higher living standard for their families. Migrants' homes are more likely to have electricity, flush toilets and modern LPG cooking facilities.

"The longer the duration of emigration, the higher is the proportion of households possessing a car, a television, a telephone or all of them," CDS noted.

Almost 1m married women remain in Kerala. These so-called "Gulf wives" may suffer loneliness, but they also grow in autonomy, social status and practical skills through having to manage their households and deal with the outside world, without the support or oversight of their spouses.

Many migrants return home as they have

practically no access to GCC citizenship. The pace of return picked up through much of the 1990s, peaking at 126,900 in 1997; but it dipped sharply, to 78,900 in 1998. By 1998 some 739,000 had returned; one in eight Keralite households had a returnee.

The CDS believes this pattern will accelerate and eventually the flow of returnees might outweigh those setting out for the Gulf. This trend will not be a function of Kerala's development or prosperity, but of trends in the Gulf, as governments promote further nationalisation of the workforce.

### UAE CONCERNS OVER NUMBERS

The UAE government and Federal National Council – the main official sounding board for public opinion – are concerned about the size of the migrant presence. A report presented to the FNC in June 2001 estimated that Indians accounted for one-third of the UAE population.

Personal and unofficial connections account for much of the labour flow. While 83% of the workers come to the UAE on proper work visas, the balance arrive as tourists or other categories of visitor and sort out the paperwork later. Only 23.6% of migrants surveyed by the CDS had secured their visa through a licensed recruiting agent, whereas 43.7% arranged it through relatives and 6.9% relied on an unlicensed agent.

The UAE government has begun to take steps to curb the flow of migrants. In July 1999 it stopped accepting visa applications from unskilled workers. The Ministry of Labour and Social Affairs' *Labour 2000* report expressed fears that an overabundance of cheap foreign labour would leave business with little incentive to invest in less labour-intensive technology. In other words, the low cost of employing subcontinent workers was actually undermining prospects for the long-term upgrade of the UAE's competitiveness.

Some 80% of the applications for migrants' work permits received by the Ministry are for unskilled manpower. But the demand for unskilled labour depends to some extent on trends in the construction sector.

Since May 1999, labour cards have not been renewed for private sector employees aged 60 or more, with the exception of certain priority professional and technical posts where skilled locals remain in short supply.

The government has tried to positively promote Emiratisation – setting a goal of seeing locals hold half the jobs at national telecommunications operator *Etisalat* by end-2000. Nationals who work in the private sector are legally guaranteed the same social security benefits as public sector employees.

\* *Kerala's Gulf Connection*, Centre for Development Studies, Thiruvananthapuram, 2002. Rs 250/\$25.

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# Middle East Insider – IRAQ

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## Kurds' Military Dilemma: Defence Or Expansion?

**A**s conflict draws close, the din created by rattling sabres echoes through the valleys of the *Kurdistan Regional Government (KRG)* zone in northern Iraq. Since the start of 2003, Kurdish factions, Iraq, **Turkey**, the **USA** and **Iran** have all been in a belligerent mood over the area – where Washington (and now the **UK's Tony Blair**) has revived claims of a “smoking gun” in the Ansar Al-Islam enclave. This point was raised again by Secretary of State **Colin Powell** when he set out the USA's case against Iraq on 5 February, without delivering any really conclusive evidence.

Events in Kurdistan will play a crucial role in the possible fall of President **Saddam Hussein's** regime and post-war stability of Iraq. The key question is whether the Kurds will restrict themselves to defence or pursue a policy of expansionist opportunism?

The *Kurdish Democratic Party (KDP)* and *Patriotic Union of Kurdistan (PUK)* maintain what US military sources describe as “competent and credible infantry forces” – a polite description for troops that are unable to engage in high-intensity warfare against armoured forces such as those facing the KRG from Iraq (if they fight) and Turkey.

The KDP and PUK's irregular Peshmerga forces number between 75,000 and 100,000, and have very few heavy weapons or armoured vehicles.

According to PUK General **Simko Dizayee**, the conventionalisation process is at an embryonic stage. Kurdish forces lack the ammunition, logistical systems and communications equipment to develop offensive capabilities in open terrain. Instead the Peshmerga's traditional strengths lie in their defensive capabilities in broken terrain.

PUK military leader General **Mustapha Said Khadir** said the Peshmerga's capabilities stemmed from “our willingness to sacrifice our bodies, from our high morale, and – if those fail – we always have the mountains.”

Morale is high, buoyed by growing Kurdistani pride, by the long military tradition of the Kurdish provinces, and by successful offensives against the Iraqi armed forces in 1991 and 1995, when Kurdish factions showed they could break the uncertain morale of government troops. On those occasions, the regime was allowed to regain its balance, but such a recovery may not be possible in a future conflict. A strong Iraqi counter-offensive such as in 1991 and 1996 is unlikely under war conditions, and since the imposition of the no-fly zones and the effective cessation of Iraqi helicopter flights, the

mountains have once again have become the Kurds' greatest friend.

The KRG has much to lose from any alteration in its status, regardless of whether this is instigated by a *Baathist* or US-backed Baghdad government, or indeed by another actor such as Turkey – which will want guarantees about the future shape of Iraqi Kurdistan in its package of demands for Washington to buy into an invasion.

An attack by the Baathist regime before a war looks unlikely, as it would provide a clear *casus belli* for a US invasion. But it cannot be discounted completely given Saddam's penchant for bold gambles. The Iraqi government could strike preemptively at the KRG either for hosting the Iraqi opposition conference in February, or because it does not want to see the USA use the KRG as a stepping stone on its way to Baghdad.

The opposition conference – which may be attended by US Special Envoy to Free Iraqis **Zalmay Khalilzad** – is scheduled to be held on 5-15 February in Salahuddin, a mere 60km from Iraq's frontline cantonments.

### US MILITARY BUILD UP

More evidence of the KRG zone's role in future US operations is leaking out of Kurdistan, providing the first concrete evidence of American preparation of local airstrips. Although minimal work has been undertaken at Irbil, Harir or the Turkish-occupied Barmani airstrip (some 40km inside Iraq), extensive work is now under way on the PUK-held Bakrajo airstrip and Tajarro heliport in Sulaymaniyah. **Bavel Talabani**, son of PUK leader **Jalal Talabani**, is leading liaison with US advisors.

Using firetrucks, Bakrajo's asphalt runway is being uncovered and surveyed, and will be repaired to US specifications. A US airfield support package may be flown in shortly before hostilities, allowing the runway to be cleaned, painted, lit and provided with a control tower.

PUK contractors are repairing the base's entry road, installing a perimeter fence and building infantry bunkers to protect it from attack; the base is sited only 30km from Iraqi forces.

According to General Khadir, the PUK could defend the Sulaymaniyah area and airfield for 48 hours against a determined assault – a period that could prove decisive in a war where Baghdad is under sustained attack. Under more testing conditions in 1991, Kurdish forces held Kirkuk for ten days against escalating government attacks.

Although pre-emptive strikes against US

interests in Kurdistan cannot be discounted, senior KDP representative **Farhad Barzani** told GSN that the Kurdish factions believe an Iraqi attack will only come once general war starts.

Reporting from Kurdistan, veteran British journalist **Patrick Cockburn** said officials were preparing for attacks aimed at triggering panic. In 1991, government forces used this tactic by simulating chemical weapon attacks, dropping flour from helicopters to empty Kurdish villages. The region's problems could well be exacerbated by the flow of refugees arriving from central and southern Iraq.

Despite numerous requests, the USA has refused to provide missile defence or passive defences (alarms, gas masks) to the KRG, which must rely instead on local civil defence initiatives. KRG representatives canvassed by GSN said these have included dissemination of leaflets on preparedness against chemical and biological attacks, first responder training, school and urban area evacuation plans and contingency plans to remove government and cultural artifacts to cave systems.

#### **TURKISH THREAT**

Another ever-present threat spurring defensive planning is the possibility that Turkey will intervene to quash any remaining aspirations that Iraqi Kurds may harbour for an independent state.

Turkish sabre-rattling is evident inside the 40km-deep swathe of Iraq that Turkey occupies, with its usual 6,000 troops swelling to 12,000 now and possibly doubling again as war in Iraq draws closer. One battalion of Turkish tanks has been deployed to Bamarni airfield in northern Iraq, and bridging equipment seen in the area suggests that Turkish troops may be planning to move more troops south across the Hazil River.

The numbers of US forces that Turkey is accepting has been limited, not least to allow it to give priority to its own operations from its eastern airbases and heliports.

Kurdish response to the Turkish build-up was swift and unequivocal. The KDP deployed anti-aircraft guns to the border. London representative **Hoshayr Zebari** said that "external intervention by regional states, under whatever pretext, will be resisted by the people of the region".

In a dangerous development, the Turkish General Staff has identified the possible capture of Kirkuk by the Kurds as being sufficient to potentially spark a renewed Kurdish struggle for autonomy. In the confusion and heat of a wider war, such a move could easily trigger a Turkish-Kurdish confrontation at a difficult moment.

#### **PESHMERGA REASSESS STRATEGY**

The Kurdish Peshmerga are unlikely to have a sanctioned role to play in regime change.

In early 2002, Kurdish leaders such as PUK chief Jalal Talabani still entertained hopes that they might emulate the *Northern Alliance*, riding into

#### **Rekindling Media Power To Deter Turkey**

The **Kurds** would have to be very determined to stop **Turkish** forces militarily, and are more likely to rely on the considerable 'soft power' they have learnt to wield since 1991. Television footage of the Kurds' suffering was directly responsible for the ground-breaking creation of the safe havens – and the Kurds have not forgotten their media allies. The **Kurdish Democratic Party's** London representative **Hoshayr Zebari** recently commented: "We are not isolated in the mountains anymore, as we have learned to master public diplomacy and therefore western public opinion – we can affect policy."

Despite KRG efforts at confidence building, Turkey maintains a clouded view of the ambitions of **Iraq's** Kurds, not recognising what some regional observers have seen as a downsizing of Kurdish expectations. In this case, the Kurds will need all the friends they can get.

Kirkuk as their **Tajik** and **Afghan** counterparts rode into Kabul. Talabani noted at the time: "If the US helps the real opposition with its air force and special forces, it won't need to send a large army. It doesn't need to send so many of its sons to die in Iraq."

But US inability to stop the Northern Alliance from seizing Kabul and the failures of local allies at Tora Bora made such a dream untenable. Kurdish leaders are now pragmatic about integration into a US military campaign, with PUK Interior Minister **Freydoun Abdul Kadir** saying candidly: "America does not want our help, it will be a high-tech war."

Lacking a designated role in regime change, the Peshmerga are likely to follow hot on the heels of the Iraqi forces in the north, if, as seems likely, they collapse quickly. The PUK's General Khadir noted that aside from US pressure to downplay mention of liberating Kirkuk, the Kurdish military has not been bought into planning, or enjoyed any high-level liaison with the US military.

This has been due partly to standard operational security concerns, but also due to the Turkish General Staff's close lobbying of the US Office of the Secretary of Defence (OSD). In the absence of direction, Khadir noted, "we don't have any choice, we will make our own move."

The more reticent KDP Peshmerga Minister **Hamid Afmandi** agreed that KDP forces would slowly push south to fill the vacuum left by collapsing government forces. "We will try to be everywhere to keep order," he said. Due to the small distances involved, even if the Peshmerga were to advance slowly, liberation would be almost immediate. As in 1991, Kirkuk is unlikely to be stormed by the Kurds, but instead swallowed up by its own Kurdish inhabitants.

Government preparations for war in Kirkuk reflect the dual threat from within and without. To face the external threat, Iraqi forces have been digging trenches, mining oil wells, and positioning armoured forces – including Republican Guard forces – within residential areas that are likely to be off-limits to US air attacks.

### Islamists On The Doorstep

Peshmerga forces may be tempted by the symbolic liberation of Kirkuk, and the leverage that distrustful Kurds of all factions would gain from capturing the region's oilfields. But **Patriotic Union of Kurdistan (PUK)** forces may be drawn to another strategic prize – the defeat of the troublesome Islamist group that has so preoccupied US officials, **Ansar Al-Islam**, based in the valleys south-east of Sulaymaniyah. PUK leaders are concerned that once liberated, some Kurdish fighters from the Kirkuk area could decide to return home, rather than fighting on in the wider region. The PUK leadership is concerned that such a reduction in its forces could decisively change the military balance in its zone – should the 2,300-strong Islamist groups in nearby villages side with the 700-strong Ansar Al-Islam. This complicated matter is likely to draw in both the USA and Iran.

Following initial visits by **UK** special forces, the US military is already on the ground, having sent its special forces to meet with **Bavel Talabani** and visit the frontlines facing Ansar Al-Islam villages. Sulaymaniyah's airfield could support future actions against Ansar Al-Islam, including stabilisation operations in support of a co-operative PUK.

The PUK's **Jalal Talabani** recently visited Tehran to discuss Iran's relationship with Ansar Al-Islam and other Islamist groups, many of which are drawn from members of the Iranian-based **Islamic Unity Movement of Kurdistan**. Although the nature of Iran's relationships with these groups is unclear, they fall under the umbrella of Iranian artillery, a facility that the PUK had relied on in previous crises. Iran's support will be critical if the PUK are to eliminate the group – a view shared by the local PUK officer, Lieutenant Colonel **Ahmed Chekha Omer**, who said: "If the Iranians don't interfere, we can finish them easily."

But equally importantly, the government has placed restrictions on evening working hours in key oil industry posts, announced its willingness to raid houses suspected of harbouring insurgents, and warned inhabitants to stay indoors during hostilities. An evacuation scheme has been devised for Baath Party members and their dependents.

These preparations implicitly recognise that while the Iraqi army is formally required to leave three miles separation between its forward posts and the KRG, the Peshmerga will spring up throughout northern Iraq as soon as war begins, seizing arms and vehicles, and co-opting defectors.

The complexity of the situation in northern Iraq is unlikely to simplify before a conflict begins. The USA will simultaneously seek to keep Turkey out of Iraq, keep the Kurdish Peshmerga out of metropolitan Kirkuk, and keep Baathist loyalists from blowing up the Kirkuk oilfields.

The fog of war, existing prejudices, and the likely speed of an Iraqi collapse make each of these aims difficult to achieve.

From Ankara, it will be difficult to differentiate between a spontaneous Kurdish uprising in Kirkuk and an organised coup de main by the Kurdish Peshmerga. In the longer-term, the Kurds are likely to remain on alert for some time, fearing a return to dictatorship. As one KDP representative put it, "if our rights are not respected, then there will never be stability in Iraq."

## A Kurdish Blueprint For The Post-Saddam State?

The Kurds have forged a functioning economy out of the only area of Iraq to be truly liberated at the end of the 1991 Gulf War – and Iraqi Kurdistan's success in extremely difficult conditions could make it a model for the wider reconstruction of Iraq.

The opposition **Iraqi National Accord (INA)** and **Supreme Council for Islamic Revolution in Iraq (Sciri)** have both expressed admiration for the area's administration, the **Kurdistan Regional Government (KRG)**. These groups, along with the **Kurdish Democratic Party (KDP)** and **Patriotic Union of Kurdistan (PUK)**, outlined the lessons that could be taken from the KRG's experience and used in Iraq's political and economic recasting at a 27 January conference hosted by the **Royal United Services Institute (RUSI)** in London.

The KRG rules an area in which an estimated 80-85% of physical infrastructure had been destroyed when "cleared areas" were set up under the protective umbrella of the northern no-fly zone. Up to 500,000 refugees needed to be rehoused in a region where as many as 4,500 settlements had been destroyed.

The early years were tough: the KRG zone was officially severed from Iraqi government service provision, and before the Oil-for-Food Programme

(OFP) began in 1996 reconstruction revolved around grants, proceeding relatively slowly. It has witnessed a dramatic rejuvenation since OFP began. The KRG's Ministry of Reconstruction and Development and over 100 municipal groups produced a blueprint for reconstruction and have worked closely with the ten UN and two non-UN agencies that provide the conduit for OFP funds.

Unlike central and southern Iraq, President **Saddam Hussein's** government does not plan how the KRG's OFP funds are spent. Of over \$61bn of OFP funding collected since 1996, the KRG has been allotted \$8bn. Due in part to poor accounting and oversight by UN agencies, it has only been able to spend \$4bn of this money, with the rest held as a cash reserve, out of reach of the local authorities.

The KRG has made effective use of the \$4bn released so far and previous overseas funding, extensively remodelling an estimated 70% of the zone's infrastructure. KRG Reconstruction and Development Minister **Nareen Sideek** told GSN that of 4,500 destroyed settlements, 3,000 had been returned to habitation. Running water was available in 90% of rural and 95% of urban households; 65% of houses have adequate sanitation and 70% of households are connected to the electricity grid.

The KRG has part-funded private sector telecommunications developments, including digital switching equipment and GSM infrastructure. Healthcare and education provision have been a particular focus. From 20 hospitals and 150 health centres in the KRG area in 1991, there are now 24 hospitals and 600 health centres. Immunisations rates are now around 80-95%. Infant and maternal mortality rates have fallen by 25% and 31% respectively.

In education, the enrolment rate in the KRG is 88%; 800,000 children are in schooling, almost half of them female. From 890 schools in 1991, there are now 3,038, served by 50,000 teachers. The KRG has upgraded its three main universities.

These achievements bode well for reconstruction in Iraq when oil wealth no longer has to flow through the UN's cumbersome channels. But perhaps the most interesting feature of the KRG is its potential as a model on which to base a federal style of government in Iraq.

Scholar-in-Residence for the Middle East Initiative at the *American University Center for Global Peace* Professor **Carole O'Leary** described developments there as "a fragile experiment in democracy and civil society-building". O'Leary's research, plus the words and deeds of KRG officials, suggest something more than political expediency is driving the increasing integration of factions in the KRG.

The INA has partly modelled its strategy for inculcating civil society and democracy on the KRG experience, highlighting its licensing of political parties and media development.

Reforms in press freedom, education and human rights have stimulated a growing sense of cultural tolerance; if this model could be applied elsewhere in Iraq, sectarian and federal tensions

might be greatly reduced, giving the state a much better chance of making the transition to real democracy than many Western analysts predict.

According to O'Leary, the development of a multicultural "Kurdistani" identity has been driven by common geography, a decade of self-rule and cultural tolerance, and a long common experience of marginalisation by central government. The Kurdistani identity – an inclusive, pluralist identity that does not threaten deeply rooted linguistic and ethnic affiliations – has provided cohesion within the KRG zone.

#### SECESSION SEEMS OFF THE AGENDA

However, it has not sparked a desire to secede from Iraq. This was clear as early as 1992, when monitored exit polls from elections stated that 82% of KRG inhabitants wanted to stay within Iraq. KRG officials and factional leaders are now willing to openly state that independence is not their aim.

The growing prospect a change of ruler in Baghdad is viewed in the KRG region with more mixed feelings than might be expected. "We welcome, but fear the process of regime change," Sideek said.

Key longer term issues include the post-regime change distribution of OFP revenues. On the political front, the KRG is clearly pressing to become one of the federal zones of a post-Baathist Iraq. According to KRG representatives canvassed by GSN, they do not care how many other zones there are in Iraq, as long as it is not split up.

This is by no means certain. The broad spectrum of possible models for a post-Saddam Iraq ranges from adoption of the KRG model across Iraq to the breaking down of the KRG on historical provincial lines – a development that could prompt further unrest in the future.

#### Speculating On The KRG's "Swiss Dinar"

While the Kurdistan Regional Government's gains can only be made permanent by regime change, uncertainty over recent weeks has produced a volatile cocktail of currency and price swings that have unsettled the local economy. High hopes for imminent regime change have triggered hoarding of the limited supply of pre-**Baathist Iraqi** dinars – the KRG's local currency. This has driven the value of the currency up sharply in relation to the **US** dollar, also widely in use. Such hoarding has been driven by the belief that after a war pre-Baathist Iraqi dinars will be reinstated as the national currency, not least because they do not carry the face of President **Saddam Hussein**. This currency is known locally as the "Swiss dinar", although the 2bn tattered notes in circulation were actually printed in the **UK**.

In the face of higher demand, and scare-stories that Iraqi and **Iranian** government agents had been mass buying notes, the dollar's value fell from a pre-crisis exchange rate of \$1=19 Swiss dinars to a low of 6.5 Swiss dinars; it has settled in the \$1=7-9 Swiss dinars band.

For **UN** agencies, UN-paid workers and those reliant on overseas remittances paid in dollars, this devaluation is highly unwelcome in the short-term. In the long-term, those investing in the Swiss dinar could be deeply disappointed if a new currency is introduced. Further economic instability has been caused by Iraq's intermittent closure of border posts. Heating oil shortages are likely to hit hardest in coming weeks. Lost trade will cost up to \$9m/month in the **PUK** sector alone.

The KRG has acted to reduce the impact of financial instability and the interdiction of trade. Although lacking a formal central bank, the KRG has attempted to calm nerves over currency speculation, stating that it will pay its own employees in dollars to dampen rampant enthusiasm for the Swiss dinar. It has released Swiss dinar stocks to lower demand. The KRG's Dr **Roush Nouri Shaways** has tried to talk down the market, saying that compared to the dollar, the euro, land and even vehicles, the local currency was "a bad investment".

Iraqi interdiction of fuel supplies prompted the KRG to stockpile fuel and slash petroleum rations by one-third. The KRG has begun stockpiling potable water and wheat flour.

# Gulf Braces Itself For Another Ecological Disaster

Iran and the *Gulf Co-operation Council* states have drawn up a detailed action plan to counter any Iraqi threat to repeat its 1991 bulk oil spillages into the Gulf.

The greatest fear of the Kuwaiti authorities' remains a direct assault on their territory with chemical or biological weapons, but oil contamination – either through direct Iraqi releases into the Shatt Al-Arab or through rocket attacks on Kuwait's oil facilities – remains a big worry (*GSN 701/13*). Even the much-strengthened US Patriot missile presence around vulnerable sites cannot guarantee 100% protection.

The Iranian/GCC preparations have been made under the aegis of the *Regional Organisation for Protection of the Marine Environment (ROPME)*. Senior officials have confirmed that plans for the emergency deployment of equipment to contain any new oil assaults have been drawn up.

Much is at stake in ecological terms. "The Arabian Gulf is a particularly rich area for biodiversity," said *World Wide Fund for Nature* Director-general Dr **Claude Martin**, pointing to the region's large populations of dugongs (sea cows) and coral reefs.

US forces might be able to secure control of key Iraqi oil installations before Baghdad could order the release of significant quantities of oil. Some believe that Iraq may be more reluctant to waste its own crude – in contrast to its spiteful opening of Kuwaiti taps as its invading forces were driven back in 1991. This is the signal coming from some Iraqi oil officials.

But Kuwaiti planners believe crude could still easily be released from Iraq's Mina Al-Bakr terminal on the Shatt Al-Arab. This would threaten the Iranian coast and the low-lying Kuwaiti islands of Bubiyan and Warba. Gulf waters south and east of the islands are important fish breeding grounds, while the mudflats, inlets and channels surrounding the islands are both fertile and fragile, home to large populations of marine wildlife and birds. Kuwait has drawn up a plan

to develop prawn and fish farming in this zone, but this has been kept on hold because of fears that Iraq might once again pose a threat.

### THE FALLOUT FOR KUWAIT

Speaking in Abu Dhabi, Kuwait's *Environment Public Authority* director Dr **Mohammed Al-Sarawi** told *GSN* that Iraq's draining of its southern marshes had reduced the flow of fresh water into the estuarine area around the islands. There is also concern about the flow of Iraqi industrial pollutants into the northern Gulf from the Shatt Al-Arab.

Bubiyan is uninhabited at present, but there are plans to develop agriculture. The bridge linking the island to the mainland, destroyed by Iraqi forces during the last Gulf War, has been rebuilt.

Any air assault on Kuwait's more than 1,000 oil wells, processing facilities, or its Sea Island export terminal, could trigger leakages of crude or wellhead fires, with devastating long term consequences. Some 11 years after the end of the last war, two important aquifers remain contaminated and unusable – although the Al-Rawdatain aquifer alongside the oilfield of the same name, just south of the Iraqi border, was not damaged.

Despite a massive pumping effort to suck up 21m barrels of oil left after the 1991 oil releases, the country is still littered with some 320 oil lakes. Evaporation from the lakes continues to damage the air.

It took four years after the war to clean the two main agricultural zones, Wafrah, in the south, and Al-Abdaly, close to the Iraq border. These are now fully restored, supplying fruit and vegetables to Kuwait City. There are fears that both areas could be damaged once more by renewed war-related air pollution.

Oil spills pose a particular threat to Kuwait's six power and desalination plants, at Shuwaikh, Doha, Shaiba and Ras Azzor.

Sarawi said that booms and dispersants were being kept ready to prevent water entering the plant intakes. If the inflows are polluted,

reserve tanks of clean water will keep the plants operational for four to six months. In 1990-91 power and water plant operations were undamaged.

The *United Nations* has allocated \$108m from Iraqi compensation payments to finance studies of the overall impact of the 1990-91 oil releases and well fires on Kuwait's land, air, marine and groundwater and health situation. These will need a further two years' work.

Even if there is no new direct assault on Kuwait, the country could suffer some overspill air and water contamination from warfare around Basra and surrounding industrial zones.

## Doubts Still Surround Qatar-Kuwait Pipeline

*GSN* learns that **Saudi Arabia's** blessing for the \$2bn Qatar-Kuwait gas pipeline is far from guaranteed, despite press reports in January that said Riyadh had given its full backing to a link which is set to go through Saudi territorial waters (*GSN 702/15; 701/1; 699/6; 695/3*).

A senior Doha-based energy official told *GSN* in early February that *Qatar Petroleum's* popular Director of Oil and Gas Ventures **Nasser Jaidah** had had his knuckles rapped for telling a conference in Doha last month that the Kingdom's support was assured.

It appears that some within the Saudi hierarchy want to continue to target Qatar, even to the extent of threatening economic weapons against its neighbour in an attempt to force it to rein in the outspoken Doha-based *Al-Jazeera Satellite Channel*.

The energy official indicated that senior Saudis had let it be known that Jaidah was premature in assuming that Riyadh had come to an agreement over the proposed 1bn ft<sup>3</sup>/day pipeline.

QP is particularly anxious that some of its pet energy schemes do not become entangled in the diplomatic spat between the two GCC states. They will be hoping that Kuwait's clout with the Saudis ensures it will take off as planned.

## GSN Risk Grade – B/2+: Tensions under control in pre-war atmosphere, gas sales boom

### Political And Social Development

**Overview:** Emir Sheikh Hamad Bin Khalifa Al-Thani has pushed conciliatory rhetoric to avoid an anti-US backlash, and to reinforce his grip on power amid rumours of in-fighting within the ruling family. A cautious democratisation continues in a small country where 11 of the 21 government portfolios are held by Al-Thanis. A 45-member, two-thirds elected Parliament is expected in 2003/04 with all Qataris over 18 allowed to vote; political parties will not be allowed.

**Social forces:** Although there is little sign of mass dissent, many Qataris dislike closer military links with the USA. Qatar-based Islamic scholar Youssef Al-Qaradawi is proof the country is not free from conservative Islamist thinking. In a recent interview Qaradawi said those killed fighting US forces were "martyrs" as they consider them "invading troops an enemy within their territories but without their will". He made no direct reference to US forces in Qatar and stressed he did not condone attacks on civilians. There was no big public response but the authorities will maintain a close watch on Qaradawi and Daawa groups.

**Iraq conflict:** Despite the US military's growing presence – the US Central Command complex at As Sayliyah is now complete – Sheikh Hamad's rhetoric remains conciliatory. Qatar may play a diplomatic role in the aftermath of war; it holds the GCC and Organisation of Islamic Conference (OIC) chairs, while Oil Minister Abdallah Bin Hamad Al-Attiyah is President of OPEC; Qatar was the first GCC country to normalise diplomatic relations with Iraq following the 1991 Gulf war.

**External factors:** US airbases are an insurance policy against regional threats, but pose awkward policy questions. Historical animosity with Bahrain was overcome by the 2001 Al-Hawar Islands agreement, although Qatar recently seized Bahraini fishing vessels for alleged incursions into its waters suggesting some continued sensitivities. Relations with Saudi Arabia remain strained. Qatar has angered most regional governments for its sponsorship of Al-Jazeera Satellite Channel, but the independent-minded Sheikh Hamad and his close ally Foreign Minister Sheikh Hamed Bin Jassem Al-Thani (a major Al-Jazeera shareholder) seem able to live with this.

### Economic Outlook

**Overview:** The threat of terrorism and possible war with Iraq could influence investor decisions in the short-term but will not prove a major brake on the hydrocarbons industry. Qatar National Bank has forecast surprisingly low 2% GDP growth for 2003, compared to an estimated 4% in 2002. Oil production of 650,000 b/d is forecast for 2003 compared to an average 638,000 b/d in 2002. Qatar's production ceiling under the OPEC quota arrangement was raised by 39,000 b/d to 635,000 b/d in January. Privatisation is planned but hydrocarbons wealth may stifle any great feelings of urgency.

**Energy development:** Qatar's five-year plan aims to attract \$16bn investment by 2007 – \$4.7bn for the North Field gas development, \$2.5bn for petrochemicals, \$4.1bn to enlarge refineries and \$825m for natural gas liquids. Qatar has been proactive in reassuring its clients that oil and gas supplies will continue in the event of war. The award of contracts for several North Field-associated projects including the Dolphin pipeline to the UAE and an enhanced gas utilisation (EGU) project is expected in 2003. Award of the first of three new offshore exploration blocks (3, 4 and 14), made possible by the 2001 border agreement with Bahrain, is expected in March.

**Gas sales:** Qatar has expressed concern at EU plans to move away from long-term gas supply deals to shorter term contracts. Energy Minister Abdallah Bin Hamad Al-Attiyah is concerned this will impact on investment plans – such as Qatargas II – by reducing the security of investment returns. Moody's Investors Service's has placed Ras Laffan LNG Company's Baa2 rating on review for possible downgrade, citing a worsening risk profile, but RasGas's track record suggests it will overcome negative short-term risk perceptions. Projects expecting to close financing in 2003 include EGU and the Qatar Petroleum (QP)/Sasol gas-to-liquids (GTL) scheme.

**Liberalisation:** Privatisation of power distribution assets is planned. 100% ownership in agriculture, and tourism sectors is mooted, as are sales of health and education assets. The GCC customs union was launched in January, a significant step towards a GCC/EU free trade agreement.

### Qatar: Key Projects

**Q-CHEM:** Units at Mesaieed inaugurated in January for the \$1.12bn 51/49% JV of QP and Chevron Phillips Chemical.

**QATARGAS II:** Two 7.5m t/yr trains LNG project being studied by QP and ExxonMobil, with first deliveries targeted for 2007. Royal Bank of Scotland is advising on financing.

**RAS LAFFAN LNG:** A third train well under way; there will be a capacity hike to 10m t/yr with RasGas' fourth train, for 2005 completion.

**PETROCHEMICAL PROJECTS:** These include the \$1.1bn Q-Chem II (with an EPC award expected in Q4 04 for completion in 2007); \$550m Qatofin low-density polyethylene project; and \$470m 1.3m t/yr Ras Laffan ethane cracker (2007 start-up).

**RAS LAFFAN IWPP:** Qatar's first independent water and power project has initial 750MW and 40m g/d capacity. First power expected in April for full operation May 2004 by US developer AES Corporation.

**IDD AL-SHARGI FIELD:** Development contracts signed by QP and Occidental Petroleum for full field development of south dome and phase two of north dome.

**2006 ASIAN GAMES:** This major event implies massive infrastructure requirements including \$233m sports complex in Doha, \$30m shooting range, and redevelopment of Doha's stadiums. Work has recently been accelerated.

### GSN Risk Grades

The GSN Risk Grading is based on GSN's assessment of the outlook for political and payments stability. The political outlook is reflected on a letter rating, where A is most stable and E least. Payments conditions are represented by a number: 1 is most favourable and 5 least. + or - represents a slightly higher or lower than average score.

### QATAR: Selected Economic Indicators

(\$ billion)	1998	1999	2000	2001
GDP	10,255.5	12,393.1	16,454.1	16,152.2(p)
Oil sector (as % GDP)	34.8	45.8	58.4	56.4(p)
GDP growth (%)	-9.2	20.8	32.8	-1.8(p)
Consumer Price Index				
(% change)	2.9	2.2	1.7	1.4
Exports (fob)	5,030.5	7,213.7	11,594.0	10,870.1
Imports (fob)	3,070.6	2,251.6	2,929.7	3,385.7
Trade balance	1,959.9	4,962.1	8,664.3	7,484.4
Current account	-455.5	2,171.2	5,473.9	4,263.7
Reserve money (MO)	683.2	787.9	840.9	938.5
p-preliminary				

Source: Qatar Central Bank

## GSN Risk Grade —

**Political And Social Development**

**Overview:** The Saudi government continues to push for a peaceful resolution to the Iraq crisis with political thinking shaped by internal dynamics and the prospects of civil disturbance within the Kingdom. Problems with radical Islamists, largely denied by the authorities, are a cause for concern against a background of growing poverty, unemployment and grassroots hatred of the US military presence. US use of Saudi airbases remains a sensitive issue; seemingly conscious of this the Bush administration has resisted public pressure on the government.

**Government:** The Basic Law of Government affirms the monarchy's central role. Crown Prince Abdallah bin Abdelaziz has drafted a Charter for Arab Reform – to be formally unveiled in March – that will set goals for the Arab world and could launch internal reforms; the prospect of elections have been mooted, first at municipal level, followed by the 120-member Majlis Al-Shura, now appointed by the ailing King Fahd.

**Internal security:** Despite an annual security budget of around \$7bn Saudi Arabia has been criticised for its handling of Al-Qaeda. Innate conservatism is represented by the powerful Interior Minister Prince Nayef Bin Abdelaziz. The extent and cohesiveness of the underground Islamist movement is unclear. Dissidents claim that recent shootings represent an armed response by Al-Qaeda to belated crackdowns by the security services. The authorities have in the past been in denial; it is widely thought that Islamists were responsible for some recent bomb attacks blamed on Western bootleggers. Prince Nayef has even claimed that there are no active or dormant Al-Qaeda cells in Saudi Arabia. The use of Saudi airbases against Iraq may lead to further civil disturbances.

**External factors:** Bilateral spats will continue to complicate relations with the West; religious freedoms, human rights, terrorist financing and governance are issues of concern. Relations with Qatar are still sour due to Doha's patronage of the Al-Jazeera Satellite Channel, other regional ties are solid, notably with new ally of convenience Iran.

**Economic Outlook**

**Overview:** Finances are strained with budget deficits pushing up debt despite high oil prices, while unemployment pressures remain unchecked, fuelled by population growth of 4-4.4%. Plans to reduce the number of foreign nationals working in the Kingdom to 20% of the population by 2013 could create vacancies. Saudi American Bank (Samba) estimated only 0.7% real GDP growth for 2002 with 3.8% forecast in 2003. Despite three years of high oil revenues, debts have grown and foreign reserves have fallen (to \$41.2bn in November).

**Oil exports:** Saudi Arabia should export 7.963m b/d under the OPEC quota arrangement (increased by 488,000 b/d in January) and has pledged to pump more should it be needed during a war in Iraq. Samba has raised concern that Saudi support for the OPEC \$22-28/bbls price range may cause long-term economic damage as non-OPEC members look to boost market share during a time of high oil prices.

**Budget:** The 2003 budget has been set at a conservative \$17.5/bbl oil price, with a \$10.4bn deficit envisaged – the third in a row. The government will borrow to cover this. A deficit of around \$5.6bn is expected for 2002, despite a \$5/bbl above-forecast average price for Saudi crude. Total 2003 revenue is projected at \$45.3bn, with expenditure at \$55.7bn. Finances are stretched and transparency remains an issue. In December, Dresdner Bank and Barclays Capital launched legal action over a \$48m unpaid loan. Crown Prince Abdallah is attempting to rein in public spending but to no obvious immediate effect apart from some reports of slower payments.

**Liberalisation:** The limits of reform were shown when draft plans to levy a 10% tax on expatriates earning over SR3,000/month were rejected by the Majlis Al-Shura. The GCC customs union launched on 1 January brought a free trade pact with the EU nearer, but Saudi membership of the World Trade Organisation remains problematic. State and entrenched interests remain dominant. An IPO for 30% of Saudi Telecoms was launched in December, with a listing expected by 15 February. Smaller sell-offs, such as the privatisation of some state hospitals, are likely to accelerate.

**IRAQ DIPLOMACY:** Saudi Arabia is inked with an initiative to persuade President Saddam Hussein to avoid war by opting for exile. The issue was discussed at an Istanbul meeting of Saudi, Syrian, Turkish, Iranian, Egyptian and Jordanian foreign ministers. Iraq has denied the reports, while Saudi sources suggested the idea was the brainchild of US hawk Richard Perle and is all show and little substance. If Saddam is to go into exile, Saudi Arabia might prove the one acceptable destination.

**Saudi Arabia: Selected Economic Indicators**

(\$ billion)	1999	2000	2001	2002(f)
Nominal GDP	161.0	188.4	186.2	182.8
Nominal GDP growth rate (%)	10.4	17.1	-1.2	-1.8
Real GDP growth rate (%)	-0.8	4.9	1.2	0.2
Current account	0.4	15.6	14.5	10.5
Central gov. domestic debt	44.4	43.8	45.6	48.8
as percentage of GDP	119.0	87.0	90.0	95.0
Oil price Saudi Average (\$/barrel)	17.45	27.0	21.5	21.8
Official Foreign Assets	69.4	73.5	82.6	78.5
Cost of living (% change)	-1.2	-1.0	-0.8	-0.5

f = forecast

Source: Saudi American Bank, Ministry of Planning, Central Department of Statistics, Saudi Arabian Monetary Authority, IMF

**Saudi Arabia: Key Projects**

**GAS PROJECTS INITIATIVE:** Final technical negotiations for the Shell-led Core Venture Three (partners Conoco, TotalFinaElf) are under way, with technical talks on the ExxonMobil-led \$15bn Core Venture One South Ghawar project (with Shell, BP and Phillips Petroleum) expected soon. The \$5bn Core Venture Two Red Sea project, also led by ExxonMobil (with Marathon and Occidental), has been postponed pending an economic review. Saudi Aramco (backed by Al-Saud conservatives) privately opposes the international oil company influx.

**POWER:** Demand is forecast to more than double by 2020, with an estimated \$90bn investment requirement over 1999-2023. Aramco launched a request for proposals for four 200-300MW IPPs in November. A tender is expected February for the Shouaiba phase two project (3x350MW turbines), while progress is expected with the 400MW Jeddah PP3 and Riyadh PP9 expansion projects.

**HARADH AND HAWIYAH GAS PLANTS EXPANSION:** Tenders expected H1 and H2 respectively for 500m ft<sup>3</sup> new capacity at each plant.

**OIL REFINERIES:** Award expected February for the expansion of the Yanbu refinery. Bidders include South Korea's Daelim Engineers & Contractors and Italy's Snamprogetti. Work includes a new isomerisation unit and expansion of the plant's catalytic reformer. Tenders were launched in January for new diesel hydrotreaters at Yanbu and Riyadh.

## IRAN: Export Credits Flow For NPC

HSBC has announced a \$108m facility backed by the UK's *Export Credits Guarantee Department (ECGD)* and reinsured by Italy's *Sace* to support the construction of a styrene monomer facility at Bandar Assaluyeh developed by *National Petrochemicals Company (NPC)*. Security from offtake arrangements is also written into the deal.

The facility will back a contract awarded in Q3 01 to the UK office of Italy's *Snamprogetti* with Tehran-based consultant engineers *Sazeh Consultants*. The ECGD/Sace insurance/reinsurance tie-up points to the growing global importance of co-operation agreements between export credit agencies – such as ECGD's accord with The *Japan Bank for International Co-operation (JBIC)*, which underwrote a \$34m export credit to *Bank Tejarat* last March, also arranged by HSBC.

The trade and project financing market seems set to grow further, even if problems emerge along the way – as is likely when introducing complex financing structures to inexperienced administrations.

Such facilities may face opposition in the Majlis (Parliament) as the extent of new foreign financing obligations becomes apparent, but this is unlikely to halt the trend towards export credit.

Bankers report substantial structured trade finance activity in the hydrocarbons, petrochemicals, power and mining sectors. *National Iranian Oil Company (NIOC)* and NPC are widely seen as the top corporate risks.

Other sectors are do-able when

medium-term project guarantees are available through the Ministry of Finance or *Bank Markazi Jomhouri Islamic Iran (Central Bank of Iran)*.

Bankers believe that major export credit facilities will play a role in the financing mix for development of the South Pars gas field.

Reports that *Société Générale* has secured an advisory mandate for the Persian LNG project sponsored by *Royal Dutch/Shell, Repsol YPF* of Spain and NIOC point to the potential in the gas sector, where project finance is starting to emerge.

The Persian LNG deal – involving sales by NIOC of dry gas feedstock – might be suitable for a tolling-type arrangement, as Société Générale has deployed for the *Egypt LNG* scheme.

### PETROCHEMS ACTIVITY

NPC is very active at Bandar Assuleyeh, where a \$297m methanol scheme secured a \$139m excred facility from *HypoVereinsbank*, channeled through Bank Tejarat. This is backed by the *Austrian, German and Spanish ECAs*.

*Crédit Agricole Indosuez* led a \$319m facility backed by France's *Coface*, the Netherlands' *NCM* and Sace for 1.35m t/yr ethane cracker.

ECGD has been showing strong support for NPC projects, in January announcing a move to loosen up its terms for transactions involving the state-owned NPC (*GSN 702/18*).

This points to continued strong interest from European and Asian ECAs, as well as the British government's determination to use business links as an incentive to promote constructive engagement with Tehran.

ECGD sees NPC as a good risk for smaller business, and as a "strategic

player" in the global petrochemicals market (*GSN 695/9*). Since the early 1990s payments problems, Iran has re-established itself as a good payer: on this basis ECGD limits could be extended in future, officials said.

### A WIDE RANGE OF SUPPLIERS

Despite the threat of a new regional conflict and continued US sanctions, market soundings suggest considerable exporter demand for a range of ECA-backed project facilities and credit lines.

The *Export-Import Bank of India* has approved its largest ever line of credit – worth up to \$200m – to cover 85% of contract values. Seven local banks qualify to draw on this line.

Belgium's *Ducroire/Delcredere* recently announced a medium/long-term capacity increase, and dropped a requirement for bank guarantees in transactions below €10m (\$10.8m).

### UAE: Ajman Water Complete

A \$140m project financing structure to back the \$450m Ajman integrated wastewater project has closed, allowing for the launch of new utility *Ajman Sewerage (Private) Company Ltd (ASPCL)* and the start of work, to take four years, to connect 45,000 properties – and 350,000 people – to modern sanitation for the first time.

Project sponsors grouped into ASPCL are *Thames Water* (60%), *Black & Veatch International*, *Belgian* contractor *Six Construct* (both 10%) and the Government of Ajman (20%). Black & Veatch and Thames Water were advised by lawyers *Denton Wilde Sapte's* London and Dubai offices.

As with many private utilities schemes, Ajman required new legislation – in this case a *Sewer Law* – for the project to function.

Financial close came 13 months after commercial close. The London-based *Mizuho Corporate Bank's* project finance team was ASPCL's financial advisor for a structure including \$38m equity, a \$77.5m 14-year club loan and payments linked to connection fees.

Arrangers for the debt were Germany's *Bayerische Hypo-und Vereinsbank* and *Bayerische Landesbank*, and *Mashreqbank* and *United Arab Bank*, both of the UAE.

### Gulf Currency Box

	\$	£	€	¥ (x 100)
Bahrain	0.3770	0.6209	0.4097	0.3143
Iran	7981.0	13,142.5	8673.5	6654.44
Iraq	0.3110	0.5122	0.3380	0.2593
Jordan	0.7096	1.1686	0.7712	0.5917
Kuwait	0.2988	0.4920	0.3247	0.2491
Oman	0.3851	0.6342	0.4185	0.3210
Qatar	3.6404	5.9952	3.9562	3.0353
Saudi Arabia	3.7502	6.1761	4.0755	3.1269
Syria	51.5750	84.9363	56.0517	43.0025
UAE	3.6730	6.0489	3.9916	3.0625
Yemen	177.890	292.958	193.331	148.322

Source: *Financial Times*.

## INSTITUTIONS

AES Corporation	16
Ajman Sewerage (Private) Company Ltd	18
Al-Assalah	1
Al-Jazeera Satellite Channel	15-17
Al-Qaeda	2, 6, 17
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Aluminium Bahrain (Alba)	1
American University of Beirut	8
Ansar Al-Islam	2, 13
Ansar-e Hizbollah	20
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Bahrain Petroleum Company (Bapco)	1
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Bank Tejarat	18
Barclays Capital	17
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## Iran Welcomes The Release Of An Ailing Object Of Emulation

TEHRAN—The release from house arrest of a senior cleric who was the late Ayatollah **Ruhollah Khomeini's** anointed successor before Rahbar (Supreme Leader) Ayatollah **Ali Khamenei** could be nothing but big news in an Islamic Republic. The 80-year-old Grand Ayatollah **Ali Montazeri** is a celebrity with big support within the religious establishment and wider population; he is a threat to hardline factions in the conservative ruling group – including his junior in the Shiite clergy, Khamenei – and an international reminder of human rights problems in Iran. It was Montazeri's questioning of religious Khamenei's authority that led to his house arrest in 1997.

Initial reports from the conservative camp said Montazeri was released on condition he refrained from politics. This may be wishful thinking: Montazeri said he had accepted no "conditions", and would continue to defend freedom and democracy – and reforms promoted by President **Mohammad Khatami**. Montazeri is a focus for reformists and dissident clergy. Ayatollah **Jalaludine Taheri** – who famously resigned last year as Isfahan's Friday prayers leader in protests at the political situation (*GSN 691/MEI 3*) – had written to senior clerics calling for his release.

Once the *Supreme National Security Council (SNSC)* agreed to Montazeri's release supporters gathered outside his Qom home. The Grand Ayatollah, his two sons and relatives and friends then attended a small mosque near his home – where he made speeches before house arrest – and the tomb of his son Mohammad. Speaking to some 600 supporters, including some senior clerics, an emotional Montazeri observed: "God, whose property we all are, has given to all believers religious leadership but not unlimited leadership."

No wonder reformists welcomed Montazeri's release. However, the event did not represent any major concession to majority opinion – rather it was a defensive move promoted by hardline strategists. The death of an ailing Montazeri

while under house arrest could lead to protests and unrest of the sort the *Basij, Ansar-e Hizbollah* and other hardline groups could find more difficult to suppress than their usual business of cowering reformists. Bazaari backers of the conservative camp and the hardline *Motalefeh (Society of Islamic Coalition)* were wary.

Montazeri's health is at the very least fragile – of sufficient concern for over 100 Majlis deputies to sign a petition asking Khatami (who heads the SNSC) to lift restrictions on the Grand Ayatollah. His death could crystallise opposition, especially in Qom, Isfahan and Montazeri's native Najafabad regions. So would possible future disputes over Montazeri's eventual final resting place, a big issue in a branch of Islam where the religious leaders' tomb has great status.

A majority of senior clerics are conservatives, and some are firmly in the hardline camp. Khamenei tends in this direction, while keeping analysts guessing with periodic shifts towards the centre. Khamenei's control over security organisations and the Judiciary – whose head Ayatollah **Seyyed Mahmoud Hashemi Shahroudi** takes his orders from the Rahbar – has proved a critical component in the conservatives' continuing hold over Iran. Not all clerics agree with this. Several grand ayatollahs condemned the verdict in the recent **Hashem Aghajeri** case; even the leading conservative Grand Ayatollah **Nouri Hamedani's** office denied he had approved Aghajeri's death sentence (*GSN 701/6; 698/11*).

Splits within the clergy reflect a religious/political environment where hardliners are becoming more hard line and reformists more exasperated. With ultra-hardliners talking about a "revolutionary jihad", possibly in the form of a coup against Khatami, an ugly situation is forming that even the political manoeuvrings of Khamenei and man for all seasons Ayatollah **Ali Akbar Hashemi Rafsanjani** will not be able to contain without considerable damage.

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