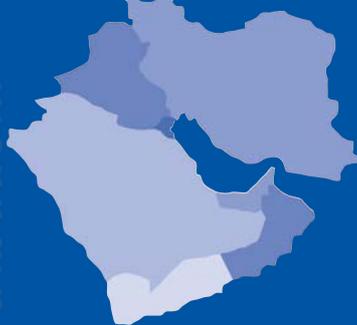


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GSN

Companies & People

Iraq: UN Come Back

The United Nations system was humiliated by the Anglo-Saxon "Coalition of the willing's" decision to enact US President **George W Bush's** policy on Iraq sooner rather than later, but the UN is preparing for a major role in post-war Iraq – managing aid and oil revenues. This *post-facto* effort will give a multilateral aspect to President **Saddam Hussein's** expected fall, and could help to save the face of key Bush ally UK Prime Minister **Tony Blair**, whose totemic International Development Secretary **Clare Short** could play a big role (see page 20).

UN Secretary-general **Kofi Annan** has appointed Portugal's **Ramiro Lopes da Silva** as UN Humanitarian Co-ordinator For Iraq, initially based in Larnaca, **Cyprus**. He will operate under the aegis of the UN's **Office for the Co-ordination of Humanitarian Affairs (OCHA)**. How this fits in with the US reconstruction contract-fest is unclear: within a multilateral framework of strict tendering rules, hastily-awarded US contracts could be questioned (see page 9).

OCHA told *GSN* it had received \$42m of the \$123.5m emergency aid it had sought from donors for Iraq in recent months. More is pledged – but some donors are holding back until war starts, triggering a humanitarian crisis.

Across The Region

Crown Prince Abdallah has promised change but has yet to deliver, and Saudis are asking whether the new Iraq crisis will act as a spur for reforms in the Kingdom. Economic, social and human rights reforms could be announced by June, but opponents canvassed by *GSN* remain sceptical. Divisions within the ruling Al-Sauds point to very differing views over what reform means. PAGE 10

Interior Minister Prince Nayef says there are no Al-Qaeda sleeper cells in Saudi Arabia, but resentment over the US alliance is fuelling support for militant jihadi Islamism and threatens new security problems. *GSN* examines the extent of jihadi support. PAGE 11

The international community may not like it, but eve of war signs from Washington suggested that Iraq could be governed by US officials for some time after Saddam Hussein falls. This puts opposition parties in a difficult situation and threatens to leave "Coalition" forces exposed. *GSN* examines the US team and the opposition's role. PAGE 5

Ahmed Chalabi's neo-conservative supporters may lose out in the tug-of-war for influence to come. PAGE 6

Three to watch on the US team: Lieutenant General John Abizaid, Liz Cheney and Zalmay Khalilzad. PAGE 9

USAID has outlined measures the USA will take to ensure the transition from the destruction of war to the reconstruction of nation-building. The rehabilitation of Iraq's oil industry will be achieved in three initial phases. PAGE 7

The Oil-for-Food Programme is dead! Long live the OFP (and Clare Short)! *GSN* explains how the UN and other agencies could yet win the peace. Although UN diplomacy failed, British and American diplomats have begun drafting a new Security Council resolution that would place control over Iraq's OFP in the hands of Secretary-general Annan. PAGE 20

Oman's Sultan Qaboos has given Sheikha Aisha Bint Khalfan Bin Jumiel Al-Siyabiah ministerial rank. She is the GCC's first female cabinet minister. PAGE 17

Citibank and other banks have pulled back from Bahrain's offshore. PAGE 14

GSN's Analysis

The USA's "Coalition of the Willing" should quickly win the war launched on 20 March, but many questions remain about the shape of post-war Iraq and the wider region. *GSN* examines the myriad options, offering best case, worst case and base case scenarios built around key factors in the third Gulf War. PAGE 3

The GCC can never be the same again after the third Gulf War – and reform in the Gulf monarchies could yet be a legacy of regime change in Iraq. Militarily, the Peninsula Shield force has mobilised, regardless of local squabbles and misgivings. The key question is whether monarchies can maintain stability through political and economic evolution – without resort to internal security or media clampdowns – thereby renewing the social compacts that have kept them in power for decades. GSN VIEW, PAGE 2

Kuwait is on the front line of the Iraqi conflict, but barring unforeseen disasters, the Emirate should emerge relatively unscathed. *GSN* is more concerned with perennial Kuwaiti problems – political paralysis and signs of real strain in the Al-Sabahs' social compact with the population. Signs from Project Kuwait and other energy schemes are cautiously positive, so for now we maintain Kuwait's C and 2 Risk Grades. RISK MANAGEMENT REPORT, PAGE 16

Oman remains on *GSN's* Risk Grades B and 3, despite a regional conflict that creates a very ambiguous situation for Sultan Qaboos. Energy continues to draw in investment and project finance flows should weather short-term turbulence. RISK MANAGEMENT REPORT, PAGE 17

UAE's generally favourable economic performance was undermined by a marked deterioration in the fiscal position, the IMF said in its first published Article IV assessment. PAGE 13

UAE economic data and forecasts to 2007. PAGE 14

Controlling inflation and raising the external value of the dinar will be the top priorities for the new economic policy-regime in Baghdad. But there is all to play for, and reports that an incoming US administration might opt for a dollar economy can't be discounted. PAGE 15

Kuwait is the launch pad for an invasion of Iraq; Qatar, Bahrain and Oman are among those providing basing for US forces. But Kuwait and Qatar were not even among the 30 countries listed by the US State Department as members of President George W. Bush's "Coalition of the Willing" – a list that included Colombia, Eritrea, Ethiopia and Iceland. The modesty of the USA's Gulf Co-operation Council (GCC) allies in publicising their role in the conflict reflects the ambiguous situation that Gulf monarchies find themselves in. Dependent on the *Pax Americana* for their security, more than ever before they must listen to their youthful population's concerns about geopolitical and social issues – and a US-led war, even against the hated Saddam Hussein, does not play well among the *shabab*.

Global media attention will soon focus elsewhere, but the GCC can never be the same again after this third Gulf War.

A positive military side effect of the Iraq crisis has been a first major deployment "for real" of the GCC's Peninsula Shield force, to defend Kuwait. Sceptics may doubt its military effectiveness, or point to internal political tensions, reportedly reflected among some Saudi military personnel (see page 11). But the fact remains: faced with a major threat – the risk that Iraq will launch a retaliatory attack on Kuwait – Gulf monarchies have put a force of 20,000 well-equipped troops into the field in a matter of weeks. Regardless of local squabbles, such as the ongoing dispute between Saudi Arabia and Qatar, GCC states have acted together in the interests of common security.

But beyond the war itself, can the small Gulf states maintain stability through political and economic evolution, and without resort to internal security or media clampdowns?

The international context is unhelpful. Given his reluctance to pressure Israel into big concessions, Bush's last minute promise to set out the "roadmap" to Middle East peace cannot produce the justice for Palestinians demanded by Arab opinion. While the Palestinians remain under effective Israeli occupation, even a US invasion of Iraq that met unrestrained popular welcome in Baghdad and Basra would not be enough to calm popular resentment of US policy.

In this situation, with the understandable exception of Kuwait, even close allies such as Bahrain's King Hamad Bin Isa Al-Khalifa have kept a public distance from the US attack on Iraq. Few Gulf citizens will shed tears for the brutal Saddam Hussein regime, but (a majority of Kuwaitis apart) that does not make them supportive of the USA. The popular emotions stirred by the Iraq crisis, as by the plight of the Palestinians, have highlighted the need for Gulf ruling elites to consolidate stability through the creation of deeper and broader economic and political structures.

Old style top-down monarchical government left ruling families entirely accountable for national policy – and potentially exposed to blame for unpopular decisions, such as the hosting of foreign military forces. Inching towards more participatory structures, as regularly recorded in GSN – in this issue through new women's rights in Oman (see page 17) – allows for decisions to be rooted in a wider legitimisation. But it will be a slow process, as we have been reminded by UAE President Sheikh Zayed Bin Sultan Al-Nahayan's recent failure to appoint women to the Emirates' consultative council.

It is hard to imagine any Gulf ruling family surrendering control of defence and foreign policy to their emergent elected assemblies. In seeking to strengthen national cohesion, they will explore the scope for broadening economic participation first of all – through the creation of more jobs for locals, the upgrade of services and, in some cases, through democratic accountability for economic and social policy. Such intelligent steps to address basic everyday issues – jobs, public services, living standards and corruption – should help most Gulf governments to maintain popular support, rebuilding the social compacts that have kept them in power for decades.

Those Gulf dynasties that have kept corruption and privilege in check and achieved a good record of public service delivery are demonstrably more popular than weaker performers, even where there is – as in Qatar – a degree of public unease at the close alliance with George Bush's USA. Reform in the GCC could yet be the legacy of regime change in Iraq.

Perspective: Fourteen Years Ago

The Bush Administration's Middle East policy has at last begun to emerge from the screen of obfuscation and inaction that characterised the first months of the Bush presidency. Earlier this month, European foreign ministers hoping for Washington's support for an international peace conference on the Middle East were given a dusty answer by US Secretary of State James Baker III. In Vienna for talks on disarmament with the Soviet Foreign Minister Eduard Shevardnadze, Baker told the foreign ministers of France, Greece and Spain – the three countries charged by the European Community to promote the EC's Middle East peace efforts – that the USA was not prepared to join them in backing an international conference on the Middle East.

However great the Europeans' disappointment over this setback, it would be small compared with the dismay felt by most of the Arab states over the US rejection of the Arabs' preferred path to a Middle East peace settlement. The Gulf Arab countries especially were – and still are – firmly

committed to the holding of an international peace conference and had nourished high hopes that President Bush would adopt a more favourable position on the issue than the previous Reagan Administration.

At his Vienna meeting with his Soviet counterpart, the Secretary of State no doubt had in mind Shevardnadze's recent high-profile visit to the Middle East when he said the USA "welcomes Soviet interest in the Middle East" but came no closer to suggesting a joint superpower approach regarding the Middle East peace process was on the cards (GSN 357).

Last week, in moves which officially-inspired sources in Washington described as "regaining the diplomatic initiative in the Middle East", the USA put to visiting Israeli Foreign Minister Moshe Arens its request that the Israeli government cease some of the harsh measures it has adopted to deal with the Palestinian *intifada* in the Occupied Territories.

Gulf States Newsletter, Vol. 14, No. 358, 20 March 1989

Between A Virtuous Outcome And Catastrophe: Three Scenarios For An Uncertain Future

Even before Iraqis are confronted with the awe and terror of an unprecedented US-led bombardment – expected soon after the initial assault on the *Baathist* establishment and its defences, launched on 20 March as GSN went to press – businesses have been steeling themselves to chase the opportunities that will be offered by a post-Saddam Hussein Iraq (see below). Even before the war starts, it seems to be over for Saddam Hussein, with the USA awarding reconstruction contracts – whose legality of which is questionable (see page 20) – and companies already dreaming about the contracts on offer.

GSN has long argued that the growing grip of neo-conservative thinking on the Bush Administration, and the loss of control over events of players from UK Prime Minister Tony Blair to the *League of Arab States*, was most likely to lead to war and regime change in Iraq. Follow the neo-con agenda and you have a road map for change in the Middle East – but this is a road map whose routes established in the period since 11 September 2001 (and well before by leading hawks attached to the US Administration), lead into uncharted territory.

The future of Iraq as a territorial entity is in play – although we believe that with intelligent and sensitive post-war governance, and the pragmatism of Kurdish and Shiite leaders it will most likely remain a unitary state – as are the prospects for a better life for a majority of Iraqis.

Anger at the nature of this war with Iraq, for all that Saddam is loathed by many across the Gulf and in Europe, will add to the bitter mood in the Middle East. Ironically, while all eyes are on Iraq, some of the biggest hits in the war against terror have happened in Pakistan. *Al-Qaeda* will miss Khalid Sheikh Mohammed, just as it will eventually miss Osama Bin Laden and Ayman Al-Zawahiri. But the conflict will go on.

The 16 March warning by the US Embassy in the UAE of potential danger based on “indications of a possible terrorist attack against night clubs in Dubai” underlined the extent of jitters that even the Dubai spin machine cannot overcome. Further attacks against soft Western targets across the Gulf are feared (see page 6; GSN 705/7).

Efforts to show the US “alliance” is a benign, rather than imperial force, will focus on rebuilding Iraq as a modern, just state and in a more short-term initiative to resolve the Israel-Palestine conflict on a dual-state basis.

Such moves should be much welcomed, but from an Arab perspective they smack of tokenism, at least on the part of President George W Bush and a majority of his team. Bush’s grudging acceptance on 14 March that war with Iraq should be matched by a new effort to resolve the Israel-Palestine dispute was not a diversion from the neo-con agenda. While an exhausted Blair played up the possibilities offered by *Palestinian Authority* President Yasser Arafat making his old ally Mahmoud Abbas (Abu Mazen) Prime Minister – an issue where the British Premier has exerted effort – Bush’s lack of enthusiasm was palpable.

Bush’s largely pro-Israeli Administration has not changed the substance of its policy to the extent that the 100-plus cavils to the policy interjected by Prime Minister Ariel Sharon’s government will be ignored. Neither is it likely to object too loudly when, as seems possible, the *Israel Defence Force (IDF)* creates a sideshow in the war on Iraq by moving back into southern Lebanon to take on *Hiszbollah* and attacks *Hamas* in Gaza.

This would put Syria and Iran, both now anxiously looking on from the sidelines, into play – adding a significant further factor of destabilisation.

In this context, GSN sees a number of scenarios that the region could follow in the coming months, described in brief below.

• BEST CASE SCENARIO: A VIRTUOUS OUTCOME

If the very best case is not achievable – and Saddam and family leave Baghdad for good – a very short war sees the *Baathist* regime obliterated without too great a loss of civilian life and with easily controllable damage to Iraqi oilfields.

Key regional players Israel, Turkey, Syria and Iran stay out of the conflict. The USA’s use of military facilities in Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and Jordan does not reflect too negatively on the monarchies’ rulers.

Terrorist incidents and demonstrations are kept to a minimum and Gulf hotels soon start to fill again allowing the Dubai *IMF/World Bank* Annual Meetings and other events to go ahead.

The oil price stabilises in a \$20-30 band for the rest of 2003 and major projects continue in the Gulf after only a short pause. The war’s virtuous outcome helps stimulate the US, Japanese and other major economies, kick-starting growth.

A brief period of US-led military control is followed by the appointment of a genuine government of national unity, which has sufficient

credibility to hold Iraq together and oversee a wide-ranging programme of reconstruction. Huge flows of aid and technical assistance quickly help to unlock Iraq's own substantial human resources, encouraging new investment in the Arab world.

The Palestinians are not forgotten, with serious moves to tackle Israeli settlements, final status and other critical issues, as well as effective demilitarisation in southern Lebanon, creating a new security framework in which President **Bachar Al-Assad** can more comfortably move Syria into the mainstream and Iranian reformists can re-engage with the West, outflanking their hardline rivals.

• **WORST CASE SCENARIO: REGIONAL MELTDOWN**

Either short but cataclysmic or much longer than expected as Baghdad becomes the 'Arab Stalingrad', the war involves more civilian casualties and essential infrastructure damage than predicted. Oil prices hit \$50/bbl after Saddam sets up a wall of flame around his major oil fields which sets off very deep fires; oil fields and pumping stations suffer major damage, with sabotage in Saudi Arabia and other countries creating panic and showing radical Islamists just what damage they can achieve by targeting the oil industry.

Around the periphery, bush wars flare with Turkey entering Iraq, and Syria and Iran backing Hizbollah in a standoff against Israel – whose offensives in southern Lebanon and against *Hamas* in Gaza and the West Bank earn new international opprobrium, but only a mild telling off from Washington. Arab populations and Western peace movements mobilise against governments that backed the war, and the eventual successor regime in Iraq is totally discredited.

Policing Iraq proves a nightmare and communities split to best protect their interests; the Kurds are sold out again; trouble in the south spills over the neighbours.

In a volatile situation, the *GCC* leaderships become more isolated; Westerners stay away and opponents gain momentum. Radical Islamists argue that only they can offer an alternative; in response, governments crack down on dissidents while tightening rules of Islamic behaviour.

In Iran, hardliners make gains against President **Mohammad Khatami's** government, arguing that reformers have sipped with the devil for no material gain, while street fighters force all but the most militant student reformists off the streets.

• **BASE CASE: 'BAGHDAD SPRING', FRACTIOUS SUMMER**

A short war sees the Baathist regime obliterated and Iraqi oilfields restored to current levels of production at around 2.1m b/d by end-2003. However, after a very short "Baghdad spring", as those Iraqis not in mourning celebrate their liberation, disillusion sets in at the US Administration's inability to disengage from making

basic political and economic decisions in Iraq, while failing to commit adequate troops and resources to the cause. President Bush's attentions move on to pasture new, creating new international friction as neo-conservatives push for action on Iran and Syria.

The *UN Security Council* rift between the USA and UK on one side and **France** and **Russia** on the other may take a long time to heal while each of these parties manoeuvres for position, making the expected post-war flow of debt relief and funding more difficult to achieve. This will add to pressures on the new Iraqi administration to deliver anything other than emergency assistance – at least outside the scope of contracts awarded by the USA to predominantly US companies. In a sour situation Iraq becomes a difficult policing problem, especially as deals to accommodate Turkey in the removal of Saddam compromise the Kurds.

Some oil fields could be badly damaged in the coming conflict, but more difficult still will be the task of overhauling the majority of existing fields that are already in a poor state. Biggest gainers here will be drilling companies like (Vice President **Dick Cheney's**) *Halliburton* and *Schlumberger*.

Major oil development contracts will depend on a new law being introduced and contracts being negotiated, which could drag on into 2004-05.

The world is currently in a very tight oil supply situation; while some of the factors contributing to this will ease (such as the Q1 03 Japanese shutdown on its nuclear power capacity and the bitter North American winter), a post-liberation glut of Iraqi oil is unlikely to materialise quickly. Oil prices could yet average \$25-28 in 2003, but substantial newsflow-generated volatility can be expected through 2003-05.

Turkey will be unable not to intervene in the Kurdish region; a military occupation on 'security' grounds cannot be ruled out, but more likely is political pressure that confirms the Kurds will not seek independence but rather settle for autonomy in a government of national unity. The extent that groups like the Kurds and Shiites press for full autonomy in this new dispensation will possibly depend on the extent to which this government succeeds in delivering results.

A failed recovery programme will add to communal pressures and could see increasingly desperate efforts to create a new political dispensation in Iraq. This process could take up to three years to unwind.

GSN is pessimistic about Iraq's northern neighbours. A likely Israeli sideshow during the coming Iraq conflict could seriously destabilise the Levant. The promise of a new Israeli-Palestinian peace initiative must be tempered by the mood of geopolitics in which it is launched. Sharon's hold over Israeli politics has not diminished – and only a US Administration that is genuinely committed to forcing Israel to change its behaviour can effect

change. That seems unlikely coming from Bush, for all that his diplomats led by **Colin Powell**, abetted by a damaged Tony Blair, will pay lip service to brokering the peace demanded by Arab governments.

Pro-Western governments such as **King Abdallah II's** in Jordan and even President **Hosni Mubarak's** in Egypt will be squeezed yet again by popular alienation. These sentiments will affect

GCC populations – with their frustration reflected in everything from student demonstrations to terrorist attempts on Western targets.

For now, the GCC leaderships seem sufficiently robust to weather the storm. But it is highly unlikely that the outcome of the Iraqi war and/or regime change will leave the Middle East a happier place, however much the region, as well as the Iraqi people, will gain from Saddam's demise.

Iraq's 'Day After' Men Face A Long Wait In The Wings

The carpetbaggers are heading south and for companies, international organisations, and governments looking to position themselves with the expected post-*Baathist* Iraqi government the message is becoming increasingly clear – unless current trends reverse, Iraq will be governed by US statesmen and military leaders for 12-18 months. The 'day after' men of the external Iraqi opposition parties look likely to be relegated to 'years-after' men, fated to fill out the ranks of a future Iraqi legislature rather than the near-term executive branch.

The future of post-war Iraq – rather than the likelihood or course of a drive on Baghdad, continued to dominate thinking in Washington at the 11th hour – in a fluid debate influenced by a mixture of day-to-day bureaucratic plays by US government agencies and more contemplative attempts to learn from history, focusing particularly on the lessons learned from the UK's involvement in Iraq throughout the 20th century.

US government agencies have broadly divided over two contending approaches to the transformation of Iraq:

- **IN AND OUT:** The first approach calls for a US military governorship that lasts for months, according to Defence Secretary **Donald Rumsfeld**. This would initiate an extensive de-Baathification and democratisation process, building an interim government around external and internal opposition groups flown into Baghdad. This approach is championed by Rumsfeld's Office of the Secretary of Defense (OSD), its neo-conservative backers in the *American Enterprise Institute* and other think tanks, and **Ahmed Chalabi's Iraqi National Congress (INC)**; the INC would be placed in pole position, including a potential figurehead role for its leader.

- **A LONGER ENGAGEMENT:** Rapidly gaining ascendance has been a second approach, which envisages a longer and closer US engagement in nation-building, involving 12-18 months or longer of US military governorship, a slow transition to democracy, and the intermeshing of technocrats from the Iraqi diasporas and from existing

government ministries. The model, which would see external opposition groups effectively marginalised, is championed by the *State Department (USSD)*, Envoy for Free Iraqis **Zalmay Khalilzad** and the *Central Intelligence Agency (CIA)*.

PENTAGON-VERSUS-STATE

The ongoing debate between both camps was starkly apparent when OSD Under-secretary **Douglas Feith** and his USSD counterpart **Marc Grossman** went toe-to-toe in Senate committee hearings on 11 February. Neo-con totem Feith mapped his vision of a rapid handover of power to Iraqi leaders and a de-Baathification process mirroring the de-Nazification of **Germany**. Grossman outlined the need for "two years" of close engagement and integration of existing leadership figures.

Emerging trend lines suggest that while OSD may get the war it has pushed so hard for, USSD has won the peace.

According to Pentagon insiders, Vice President **Richard Cheney's** expression of doubts over the feasibility of OSD's concept and the specific credibility of **Ahmed Chalabi** – a controversial figure ever since the *Petra Bank* scandal of the 1980s in **Jordan** – have handed the reins to the State Department.

The outlook for a post-Baathist government will conform to the slow transition model, albeit with the potential for modifications injected by Cheney and key Bush advisor **Karl Rove** in the lead-up to the USA's 2004 presidential elections.

TRANSITION TEAM

Where once analysts talked about a transition from US to Iraqi control, the debate is shifting to how control will transition from military governorship to a joint US military and civilian administration, and thence to Iraqi civilian control.

The first mechanisms are now being put in place. In the immediate aftermath of war, US Central Command Commander-in-chief General **Tommy Franks** will maintain overall control of Iraq as expected, but day-to-day security issues will take up most of the Viceroy's time.

Below Franks, the USA has appointed retired

Lieutenant General Jay Gardner and his deputy Retired Lieutenant General Ron Adams to head up the OSD's *Office of Reconstruction and Humanitarian Development* (see box).

The OSD ORHD is due to appoint three US administrators to govern US-delineated Northern, Central, and Southern sectors of Iraq. The Southern sector administrator has not yet been appointed, but the Central Iraq sector will be administered by USSD veteran Barbara Bodine, a tough-minded former ambassador to Yemen.

Bodine spent two tours in the State Department Office of Arabian Affairs and served as USSD Principal Officer in Baghdad. The October 2000 bombing of the *USS Cole* took place on Bodine's watch in Yemen, where she took a firm stance in dealings with the US *Federal Bureau of Investigation* to maintain relations with the Yemeni government.

The Northern sector may be treated as a special case according to Washington-based Gulf experts canvassed by *GSN*.

In Washington recently, *Kurdistan Regional Government (KRG)* Prime Minister Barham Salih told *GSN* that the KRG's highly successful experience of self-administration makes it likely that Washington will employ a light touch in the North, utilising the existing bureaucracy to allow it to focus efforts in the Centre and South.

Patrick Clawson of the *Washington Institute for Near East Policy* concurred, stating that the USA would largely "leave the KRG to it and get back to it later".

This, of course, depends on just how pre-emptive the Turks plan to be during the conflict.

TECHNOCRATS NEEDED

The three administrators are likely to receive lavish financial support and some technical assistance. In the immediate post-conflict phase, the US administrators are likely to directly pay the

The Gardner Minefield

OSD *Office of Reconstruction and Humanitarian Development* chief Lieutenant General Jay Gardner is seen by some US government agencies as a problematic candidate for a role that will involve close interaction with Arab partners. A friend of Rumsfeld, Gardner is closely associated with the *Jewish Institute for National Security Affairs (JINSA)*, a Washington think-tank advocating closer ties between the USA and Israel. In October 2000, Gardner supported an initiative launched by JINSA to forge closer ties between the US and Israel in response to the Palestinian intifada, and signed a letter that praised "Israeli restraint" in that uprising.

Gardner has managerial and investment links to US arms manufacturers and has been heavily involved in Israel's ballistic missile defence programme. His deputy Lieutenant General (Retired) Ron Adams is expected to play a more hands-on role and is qualified by experience in post-war reconstruction and humanitarian assistance as a former commander of the SFOR *NATO* stabilisation force in Bosnia.

Whither Chalabi?

Diehard supporters of Ahmed Chalabi are unlikely to give up their dream of seeing the urbane *Iraqi National Congress* Chairman appointed as leader of an interim leadership council or triumvirate. Chalabi retains the loyalty of powerful allies, including US Defence Secretary Donald Rumsfeld, Deputy Defence Secretary Paul Wolfowitz, State Department Under-secretary John Bolton, Lewis Libby of the Office of the Vice President, and Richard Pearle's *American Enterprise Institute*. Were US commitment to its Iraq engagement to wane – which is quite possible leading into a 2004 election race where the USA's economic problems start to loom large – neo-conservatives maintain some hope that Chalabi could still replace the 'Viceroy', probably General Tommy Franks, after a short period of military governorship.

At the moment, this remains a dim prospect, with an equally powerful range of enemies ranged against the INC leader. Added to scepticism from Vice President Cheney and Special Envoy Zalmay Khalilzad – who believe they know schemers when they see them – Chalabi and his backers remain on the defensive due to intractable opposition from the State Department and CIA. In their most recent attempt to undermine Chalabi, Khalilzad sought to groom *Democratic Centrist Tendency (DCT)* leader and former diplomat Adnan Pachachi as an alternative figurehead, despite the octogenarian's notorious views on the statuses of Kuwait and Israel. Although Pachachi eventually stepped back from an invitation to join the consultative council established in Sulaymaniyah, the attempt – including a personal visit to the UAE by Khalilzad – illustrates the depth of antipathy felt towards Chalabi as well as the USA's search for credible Iraqi allies.

Meanwhile in mid-March, 50 US military-trained exiles left to join US units in the Gulf. They represented the first batch of the supposed 5,000 INC volunteers who are being trained in Hungary.

salaries of up to 2m government employees for one to three months. Certain Iraqi military personnel may immediately be utilised in reconstruction roles, assisting demobilisation and injecting employment and wages into the economy.

Iraq's local government structure is likely to be firmly enmeshed with the new military governorship. As Barham Salih noted after meeting with Vice President Cheney: "Washington does not want the US military blamed for local shortages of water, electricity, and garbage disposal – low-level issues will still be dealt with by the local bureaucracy."

The OSD will draw heavily on USSD technical resources to execute its long-term mission. Senior State Department officials are set for major roles:

- Thomas Warrick – Special Advisor in the USSD Office of Northern Gulf Affairs, formerly a long-term resident at the USSD human rights desk;
- Meghan O'Sullivan – USSD Assistant Director of Operations and Plans, bringing experience on the economic aspects of US foreign policy and ethnic violence; and
- Sherri Kraham – Special Assistant to the Office of the Undersecretary for Arms Control and International Security (USSD hawk John Bolton). Kraham, a Clinton-era USSD Iraq desk officer, was a *bête noire* of the neo-conservative camp for her opposition to the 1998 *Iraq Liberation Act*.

The three US regional administrators are due to be supported by a network of USSD-hired Iraqi technocrats. In part, this community is being hastily assembled from the Iraqi diaspora in the USA (notably the Michigan area), the UK, and Europe (particularly Germany, Sweden and Switzerland).

The State Department aims to hire 30-50 rapporteurs, sending two or three to visit each of Iraq's 17 provinces to survey reconstruction and governance requirements, hiring them on initial three- to five-month contracts. The USSD will also support the sector administrators with products and personnel involved in the *Future of Iraq Project*. The USSD project's working groups cover economics and infrastructure, transitional justice, public health, public finance, media outreach, water, agriculture, and the environment.

As well as creating road maps for US administrators and identifying potentially recyclable officials within Iraq, some members of the working groups are likely to visit Iraq to liaise with local technocrats.

The project is likely to lead to spin-offs in Iraq such as the planned Iraq Development and Reconstruction Council announced at the December meeting of the Economic and Infrastructure Working Group.

... POLITICIANS NEED NOT APPLY

While the USA is desperately searching for technocrats throughout the diaspora, it is attempting to freeze the opposition politicians that it has carefully cultivated over the last decade – some of whom, like Chalabi, have been promoted by neo-con icons like Paul Wolfowitz and Richard Perle (see box).

Instead of flying the opposition into Baghdad as a government-in-exile, the USA government looks likely to deny many of the external opposition figures any political role until long after the stabilisation period, thawing them out to participate in future Iraqi party politics.

The USSD views the external opposition as unelected representatives and is unlikely to grant them even an interim governing role.

The *Kurdish Democratic Party (KDP)* and *Patriotic Union of Kurdistan (PUK)* – by dint of the KRG's elections and the presence of both organisations in Iraq – are viewed as different cases, as is the *Supreme Council for Islamic Revolution in Iraq (SCIRI)*, which at least retains close ties to the Shiite community in Iraq.

Opposition groups excluded from this US planning – notably the INC, *Iraqi National Accord (INA)* and Sharif Ali Bin Al-Hussein's *Constitutional Monarchy Movement* – are in disarray. Failing a change in current trends, which cannot be excluded, their remaining role is to group together in a parallel system that will seek to interact with the slowly coalescing US-backed administration in Baghdad.

At the opposition's recent Sulaymaniyah meeting, a six-member "consultative body" was established to represent the opposition groups, backed by 14 committees that would give input on the work of most of the key government ministries. Considering the time and effort required to make meaningful progress on the USSD Future of Iraq project, these groups may represent too little, too late even though National Security Advisor Condoleezza Rice said on 15 March that this "Iraqi Interim Authority" would assist the US-led administration.

Plans Emerge To Stabilise Iraqi Oil Exports

With the Bush Administration now focusing on preventing a humanitarian or refugee crisis from following the outbreak of hostilities in Iraq, a leaked *US Agency for International Development (USAID)* document, *Vision of Post-Conflict Iraq*, has outlined a number of measures that the USA will take to ensure an apparently seamless transition from the destruction of war to the reconstruction of nation-building.

In this *Vision*, the rehabilitation of Iraq's oil industry will be achieved through a raft of programmes divided into three initial phases.

Phase One: Efforts to limit new damage

A key objective of the US military will be to minimise the infliction of new damage on Iraq's oil infrastructure by either US attacks or Iraqi sabotage.

The USA has integrated the protection of Iraq's oilfields into its concept of operations to avoid itself doing too much damage. The needs for a functioning post-war humanitarian transportation system and the expedient return of Iraqi oil to market make it unlikely that petrol, oil, and lubricants targets such as oil refineries will be extensively targeted.

Cracking (distillation) towers were not considered as targets even in the *Desert Storm* air offensive in 1991, though such targets were struck in the north of Iraq due to faulty transmission of targeting directives.

Refined oil storage may be attacked to immobilise Iraqi armoured and mobile formations, but strikes are likely to be far less extensive than those in 1991 due to the low likelihood that Iraq will be able to mount a prolonged defence or employ manoeuvre warfare.

Associated infrastructure – including road and rail networks and bridges, and port facilities – has also been ring-fenced as ‘dual-use facilities’ that are not to be attacked without special authorisation.

It will be much more difficult to prevent the **Baathist** regime for committing acts of sabotage against oil infrastructure should it choose to do so. But while the regime may attempt to carry out ‘scorched earth’ attacks, these actions may be less successful than the destruction of **Kuwaiti** infrastructure in 1991, due to the likelihood of non-implementation by defecting loyalists or intervention by better-prepared western and opposition forces.

Though stretched by the simultaneous need to suppress Iraqi Scud launches against **Israel**, the USA will act quickly to secure as many oil fields as possible with special and light forces; it also understands how to shut down communications nodes that contain the supervisory control and data acquisition (SCADA) systems that run Iraq’s oil pipelines.

Phase Two: Immediate reconstitution of existing fields

The second phase of US operations will occur under the umbrella of an initial \$600m-900m investment by USAID in immediate stabilisation and repair operations on Iraq’s existing oil fields.

The tendering process for these services will continue to strongly favour large US firms, who can meet the security clearance, reliability, and accounting standards set by USAID.

In co-operation with the **US Army Corps of Engineers, Brown & Root Services** – a subsidiary of **Halliburton** – has been contracted to extinguish oil-field fires as soon as areas are secured. Further invitations to tender were extended to US firms by the Pentagon on 11 March (see box).

Immediate repair needs in the water and sanitation sector will be undertaken by **Contract International**, a Washington-based subsidiary of

US Construction Companies Invited To Tender For US Army Contracts in Iraq, 11 March 2003:

- **J.A. Jones Construction**
- **Washington Group International**
- **Perini Corporation**
- **M.A. Mortensen**
- **Chicago Bridge & Iron Company**
- **The Dick Corporation**
- **Parsons Infrastructure and Technology Group**
- **Fluor Corporation**
- **Parsons Brinckerhoff**
- **Earthtech**
- **Black & Veatch**
- **Bechtel**
- **Contract International**

Egypt’s Orascam, and **Morganti**, the US arm of Athens-based **Consolidated Contractors International Company (CCC)**.

US construction companies are currently securing exact dimensions for Iraqi bridges to ensure that replacement infrastructure can be quickly fabricated in the event of destruction.

After the initial weeks of stabilisation activities, mid-term repairs to existing oilfields will be undertaken under the rubric of an overarching project management programme. **Bechtel Group** is tipped by industry insiders to administer the umbrella contract, as it did in Kuwait in 1991.

The other frontrunner is Halliburton/Brown & Root – closely tied to Vice President **Richard Cheney** – to which **Parsons Corporation** has tied itself. Among other major players, **Louis Berger Group** and **Fluor Corporation** are also bidding as a group; with **Foster Wheeler** they are seen as less likely options for the main contract.

For those looking for big business and Bush Administration links, the **Center for Responsive Politics**, a watchdog group, observes that these companies made official political contributions of a combined \$2.8m between 1999 and 2002, more than two-thirds of which went to the **Republicans**. **Bechtel** was the largest single donor, with \$1.3m.

Key activity would include the installation of new gathering centres, gas-oil separation plants, and pipeline and pumping equipment – largely designed to fit with existing Iraqi specifications for speed of integration.

It remains unclear to what extent non-US companies will be integrated into US plans as sub-contractors. USAID’s tendering process represents an effective bar to open non-national procurement, forcing international firms to consider their options:

UK industry bodies including the **Institute of Civil Engineers** and **Amicus** have expressed concern that despite the closeness of US/UK military integration in the Gulf, UK firms are unlikely to navigate the opaque tendering process put in place by USAID.

Bilateral grant aid by the Department for International Development (DFID) may make up some of this shortfall (see *Backpage*).

EU-based firms like France’s **Technip** and Italy’s **Snamprogetti** will require some European backing. Germany’s **Kreditanstalt für Wiederaufbau (KfW)** is also likely to be heavily involved in the reconstruction effort. KfW does not tie procurement to specific countries, but it is rare to see non-EU companies winning contracts financed by the agency.

France seems sure to provide bilateral grant aid. A further source of European incentives will be provided by the **European Investment Bank**, which again has an open procurement policy.

Japan may stimulate involvement through **The Japan Bank for Overseas Development**.

South Korean firms *Hyundai* and *Samsung* are reported by market analysts to be the strongest non-US and non-European prospects for business in Iraq.

Other firms such as the UAE/US/UK *Petrofac*, India's *Dodsal* and Argentina's *Techint* may struggle without government support.

Existing contracts with Russian and Chinese firms may form the basis of new partnerships with Western firms.

Arab companies, including Petrofac and a number of Saudi construction firms, look set to capitalise on their advantageous geographical positions, pre-Baathist ties, and heavy material production and construction capabilities to slot into US projects as sub-contractors. Saudi firms are particularly likely to be co-opted due to their close ties to the defence-related US firms named in

relation to Iraqi reconstruction, as well as their habitual use of US business practices and principles, and their high incidence of bilingual Arab-English operators.

Phase Three: Structural reform

Before new oilfields can be developed, the Iraqi oil sector will have to undergo extensive structural reform. This process will not begin meaningfully in the first nine to 12 months after a conflict ceases.

A new constitution and legislature will probably be required before any substantial agreement on Iraq's future oil revenues – enshrined in a new hydrocarbon law – can be enacted. Numerous legal issues concerning Baathist-era contracts need to be resolved with reference to the new law.

Experts canvassed by GSN at sources as diverse as *ChevronTexaco*, *JP Morgan* and *Cambridge Energy Research Associates* suggested that Iraq will be a far tougher negotiator than many analysts suspect. Times have changed since *BP* and *Royal Dutch/Shell* last held a majority share in the then Iraqi Petroleum Company in 1972 – the battle of *Iraqi National Oil Company (INOC)* and its assets could be longer and harder than many within the Beltway expect.

With a raft of legal, production and marketing issues to deal with, the USA may be hard-pressed to dramatically raise Iraqi oil revenues in the short-term, however skilled its majors and drillers are at exploiting opportunities.

This will provide little comfort to Iraq's exchequer or to a Bush Administration already eyeing the beginning of a new US presidential campaign in late 2003, and counting on Iraqi oil to help it keep the price of oil low and show improvements to the US economy.

International Concern

The Bush Administration's decision to pre-select five such well-connected US companies as prime candidates for post-war reconstruction and oil sector contracts gives these chosen few an unparalleled chance to establish an early foothold in Iraq. Paradoxically, it has also increased the international community's determination to insist on the need for full UN authority over reconstruction.

International agencies canvassed by GSN – all of whom preferred to speak off the record – noted the flagrant contrast between the pre-selection of the favoured US-only five and the normal transparent and internationally neutral procurement procedures that they themselves apply.

The governments of the UK, Spain and Italy, which have taken a big political risk in backing Bush's plans for military intervention, cannot take kindly to seeing their own highly capable contractors and oil companies so blithely sidelined by the US contracts hand-out.

The US Team: Three To Watch

JOHN ABIZAID: MILITARY FRONT MAN

Lieutenant General John Abizaid, formerly director of the Joint Staff at the Pentagon, will assist Centcom Commander General **Tommy Franks** as his front-man in dealings with Arab and Kurdish community leaders. Abizaid is of Lebanese-American descent, a fluent Arabic speaker, with a masters degree in Middle Eastern studies from *Harvard University*. His professional experience includes service with the *United Nations* Truce Observer Unit in southern **Lebanon** in the mid-1980s, service as a liaison to the **Iraqi** military in the late 1980s, and a posting at **Jordan University** as an Arab affairs researcher, during which time he made frequent visits to Iraq before the 1991 Gulf War.

Abizaid is familiar with northern Iraq, where he commanded a battalion during the establishment of safe havens in 1991. In time, Abizaid's role is likely to change from diplomatic troubleshooting to reforming the Iraqi military. Although US military officers call him the "Mad Arab", he is more appropriately compared to **John "Pasha" Glubb**, British founder of the *Jordanian Arab Legion*.

LIZ CHENEY: STATE DEPARTMENT PLAYER

Liz Cheney, daughter of US Vice President **Dick Cheney**, looks set to play an important role in the **Iraqi** structural reform process. Embedded within the US State Department's Near East Bureau, Cheney is regarded by some as the most senior **USSD** official on the economic aspects of foreign relations in the Middle East. Cheney has a background in international project finance, primarily in the Middle East. From 1989 to 1993, she served at the Department of State and at *USAID*. Following a period in the private sector, she was brought back by Secretary of State **Colin Powell** in March 2000. Responsible for inter-agency co-operation on Iraqi energy issues, Cheney is considered to be an effective communicator and energetic contact-builder in the Middle East community, bringing "constructive ideas about cultural relationships as well as commercial," according to one official at **Saudi American Bank**. He noted: "If the reconstruction goes poorly, she will be among those who feel the pressure."

ZALMAY KHALILZAD: MORE THAN ACADEMIC

The Afghan-American academic's star has been in the ascendant, leading President **George W Bush's** efforts in **Afghanistan** and now Iraq (for profile, see *GSN 703/8*). His apparent willingness recently to counter some hawkish Pentagon thinking may reflect a politician growing in confidence.

Pre-war Saudi Arabia Puts Reforms In Reserve

War in Iraq will add to pressures on Saudi Arabia, which for all its careful positioning finds itself in the front line with US forces now authorised to use Prince Sultan Air Base near Riyadh and Special Forces operating along the Iraqi border. In this tense situation, Saudis are asking whether the new Iraq crisis will act as a spur for reforms in the Kingdom?

Several thousand US troops have been moved close to the Iraqi border, Arar and Tabuk airports have closed, officially to cope with any consequences from the attack on Iraq. Senior Al-Saud princes and the ulema (religious establishment) have warned zealots not to react.

The Saudi government has linked the deployments of recent weeks to the policing of the Iraqi no-fly zones and to fears that up to 100,000 refugees could be displaced in the expected war. The US deployment would thus be a humanitarian gesture – although it also involves US Special Forces units, as the Saudi authorities know only too well.

With troops building up, the Saudi government has again been squeezed between popular anti-American sentiment and the Al-Sauds' alliance with the USA. The US/Saudi relationship has improved in recent weeks with apparent Saudi agreement to provide quiet support for Saddam Hussein's removal, while Washington has accepted that senior Saudis will publicly argue that it is "unacceptable to go into another country by force to fix its situation", as Interior Minister Prince Nayef Bin Abdelaziz put it.

Underlining the tensions, the Interior Ministry on 18 March announced that a man was accidentally killed in Riyadh while apparently making a bomb. The explosion came after a period when (apart from a widely reported bomb scare in a Jeddah shopping mall) things had been quiet following a tightening of security (GSN 705/7).

The impending war will focus most attention in coming weeks, but many Saudis also expect domestic policy and economic reform initiatives to move ahead.

According to Saudi analyst Nawaf Obaid, economic, educational and human rights reforms will be announced by early June, when the four-yearly government reshuffle should be unveiled, promoting younger, more reform-oriented and Western-educated technocrats.

While much attention has focused on the oil industry and Oil Minister Ali Al-Naimi's expected departure, Obaid gives prominence to expected changes in the Commerce Ministry (notably responsible for *World Trade Organisation* accession), the creation of an Information Technology Ministry, and the dismantling of the Post and Telegraphs Ministry, which will give *Saudi Telecom* a bigger role.

Obaid argues that the royal family and ulema have reached consensus on education reform – in the face of opposition from religious hardliners, including some members of the royal family. There will be an evolution in human rights policy, underlined by the February visit of *Human Rights Watch*, and an opening of key economic sectors to Saudi women.

Such shifts are not certain, however, for all that

political reform proposals generated huge interest at the beginning of the year, when they gained the apparent endorsement of Crown Prince Abdallah Bin Abdelaziz ('CPA'), prime mover in the Kingdom at present, for all his nearly 80 years' age.

Recent weeks have produced a spate of media interviews accorded by signatories of the late January petition that called for elections to the Majlis Al-Shura (Consultative Council) and a more constitutional and transparent national structure. They have optimistically recounted CPA's indications of support for ideas outlined in the petition.

Not all of reform's natural allies are comfortable with this. Some liberals oppose any precipitate rush to elections, fearing these would hand a sweeping victory to conservative Islamists.

Meanwhile, exiled opponents remain deeply sceptical of suggestions that CPA will be able to deliver on (or even countenance) major changes. They regard reformist talk as a public relations exercise to placate a US government that has piled pressure on the Al-Sauds to move towards a more modern political regime that can survive into the long term.

CPA has adopted a cautious approach in recent weeks, and especially since the meeting of Arab leaders in Sharm El Sheikh, Egypt, where he chose not to push forward his pre-summit paper. This had called on Arab governments to admit to their shortcomings and recognise the huge problems and frustrations facing their societies; it looked towards a more participatory form of government (GSN 703/3).

CPA is keeping these ideas "on the table", but for now he appears to be waiting to see how the Iraq crisis plays out. His veteran adviser Abdelaziz Al-Tuwaijri – whose son Khalid is increasingly influential at court – is said to be extremely wary of liberalisation. CPA has a wide circle of nominal "advisers", drawn from across the political and religious spectrum; but only a few voices, such as Tuwaijri's, really count.

The reform petition attracted the signatures of 104 liberal and Islamist intellectuals, including academics, business figures, technocrats and – notably – Sunni and Shia religious figures. Within fundamental Saudi religious principles, it pressed for the holding of local and national elections, freedom of assembly and expression, an independent judiciary and an end to corruption. It also called for the granting of full rights to women, although it failed to specify any clear demand for women's full political rights.

Some critics say the petitioners initially met with a cold shoulder from the Crown Prince's office. They claim that it was only after they threatened to go public in the international media that CPA suddenly invited them to a meeting, on 22 January. It was at this meeting that he said the Saudi leadership had been contemplating reform for some time and that change was "a question of time".

One of those present, Abdelaziz Al-Dakheel, said that further meetings with CPA and officials were expected.

But CPA seems to have held back from committing to any specific measures. Reformers have sounded him out about his possible support for a request to the Education Minister to hold elections for senior university posts, such as faculty deans – but these are said to have received an oblique response. Nor, reportedly, would CPA be drawn on prospects for the release of academic and cleric **Sheikh Said Al-Zuair**, who has been held without charge for eight years (see below).

AL-SAUD DIVISIONS

Even if Crown Prince Abdallah does favour change, some other powerful members of the royal family are reluctant to see the status quo eroded. The Kingdom has yet to see a generalised Al-Saud acceptance of the need for moves towards a more established culture of rights, constitutional law and accountability.

In early February, Prince Nayef gave an interview to the *Okaz* newspaper stating that CPA's readiness to meet the petitioners in no way indicated the government's willingness to accede to their proposals.

This was a reminder of the extent to which Saudi Arabia is governed by competing and overlapping power centres within the royal family, with their own favoured channels for conveying their views. CPA's views tend to surface through *Al-Watan*, owned by **Prince Khalid Al-Faisal** – who is also close to the Crown Prince's half brother and rival, Deputy Prime Minister, Defence and Aviation Minister **Prince Sultan Bin Abdelaziz**. Prince Sultan's full brother Riyadh Governor **Prince Salman** has good contacts with *Al-Sharq Al-Awsat*. Sultan's son, Deputy Defence Minister **Prince Khalid Bin Sultan** owns *Al-Hayat*. Prince Nayef tends to communicate through the columns of *Okaz* and *Al-Riyadh*.

CPA is often described in Western media as “*de facto* ruler” and has held executive powers since **King Fahd's** infirmity. However, other leading princes appear to retain an effective block on change. Nayef, in particular, is a powerful influence: as Interior Minister he controls security; all provincial governors – although, in reality, perhaps not Prince Salman – are answerable to him (*GSN 703/7*).

...REFLECTED IN THE ZUAIR AFFAIR

Prince Nayef's strength is demonstrated by the continued imprisonment of Sheikh Said Al-Zuair, an academic and preacher from the southern Najd's Wadi Diwasir region, who was detained in the 1994 crackdown on Islamists, alongside well-known preachers such as **Salman Al-Awda** and **Safr Al-Hawali**.

The Interior Minister refuses to contemplate Zuair's release, even though the 1994 arrests were rather haphazard. Zuair shared many of the same critical Islamist views as Awda and Hawali, but he had not publicised these through sermons or writings, and has never been formally charged. Zuair refuses to apologise and promise future silence – thereby paying the authorities' apparent price for his release.

CPA has tried to secure agreement on a low-key release, with no apology sought, provided the Zuair family does not make a public fuss. But Prince Nayef continues to insist Zuair must eat humble pie, seeing it as a matter of the government's and his personal authority. “If he signs now he will be released within an hour,” Prince Nayef told a **Kuwaiti** newspaper.

The affair is turning into a symbolic confrontation. Two years ago Zuair insisted that he should be brought before a judge who would rule on whether he should

ever have been detained. Opposition sources claim he is refusing government attempts to accord him special treatment in prison, is refusing family visits, has turned down the offer of a free international mobile phone, and is paying for his food to be brought into Hayer jail from outside, rather than accept state “hospitality”.

Prince Nayef is also holding out against exiled dissidents, such as **Saad Al-Fagih** of the *Movement for Islamic Reform*, that other royal family members might seek to co-opt. Nayef used an *Okaz* interview earlier this year to offer the exiles a “pardon”, but only in return for abstaining from political activity.

The London-based Fagih told *GSN* he was not willing to accept an amnesty on these terms. He would be prepared to turn down the volume of his campaign, as a first step, if the authorities allowed genuine freedom of expression. But Fagih says a return home would only be on the cards once the Kingdom had a demonstrated track record of allowing free political activity – not an outcome for which he holds out much hope under the present government.

MUFTI APPOINTMENT

The Al-Sauds are working to maintain control over the ulema and potentially dissident religious authorities. In early March, CPA, acting in the name of King Fahd, extended Grand Mufti **Abdelaziz Al-Sheikh's** mandate for another four years.

This move that underlined the ruling family's control over the ulema and its historic alliance with the Al-Sheikhs, the family descended from the Wahhabi movement's founder **Mohammed Abdelwahab** who have led the Saudi ulema for decades – providing their Al-Saud allies with ruling legitimacy in the process.

Saudi Opponents Claim Upturn In Jihadi Recruiting

Interior Minister **Prince Nayef Bin Abdelaziz** denies there are *Al-Qaeda* sleeper cells in the Kingdom, but resentment over the government's alliance with the USA is fuelling support for militant jihadi Islamism, especially among disaffected youths. Estimates vary of the extent of active support for violent radicalism – for whom **Osama Bin Laden** is totemic figurehead – but even moderate Islamist groups and Western analysts believe support for hardliners is rising rapidly.

There are reports of discontent among Saudi officers in the Peninsula Shield units assigned to protect **Kuwait**. At least four Saudi officers have been publicly reported as refusing to serve in the force – whose role they regard as tantamount to facilitating US/UK moves against **Iraq**.

Some observers believe the number of refuseniks may be much higher. Many Imams have issued fatwas condemning the Kuwait deployment as anti-Islamic.

The rumour mill even claims that some Saudi units of the Shield force, stationed near US troops, have been deprived of live ammunition, to guard against possible attacks on the Western troops.

Questions about this to official Saudi channels had not received replies as *GSN* went to press.

Saudi Arabia faces many problems. Unemployment is now generally estimated at around 30% – although the government has denied this is the official figure – and crime is on the up, even in rural areas. There were reports in late February of trouble in Taif over unemployment. Resentment at corruption and the royal family's ostentatious wealth is increasingly widespread.

But it is the Al-Sauds' close alliance with the USA that appears to be the main factor behind the upsurge in support for a militant, sometimes violent interpretation of the religious concept of *jihad* (struggle).

The arrival of US forces at Arar airport near the Iraqi border and at Tabuk, and the consequent transfer of local civilian flights to Sakakah, 150km further south, has fuelled speculation, despite denials by Foreign Minister **Prince Saud Al-Faisal** and other officials.

Western security sources point out that US forces have entirely official arrangements to patrol the no-fly zones over Iraq. But such clarifications have not been enough to allay opposition claims.

The extent of tacit support for jihadi ideas is impossible to ascertain. Most observers accept there is a widespread degree of sympathy for Bin Laden. Some radical opposition sources claim that as many as 80-90% of Saudis support the loose concept of militant action – although this view is dismissed by mainstream Islamists, who put the figure much lower, at perhaps 30-40%.

The proportion of sympathisers who seek to join a militant group is much smaller, but it could be significant. Besides Al-Qaeda members and other returned Arab “Afghans”, there appears to be growing activist involvement by young Saudis who have never had anything to do with Afghanistan and the *Taliban*. One opposition leader said those seeking to find weapons and undergo paramilitary training could now number well into the thousands.

These hard line groups appear to be attracting support even in quiet provincial areas – such as the southern Red Sea town of Jizan, villages around Medina, and Wadi Diwasir, around Sulayil in southern Najd, on the fringe of the Rub Al-Khali (Empty Quarter).

Jihadi support is drawn from across the Kingdom, but is believed to be strongest in the far north, the south-west and conservative parts of Najd, such as Qassim. Varying influences come into play in different areas.

Northern areas such as Al-Jawf and Tabuk have tended to be more independent-minded. Riyadh's writ runs more lightly here, while local tribal influences are strong. But there is also considerable contact with nearby **Jordan**, and thus with radical movements that have support among the **Palestinians**, such as *Hamas* and *Hisb-Ut-Tahrir*. This connection helps to explain Jordanian security crackdowns in recent months.

In mid-February, Al-Jawf Vice-governor **Hamad Bin Abdelrahman Al-Wardi** was shot dead as he was driving to his office in Sakakah (*GSN 704/7*). According to one version, Wardi angered local conservatives by arranging a meeting between some women and Governor **Prince Abdililah Bin Abdelaziz**. The Prince – a son of **Ibn Saud**, full brother of *Saudi National Guard* Deputy Commander **Prince Badr Bin Abdelaziz** and long-time ally of Crown Prince Abdallah – subsequently resigned.

In September, Islamic court president **Sheikh Abderrahman Al-Sahibani** was assassinated in Sakakah after he had sentenced a returning “Afghan” to several years' imprisonment.

Mountainous Asir in the south-west has proved a fertile recruiting ground for the radicals, because of its openness to outside cultural traditions and political ideas, through Red Sea trade. Many Afghans came from this region, which is near to **Yemen**.

In Qassim support for the jihadis has also been rising. But this conservative north-central province of Najd, home to influential preachers such as **Sheikh Salman**

Al-Awda, has not been at the forefront of the movement.

This is partly because the area's influential Wahhabi clerics were strong supporters of the Al-Saud monarchy, and their conservatism was particularly focused on social religious issues, such as strict dress codes for women. Meanwhile, local businesses were engaged in trade with Iraq and keen to preserve stability.

In the main urban centres of Eastern Province and Hejaz, the upsurge in support for militants has been less obvious, although a significant number of “Afghans” came from Eastern Province. The east's Shia populations showed no interest in joining the jihad in Afghanistan, which was perceived as essentially a Sunni affair.

But opposition sources claim that jihadi support has been rising among working class Sunni in Eastern Province, many of whom are descended from Najdi migrants attracted by the oil industry (which for many years tended not to recruit Shia in large numbers) and who were attracted by the Afghan jihad.

The major cities of Hejaz provide a substantial base of Al-Saud support, which is seen as the best protection for the political stability so necessary for business and for pilgrimage traffic. But the region has produced some leading radicals; a number of those particularly active in Chechnya came from the Medina area.

SHIFTS IN WAHABI HEARTLANDS

Over the past decade patterns have evolved, even in heartland Wahhabi areas such as Qassim. Traditionally, Muslim radical groups such as Hizb-Ut-Tahrir did not attract much support from the Wahhabi clergy, many of whom espoused the conservative Salafi philosophy. For figures such as Al-Awda, Safr Al-Hawali and **Nasser Al-Umar**, associated with the *Soruri Al-Ikhwan* (Muslim Brotherhood) faction, the creation of political movements and parties was seen as a divisive threat to the unity of the wider Umma (Muslim community).

Gradually, a more politicised language has appeared. **Sheikh Suleiman Al-Ilwan** from Buraydah has issued fatwas condemning sanctions against Iraq as un-Islamic. **Sheikh Humud Al-Ukhla Al-Shuaibi** – a Buraydah scholar who died a few months ago – even issued a fatwa setting out a justification for the 11 September 2001 attacks. In 1995 he was detained for stating that political vigils and demonstrations were legitimate.

This evolution is creating a climate in which potential jihadi recruits come to feel legitimised in moving towards active opposition to the Al-Saud regime, even if that has not been openly endorsed by clerics.

Osama Bin Laden – now referred to by some Saudi jihadis as Imam (leader) – appeared to break new ground in the statement attributed to him a few weeks ago, in stating that the Al-Saud regime was not Islamic and had to be converted or replaced.

Afghan Front Reopens On War's Eve

Some 1,000 US troops launched operations in eastern Afghanistan on 20 March in a hunt for *Al-Qaeda* members, a US Central Command spokesman said in **Qatar**. The US Army's 82 Airborne Division flew from Kandahar to areas around Jalalabad and Mazar-e-Sharif. *Operation Valiant Strike* is planned as the biggest by US forces in eastern Afghanistan since an eight-day battle against *Taliban* and Al-Qaeda fighters over a year ago.

US invasion commander for Iraq General **Tommy Franks**, now based in Doha, is also responsible for operations in Afghanistan.

UAE: Ahead Of Autumn Meetings, IMF Delivers Data Lesson

A generally favourable macro-economic performance was undermined by a marked deterioration in the fiscal position since 2001, according to the first-ever Article IV assessment on the UAE to be published by the International Monetary Fund.

In this public assessment posed in mid-March, the Fund prescribed a potentially painful tightening of the public finances in the wake of this deterioration, involving cuts in current expenditure, with priority given to the phasing out of water, electricity and agricultural subsidies. It said that restoring fiscal discipline – particularly at the Emirate level – remained a critical element to secure and broaden economic progress.

The Fund's strongest language was reserved for the quality of its statistics. It cited "numerous shortcomings in the UAE economic data", which reflected "inadequate compilation techniques, shortage of trained staff, insufficient resources assigned to data-gathering and information flow among Federal and Emirate government departments, and public sector entities. As a result, provision of data to the Fund between missions, except for monetary and fragmentary trade statistics, remains poor."

In Fund-speak, this is a damning charge sheet for the Emirates authorities, particularly in a year when Dubai is due to host the IMF/World Bank Annual Meetings – the official opening to the global financial year.

The two events are hardly coincidental. IMF directors are applying greater pressure on the UAE authorities to revamp their data collection and dissemination processes – the perennial UAE economists' bugbear, which has consistently stymied effective scrutiny of the country's accounts.

A Fund spokesman acknowledged to GSN that the looming IMF meetings in Dubai were relevant to the publishing of the assessment, but said it was consistent with a general trend towards greater transparency in the region, which saw the publication of Saudi

Arabia's first Article IV assessment last year. "It clearly didn't hurt that they are hosting meetings this year, but it is more reflective of a wider trend to transparency," he said.

Like other Gulf states, the UAE remains deeply wary about opening up the books to prying foreign eyes. According to the Fund, available data was provided by the authorities on a "confidential basis".

ERRATIC DATA FLOW

The UAE's reporting of data has long been erratic. The *Central Bank of the UAE* and the Planning Ministry rarely sing from the same sheet of statistics. For 2001, the Central Bank estimated a 1.3% rise in GDP to Dh217bn and the Ministry a 4.2% contraction to Dh248bn.

The IMF estimates current GDP at Dh256.6bn for 2001 and Dh262.2bn for 2002, with real GDP growth in 2001 at about 4%, as a number of projects were launched in construction, electricity and water and downstream oil sectors. A continued rapid increase in current spending in the face of declining oil revenue led to a sharp deterioration in the fiscal accounts.

The 2002 macro performance was mixed. Although average crude prices rose by 4% to \$24.7/bbl, oil output is likely to have declined by about 9% in line with OPEC cuts.

It said these cuts contributed to a fall in real GDP growth, even though non-hydrocarbon growth remained robust on account of ongoing construction projects and rising petrochemical output. Lower crude oil receipts, together with rising imports and lower investment income, contributed to reducing the current account surplus.

Amid declining revenue, government spending is expected to have remained broadly unchanged, leading to the sharp deterioration in the fiscal counts. The estimated consolidated fiscal balance registered a deficit of 9% of GDP.

BATTLING MONEY LAUNDERING

On the positive side of the balance sheet, the IMF commended the institution of a comprehensive regime to combat money laundering and terrorist financing that also

covered informal fund transfers.

The IMF also welcomed ongoing efforts to foster the non-oil sector, encouraging the authorities to adopt a common strategy for foreign ownership across the Emirates.

It noted that the UAE's "open border" foreign labour policy has enabled employment growth to contribute significantly to non-hydrocarbon sector growth and diversification. The banking system remains strong, highly profitable, well supervised and capitalised, it said in a significant show of support. Many international bankers believe the UAE is over-banked.

But the abiding message left by the debut Article IV assessment is for the authorities to make stronger efforts to improve the quality, coverage and timeliness of official data to support policy-making in an increasingly complex economy.

"Obviously the more statistics they publish the better," said the Washington-based official. "It's not the only thing we focus on, but in any country with a track record of opaqueness, we urge them to be more transparent in their data as it's the most basic barometer of economic policy. It tells you what's happening."

See page 14 for IMF data and forecasts on the UAE.

BAHRAIN: Big Guns Pull Out Of Offshore

Bahrain's offshore banking sector is reeling from the withdrawal of billions in assets from leading US and European institutions, prompted by the onset of war jitters late in 2002. *Bahrain Monetary Agency (BMA)* reported a 33% decline in offshore banking unit (OBU) assets in Q4 02. A BMA statement said *Citibank* had moved assets in Bahraini OBUs, due to fears of a US-led war in Iraq.

BMA figures show the slump in OBU assets began in October when they dropped by more than \$30bn. Total assets at Bahrain OBUs were \$89.16bn in September 2002, falling to \$57.08bn in October. The end-2002 figure was \$58.8bn.

According to the BMA, the

“measures taken by Citibank are in no way a reflection on Bahrain”. It had been assured by Citibank that “there would be a return to the status quo as soon as the war situation is resolved.” Sources suggested that Citibank pulled out around \$10bn. According to BMA, the bank moved its assets to another location outside the region.

But even if the Iraq conflict goes according to the US’ plans, analysts doubt whether all the assets will return. “Some will come back, but not everything,” said *CI Ratings’* Gulf bank analyst **Darren Stubing**.

Foreign banks’ decision to reduce their exposure has impacted on Bahrain’s embattled investment banks. Institutions like *Bahrain International Bank*, *BMB Investment Bank* and *Investcorp* have been through a difficult two years and the scaling back of credit lines will hardly boost their performance. “They’re still holding on but it’s touch and go,” said Stubing.

Bahrain-based *Arab Banking Corporation* has just posted a \$51m net loss in 2002, against profits of \$102m in 2001.

CITIBANK SPECULATION

Citibank’s pullback in Bahrain has set tongues wagging about its commitment to its stake in *Saudi American Bank (Samba)*.

Aside from political issues surrounding US-Saudi relations, the shareholding in Samba restricts both banks’ ability to move into other GCC markets.

Citibank’s stake has been steadily declining in the past five years, and speculation about a possible divorce will only increase as a result of its removal of assets from Bahrain.

UAE: Medium-Term Baseline Scenario, 2000-07

	2000	2001 ^p	2002 ^e	2003 ^f	2004 ^f	2005 ^f	2006 ^f	2007 ^f
Crude oil production (m barrels/d) ¹	2.41	2.44	2.21	2.21	2.21	2.33	2.33	2.33
of which: condensates	0.22	0.32	0.32	0.32	0.32	0.44	0.44	0.44
Average UAE oil export price (\$/barrel) ²	27.21	23.78	24.70	24.50	22.00	21.50	20.50	20.50
Nominal GDP (Dh bn)	259.0	256.6	262.2	275.2	281.0	297.0	307.8	322.7
Real GDP at factor cost (% change)	10.0	3.8	1.5	4.0	4.0	5.1	3.6	3.7
of which: crude oil and natural gas ³	11.1	1.2	-9.4	0.0	0.0	5.4	0.0	0.0
Consumer prices (% change)	1.4	2.2	2.8	2.9	2.1	2.1	2.1	2.1
National accounts (as % of GDP)								
National savings	49.1	40.0	32.4	35.6	36.5	35.9	33.7	32.5
of which: government	11.1	2.0	-3.8	-2.7	-2.3	-1.7	-2.2	-2.4
non-government	38.0	38.0	36.2	38.4	38.8	37.6	35.9	34.9
Gross domestic investment	23.2	24.4	26.6	26.8	28.3	28.0	28.0	27.7
of which: government	4.3	5.2	4.7	4.7	4.9	4.8	4.8	4.8
non-government	18.9	19.2	22.0	22.1	23.4	23.2	23.2	22.9
Consolidated fiscal accounts (Dh bn)								
Revenue	100.0	82.5	71.5	75.5	76.7	78.1	76.5	75.8
of which: hydrocarbons	56.6	48.5	45.0	45.3	40.7	40.7	38.8	38.9
non-hydrocarbons	44.0	34.0	26.5	30.2	35.9	37.4	37.7	37.0
investment income ⁵	25.5	15.6	7.1	10.1	15.4	16.4	15.4	14.3
Expenditure	84.3	96.1	94.8	97.1	97.9	98.6	99.4	100.3
of which: current	71.2	77.4	81.5	83.0	83.1	83.2	83.4	83.7
development	11.2	13.3	12.2	12.9	13.7	14.3	14.8	15.4
Overall balance	15.6	-13.6	-23.3	-21.5	-21.3	-20.5	-22.9	-24.4
as % of GDP	6.0	-5.3	-8.9	-7.8	-7.6	-6.9	-7.4	-7.6
External accounts (\$ bn except otherwise stated)								
Exports	49.6	48.2	47.9	50.3	49.9	51.9	53.2	55.6
of which: crude oil and products	23.4	19.9	18.9	19.4	17.5	17.8	17.0	17.0
Imports, fob	-30.8	-32.8	-35.0	-36.8	-38.9	-41.0	-43.2	-45.7
Services (net)	-6.2	-6.4	-6.4	-5.5	-5.8	-6.1	-6.5	-6.4
Investment income (net) ⁴	9.6	6.1	2.9	4.4	7.3	8.2	8.2	8.2
Transfers (net)	-4.0	-4.6	-5.3	-5.8	-6.2	-6.6	-7.0	-7.5
Current account balance	18.3	10.4	4.1	6.6	6.3	6.4	4.7	4.2
as % of GDP	25.9	14.9	5.8	8.8	8.3	7.9	5.6	4.8
Central bank reserves	13.8	14.3	14.3	15.0	15.6	16.2	16.7	17.1
in months of imports	5.1	4.9	4.7	4.6	4.6	4.5	4.4	4.4
External debt ⁶	18.2	14.1	14.2	14.6	14.9	15.1	15.4	15.7

^p Preliminary. ^e Estimate. ^f Forecast. ¹ Includes condensates, which are not subject to the OPEC quota. ² Based on World Economic Outlook oil price projections. ³ Crude oil output includes condensates. The increase in 2005 reflects the completion of ongoing condensate projects. ⁴ Based on WEO global short-term interest rate projections. ⁵ Includes liabilities of resident banks.

Sources: UAE authorities; IMF staff estimates and projections.

Post-War Iraq: Thoughts Turn To Inflation And Exchange Rates

CONTROLLING INFLATION and raising the external value of the dinar will be the top priorities for the new economic policy-making regime in Baghdad, according to Iraqi economic experts. But there is all to play for – and reports that an incoming **US** administration might opt for a dollar economy cannot be discounted. Such reports add to the fears of conspiracy theorists, who see Washington's determination to ensure the dollar's primacy over the strengthening Euro – in which currency Iraq has traded its oil since 2000 to some profit – as one factor behind the coming conflict.

Obtaining hard economic data about Iraq is as difficult as finding evidence to back most conspiracy theories. Iraq's last **International Monetary Fund** Article IV consultation was back in 1980. Since then, hard fact about the economy has been hard to come by, but broad-brush analysis suggests its most urgent requirement is for a huge injection of foreign currency.

The focus on inflation, estimated at around 60% in the pre-military action period, is considered fundamental to implementing macro and development policies effectively. But it will need the full panoply of resources to be delivered quickly if inflation is going to be contained. Consultant to the **United Nations Conference on Trade and Development (UNCTAD)** **Sinan Al-Shabibi**, a former economist in the Planning Ministry in Baghdad, told *GSN* that Iraq will need emergency assistance – through what is available in the Oil-for-Food Programme (OFP) and external aid – plus early signals that the economy will not be burdened by onerous debt and reparation obligations. "If they do these things, inflation is going to be fought," he predicted.

Shabibi outlined a blueprint for the recovery of the Iraq economy in a paper delivered at the **Centre for Global Energy Studies (CGES)** in London on 14 March. He said Iraqi inflation was closely linked to the dollar's value. Once external assistance is forthcoming, the situation should improve. "These inflows will support the value of the dinar, and once it is supported inflation will be reduced." Inflation has also been stoked by the **Central Bank's** excessive money printing, under orders from a regime that showed little interest in fiscal or monetary prudence.

Iraq has suffered in the past decade from a split exchange rate: the so-called "Swiss dinar" in use in the autonomous **Kurdish Regional Government (KRG)** and the "**Saddam** dinar" in the rest of the country.

The former is regarded as the "real" exchange rate, worth around \$1=ID8-10. On 18 March, the Saddam dinar fell sharply, trading at exchange bureaux across Baghdad at \$1=ID3,050, from ID2,800 the previous day, when a UN-based solution still seemed possible.

Shabibi's recipe for economic stability involves the mobilisation of substantial volumes of domestic and international financial resources. At the global and regional level, this would require releasing Iraqi assets, a standstill on the payment of debt and reparations, releasing the unspent balance in the OFP escrow account held by **BNP Paribas** in New York, allowing Iraq to approach maximum oil export capacity and substantial financial assistance from external sources. On the domestic front, the authorities should refrain from printing money and limit unproductive spending. The accumulated resources should be used immediately to pay for imports, especially food and consumer goods, social services and a new programme of human development.

Once a semblance of stability is restored, domestic efforts and macroeconomic policies would become more important than access to financial resources. During this period, co-operation on oil prices and the renegotiation of obligations should be worked out.

DOLLARISATION, OFP PROSPECTS

Speculation that Iraq will move to adopt the dollar as its official currency was downplayed. "There's a lot of problems with dollarisation. Once you embark on it there's a risk you won't return to your currency in the end," Shabibi said. But the dollar will be widely used informally, as it was in civil war **Lebanon** for a while."

Iraqi exchange rate policy has historically been determined by the oil sector surplus. However, an oil-dominated, over-valued exchange rate would be detrimental to the non-oil economy's prospects. A realistic exchange rate for the non-oil tradable sector would improve competitiveness. Rate changes will not affect oil exports since these are dollar-denominated, Shabibi argued (apparently overlooking Saddam's Euro shift). As a result, the government's import capacity will not be affected by changes in exchange rate policy. "The government should use its oil revenues to mitigate the harmful effects of a more realistic exchange rate on the import capacity of the private sector."

The unspent balance in the escrow account will be a priority for the authorities in the

initial "international" phase of Iraq's reconstruction. According to **CGES** Executive Director **Fadhil Chalabi**, a former director of oil affairs in Iraq, the OFP is likely to continue in its present guise for the foreseeable future.

Shabibi said fiscal policy should be geared towards diversifying the structure of government finance, through the creation of an efficient tax system and a rationalisation of expenditure. The latter will be eased by a reduction in military expenditure. Reducing the budget deficit will give greater latitude for monetary policy to aid the development process.

The state's monumental debt burden will limit its ability to play a leading role in the development process, offering scope for the private sector to become an engine of growth. Iraq is no stranger to privatisation, although state sell-offs in the 1980s were designed to raise cash in the war against Iran rather than through a conversion to neo-Thatcherite economic orthodoxy. Many state enterprises were sold at book value to the government-linked private sector, reflecting the widespread cronyism of the Saddam years.

In the productive non-oil economy, agriculture is regarded as a prime candidate for development as it will provide a useful source of foreign exchange. Light industry will also be a priority.

In the long-term, the fostering of a transparent legal code will boost prospects of attracting foreign direct investment (FDI). Another key source of investment that has often been overlooked is the significant numbers of Iraqis resident overseas. Post-war Lebanon's reconstruction was dependent to a substantial degree on Lebanese exiles ploughing cash into real estate and the service economy. There may be no **Rafiq Hariri**-style billionaire waiting in the wings to take over Iraq Inc, but the repatriation of a proportion of Iraqi capital could prove a useful source of investment.

Syria Squeezed On Crude Liftings After Record Month

Syria, which has been taking around 200,000 b/d of **Iraqi** crude, has told its term customers that liftings could be reduced – and even halted – with war in the region. Iraq is expected to halt exports through the Kirkuk-Banias pipeline in the event of war, making it impossible for Syria to maintain exports at the recent 377,000 (February)-450,000 (March) b/d level. Syrian output is around 550,000 b/d and consumption around 300,000 b/d.

GSN Risk Grade – C/2: New Gulf storm to be weathered, domestic problems remain

Political And Social Development

Overview: Kuwait is ready for war. Civil defence forces have held mock chemical attacks and evacuation drills, while Raytheon Patriot missile systems and WMD early warning systems have been installed. Kuwait will be hoping the Patriot system proves more reliable than in the last Gulf War. While most Kuwaitis would be happy to see the back of Saddam, the authorities will be working hard to prevent ultra-radical Islamists from opening their own war front targeting US/UK forces and civilians and even Kuwaiti officials. The US and UK are among those to order the immediate evacuation of their civilians. Airlines have started to suspend flights. Most Kuwaiti nationals will stay put.

Government: The poor health of Emir Sheikh Jaber Al-Ahmed and Crown Prince Sheikh Saad Al-Abdallah has left reform-minded Acting Prime Minister, Foreign Minister Sheikh Sabah Al-Ahmed, to make the running. Other key personalities include Sheikh Mohammed Sabah Al-Salem, Oil and Information Minister Sheikh Ahmed Al-Fahd, Interior Minister Sheikh Mohamed Khalid Al-Hamad Al-Mubarak and Defence Minister Sheikh Jaber Mubarak Al Hamad Al-Mubarak. A no-confidence motion in Deputy Prime Minister and Minister of State for Cabinet Affairs Mohammed Deifallah Sharar was defeated by 30 votes to 15 on 17 March, easing fears that Parliament would be dissolved. Elections are expected in July.

Security: Kuwait has upped security since the January shooting of two US civilian contractors and dealt out swift justice. The trial of a national is underway for the January shooting, while a policeman was jailed in early March for a November attack on US soldiers. These trials follow the arrest of three men in mid-February on suspicion of planning attacks against US forces; four men were sentenced in February for training in Al-Qaeda camps in Afghanistan. Two men have been arrested on charges of spying for Iraq. Parliament approved KD500m to pay for increased security in mid-March.

External factors: Closer relations with Iran are a priority with negotiations on the import of Iranian gas and water supplies progressing. Post-Saddam relations with Iraq will be very important, notably to develop infrastructure links along the Kuwait/Iraq/Iran Gulf coast.

Economic Outlook

Overview: Strong macro position, with fiscal and external current account surpluses, and low inflation, at under 2%. High oil prices have led to strong oil revenues which have been channelled into public (notably Kuwait Investment Authority) and private investment. The IMF see a positive medium-term outlook but warns that unemployment pressures will grow if non-oil growth is not addressed. Parliament is a significant hurdle to market reform and Kuwait's strategic position remains an unavoidable drawback for investors; it is expected that oil output will be temporarily affected by war in Iraq.

Reforms: A new four-year plan, privatisation bill, subsidy cuts, service fee increases and sales tax are not expected to be introduced until H2 03 or Q1 04. Even after elections Parliament may take some persuading to pass new tax measures. The authorities plan to implement regulatory reforms that do not require parliamentary approval first. Decrees setting up independent regulatory bodies for public utilities are expected; transport and telecoms are priorities, with the power sector to follow.

Finance: The Kuwait Stock Exchange has said it will close during hostilities to "protect the interests of dealers and investors". The KSE index is at a five-year high buoyed by confidence that war will be swift and decisive. It closed at 2,796.1 points on 18 March, up 17.7% since the start of 2003 and at its highest point since its all time peak of 2,823.4 points in November 1997. At one point in 2002 it fell below 2,000 points. The Kuwaiti dinar was pegged to the US dollar on 5 January in preparation for GCC monetary union. A KD200m-470m budget surplus is forecast for 2002/03 (ends March).

Energy: Kuwait has closed two of its northernmost oil fields in preparation for war. Officials reported that 2.4m b/d oil was being pumped in mid-March, around 400,000 b/d over the OPEC quota (1.966m b/d in mid-January), and the same amount of capacity that officials say is at risk of closure during war in Iraq. Plans are progressing to import gas from Qatar (see below) and Iran (from 2005). Domestic gas development is also envisaged. Gas would be used to fuel new generation capacity; 2,400MW of capacity is planned for 2006.

Kuwait: Key Projects

KUWAIT-QATAR GAS PIPELINE: Saudi consent for a \$2bn undersea pipeline (passing through Saudi territorial waters) to supply Qatari North Field gas to local power stations from 2005-06 is not yet assured, despite comments by one senior Kuwait official in January. Formal sales and purchase agreements for an initial 750m ft³/d volume (rising to 1.4bn ft³) await Saudi approval.

PROJECT KUWAIT: The \$7bn scheme to develop oil fields near the Iraqi border is blocked in the National Assembly. Progress possible from H2 03. It forms an integral part of Kuwait's plans to raise oil capacity to 4m b/d (from 2.4m-2.7m b/d).

REFINERY UPGRADES: Bidding extended again (25 March) for the Al-Ahmadi oil storage and export project's estimated KD270m EPC contract; four packages are being tendered. Further renovation planned at other refineries. Bidding for a new acid gas treatment unit at Shuaiba has been extended to 30 March. Award of a vacuum distillation unit contract at Mina Abdullah is also expected.

SHUAIBA CALCINED COKE PLANT: Six groups prequalified for an estimated \$105m 300,000 t/yr facility for Kuwait Santa Fe for Engineering and Petroleum Projects Company. Bidding was expected to start in February.

IRAN-KUWAIT GAS PIPELINE: Final negotiations are underway for a 25-year agreement to supply 15m ft³/d. Subsea pipeline construction is expected to take two and a half years.

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.

KUWAIT: Selected Economic Indicators

(Kuwaiti dinars billion)	2000	2001	2002f	2003f
Domestic economy & finance				
Real GDP growth (%)	1.9	-1.0	1.4	1.2
Consumer prices*	1.8	1.7	2.4	2.5
General govt. balance (% of GDP)	31.8	17.6	13.8	9.1
General govt. debt (% of GDP)	38.6	37.4	34.5	31.4
External situation				
Current account balance (\$ billion)	14.7	8.6	6.5	5.8
Current account balance (% of GDP)	40.8	26.1	19.2	16.5
Gross external debt (\$ billion)	14.9	16.4	17.0	16.9

f = forecast. * Annual average % change)

Source: Fitch, Central Bank of Kuwait, IMF Ratings

GSN Risk Grade – B/3: Qaboos allows anti-war protests to limit conflict fall-out, finance steady

Political And Social Development

Overview: Sultan Qaboos Bin Saeed Al-Saeed desired a peaceful solution to the Iraq crisis and is sensitive to the public's strong anti-war feelings – numerous anti-war protests have been allowed. He remains committed to Western alliances, however, and the USA is likely to use Thumrait air base and other facilities during the conflict. Despite this apparent dichotomy, the threat of civil disturbance is relatively low, although the USA has taken precautionary measures by advising its nationals to depart. Gradual democratisation continues although the Sultan has yet to announce plans to share legislative powers.

Democracy: Although Sultan Qaboos retains a tight grip on policy and security he is regarded as one of the Gulf's more enlightened rulers and significant democratisation steps have been taken. A decree issued in November will allow all citizens over 21 to vote in Majlis Al-Shoura (Consultative Council) elections on 9 October. Previously only 25% of the population in each wilaya (governorate) could vote. The 82-member Majlis has no formal powers, but provides an increasingly assertive forum to question ministers.

Woman minister: In March, Sheikha Aisha Bint Khalfan Bin Jumiel Al-Siyabiah became the first female cabinet minister in the GCC. She was named president of the new National Authority for Industrial Craftsmanship.

Local sensitivities: Low-key support will be provided for US and UK forces during the war against Iraq. The authorities have allowed peaceful anti-war demonstrations; more protests are likely under the close watch of the security forces. A significant protest was staged in mid-February, when up to 200 women participated in the Sultanates first all-female march.

Defence: Since 1980 the USA has been able to use ports and air bases. Defence spending has risen sharply with big orders for US suppliers including Lockheed Martin F-16s. To support these, a new airbase is planned (for first phase completion by mid-2004) at Al-Musanaa in the northern Al-Batinah governorate.

External factors: Oman maintains ties with a wide range of states and has close relations with Japan and many Western countries. Stricter US immigration procedures have prompted Oman to advise its citizens to avoid travel to the US unless its urgent due to "inappropriate and discriminatory treatment".

Economic Outlook

Overview: The authorities expect the economic impact of war to be minimal – Omani exports under the Oil-for-Food programme will be most affected, they say. Moody's Investors Service reaffirmed Oman LNG's AAA debt rating in February. The government is targeting non-oil growth – particularly tourism, fishing and natural gas-based industries. Oil price volatility is countered by a prudent monetary policy. Oil sector investment is being encouraged to reverse a dip in output, while the gas industry and associated downstream industrial projects are fast-developing.

Finance: The Muscat Securities Market is slowly recovering, growing by 26.2% in 2002 to end at 191.86 points; foreign capital in MSM-listed companies accounted for 14.9% of the total. A OR3bn 2003 budget includes a OR400m deficit, based on \$20/bbl oil (\$18/bbl in 2002). Borrowing of OR150m is expected in 2003, with a five-year Eurobond mooted in H2. Central Bank of Oman (CBO) says the government plans to issue medium-/long-term bonds totalling OR150m in 2003 to help finance development projects under the five-year plan. Bank consolidation is under way but structural weaknesses remain, highlighted by scandals and big provisions.

Privatisation: Preparations to sell a strategic stake in Oman Telecommunications Company await a global upturn. Wholly-owned telecoms companies are expected by 2005. Electricity sector restructuring is under way; three generation companies will be created for sale in 2003-04, one transmission and three distribution companies. Privatisation of the national grid is expected by 2004 with sector reform completed by 2005. There are plans to sell up to 40% of Al-Maha Petroleum Products Company – possibly through the MSM – but no immediate plans to privatise Oman Oil Company.

Liberalisation: Reforms are planned to the 1994 *Foreign Capital Investment Law*, in line with WTO guidelines (Oman joined in 2000); this would allow 100% foreign investment in banking and insurance, IT services and securities. The 1994 law allows for up to 70% foreign ownership, with 100% in projects critical for economic development. Liberalisation of land ownership laws is also expected. A new electricity sector law is expected in Q2 03.

OIL PRODUCTION: Petroleum Development Oman, which produces around 90% of Oman's oil, plans to invest \$1.5bn in the period to 2007 to enhance output, which declined to 763,000 b/d in 2002. PDO output is expected to recover to 724,000 b/d by 2005 and around 800,000 b/d by 2007. New phased EOR schemes are scheduled from 2004 starting with the Harweel and Mukhaizna fields; this could push production costs to around \$8/bbl. A three block offshore licensing round opened in January; bidding closes 15 July.

Key Data and Forecasts

(\$ million)	1999	2000	2001	2002
Exports (fob)	7,226.7	11,301	11,056.9	8,117.4*
of which: oil & gas	5,523.2	9,361.2	8,866.5	6,249*
non-oil	522.0	644.0	690.2	486.9*
Imports (fob)	4,292.4	4,585.8	5,788.9	4,506.4*
Trade balance	2,934.3	6,715.2	5,268	3,611*
Total revenue	4,664.0	5,946.2	6,595.2	7,026.5**
of which: oil & gas	3,270.0	4,659.6	5,060	5,371.1**
Total public expenditure	5,892.0	6,897.4	7,427.2	6,148.8**
o/w: defence & security	1,784.5	2,099.7	2,422.7	1,967.8**
Fiscal surplus/deficit	-1,228	-951.2	-832	877.7**
Financing: Net loans	-	-	-182.5	-436.5**
Government bonds	-	-	15.1	72.4**

* Jan-Sep; ** Jan-Nov.

Source: Ministry of Finance, Muscat.

Oman: Key Projects

OMAN LNG EXPANSION: Japan's Chiyoda Corporation and Foster Wheeler were awarded the third train construction contract in January for LNG shipments from 2006. Two more trains are expected later.

SALALAH FREE TRADE ZONE: Government technical committee working on implementation. Project delayed but international consultant now appointed to advise on financial aspects and draft terms for project manager.

SOHAR REFINERY: Japanese consortium of JGC Corporation and Chiyoda Corporation was awarded an \$879m contract in early January. Completion of a 125,000 b/d plant is expected in Q2 2006. Sohar Refinery Company is seeking a 14-year multi-tranche facility with \$590m commercial debt. Responses to a preliminary information memorandum due by 28 March.

SOHAR IWPP: An advisory services tender was issued in January for a 400-500MW and 40m g/d desalination independent water and power plant.

ENERGY FINANCINGS: Financings expected during 2003 include the Sohar refinery (see above), Sohar fertiliser plant (estimated \$600m debt package; German export credit expected), and Oman Polypropylene's Sohar plant (\$200m-250m).

LICENSING ROUND: A licensing round for offshore blocks 18A, 18B and 41 covering a total 45,240km² opened in mid-January (bidding closes 15 July). Canada's Encana Corporation signed a three-year exploration and production-sharing agreements for blocks 3 and 4 in February.

the post-conflict reconstruction of Iraq if the country were administered by a military governor.”

The involvement of the UN in reconstruction could also alter the balance of the relationship between London and Washington. Despite his involvement in the unilateral military assault, Blair is a strong believer in multilateral foreign policy: this was particularly noticeable in the Balkans, but it has also been seen in his development of close partnerships with France in developing a *European Union* defence capacity and a co-ordinated stance towards Africa and international peace-keeping.

Whether Blair still has the international credentials is questionable – **Russians** are quietly saying their wily President **Vladimir Putin** is poised to take over as Bush's new best friend – and neo-conservative may not be listening. Recent events have demonstrated the extent of Blair's inability to hold back neo-con impatience while he tried to secure united UN endorsement for an early war.

However, reconstruction could begin to tilt the balance of argument back in favour of the multilateralists. Even after Bush's final pre-war ultimatum to Baghdad, rival elements within his Administration were unable to agree on a clear timetable and framework for Iraq's post-conflict governance – in contrast to the decisiveness with which they have drawn up war plans. Thus, for all the US planning outlined in *Geopolitics*, there is an opening for international agencies and European governments to reassert the central importance of a UN-led multilateral approach to rebuilding Iraq, politically, as well as physically.

PRACTICAL CONSIDERATIONS

One senior international official told *GSN* he thought the USA would rapidly find that it had no choice but to fall back on the post-conflict systems already well established by multilateral agencies and the wider donor community.

While the Americans enjoy overwhelming global superiority in military terms, they cannot boast the same preponderant clout in disaster relief, development or broad-ranging post-conflict reconstruction.

In these situations, it is the EU and the big multilateral agencies that have proved the most consistently reliable source of donor funding: the UN system, World Bank, IMF, regional development banks and leading non-governmental organisations have been the greatest repository of expertise and local contacts.

In Iraq, it is the UN that has battled to maintain on-the-ground programmes through the years of sanctions, ensuring OFP operations through a nationwide distribution network of 55,000 outlets. In northern Iraq, the World Food Programme operates a network of 11,000 local distributors. The EU is the leading humanitarian donor in the region, spending more than €150m in recent years.

...NEED MULTILATERAL SOLUTIONS

US planners have said they could provide emergency post-war support for 1m people. But even if Iraq's physical infrastructure escapes serious bombing and battle damage, it appears likely that the US military administration will find itself hugely dependent on existing UN structures.

USAID has set up a Disaster Emergency Response Team (DART). It has identified likely humanitarian needs and promised to meet them.

The UK's well-regarded Department for International Development (DFID) already has agreed the assignment of an adviser to the UK military Division 1 headquarters

in **Kuwait** and it is ready to finance “quick impact” aid projects carried out by the forces. DFID has also seconded an adviser to the US Defence Department's Office of Reconstruction and Humanitarian Affairs, which is leading the American planning for humanitarian work.

However, the needs are potentially far beyond the capacity of even today's beefed up US emergency aid capacity. During the last Gulf War some 15,000-30,000 refugees died from measles, diarrhoea, typhoid and cholera. New damage to water supplies could produce similar epidemics this time.

The UK parliamentary report warned that a breakdown of OFP would leave 10m people without food. It also pointed out that lasting disruption to power supplies could disrupt irrigation pumping: “Iraq depends on irrigation channels that are 5,000 years old. If the land salinates it could cease to be available for agricultural production.”

AN ONGOING REFUGEE CRISIS

Even before the war, there were 700,000-900,000 internally displaced people and UN agencies estimate that this number could double. Many southerners may flee into Iran, which already has 200,000 Iraqi refugees and struggles to cope with 2.4m **Afghan** refugees in the east. Surrounding states such as **Turkey**, **Kuwait**, and **Iran** may try to keep fleeing Iraqis just inside Iraqi territory, where they will have to be provided with emergency accommodation.

In effect the ground is already being prepared for a major UN role, with the UN *Office for the Co-ordination of Humanitarian Affairs (OCHA)* preparing to co-ordinate efforts. OCHA told *GSN* it would have liaison personnel working closely with the Americans.

However, the UK parliamentary committee warned that US plans “lack detail” and that non-governmental aid groups had had difficulty getting information from both the UN and DFID – who appeared reluctant to go public with plans for disaster for fear that this would be seen as assuming war was inevitable.

DFID Minister Short, in evidence to the committee, said that even international capacity to deal with the humanitarian needs was “limited”. US experience of Iraq was limited, while many donors had yet to fully engage with the scale of the potential crisis. There was “serious risk”, she said.

Beyond the immediate crisis weeks, there is almost universal agreement – outside the US Administration at least – on the need for a UN framework for long-term reconstruction. However, potential donors are already asking hard questions. They are determined that Iraq should not divert cash from other equally pressing crises, such as the reconstruction of Afghanistan, the Balkans and Central Africa, nor from humanitarian needs, such as the famine in southern Africa.

Given these other priorities, there will be pressure for reconstruction to be partly financed out of Iraqi oil revenues, especially after the immediate post-war phase.

The major donors have spending power – Europe disbursed \$750m in Afghanistan alone last year. Donors seem ready to deploy these resources, despite widespread anger at the launch of war without a new Security Council resolution. But the readiness to contribute will be heavily conditioned on agreement that the UN – and not a US military governor – holds the decisive voice in shaping Iraq's reconstruction. As EU Commissioner for External Affairs **Chris Patten** put it, reconstruction should be an “international” effort – and there will have to be a strict separation between military action and aid to achieve this without compromising the “humanitarian space”.

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The Oil-for-Food Programme Is Dead! Long Live The OFF!

LONDON/NEW YORK—British and US diplomats have begun drafting a new *United Nations Security Council* resolution that would place control over Iraq's Oil-for-Food Programme (OFF) in the hands of UN Secretary-general **Kofi Annan**. This could be presented to the Council as early as next week, depending on the pace of military action in Iraq. As war was about to begin, Annan announced that OFF would have to be amended to take account of the pending humanitarian crisis, and that the belligerents – the USA and UK – were ultimately responsible for the well-being of Iraq's civilian population.

In the build up to war, OFF was increasingly recognised as the prime source of interim funding to ensure a continued flow of food, medicine and other essential imports into a shattered post-war country that will initially lack any sovereign institutions. A report from the UK House of Commons' cross-party International Development Committee pointed out that 60% of Iraq's population depended on OFF for food, delivered through a government ration scheme; two-thirds of recipients had no other source of food. The OFF generates roughly \$5bn per six-month phase and expends \$250m/month on food.

The timing of any move to bring the new resolution to a vote will be crucial. The UK wants the document finalised rapidly, so that UN officials can begin practical preparations for running OFF. But British officials cautioned that to push for a vote while sovereign Iraqi authorities were still in place would risk antagonising some members of the Security Council. The UK has not ruled out approaching other key Security Council members such as **France** – which has been making doveish noises about the need to unite the international community around the task of post-war reconstruction – as possible co-sponsors of the resolution.

Just as in the pre-war arguments over legitimising military action, UK Prime Minister **Tony Blair** – egged on in this case by his controversial International Development Secretary **Clare Short**, still in post despite her earlier resignation threat – finds himself under intense pressure to secure a central role for the UN. In a public statement reversing her earlier promise to quit,

Short said that Blair had persuaded President **George W Bush** that yet another Security Council resolution would be required, formally giving the world body a mandate for the reconstruction of Iraq.

Short's about-face has been much mocked. But her view that only the UN can legitimise the rebuilding of Iraq's physical and social service infrastructure, and its institutions finds a broad degree of sympathy among officials of the big multilateral agencies that will have to finance and organise much of the work. In private conversation, many international development specialists – even Americans – reveal deep unease over the US/UK decision to attack Iraq without specific Security Council authorisation. But they also feel that standing aside while a US-imposed military government organised a post-war Iraq and set out development priorities would only compound the damage already done to the international system. Some officials canvassed by *GSN* were privately relieved that the US and UK have taken the unilateral military route, because this has spared the UN from being associated with a war that does not command broad consensus support.

In the immediate post-war aftermath or perhaps while conflict is still continuing, the big UN agencies feel they have an absolute moral obligation to do all that they can to help alleviate the suffering of Iraqis. They also feel they have an obligation to play a major role in rebuilding Iraq: the establishment of an overarching UN mandate offers a means of doing so without being seen to endorse the US/UK decision to embark on military action in the first place.

The UK push for a new UN role is a first step in Blair's efforts to reposition London at the centre of a consensus international position over the way forward in Iraq, after the bitter arguments provoked by Bush's determination to impose "regime change" on Iraq. The UK parliament committee gives a blunt warning: "It is important that the UN should have the lead role in a post-conflict Iraq as soon as possible. There is a real danger that donors and NGOs would not play a full part in

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