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GSN

Companies & People

"Little Satan" Target In Iran

Iran is a focus for the UK's policy of "constructive engagement" and Foreign Secretary **Jack Straw** remains bullish, but diplomats have taken to meeting visitors outside the Tehran Embassy's walls and security has been tightened after anti-war protestors brandished home-made grenades and bomb threats multiplied. Foreign and Commonwealth Office (FCO) officials admit the UK is serving as a "lightening rod" for popular rage against the war in **Iraq**.

The big British participation at the 16-19 April Tehran Oil, Gas and Petrochemicals Show lost its official **Trade Partners International** backing at the last minute after the FCO feared UK groups might become targets. The group, led by the **Middle East Association** and **Orient Exhibitions**, would not even get the usual Embassy briefing – although UK Ambassador **Richard Dalton** is seen as business friendly – to avoid being associated with London. Companies will receive some compensation.

Non-essential Embassy staff and dependents have left, but the FCO has not advised UK nationals to get out. Indeed, the **Export Credits Guarantee Department** is hyping "very robust" levels of cover and encouraging firms to go out and sell.

Across The Region

With the combat phase of Operation **Iraqi Freedom** winding down, the Pentagon has entered the nation-building phase. It could prove more of a challenge than fighting the war given the Coalition's aim not only to oust Saddam Hussein but also to eradicate any WMD and 'terrorist threat', create a stable government, get Iraq's infrastructure running and minimise global anger over the war. **PAGE 3**

Iraq's Shia population could have a big say in its future government. Islamist radicals are lining up, while the Pentagon pushes **Ahmed Chalabi** and other factions in the Coalition seek suitable candidates of their own. **PAGE 4**

Qatar's leaders are pushing for a big vote in the 29 April referendum on a new Constitution, while US officials are still asking about some senior Qataris' links with radical Islam. **PAGE 10**

Diplomatic skills are being tested as rich donor nations attempt to reach agreement over Iraq's path towards reconstruction and governance. The IMF and other multilateral institutions will play a big role. **PAGE 13**

The UK's **Clare Short** has a mission to reunify the donor community. She has found some allies in Europe. **PAGE 14**

Early action from Paris Club bilateral creditors to alleviate Iraq's debt burden was an issue on which Europe and the USA could agree at the IMF/World Bank Spring Meetings. **PAGE 14**

The UAE may receive post-Iraq war commercial dividends. Dubai continues to defy the sceptics and there are even signs of a move towards wider political representation. *GSN* maintains its B+/2 Risk Grade, but an upgrade could follow. **RISK MANAGEMENT REPORT, PAGE 18**

Yemen is caught between President **Saleh's** alliance with the USA and violent opposition to the war. Yemen is politically volatile and very poor – but its payments record and economic management are surprisingly good. These factors are reflected in *GSN's* D/3 Risk Grades. **RISK MANAGEMENT REPORT, PAGE 19**

GSN's Analysis

Providing a platform for Iraq's reconstruction, debt relief and a new currency could provide the context in which the USA and its bilateral and multilateral critics agree a common approach. This would constitute an important step towards rebuilding the international consensus, as well as the Iraqi economy. **GSN VIEW, PAGE 2**

US Administration hawks have threatened to use of a big stick against Iran and Syria, frightening even allies in the "Coalition of the Willing" that American tanks might just roll on to Damascus and Tehran. *GSN* analyses the prospects for a new front opening in Bush's war – and sees a confrontation with Hizbollah in Southern Lebanon as most likely. **PAGE 6**

Iran's nuclear build-up is seen as a threat by many in Washington, notably a group of hawks with close links to Israel. **PAGE 6**

Syria's leader is in out of his depth, but his regime is not yet in mortal danger. Five big issues must be tackled for Damascus to feel secure. **PAGE 8**

A "feeding frenzy" of legal cases could shortly be filed against Iraq now that a precedent-setting lawsuit on behalf of individual US claimants looks close to being judged in their favour. **PAGE 24**

One year ago, Iran's inclusion in President Bush's "Axis of Evil" had much to do with Israeli lobbying and efforts to link Iranian hardliners to events in the Holy Land. **PERSPECTIVE, PAGE 2**

MIDDLE EAST ENERGY

Global power developers are pulling out of emerging markets as quickly as they piled in during the 1990s. MidEast authorities looking to accelerate ambitious generation plans now find an increasingly barren field to choose from. **PAGE 20**

MEE Pointers on Iraqi oil management, Lukoil and West Qurna-2, the Syrian pipeline and Lebanon's EDL. **PAGE 20**

Syndication for Qatar's \$1.1bn Oryx GTL scheme has yet to be tied up, but "Oryx is a done deal". **PAGE 22**

Trade facilities for Syria and some others are squeezed, but the overall impact of war in Iraq has been limited. **PAGE 22**

Re-establishing Iraq's economic and financial structures will be a serious challenge. The World Bank and International Monetary Fund (IMF) are prepared to step in, but they may have to work harder than anyone has foreseen. Under Saddam Hussein's isolated and isolationist regime, Baghdad's financial institutions were a closed book to the outside world. Indeed, Iraq's reluctance to disclose meaningful financial information long predates the 1990 invasion of Kuwait. Saddam's reticence at one point appears to have been intended to cloak the astronomical cost of the war he had begun against Iran, and the degree to which this had left him financially dependent on aid from other Arab states as other sources of funding dried up.

The last IMF mission to Baghdad took place in 1983 and the Fund's last proper Article IV economic assessment – a procedure that all countries, rich and poor, routinely undergo – was made in 1979-80. To make matters worse, many internal economic and financial records appear to have been destroyed in the recent looting of the Central Bank of Iraq, Rafidain Bank and other institutions. Practically no information was disclosed to the World Bank after 1973, when oil wealth enabled Iraq to “graduate” from reliance on IMF financial support. Iraq still owes some \$82m on old World Bank loans, which it stopped servicing more than a decade ago. This low level of arrears should quickly allow it to resume support.

A first priority for the IMF and World Bank – once an accountable government has been established to their satisfaction – is a basic needs assessment, gathering data and background information in preparation for an eventual joint mission to Baghdad, once security conditions permit. This will be one of the few undertakings on which there will be unanimous international agreement.

In the longer term, the Bretton Woods institutions will want to steer Iraq towards a market economy. Isolated

for the past 13 years, it has retained a statist command economy and has missed out on the liberalisation experienced by most developing countries. As a result, the domestic economy – as opposed to the oil export sector – is backward and undeveloped, and may be largely unviable in formal commercial terms.

World Bank officials point out that they will be able to draw on their experience of helping the “transition” countries of Central and Eastern Europe in moving away from centrally planned economies and towards a version of market capitalism. But Western investors, having learned from the same experience, may be less than eager to buy into privatisations and new joint ventures for fear that the prime beneficiaries would be the current Iraqi business elite – most of whom got rich through their crony connections to the Baathist regime.

An early priority must be the establishment of a credible national currency and the restoration of the banking system. The looting of banks has destroyed the savings of many middle class Iraqis whose confidence and willingness to resume work or business activity will be vital to the country's revival. The dollar is already circulating widely in Baghdad and, given Iraq's dependence on sales of oil – a commodity priced in dollars – and the damage to its monetary institutions, the greenback may have to substitute for a national currency for some time. The Balkans, which have functioned largely on deutschmark – or euro-based systems in recent years, offer a model here.

Iraq could adopt the “Swiss dinar” used in the Kurdish area and printed by De La Rue. But this might antagonise non-Kurds. The IMF and the USA have both looked at the currency issue and are now likely to see if they can agree a common approach. It will provide an important step in rebuilding the international consensus, as well as the Iraqi economy.

Perspective: One Year Ago

Iran's inclusion in President George W Bush's “Axis of Evil” had much to do with Israeli lobbying and efforts to link Iranian hardliners to events in the Holy Land. This was much to the benefit of Israeli Prime Minister Ariel Sharon as he sought to demonise Yasser Arafat and the mainstream Palestinian leadership by linking them with groups such as Hamas, Hizbollah and the wave of young suicide bombers who have so rattled Israel in recent months – even if these groups are more usually seen as rivals to the wily old PLO chief.

As *Gulf States Newsletter* reported in November, “with Arafat's Palestinian National Authority in disarray, analysis by Israeli military and intelligence bodies suggests that Southern Lebanon – where, they say, Hizbollah is still acting as an Iranian ‘proxy’ – is a likely flashpoint for a future phase of conflict in the Middle East and the ‘war on terrorism’.”

This threatened a new clash in what Israeli intelligence

calls “the Northern Arena” pitting Israel against Iran (and Syria), with the Jewish state arguing that President Mohammad Khatami's reformist government had been unable to curb hardliners in the Islamic Republic. While the focus is on Arafat, the substance of this analysis has not changed. What is different is the international mood, with Sharon using the war on terrorism and the wave of suicide bombings to prosecute his long-wanted campaign to eradicate Arafat and his support structure.

Implicating Iran in this mix, now that Bush has acknowledged its membership of a mythical “Axis of Evil”, may help this aim – or speed the Middle East's rush to war... Demonisation by Republican Washington via Israel will further sour the business environment and create a self-fulfilling prophecy for Iranian hardliners who always told Khatami and his reformist allies that one could not sup with the Great Satan and his acolytes.

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Coalition Flirts With Nation-building In Iraq As Combat Role Fades Away

With the combat phase of *Operation Iraqi Freedom (OIF)* winding down, the Pentagon has been looking ahead to the nation-building work that could prove even more of a challenge than the actual fighting of the war.

Under the coalition's assault, the Iraqi Republican Guard melted away from the outskirts of Baghdad, coalition forces met little resistance inside the city and Iraqi forces all but collapsed in the north, leading US Joint Chiefs of Staff Director of Operations Major General **Stanley McChrystal** to state on 14 April that "major combat operations are over". The coalition's key task now will be to ensure that its military victory creates an environment conducive to its political objectives.

McChrystal's declaration is reflected in the fact that two US aircraft carriers have withdrawn from the Gulf and F-117A and B-2 stealth aircraft are being called back to the continental USA. Sortie rates have dropped to about 700 per day (from 1,500/d), with fewer than 200 munitions/d dropped, compared to an average of about 1,000/d during "major combat operations".

A good indication of how far the Coalition has yet to go can be seen in the fact that ground forces are unlikely to see much of a reduction of tempo.

As nation-building progresses, numerous tasks will continue to burden troops and reinforcements that are already operating at or near capacity.

The complex political objectives of OIF may be difficult to translate into military operations. The coalition has set out not only to oust the regime of **Saddam Hussein** but to eradicate any weapons of mass destruction (WMD), deactivate the state as a potential haven for terrorists, create a political environment that would support stable, broad-based government, get Iraq's infrastructure running again, and minimise global and regional anger over the war.

The first step in achieving these objectives – the high-intensity combat phase of the operation – was clearly an overwhelming success. Although it required the efforts of a significant proportion of the land forces available to the USA and UK, as well as a great investment in money and arms,

Iraq's military was defeated in 25 days and with relatively low casualties on both sides. Other goals, however, may prove more difficult to achieve.

ERADICATING WMD

How success should be judged in the disarmament of Iraq has long been a contentious issue. European diplomats have argued that inspections

themselves constituted a success: under increasingly tight monitoring, Iraq would be unable to develop or maintain the high degree of weaponisation and operational readiness that a relatively overt WMD posture required.

For the USA, the job of inspectors and national intelligence services was to find and expose WMD. This perception has translated into US military attempts to find a "smoking gun" that may very well not exist any more – potentially to the embarrassment of Coalition diplomats who continue to argue that the war was about WMD.

Numerous false alerts have attended the work of the specialist **75th Exploitation Task Force**, indicating how hard it will be to provide unambiguous proof that Iraq was in breach of WMD-related **United Nations** resolutions. Only the hardest and clearest evidence will convince international opinion that Iraq possessed WMD.

US Office of the Secretary of Defense (OSD) official **Michael Rubin** told *GSN*: "We may find chemical production machinery or bio-fermenters or precursor chemicals and growth medium, but we won't find weaponised chemical munitions."

Where finds are linked to concealment activity – such as the mobile biological laboratories reportedly found buried underneath a children's playground – suspicion increases. But finds of dual-use equipment that could be used in civilian industries have been particularly unconvincing.

For many, the regime's failure to use WMD – contrary to the belief that WMD were vitally integrated into Iraq's last-ditch defensive order of battle – is evidence enough that Baghdad has disarmed, either by destroying its WMD infrastructure or by exporting it to **Syria**.

Major **Mike Eisenstadt**, a **Central Command (Centcom)** reservist involved in OIF planning, recently noted: "Maybe we have to reassess some of our long-standing assumptions about Iraqi WMD and the regime's attitudes towards them."

It is possible the **Baathist** leadership recognised that, far from being their greatest asset, WMD represented the gravest threat to their existence.

DEACTIVATING IRAQ AS A HAVEN FOR TERRORISTS

During OIF, robust action was launched against radical Islamist group **Ansar Al-Islam** and the **Mojaheddin-e Khalq Organisation (MKO)**, both of which had established bases in northern Iraq.

In addition, the **Kurdistan Workers Party (PKK)** indicated it was ready to scale back its guerrilla operations in light of the US presence and

the increasing unwillingness of the *Kurdistan Regional Government (KRG)* to tolerate PKK operations from its territory.

Yet conventional military action has often been of questionable effectiveness against terrorism, and it is far from clear whether the threat from Iraq – nebulous in the first place – has decreased.

Ansar Al-Islam – denied sanctuary in Iran, according to US spokespersons – has dispersed and survivors might pose a threat to the Coalition, western commercial and aid workers, and pro-Western Iraqis. Substantial amounts of weaponry have fallen into the hands of Iraqis, and the potential for attacks on Coalition targets remains.

One US *Special Operations Command (Socom)* officer told GSN that former Iraqi state security personnel had very rapidly coalesced into well-armed criminal enterprises – a situation reminiscent of the break-up of the Soviet Union. Containing any terrorist threat could prove more complex than simply winning a ground war.

The publicity generated by US Special Forces' capture of *Palestine Liberation Front (PLF)* Secretary-general Mohammed Abbas (Abu Abbas) hardly convinced sceptics that Baghdad was a hive of terrorist activity. Described as a "Palestinian terrorist" by Brigadier General Vincent Brooks, Abbas was a key player in the 1985 *Achille Lauro* hijacking. But his presence in Baghdad was the result of a deal involving Israel; the Palestinian Authority complained his arrest violated the 1993 Oslo Accords.

BUILDING A NEW GOVERNMENT

Although Saddam's regime has been toppled, Iraq's Baathist leadership remains at large, with perhaps as few as three of its senior figures accounted for by the death of 'Chemical Ali' Hassan Al-Majid, and the capture of Saddam's half-brothers Barzan Ibrahim Al-Tikriti and Watban Ibrahim Hassan.

It is the shape of a new regime that will be crucial to the future of Iraq.

Most of the Coalition's goals would be helped along by the presence of a stable, broad-based government with pro-Western leanings, plus an Iraqi public willing to give the Coalition the benefit of the doubt. A successful transition to federal, multi-ethnic democratic rule is seen in the OSD and White House as a political objective that will, in time, eclipse the WMD/terrorism rationale originally used to justify the war.

The Coalition has reoriented itself with great speed to the task of shaping post-war Iraq, but its military efforts are showing mixed results in meeting the range responsibilities that fall to an occupying military power. Within Iraq, US and British military commanders continue to be the main sources of authority. Only a small fraction of retired Lieutenant General Jay Garner's *Office of Reconstruction and Humanitarian Assistance (ORHA)* had deployed from Kuwait as GSN went to press. One ORHA office had been co-located

with the KRG in Irbil with 16 staff; a second was manned by 44 staff in Umm Qasr. The remaining 240 ORHA employees remained in Kuwait due to safety concerns.

Local elements of the quickly coalescing *Iraqi Interim Authority* have three regional centres, in line with the coalition's perception that the country needs a less centralised political structure:

- **NORTH: IRBIL**—Interim authority is comprised of the KRG with a light ORHA presence.

- **CENTRE: BAGHDAD**—Establishing an interim authority in central Iraq will prove a sensitive undertaking. The USA convened a "big tent" meeting in Ur, southern Iraq, on 15 April attended by more than 70 potential stakeholders in a new government, including members of the external opposition and internal factions. Jay Garner was there. Bush's Special Envoy Zalmay Khalilzad worked the room.

However, some key figures were notably absent, including *Iraqi National Congress (INC)* Chairman Ahmed Chalabi – who has said he planned to build an independent interim government free of coalition influence or oversight – and representatives of the Iranian-backed *Supreme Council for Islamic Revolution in Iraq (Sciri)*. Former diplomat Adnan Pachachi refuses to enter Iraq, while former General Nizar Khazraji remains discredited due to the perceived blood on his hands which caused him trouble in Denmark. A second meeting has been set for 25 April.

- **SOUTH: BASRA**—The British military have placed local Sheikh Mozahem Al-Tamimi in charge of the 24-member provisional government in Basra. Ten of the 24 members are tribal sheikhs; the remainder are Iraqi technocrats. But the establishment of the interim authority there progressed too quickly for some, and concern has been expressed about the speed of vetting and what is seen as the arbitrary appointment of Sheikh Mozahem.

RE-ESTABLISHING THE RULE OF LAW

Coalition forces working with local police and militias have re-established a semblance of order in major cities and along lines of communication linking urban areas, but have not yet made areas both safe and secure – preventing aid agencies, the Iraqi government and ORHA from deploying fully.

Contrary to worst-case scenarios, a coalition role in reducing looting has been broadly welcomed by Iraqis. In addition to 2,000 returning policemen in Baghdad and other cities, the advance forces of the 4th US Infantry Division will help with policing. A specialised US military police brigade will follow the 4th's deployment.

REPAIRING CRITICAL INFRASTRUCTURE

Although Western targeting policy spared much property, looting has caused widespread damage that has made it harder for the Iraqi civic

infrastructure to operate and has reduced the country's ability to absorb aid and funding.

Information such as intelligence and financial files appear to have been hidden, destroyed or looted in many cases.

Physical infrastructure has also been damaged. Power generators supporting the national grid were looted in Basra, exacerbating the utility crisis there. The USA has focused on the industrial infrastructure of the oil and gas industry and power generation. Key hydrocarbons facilities and the Oil Ministry are under coalition control, with all major oilfields secure. The last of nine burning wells have been extinguished in the south.

Electrical power is being restored through the provision of Coalition military fuel to civilian generators, the repair of incidental damage to power stations and the resumption of gas supplies between Kirkuk's gas fields and gas-burning power stations in Baghdad.

Such initiatives indicate the Coalition is focused on at least basic rebuilding, even if it is not yet ready to take on the full task of nation-building.

Establishing a stable government, the rule of law and the operation of critical infrastructure will be vital if the coalition is to make any progress towards objectives like disarmament and an elimination of the terrorist threat from Iraq.

With most of the fighting now done, the spotlight is on the coalition's next moves and how effective they are at bringing law, order and government to the Iraqi people.

Big Tent, Big Rivalries Among Iraq's Prospective New Bosses

The mid-April "big tent" opposition meeting in Ur was seen by the USA as an important first step towards a post-war government. But in the run-up to the meeting, two power bases had already begun to coalesce in the capital:

The first is a local form of Shiite theocracy in Saddam City – the Shia area of Baghdad now renamed Sadr City by locals. It is led by **Ayatollah Ali Shawkī**, who commands armed militias, has banned looting and collected stolen goods at mosques for possible return and repatriation.

Other Shiite religious leaders are consolidating their presence in Najaf, Karbala and other towns.

In Najaf, violence between rival groups saw the killing of returning exile, cleric **Abdelmajid Al-Khoei**, 40-year-old son of the late **Grand Ayatollah Abdelqassim Al-Khoei**, head of the London-based **Khoei Foundation** and Shiite interlocutor with such luminaries as UK Prime Minister **Tony Blair**.

It signalled the potential for inter-Shia violence as leaders manoeuvre for power. In Najaf, radicals linked to **Jamiat-i-Sadr Thani** leader **Moqtada Sadr** also surrounded the home of **Grand Ayatollah Ali Sistani**, who had told Iraqis not to resist Coalition forces. The 22-year-old Sadr's family stayed in Iraq, conducting underground

opposition, and he is opposed to exiled – Iranian-backed – clerics, one of several key pressure points to watch in Iraq during coming weeks.

Still to show his hand is **Supreme Council for Islamic Revolution in Iraq (Sciri)** leader **Ayatollah Mohammed Bakr Hakim**, backed by an estimated 10,000 **Badr Brigade** fighters. Hakim's presence was notable by its absence from the big tent. Also absent was the **Hisb Daawa** leadership, including **Abu Bilal Al-Adib**, **Abdelrazaq Al-Kadhmi** and **Haydar Al-Abad**.

In Karbala, **Ridha Jawad Al-Taqi's** underground **Islamic Task Organisation** has emerged to argue for an Islamic state.

INC PROVOKES US ELITE IN-FIGHTING

The second power base is that of the Iraqi National Congress' **Ahmed Chalabi**, whose **Free Iraqi Fighters (FIF)** have been ferried around Iraq by US transport planes in recent weeks.

Powerful would-be kingmakers including US Deputy Secretary of Defence **Paul Wolfowitz** support Chalabi and have stolen a march on the State Department and **Central Intelligence Agency** by inserting the INC Chairman – sporting a black T-shirt instead of his usual suit and tie – into Nasariya, along with around 300 FIF troops.

US Army Special Forces planners told *GSN* the FIF was currently split between Chalabi's INC troops and those of former General **Najib Al-Salhi**, whose forces were trained in **Hungary** by the USA.

Chalabi's faction appears to be growing rapidly and may number between 700 and 1,000 men, having received arms and training from US Special Forces in Nasariya.

The next step will be the transportation of Chalabi's FIF to Baghdad, the subject of a brewing row between the uniformed US military and the OSD. One US **Special Operations Command (Socom)** officer told *GSN* that **Centcom** refused to convey Chalabi to Baghdad without a direct order from Secretary of Defence **Donald Rumsfeld**. This order was forthcoming, and Chalabi – who was asked by US officials to remain outside the big tent so as not to overshadow the meeting but sent representatives – said that his move to Baghdad was imminent.

Whether in Baghdad or Nasariya, Chalabi is believed by many Washington insiders to be gaining influence, not least by providing a more complete list of potential ministers than either the State Department or the CIA. The list, currently close-held, is likely to influence Garner's ORHA.

Chalabi, meanwhile, is reported by OSD officials to be nervous that he may become a victim of his own success, believing both the Iranians and the CIA want him dead. Although Chalabi may be overstating things, the CIA is doing all in its power to downplay Chalabi's successes. A recent meeting between Chalabi and Shia figures was reported by the CIA as a wash-out, but appears instead to have drawn a responsive crowd of 12,000.

After Iraq: The Fire Next Time For Syria And Iran?

Even while US troops were still confronting Iraqi forces, Administration hawks were threatening to use a big stick against Iran and Syria, with Secretary of Defence **Donald Rumsfeld** warning about alleged Syrian military supplies and escape routes, and very public expressions of alarm at the development of Iran's nuclear programme, as well as Tehran's encouragement of the *Shia Badr Brigade* as a possible proxy in Iraq.

With the hot war apparently over, the temperature has been raised further, with President **George W Bush** on 13 April saying the USA believed that Syria had chemical weapons. Syrian Foreign Ministry spokeswoman **Busaina Shaaban** – a symbol of President **Bashar Al-Assad's** new Syria – said it was news to her and Damascus was only looking for peace in the region. UK Foreign Secretary **Jack Straw** said again that Syria wasn't next on any US 'hit list' – and sent his junior Foreign Office Minister **Mike O'Brien** to Damascus and Tehran in an effort to prop up the Blair government's policy of "constructive engagement". French Foreign Minister **Dominique de Villepin** visited Assad to offer support.

With US troops 'liberating' Baghdad, one poll suggested that 42% of Americans would support an extension of the conflict to Syria. The conventional view is that senior Administration officials have drawn a line in the sand, saying this will not happen. As speculation reached fever pitch on 15 April, Bush himself intervened to say it wasn't so.

However, the signals emanating from Washington were sufficient to frighten critics of the USA's Middle East policy, including most of the Administration's remaining allies in the "Coalition of the Willing", that US tanks might just roll on to Damascus, and then even to Tehran.

So are US forces also going to 'liberate' Syria and Iran, enforcing by war the *pax Americana* over the Middle East and securing Israel's security?

The push into Baghdad and the *Baathist* regime's collapse across Iraq seemed to confirm that after a difficult period, Rumsfeld's belief in pinpoint air power and relatively minimal army forces had worked. In the run-up to the Iraq campaign, micro-manager Rumsfeld sidelined senior generals who did not agree with his views; he was ultimately vindicated by the Iraqi Baath's collapse – but only just, given the pressures US and UK forces were coming under as supply lines weakened.

The military establishment does not necessarily agree that an extension of the armed conflict is feasible. A senior *Defense Intelligence Agency (DIA)* official told GSN that Iraq had shown there were definite limits to US military power – and Iran was now in the "too hard category". But the

lesson of the build-up to the Iraq war is surely that such perceptions can shift just as quickly as a *Republican Guard* battalion will crumble under US bombing.

In the coming weeks such threats are likely to have two main aims: to push the US agenda on the revived Israel-Palestine peace process (on which Bush is now said to be a convert to action) and to help bring "closure" to the war in Iraq.

Longer term, other problems come into play.

Revelations about the extent of Iran's nuclear ambitions have received substantial play in the USA and are the harbinger of trouble to come.

Iranian reformists as well as conservatives (who have a professional interest in highlighting the potentials for American aggression) are concerned about a US push to overthrow the Islamic Republic. Iraq would provide an ideal base for this.

A new conflict between Washington and the Islamic Republic would be welcomed by Israel – which sees Iran and its *Hizbollah* allies as a major threat – but is unlikely to see immediate military expression outside proxy war in **Lebanon**.

US hawks and Israeli officials canvassed by GSN believed that regime change would come to Iran because the Islamic Republic was "ripe for counter-revolution". But while social tensions are rising and swathes of Iranian youth are disaffected, the Islamic Republic may prove more robust than they think.

Iran's commitment to developing a nuclear industry might also prove deeply frustrating. Iran has said it is open to inspections, but this may not be enough for the USA. There is growing concern that "preventative action" will be taken to slow Iran's nuclear progress until regime change occurs.

WHAT ABOUT HIZBOLLAH?

Syria under Bashar Al-Assad has sought to quietly court US investment, in line with the young president's modernisation drive, while publicly holding to more traditional Baathist ideas – pointing to the extreme ambiguity of Dr Bashar's position. This delicate balancing act seems to have been a victim of the war.

Hizbollah remains a more accessible target for covert US military and intelligence action – and linked to Iran and Syria, Lebanese Hizbollah holds a particular niche in the psyche of many Washington hawks.

Hizbollah suicide bombings – which killed 318 Americans – still mark out the organisation as an enemy of America.

Involvement in the Iran-Contra scandal, precipitated by the hostage crisis in Lebanon, was the defining event for many Washington hawks such as **Elliot Abrams**, **Michael Ledeen** and **United Nations** Ambassador **John Negroponte**.

Israeli Prime Minister **Ariel Sharon** is positioning himself as “a man of peace”, but that would not stop a new offensive in Israel’s northern arena. The Office of the Secretary Defense (OSD) remains strongly aligned with Israel, and for all the State Department plays good cop to OSD’s bad cop, some senior officials would welcome US action against Hizbollah.

Deputy Secretary of State **Richard Armitage**, who is preoccupied with terrorism, noted that “in the beginning, Syria helped us on the question of **Al-Qaeda** but this assistance has lately ebbed. They do continue to support Hizbollah and this reflects adversely on Syria.”

Armitage recently noted: “Hizbollah may be the A-team of terrorists, and maybe Al-Qaeda is actually the B-team. They’re on the list, and their time will come. There is no question about it. They have a blood debt to us, which you spoke to; and we’re not going to forget it, and it’s all in good time. We’re going to go after these problems just like a high-school wrestler goes after a match: we’re going to take them down one at a time.”

Recent intelligence agency discussion of Al-Qaeda’s apparently reduced role as the global sponsor of terrorism signals a return to public enemy number one status of Hizbollah – a genuine organisation with a territorial base, leadership and relationships with states, whose victory over an enemy, Israel, was marked by then premier **Ehud Barak**’s withdrawal from southern Lebanon.

A US-sponsored assault on Hizbollah would add further complications to relations with Iraqi and other Shia groups.

IRAN: The “Long-term Threat”

The signals, as ever, crossing between Washington and Tehran are mixed. Press reports focusing on WMD and Pentagon views suggest a new conflict is imminent. But these are tempered by a range of other indicators and, unlike Iraq, ongoing diplomatic efforts by US allies, led by the UK.

There have been leaked reports from Tehran of a mid-March “secret meeting” in Geneva between Iran’s UN Ambassador **Mohammad Javad Zarif** and President **George W Bush**’s Special Envoy **Zalmay Khalilzad**. This may have helped to set out the terms of Iran’s “active neutrality” in the conflict.

Iranian officials have sought to take the heat out of the war – even while tempers have been boiling in Tehran (*See page 1*).

Foreign Minister **Kamal Kharrazi** said that any US or Iraqi missiles hitting Iranian territory would be a “natural” consequence of the war. Government spokesman **Abdollah Ramezanzadeh** sought to take the heat out of US claims that Iran was trying to get its proxies into Iraq by saying that Iran would stop Iraqi Shia **Badr Brigade** fighters from crossing the border until the end of the war.

Iran surprised the US government by turning back fleeing **Ansar Al-Islam** fighters, who had

been pulverised by air strikes, from its borders. **Ansar Al-Islam** fighters – whose alleged links to **Al-Qaeda** were seen as a potential ‘smoking gun’ by the USA prior to the war – were sent back to their fate in Iraqi Kurdistan.

Most tantalising of all, in an interview published on 12 April, former president and Expediency Council (EC) Chairman **Ali Akbar Hashemi Rafsanjani** suggested holding a referendum on relations with the USA. In the EC’s periodical *Rahbord (Strategy)* Rafsanjani said the plebiscite was a step to resolving the two countries’ problems, and would have to be approved by the Majlis (Parliament) and Rahbar (Supreme Leader) Ayatollah **Ali Khamenei**.

Rafsanjani also said that the issue of relations with **Egypt** should be reopened. Like the USA, ties were suspended after 1979, although Egypt has maintained a more formal presence in Tehran since then.

That most supple of Iranian clerical politicians, Rafsanjani, hinted that the leadership was ready to show flexibility on these issues, observing: “We missed certain opportunities, or took late or wrong measures, or even did not take action... Our ideology is flexible. We can choose our interest based on Islam.” But in Washington, Iran is seen as an enduring threat.

NUCLEAR BREAKOUT

Although Iran has maintained its expected policy of “active neutrality” over war in Iraq, Tehran has taken what US officials see as uncompromising steps towards nuclear capability.

Under *Atomic Energy Agency of Iran (AEOI)* Chairman **Gholamreza Aqazadeh**, a former oil minister known for his ability to implement projects, the Islamic Republic has made great strides in its nuclear industries.

Recent revelations by an unreliable source, the *Mojaheddin-e Khalq Organisation (MKO)*, allowed for open-source discussion of something that intelligence agencies had been aware of for months – that Iran had developed uranium enrichment facilities.

The significance of this development is that Iran

Iran’s LEU drive

Iran’s stocks of low-enriched uranium LEU began with 2,000 tonnes of natural uranium provided by **Russia** under the January 1995 protocol. Russia has also provided assistance to Iran’s uranium mining efforts in Yazd province, where 5,000 tonnes of natural uranium was discovered in 1985 – a relatively large deposit for the Middle East. Since then Russia’s *Minatom* and **China**’s *Beijing Research Institute for Uranium Geology* have modernised the primitive Iranian mining efforts found there in the 1980s. Iran has since developed the ability to mill small amounts of uranium ore into yellowcake, the vital precursor required to fabricate fuel for heavy water reactors. A lab-scale fuel fabrication centre and large-scale uranium mill have been set up at Tehran University’s *Tehran Nuclear Research Center (TNRC)*, although this is non-operable according to the *IAEA*.

Israel's Powerful Friends

Israel has some powerful friends interested in Iranian WMD. Under-secretary of State for Arms Control and International Security **John Bolton** – State's best-known hawk – is considered "a great friend of Israel" by Israeli officials in Washington, as is Assistant Secretary of State for Counter-proliferation **John Wolf**. Of Bolton's other two deputies, Assistant Secretary of State for Verification and Compliance **Paula DeSutter** is known for her work on deterring Iranian use of WMD, while Assistant Secretary of State for Arms Control **Steve Rademaker** – married to senior **American Enterprise Institute** member **Danielle Pletka** – drove Iranian missile proliferation legislation throughout the 1990s.

In combination with the hawks in **Elliot Abrams'** Middle East section of the National Security Council, these personnel are likely to press for an aggressive line that goes beyond bolstering the US presence in the Gulf, supporting military technology transfers to Gulf states and extending a US nuclear guarantee to regional allies.

is displaying its capability to operate an independent or 'closed' nuclear fuel cycle. While previously, US counter-proliferation policy might have slowed or prevented Russian development of the Bushehr 1 and 2 light water reactors and the shipment of Russian fuel, Iran has shown that it has developed a parallel programme that utilises fuel sources found within Iran – both low-enriched uranium (LEU) from small light water research reactors and mined and milled uranium ore.

This considerably complicates US counter-proliferation policy, forcing it to consider both possible routes for nuclear breakout.

According to recent satellite images showing a heavy water plant under construction at Arak, Iran appears to be laying the foundations to develop a heavy water reactor, which would require a reprocessing plant to separate out the plutonium.

The USA maintains a broad range of military and non-military counter-proliferation options to meet this threat. Russia could be convinced to abandon the Bushehr project, fresh and spent fuel could be confiscated or interdicted in transit, and in the worst case – as with Iraq's Osiraq reactor in 1982 – a stand-off air strike would have little problem in destroying the highly visible and fixed infrastructure of any heavy fuel reactor and plant.

To comb out the weapons grade plutonium from the spent fuel, Iran would have to develop a reprocessing plant, which would be hard to conceal due to its distinctive isotopic signature, making it relatively simple to strike. If identified by the USA, this site would legally be required to be under *International Atomic Energy Agency (IAEA)* supervision.

According to Israeli intelligence officials canvassed by *GSN*, if military or intelligence action were to be undertaken against this route, the optimal time would be before the likely fuel changeover in 2005, when both cooling spent fuel and arriving Russian fuel would be on Iranian soil.

Interdicting the LEU enrichment route offers far fewer possibilities for diplomatic resolution, as well

as a more distributed target set. Aside from the high-profile site at Bushehr, there are a number of light water reactors already in Iran that would need to be attacked – others may have been concealed – yet most present a sensitive target, located in universities.

Iran's uranium mines (*see box*) would also need to be deactivated. As *GSN* has suggested before, however, the key nodes would be Iranian enrichment facilities (*GSN 689/MEI*).

The main identified site is the Nantanz facility, which has 160 functioning centrifuges in a pilot facility, while 1,000 more centrifuges are being assembled in another building that is planned to hold 5,000 centrifuges.

Depending on the capacity of the machines, the facility when completed in 2005 could produce enough highly-enriched uranium for two or more nuclear bombs per year. Other facilities may exist. Although these types of facility are often visible due to their high consumption of electricity, they can be concealed.

THE USA WANTS REGIME CHANGE

The USA could only – and would only – engage in pinpoint strikes against Iranian facilities if faced with no other option, and there is no realistic prospect of any other form of military action against Iran.

As one senior *Defense Intelligence Agency* official told *GSN*, if the Iraq conflict had shown anything, it was that there are definite limits on US military power. The DIA official confided: "I shouldn't really say this, but a land campaign in Iran is now in the 'too hard' category."

Even ultra-hawks like **Michael Ledeen**, the leading proponent of a "wider war" involving Iran, instead propose political steps to effect regime change (*GSN 704/12*).

In keeping with the hopes of Israeli officials canvassed by *GSN*, Iran is seen as "ripe for counter-revolution". This is put in the politically correct context of a counter-proliferation effort in which any new government followed **Nelson Mandela's South African** example and chose the benefits of relinquishing its pursuit of nuclear weapons.

US officials are generally less sanguine about the prospect of near-term regime change and there is growing concern that preventative action will one day have to be taken to slow Iranian nuclear progress until regime change occurs.

SYRIA: More Than An Irritant?

Until President **George W Bush** decided the time was ripe to suggest that Syria might have chemical weapons, President **Bashar Al-Assad's** recent hostile approach to the USA was regarded by many in Washington as haphazard and limited to the near-term issue of **Iraq** policy.

Assad has been seen as an advocate of modernisation in his country, if a moderniser still

in the thrall of a reactionary old guard (*GSN* 690/3). In making Syria the most vocal Arab critic of US policy in Iraq he has caught the public mood – but the Arab street does not punch the weight of a Pentagon hawk, and Assad is now under intense pressure, as are his supporters in the West.

Syria has been accused by the USA of a host of active and passive activities aimed at prolonging the war and preventing the coalition from achieving its political objectives.

Assad's policy of opposition and provocation provoked a major dispute in Washington, with hawks measuring up Syria for the slot now becoming available in the "Axis of Evil".

Until mid-April at least, the State Department and moderates such as **Condoleezza Rice** – still a powerful voice in swinging Bush's opinions – argued that Syria's policy was the result of young Dr Bashar's inexperience and miscalculations. This was shaped by Syria's broader strategic encirclement by **Israel**, **Turkey** and now a US-occupied Iraq.

There were threats from the OSD, where **Donald Rumsfeld** noted: "Whatever the game Syria is playing, it must stop for Syria's sake, the sooner the better."

According to Deputy Secretary of Defence **Paul Wolfowitz**: "There has to be a change in Syria. I think a lot of countries, including Syria, will eventually get the message from this war that it's much better to come to terms peacefully with the international community, to not acquire these weapons of mass destruction, to not use terrorism as an instrument of national policy."

Such statements were threatening with the Pentagon speedily dismembering the neighbouring **Baathist** regime – particularly since the OSD was reacting to perceived direct Syrian intervention in military operations. It could become alarming if reports that senior Iraqi Baathists have sought refuge in Syria were confirmed.

Reports from Mosul on 14 April that surrendering **Special Republican Guard** General **Ali Al-Jajawi** had talked of senior Baathists going to Syria added to the mood of tension.

Looking on is Israel. Those who fear that "Syria will be next" point to the huge influence over recent events of OSD figures such as Wolfowitz and Under-secretary **Douglas Feith**, plus members of the Defense Policy Board and **American Enterprise Institute**, all of whom played key roles in pushing a closer strategic alliance between the USA and Israel during the **Clinton** Administration.

The pressure on Damascus provides an early marker card as a new round of the Middle East peace process beckons.

When *GSN* spoke to Syria's Ambassador to the USA **Rostom Zoubi**, the strain was clearly showing. Confrontation with Syria "would not serve the interests of the USA", Zoubi said. OSD statements were "accusatory foreign policy".

SYRIA: Five Reasons To Be Scared

Five key issues are being closely monitored in Washington:

- **RESUPPLY:** **Donald Rumsfeld** has again claimed that the Mosul-Aleppo railway was a key resupply route for the **Iraqi** military. Although Syria is accused of supplying night-vision devices to **Iraq**, no such devices have yet been discovered by Coalition forces. Syria has reportedly ceased new shipments of major equipment – such as earth-moving vehicles with possible military utility – but **US** officials are less sure regarding smaller military items.

- **ESCAPE ROUTES:** The Syrian border is being closely watched as an escape route for **Baathist** leaders or WMD. Many US officials (doves as well as hawks) believe that leaders, their families, and funds have already been transferred to Syria. One report said **Saddam Hussein's** wife **Sagida** had transited through Syria on her way to a third country. Checkpoints were placed on roads between Baghdad and Syria by Coalition special forces and some vehicles – including the **Russian** Ambassador's car – were attacked. General **Ali Al-Jajawi's** claims added to the pressure, after former interior minister and Saddam's brother-in-law **Watban Ibrahim Hassan** was captured north-west of Mosul trying to get to Syria.

- **VOLUNTEERS:** With Iraqi spokesmen claiming that 6,000 foreign volunteers had entered Iraq to defend the Baathist regime before Baghdad fell, the Syrian border has been closely monitored and is officially closed. **UK** intelligence and special forces said 600 volunteers had crossed from Syria and up to 1,400 others had been issued exit visas for Iraq. Rumsfeld said Syrians made up the biggest group of volunteers – some of whom have been intercepted by **UK Special Air Service (SAS)** and US troops. The signs are that some volunteers are prepared to fight on.

- **PIPELINES:** Coalition forces in the southern oil fields surrounding Basra turned off oil pipelines leading to Syria. Damascus has advised its oil clients to expect much lower loadings in April and May, with state oil marketer **Sytrol** telling clients that export volumes for full-year 2003 would be cut by 40%.

- **SCUDS AND WMD:** The Al-Qaim area near the Syrian border was a key Scud launch basket, drawing Coalition special forces and airpower to the area. Washington decision-makers fear that Scud missiles and WMD may have been transferred to Syria. A major battle to take facilities in Al-Qaim went on through the three weeks of the war before and after Baghdad fell as US marines, SAS and other coalition forces battled **Special Republican Guard** units.

Such allegations triggered a major State Department effort in early April, when Secretary of State **Colin Powell** ruled out the possibility of attack, stating that "nobody in the American Administration [has] talked about invading Iran or Syria." Powell's close friend and Deputy, **Richard Armitage**, also played down the Syrian connection.

Hawkish Under-secretary of State for Arms Control and International Security **John Bolton**, also took a moderate line, arguing: "I think Syria is a good case where I hope that they will conclude that the chemicals weapons programme and the biological weapons programme that they have been pursuing are things that they should give up... It is a wonderful opportunity for Syria to foreswear the pursuit of weapons of mass destruction and, as with other governments in the region, to see if there are now new possibilities in the Middle East peace process."

Qatar's Consensual Politics Complement And Clash With 'War On Terrorism' Thinking

While Qatar's leaders are pushing for a big vote in the planned 29 April referendum on a new Constitution – a local event of major proportions to distract Qataris from events in Iraq – some US officials are still asking about some senior Qataris' commitment to 'liberal' values.

While his ministry (and junior minister) arranges the constitutional referendum, Interior Minister **Sheikh Abdallah Bin Khalid Al-Thani** is provoking more interest from Americans pursuing the 'war on terror'. Like his father who held the same job, Sheikh Abdallah comes from the devout Wahhabi wing of the Qatari ruling establishment – an influential but not dominant, group. Even one of the Emir's sons, **Sheikh Fahd Bin Hamad**, is said to have surrounded himself with Arab 'Afghans'.

US officials have accused Sheikh Abdallah of assisting *Al-Qaeda* fugitives, notably **Khalid Sheikh Mohammed**, who fled from Doha on the eve of his planned extradition to the USA by the Qatari authorities to seek shelter in **Afghanistan** and **Pakistan** – where it is widely believed he organised the 1998 US embassy bombings in **Kenya** and **Tanzania**, the 9/11 attacks on New York and Washington, and last year's Djerba, **Tunisia** synagogue bombing (*GSN 698/3*).

In the run-up to war in Iraq, official Washington played down these claims – which are so far unsubstantiated (*GSN 704/20*). Sheikh Abdallah remains interior minister but the questioning persists, with the *Los Angeles Times* alleging he provided shelter for Sheikh Mohammed in an article quoting former *CIA* agent **Robert Baer**.

Former White House counter-terrorism director **Richard Clarke** – who recently left the **Bush** Administration – also appeared familiar with the allegations, saying Sheikh Abdallah (who was minister of Islamic affairs in 1992-96) "had great sympathy for **Osama Bin Laden**, great sympathy for terrorist groups, was using his personal money and ministry money to transfer to *Al-Qaeda* front groups that were allegedly charities."

In February, the *New York Times* linked another member of the ruling family, **Abdul Karim Al-Thani**, to senior *Al-Qaeda* operative **Abu Mussab Al-Zarqawi**. Qatar has also been accused by **Russia** of sheltering Chechen hardliners (*GSN 700/5*).

The peninsula undoubtedly houses Islamist sympathisers within a staunch Wahhabi trend represented by Sheikh Abdallah. But does this mean Qatar is a hub of activity in the 'war on terrorism'?

In two important but very different respects it is. Ruler **Sheikh Hamad Bin Khalifa Al-Thani** has let the US base its Iraq war headquarters in his country, where *Central Command (Centcom)* Commander General **Tommy Franks** is also running operations in Afghanistan. And Doha is the media hub of this war, as home of *Al-Jazeera Satellite Channel*, a defining voice since 9/11.

These observations highlight Qatari ambiguities that mark out the peninsula as one of the Gulf region's most difficult corners to understand.

In a society – and ruling Al-Thani family – where consensus and co-option govern social and political actions, Wahhabi radicals co-exist alongside westernised elements. The latter is reflected in Sheikh Hamad's domestic liberalisation programme, which took a further step forward this month with Qatar's second municipal council election. One seat was won by a woman.

The explanation for such paradoxes lies in the regime's family-based nature and the negotiated balancing of diverse Al-Thani interests that is required to ensure the state can continue to function through consensus rather than force.

These factors are especially sharply felt in a country that has a national population of perhaps only 150,000, where the significance of personal relationships has not been overly diluted by an international business culture. The presence of senior Al-Thanis and their allies in the economy and government is ubiquitous.

The government has gone out of its way to position Qatar as a diplomatic bridge-builder, maintaining relatively good relations with **Saddam Hussein's** regime in Baghdad even as it was discussing the development of the US military facilities from which the war to depose the Iraqi *Baathists* would be run.

SO MUCH TO DO, SO FEW AL-THANIS TO DO IT

Sheikh Hamad has begun to move his country towards democracy – underlined by a new Constitution that recognises the need for staged change (*see box*). But he heads a regime in which the concentration of power in family hands has been subject to minimal challenge and critique.

A regular complaint about *Al-Jazeera* is that the one government it spares of criticism is Qatar's.

Al-Jazeera journalists say Qatar is too small to bother with – a disingenuous argument given the Emirate's full diplomatic agenda and spicy politics.

This spicy politics is personified by Foreign Minister **Sheikh Hamad Bin Jassim Bin Jabir Al-**

Qataris To Vote On Constitution, Reshaping Al-Thani Rule

Emir **Sheikh Hamad Bin Khalifa Al-Thani** on 15 April urged Qataris to vote in a 29 April referendum on a draft Constitution that will grant legislative powers to a 45-member Shura (Advisory Council), regulate ruling family affairs and lay out a separation of powers in a significant step towards democratisation in the **GCC** region. Once voted in, the Constitution is not open to amendment for a minimum period of ten years.

The Emiri decree – of which details and an unofficial translation were published in the Doha daily *The Peninsula* on 15 April – provided for the formation of a Public Referendum Committee to supervise the plebiscite and announce the result; this will be under State Minister for Interior Affairs **Sheikh Hamad Bin Nasser Al-Thani**.

Some 30 members of the 45-member Shura will be elected by the citizens aged 18-plus and 15 members will be appointed by the Emir. They will serve a four-year term. The Shura will have the right to propose laws, and will set up specialised sub-committees to study them. It will also approve the State Budget – and will be able to question the prime minister and ministers on it. Pointing to the Shura's potential to develop as a genuine parliament, ministers will have to hold themselves responsible to the Council for the functioning of their ministries.

The Constitution will vest executive authority with the cabinet, to be headed by a prime minister. The Council of Ministers and Cabinet will have the right to propose legislation. The Cabinet will be formed by the Emir – signalling the Al-Thani family's continued primacy, albeit under new checks and balances. The Constitution also lays down the foundation for an independent judiciary, stipulating that no other agency has the right to interfere with the judicial process. Islamic Sharia law remains the main source of Qatari legislation.

The Emir is not voting himself out of a job – and the Constitution enshrines the Al-Thani's leading role. Article 8 states: "The Rule of the State shall be hereditary within the Al-Thani family and by the male successors of **Hamad Bin Khalifa Bin Hamad Bin Abdallah Bin Jassim**. The inheritance of the Rule shall go to the son to be named by the Emir as Heir Apparent. If there is no male offspring, the Rule shall be transferred to the one from the family whom the Emir names as Heir Apparent and, in this case, the Rule would then be inherited by his male successors. A special law shall organise all provisions related to the ruling of the State and its inheritance, to be issued within one year of the date of this Constitution coming into force, and should have a Constitutional validity."

Once approved by the Shura, laws must be endorsed by the Emir. But he will have to give reasons for rejecting a draft law submitted by the Council – and he must approve the law if it is sent to him a second time by the Shura with a two-thirds majority support. The Emir has the right to stop implementation of such a law for a period if he believes it is in the country's greater interest.

The Emir has the right to dissolve the Shura, but not without giving his reasons for such an action. The Council cannot be dissolved twice for the same reason – potentially giving it some power over the Emir in standoffs to come. Pointing to another potential area of conflict as the Shura develops its teeth, no-confidence motions can be moved against a minister with an application signed by at least 15 Shura members; it would be carried with a two-thirds majority.

The Constitution also provides for the creation of an Al-Thani Ruling Family Council. Among its tasks will be to decide who rules in the event of the Emir's death or disability. A Council of Guardians would be formed to manage Emiri functions should the heir apparent not have reached the age of majority (18).

Thani. A major Al-Jazeera shareholder, Sheikh Hamad Bin Jassim made headlines in the UK by persisting with legal action in Jersey to block media coverage of an embarrassing official probe into business payments made to a personal trust held in the Channel Island. He finally abandoned his appeal and was rewarded with a typical write-up in the 4 April issue of the widely-read satirical fortnightly *Private Eye*.

The paradoxes that characterise Qatar are partly a reflection of its struggle to adapt to the changing global environment and develop some fresh thinking. Such enterprises inevitably risk the occasional misjudgement, especially when the entire burden of policy thinking falls on the shoulders of a few hundred senior officials at most.

Their task is complicated by the need to cultivate the international alliances through which Qatar can find security. Sheikh Hamad cannot forget that, just a year after peacefully deposing his father, **Sheikh Khalifa Bin Hamad Al-Thani**, he was threatened with a serious putsch attempt that enjoyed the tolerance of powerful conservative elements in Saudi Arabia.

Parts of the new Constitution can be read in this light. Article 147 says: "The authority of the Emir... shall not be discussed for amendment

during the period when someone else is deputising for him."

The *Gulf Co-operation Council (GCC)* does not really provide protection against the potential threats about which Qatar is most concerned. In the leadership's eyes, effective security has to come from the close partnerships developed with France, the UK and USA.

POWERFUL FRIENDS, DOMESTIC RIVALS

In allowing the USA to transform Al-Udeid into a major airbase and Camp as-Sayliya into the command HQ for the Iraq war, Sheikh Hamad has publicly demonstrated his commitment to the alliance with Washington, at the price of further annoying the Saudis and local Wahhabi opinion.

Lining up with such powerful friends has bought Sheikh Hamad a measure of room for manoeuvre and compromise in dealing with domestic pressures, particularly within the family and religious leadership. His father, Sheikh Khalifa – although very much a liberal in his personal lifestyle – had indulged a powerful hardline conservative clique within the ruling family.

Interior Minister Sheikh Abdallah's father, **Sheikh Khalid Bin Hamad Al-Thani**, oversaw an influx of fundamentalist fugitives from Saudi Arabia after the violence at the Grand Mosque in

Mecca in 1979. Abdallah Bin Zaid Al-Mahmoud, from the Saudi Wahhabi heartland of Najd, was appointed as senior imam.

After seizing power in 1995, Sheikh Hamad began gradually to steer Qatar back towards its more relaxed indigenous traditions, opening up new social freedoms and political rights for women. In the municipal elections, **Sheikha Al-Jufeira** became the first woman in a Gulf monarchy (Oman excepted) to be elected to office.

But rather than confront his father's erstwhile supporters within the family, the Emir has sought co-opt them and reconcile hardliners around a new consensus. Consequently, he appointed Sheikh Khalid's son – Sheikh Abdallah – as Minister of State for the Interior in 1996, promoting him in 2001 to the full ministerial post his father had held almost two decades before. In this way, the Al-Thanis' voice of conservative Islamism has been kept "inside the tent".

Sheikh Abdallah has not been allowed to block the wider liberal drive of domestic policy. But it appears he has been accorded a degree of freedom to indulge radical friends from abroad.

TRoublesome Consensus

This unspoken arrangement is the result of his consensual approach to governance. Qatar's Emir seeks to advance reform through top-down but gradualist and low-key leadership, reflecting the need to accommodate Islamist sympathisers among the Al-Thanis while following a pro-Western, liberalising policy.

In taking this approach, Sheikh Hamad has left himself heavily reliant on the ebullient figure of his high-profile Foreign Minister. The complications of running Qatar as a "family firm" are epitomised in the multiple roles played by Sheikh Hamad Bin

Jassim – who was close to the Emir before he took power and remains among his closest advisers on foreign affairs, political reform and media policy.

Sheikh Hamad Bin Jassim finds himself defending media freedom and the government's refusal to control Al-Jazeera's often controversial output even while, as a private investor, he retains a substantial shareholding in the TV station. His paradoxical personal situation has impeded Doha's attempts to calm Saudi anger at Al-Jazeera's coverage of the Kingdom – and criticism of Sheikh Hamad Bin Jassim has been personalised in the Saudi media to an unprecedented extent for a senior GCC official.

In the Jersey case – where he eventually abandoned attempts to block the *Jersey Evening Post* from reporting on the probe into arms company payments into *Grindlays Trust Company* accounts on the island – Sheikh Hamad Bin Jassim presented himself as a private citizen, whose business relationships were not in conflict with his position as a minister.

Outside the family, Emir Sheikh Hamad has had to accommodate some local unease at the US use of his country as a base for the war on Iraq. He has been careful to allow a degree of space for prominent moderate Islamists such as influential Qatar-based Egyptian scholar Yusuf Al-Qaradawi, who is Dean of the *College of Sharia and Islamic Studies* and commands an audience across a diverse spectrum of international Muslim opinion.

Qaradawi was quick to condemn the 9/11 attacks on innocent civilians as a "grave sin" and the Bali bombing as "total barbarism". But he also publicly opposed the war against Iraq, warning that "by opening our ports, our airports and our land, we are participating in the war".

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As ever, we look forward to to hearing your comments on *Gulf States Newsletter* and its sister publications.

—JON MARKS, EDITORIAL DIRECTOR

Business, Multilaterals Will Look To Shape Of Post-War Administration in Iraq

Diplomatic skills are being tested as rich donor nations attempt to reach agreement over a future path for the reconstruction and governance of Iraq. It will be that path as much as anything else that determines business prospects for the nation.

The challenge is as much political as it is practical. Failure to secure consensus on an institutional framework could cripple prospects for the post-Saddam era, weakening any new administration's legitimacy and diverting attention and resources away from the serious development problems to be overcome.

But ensuring the legitimacy of the Iraqi interim authority could accelerate the process of rebuilding and reform, bring in more aid and investment and go some ways towards healing the diplomatic wounds left by pre-war rifts in the *United Nations*.

Iraq faces massive problems – political uncertainty, major social and humanitarian challenges, a damaged physical and institutional infrastructure, a crushing debt burden, limited short-term cash resources and the long-term challenge of economic diversification and reform.

But it also has considerable assets. With possibly the world's second-largest oil reserves, and low production costs, it is assured of long-term economic viability if those assets can be honestly developed and exploited. At home and among the 4m Iraqi exiles – of a national population estimated at 24m – there is a large pool of educated personnel trained in modern technical skills.

Because of its suffering and its strategic importance, Iraq can call on a deep well of global goodwill and practical support – provided that agreement can be reached over the role of the UN and the international development system.

SETTLING THE INTERNATIONAL FRAMEWORK

There is no secret about the deep rifts between Europe and the more conservative elements of the US Administration over the role of the UN and the Bretton Woods institutions.

In order for those rifts not to hold up or delay reconstruction, a balance will have to be achieved between the Pentagon's reconstruction team and the interim Iraqi authority that would be formally backed by the Security Council.

It is the presence of an internationally recognised interim authority that will be most crucial to mobilising outside funds.

Pentagon hardliners feel the victors of the war

should set the ground rules for the new Iraq. Their version of the "vital" UN role promised by President **George W Bush** is essentially to provide humanitarian aid and to endorse the interim authority chosen by Iraqis under US guidance. But there is room for manoeuvre in Washington.

The State Department and significant players on Capitol Hill – such as the moderate Republican Senate Foreign Relations Committee Chairman **Richard Lugar** – prefer an approach in accordance with the international norms already established for other post-conflict territories, like **Afghanistan** and **Kosovo**, where the UN played a central role.

UK Prime Minister **Tony Blair** has pressed Washington to accept that the UN role should be genuinely important and extend beyond the humanitarian sphere into that of political authority.

At the same time, Blair has sought to win over sceptics such as **France**, who feared that unquestioning UN approval of the interim Iraqi authority might amount to *post-facto* legitimisation of the war. The UK government view, articulated strongly by International Development Secretary **Clare Short**, is that the World now has a moral duty to help rebuild Iraq, regardless of pro- or anti-war views (*see box*).

The key to an agreement that both the USA and Europe will endorse to appears to be striking a balance between the Pentagon's *Office of Reconstruction and Humanitarian Assistance (ORHA)*, headed by retired General **Jay Garner**, and the interim Iraqi authority to be backed by the Security Council.

In the USA, ORHA has been widely presented as Iraq's post-war administration and the father of a new interim political structure – and, implicitly, the power behind the process of drafting a new constitution and setting up a permanent political system. This is reflected in the flow of contracts, such as the *US Agency for International Development (USAID)*-funded order to reopen schools from September, awarded to consultancy *Creative Associates International (CAII)*.

BRITISH PERSPECTIVE

But the UK has painted ORHA in a different light, as the agency for meeting the immediate post-war Geneva and Hague obligations of the occupying powers, the USA and Britain (who are legally enjoined to deliver civil order, basic administration and humanitarian essentials).

For the UK, the dominant role in the transition

Clare's Consensus

The mission of UK International Development Secretary Clare Short – who nearly resigned her post over reconstruction issues – is to reunify the donor community around a shared belief in the duty to rebuild Iraq. In the process, she hopes to make reconstruction contracts available to more than the few US firms hand-picked by Washington to bid on the job.

At the IMF/World Bank Spring Meetings in Washington, Short met with French, German and Nordic development ministers to explore the scope for a common approach. She sought out governments who had been central pillars of the bilateral aid effort in past crises – and who have a major voice on development issues in the European Union, itself one of the biggest post-conflict donors.

The British – pro-war but also pro-UN – effectively appear to be arguing that the best way to preserve the UN's standing is for the Security Council rapidly to endorse an interim authority in Baghdad. This would deny Pentagon unilateralists the opportunity to sideline the institution, and would also lend some discipline to the reconstruction's procurement process.

The British have made no secret of their annoyance at the Pentagon decision to pre-select favoured US bidders for a series of major contracts. At a 14 April London press briefing, Short pointed out that international organisations would insist that an interim Iraqi government follow proper tendering rules in procuring reconstruction and supply contracts.

will lie with the interim authority. The unspoken hope of the British is that ORHA will gradually fade into the background at the political level, leaving the interim authority to assume effective leadership. This model would be much more acceptable to Europe and the Arab world, and would allow the UN to establish itself gradually in a central role, as a key partner of the new authority.

TIME FOR A DONOR CONFERENCE

Once the immediate post-war instability has settled down, an early priority will be an international donor conference to assess reconstruction needs and mobilise funding pledges. It is at this stage that the question of international authority will become crucial.

The normal donor process – and the capacity of some players such as the EU institutions and the IMF and World Bank – would be crippled by the absence of UN Security Council authority for Iraq's interim government.

But if that political authority is in place, the experience of previous post-conflict situations suggests donors will be generous and that they can be flexible in devising the detailed institutional arrangements for delivering their cash.

LEVERAGING OFFP FOR IMMEDIATE NEEDS

At this stage, few donor officials feel able to put firm figures on Iraq's immediate post-war needs – or its long-term development requirements. And without a distribution system in place, there is little prospect of current aid stocks reaching those who need it most.

A temporary solution may be found in the Oil-

for-Food Programme (OFFP). A Security Council vote has already transferred to UN Secretary General Kofi Annan the OFFP spending powers previously vested in the Baghdad government; he has begun to authorise shipments under the OFFP, whose current phase has been extended for 45 days; but the normal six-month roll-over of the programme will have to be approved fairly soon.

Despite its name, the OFFP is authorised to fund a wide range of imports, and the procurement and payment mechanisms are already well-established. It could potentially be used to bring in equipment and spare parts for a broad range of infrastructure needs – even while sanctions remain formally in place. Last year's reform of sanctions simplified and speeded up the approvals process.

Although almost no financial data is available on the country, data on social conditions is available through the OFFP, but even this is patchy. Saddam's Iraq did not have a wide range of western non-governmental organisations (NGOs) on the ground, other than the Red Crescent/Red Cross. In Afghanistan, NGOs proved to be a vital source of detailed information on local social and development needs.

Immediate humanitarian needs are serious. Some 16m Iraqis are totally dependent on OFFP and many others are partially reliant on it. Just before the war, the 55,000 OFFP outlets in Iraq made a one-time release of a full two months' rations, which has assured most people of adequate essential supplies throughout the fighting.

But these will run out in weeks. Following last month's UN appeal for \$2.2bn in assistance, the UN Office for the Co-ordination of Humanitarian Affairs has substantial pre-positioned aid in the region, ready to bring into Iraq as soon as security conditions permit.

There are clear regional differences. Conditions are much better in the three northern governorates of the Kurdish autonomous zone, where the OFFP has been run in much closer partnership with the UN than was the case in Saddam-controlled Iraq. Saddam's regime frequently failed to take full advantage of the funding and procurement rights it held under OFFP, even for high-priority humanitarian goods.

Basic living standards and social conditions are far worse than during the 1970s, before Saddam launched his war against Iran. World Bank Vice President for the Middle East and North Africa Jean-Louis Sarbib has cited one estimate suggesting average per capita income may have fallen from \$3,700 in 1980 to \$1,200 in 2001. The impact of sanctions and Saddam's misrule over the past 13 years have also taken a toll.

Early Entry For The Paris Club

Early action from the Paris Club of bilateral creditors to alleviate Iraq's debt burden was one issue on which Europe and the USA were able to

agree last weekend, with US Treasury Secretary **John Snow** quietly dropping his demands for an immediate write-off.

The debt has been estimated between \$60bn and \$125bn or even higher. A large part is thought to be export credit owed to Paris Club governments, UK International Development Secretary **Clare Short** said this week. There are also substantial sums claimed by Gulf Arab states that supported **Saddam Hussein** during the war against **Iran**. The Washington-based **Council on Foreign Relations** has suggested \$55bn may be owed to Gulf governments (out of total debt of \$116bn), with \$25bn owed to **Saudi Arabia** alone.

On top of this, war reparation claims awarded in the wake of the invasion of **Kuwait** are projected to range as high as \$300bn, should the **UN Compensation Commission** continue to make awards on the same basis it has up to now.

However, there is universal recognition that Iraq could not possibly meet the burden that servicing all these obligations would imply. Western governments have already made public their readiness to contemplate big debt cuts, especially as most had written the money off anyway. Banks, who are expected to convene a London Club group can expect a big “haircut” on their debt obligations – of at least **Yugoslav** proportions.

The Arabs have been more reluctant. But it seems unlikely they would refuse to show similar generosity, provided Iraq recognises the debt in the first place, before it is reduced or cancelled. **Saddam Hussein** tried to repudiate it, claiming the money had been a gift.

As a first step, the Paris Club – which now includes **Russia**, the inheritor of the old Soviet Union’s debtor and creditor relationships – will initially try to clarify exactly how much the debt amounts to, and to calculate its theoretical value when allowance is made for unpaid interest. European governments would prefer simply to negotiate a big write-off.

The 70% debt-cut accorded to **Serbia** and **Montenegro** has been cited as a precedent. Once agreement has been reached on a face value figure, a task likely to take several months, it will probably hold talks with the interim Iraqi authority on a potential write-off.

IMF ROLE

The starting point will be an assessment by the IMF of Iraq’s ability to repay. That is sure to be extremely low initially, because OFP-funded imports of essential supplies will consume most export revenue, with one-quarter already earmarked for reparations claims.

Given Iraq’s oil assets, the IMF and European Paris Club members will

probably want to see Baghdad making some form of payment, however minimal.

Officials note that even poor African and Central American countries that qualify for the Heavily Indebted Poor Countries (HIPC) debt cancellation initiative have been expected to pay something, if only to preserve their financial credibility for the future.

Iraq, which will need to attract foreign investment and credit for oil and infrastructure projects in the relatively near future, has an even stronger incentive – after years of corrupt isolation – for pursuing this course. It will want to show foreign financial markets that it can again be a reliable partner.

THE REPARATIONS ISSUE AND ‘ODIOUS’ DEBT

On paper, the reparations issue poses a further dilemma, because of the damage wrought to so many lives in **Kuwait** and **Iran** by Iraq’s invasions.

However, most of the claims relating to individuals whose lives were damaged have now been dealt with – save for some of the missing Kuwaiti prisoners.

In political terms, therefore, it should be feasible to adjust the level of new reparation awards down to a symbolic affordable level.

Various methods for forgiving some debt have been mooted. The concept of declaring the debt “odious” and not liable for payment because it was incurred by a dictator will probably not fly.

This would open a Pandora’s box of cases in other countries that have moved from dictatorship to democracy, with the attendant difficulty of deciding which dictatorships had been so bad as to justify the “odious” classification.

Clare Short warned this week of the dangers of treating Iraq as **Germany** was treated after the First World War – when the fragile new Weimar Republic democracy was so burdened with penal reparation claims that it crumbled financially, opening the way for a new militaristic dictator, **Adolf Hitler**, to take power.

Gulf Currency Box

	\$	£	€	¥ (x 100)
Bahrain	0.3770	0.5916	0.4068	0.3167
Iran	8144.0	12,780.0	8788.19	6841.11
Iraq	0.3110	0.4881	0.3356	0.2613
Jordan	0.7095	1.1134	0.7656	0.5960
Kuwait	0.3000	0.4708	0.3238	0.2520
Oman	0.3850	0.6042	0.4155	0.3234
Qatar	3.6407	5.7132	3.9285	3.0583
Saudi Arabia	3.7502	5.8851	4.0467	3.1503
Syria	46.000	72.1855	49.6386	38.6409
UAE	3.6731	5.7640	3.9635	3.0855
Yemen	177.890	279.154	191.961	149.431

Source: *Financial Times*.

UAE Finance: DIFC Looks To Plug The Credibility Gap

The backers of Dubai's latest bid to world superstar status, the *Dubai International Financial Centre (DIFC)*, are gearing up to open their doors in earnest by end-May – by which time they expect the UAE federal authorities to have passed the requisite laws allowing the establishment of financial free zones.

But with just three financial institutions signed up so far, DIFC has a lot of convincing to do if it is to live up to its ambitions of rivalling the established global exchanges in New York, London, Frankfurt and Hong Kong (*GSN 689/10*).

DIFC's double act of Chairman **Anis Al-Jalaf** (also CEO of *Emirates Bank International*) and Regulatory Council chief **Ian Hay Davison** (a former *Lloyd's of London* chief executive) launched into London's prawn cocktail circuit in mid-April to proselytise the Emirate's case for becoming the region's missing financial centre.

With the combined muscle of Dubai's banking heavyweights behind it, DIFC appears serious about attracting world-class financial players.

DIFC has pitched for a slice of the burgeoning Islamic finance market, but its overall strategy is based on the five pillars of Mammon, rather than Mohammed, with the focus also on asset management, capital markets, reinsurance and institutional finance. It wants to set up a truly regional stock exchange that will allow major Gulf players to raise capital – and to get pension funds to base in Dubai and become a centre for syndication, whether project finance or interbank facilities.

Hay Davison stressed that Dubai was not looking to compete with the 29 other relatively illiquid regional exchanges. "We've got a regional, not a local ambition. We intend to be a financial hub licensing world-class players. There are 150 companies in the region as large or larger than *Emirates Airlines* with no local listing."

Reinsurance looms large in DIFC's plans. "Some of the top reinsurance companies are very keen to get on board once we've opened the doors, as reinsurance currently has no home in the region," said Jallaf. **Bahrain**, home of *Arab Reinsurance Group (Arig)*, may disagree with this.

The new focus on Islamic finance indicates a willingness to take on Bahrain, which itself is hyping its Islamic financial services excellence.

Previously, DIFC has played down suggestions that it is attempting to displace Bahrain as the region's key financial centre. But with its doors set to open and just three institutions on board – including *Deutsche Bank* and *Julius Baer* – the sponsors are giving Dubai a more aggressive push.

Jallaf indicated that DIFC was ready to take on all comers. "We're in competition with any market – though what we want to do is completely different to what anyone else in the Middle East is doing," he said. "We are not an offshore haven [like Bahrain]. We will tax – but at a rate of 0% fixed for 50 years."

DIFC's emergence is another sign of intra-emirate rivalry, with Dubai looking to score a victory to match Emirates Airlines' achievements over Abu Dhabi's troubled *Gulf Air*. After Abu Dhabi's failed Saadiyat Island initiative Dubai's leading financiers saw the chance to steal a march on their richer rival.

DIFC still awaits the final say-so from the Abu Dhabi-based federal authorities, but according to *Central Bank of the United Arab Emirates* Governor **Sultan Bin Nasser Al-Suwaidi**, they are relaxed – so long as it "keeps its hands off our dirhams".

One Abu Dhabi-based banker canvassed by *GSN* was sanguine about the impact on local banks. "It's an opportunity for the Emirates and we have to cheer the efforts that have been made. It's a case of coming to terms with globalisation – recognising the importance of accessing capital from foreign market."

Hay Davison said local banks had little to fear as DIFC would focus on wholesale banking and "there will still be a need for a local retail market". Jallaf promised there would be co-listings with the *Dubai Financial Market*.

Others are more sceptical, seeing DIFC as another Dubai "property play", designed to net rental yields off international financial institutions. DIFC's only source of income will be through rents.

CITY ON THE CREEK

DIFC's free zone status means it will be largely immune to federal regulation, with its own rules and regulatory agency. It will only handle dollar business and is unlikely to prove a recruiting ground for local talent.

Many fear DIFC is shaping up as an "English racket" with a string of former UK financial services industry worthies serving as regulators.

Hay Davison is adamant that it should have an Anglo-Saxon bias – which he regards as meaning an affinity with the financial centres of Hong Kong, London and New York, rather than a strictly **British** membership. "We have a polyglot membership of 30 experienced regulators," he said. The Regulatory Council's Chief Commissioner **Philip Thorpe** is a **New Zealander**. Managing Director of Supervision **David King** is a

Iran After Nourbakhsh Looks To Cut Oil, Bonyad Dependence

Even as he paid tribute to **Bank Markazi Jomhuri Iran** (Central Bank of Iran)'s respected Governor **Mohsen Nourbakhsh** – felled by a late March heart attack at only 54 – Finance Minister **Tahmasb Mazaheri** publicly committed the government to an audacious new reformist goal: everyday financial life without oil. Should Mazaheri make significant progress towards ending Iran's reliance on oil money to pay for routine expenditure he will have pulled off a feat that is rare indeed among oil exporting countries, especially those with large populations.

During the *International Monetary Fund (IMF)/World Bank* spring meetings in Washington Mazaheri announced that by the end of the Fourth Development Plan, in 2010, the Islamic Republic aimed to stop financing current public expenditure out of oil revenues. These will be reserved for capital projects and for the hard currency Oil Stabilisation Fund. That timetable gives the government less than seven years to build up alternative sources of fiscal revenue. The self-denying new policy can almost certainly only be applied if the authorities also engage in a controversial pruning back of the subsidised credit that sustains a host of enterprises and programmes – euphemistically described by the IMF in a recent report as “quasi-fiscal activities” (QFAs).

NOURBAKSH'S LEGACY

Nourbakhsh was often portrayed as the apostle of economic reform in the Islamic Republic, a man surrounded by “left-wing” colleagues who were less committed to the transformation of its statist financial and economic structures into a competitive market system. But this characterisation may have been too simplistic. There was undoubted personal rivalry between Nourbakhsh and Mazaheri, and it is rumoured by some that parliamentarians were plotting to force the Governor's removal well before his untimely death. But the central issue seems to have been not intellectual disagreement but power and the struggle over which man, and which institution, had the ultimate say over economic policy.

Under Nourbakhsh – who had already served once as Governor in the 1980s and then spent six years as finance minister – Bank Markazi had grown into much more than a technical reserve bank. It had a big say in shaping policy and the reform agenda – and, beyond its monetary functions, a significant direct economic role as a provider of QFA financial support to many areas of the Iranian system. There is no doubting the impressive reform track record of the late Central Bank Governor. He was pivotal in successfully abolishing the massively subsidised official exchange rate last year, and establishing a unified and economically credible market value for the riyal. The exchange rate has withstood even the confidence shocks of war in **Iraq** and his own sudden death at a time of regional conflict.

Nourbakhsh was a key architect of Iran's determined pursuit of financial credibility, climbing away from the humiliation of trade debt rescheduling a decade ago and culminating in the successful launch of

two major euro-denominated bond issues, in the teeth of US sanctions and attempts to talk the issues down. After his death, the IMF praised Nourbakhsh's role in steering Iran towards greater financial transparency. In 2002 the Islamic Republic invited the IMF to carry out a Report on the Observance of Standards and Codes – a technical Fund exercise that nevertheless risked producing controversial results. The resulting recently published Fund report has pointed up shortcomings in government budget systems and financial planning – and also began to expose the politically important bonyad foundations to public scrutiny.

BONYADS UNDER SCRUTINY

The bonyad foundations have acted as holding vehicles for assets abandoned by members of the overthrown regime of **Shah Reza Pahlavi** in 1979. But they have also taken on a vast array of charitable and economic activities, and benefited from a host of financial privileges, such as access to cheap credit and, until recently, exemption from income tax. They are now being subjected to the same tax regime as other enterprises.

The new IMF report reveals that the biggest and most diverse foundation, ***Bonyad Mostazafan va Janbazan (BMJ) – the Foundation of the Oppressed and Injured***, which was set up on the orders of **Imam Khomeini**, has a turnover of \$3.5bn. Its public credit institution, which provides soft loans to the self-employed, holds \$400m in public deposits. BMJ provides social assistance to the families of 140,000 war veterans. It has 60,000 employees and is active in six economic sectors; its affiliated companies operate on a commercial basis. BMJ is a significant investor on the ***Tehran Stock Exchange***.

But the accountability of BMJ and other bonyads is patchy. Their business enterprises – at least 498 in number – are subject to public sector audit procedures and consolidated data on these is presented to parliament, while the full reports go to the Supreme Audit Court (SAC). However, audit reports on the non-business activities go only to Rahbar (Supreme Leader) **Ayatollah Ali Khamenei**. Neither the government, headed by President **Mohammad Khatami**, nor the Majlis (Parliament) sees these documents.

For its new report, the IMF was invited to carry out an apparently technical exercise that was certain to open up delicate questions about the role of the bonyads and their relationship to Khamenei. This required real political courage on the part of the government. Given its far-reaching implications, the exercise must have been allowed only with Khatami's express authority.

Mazaheri has been closely associated with the reformist approach. His ministry was a prime interlocutor of the IMF mission. Now he has seized the occasion provided by a conference held in Nourbakhsh's memory in Washington during the Spring meetings to loudly reiterate the government's commitment to reform and set out the brave goal of ending reliance on oil for current spending.

former ***London Metal Exchange*** chief executive; other key regulators **Robert Owen** and **Michael Blair** are also British. Hay Davison is interviewing retired English High Court judges to preside over DIFC's internal judicial authority.

With the Chairman of the DIFC Stock Exchange due to be announced imminently, the smart money is on another City appointee. One banker quipped: “There'll be no Johnny Foreigner here!”

Indeed, Anglo-Saxon jealousies could yet break out. Said one US-based ratings agency source: “I'd feel a whole lot more comfortable if they were packing the regulatory council with a bunch of guys from the [US ***Federal Reserve***] Fed rather than the [UK ***Financial Services Authority***] FSA. The FSA guys aren't the sharpest tools in the box.”

DIFC's progenitors recognised from the outset that Dubai's reputation for money-laundering necessitated a strong regulatory push. Much has been done, yet qualms remain about stuffing DIFC's Regulatory Council with former City heavyweights – hired by a board of directors that just happens to comprise the cream of Dubai's banking fraternity.

But woe betide those who bet against the Al-Makhtoums. Dubai's track record at making major projects work against the odds has confounded sceptics before. DIFC's focus on back office and reinsurance may give it a specialisation that other financial centres lack. DIFC needs to get a few more credible players signed up if it is to live up to the prodigious hype.

GSN Risk Grade – B+/2: Post-war dividends for commerce, gradual move to representation

Political And Social Development

Overview: The Emirates remained an oasis of stability throughout the war and have been a high-profile provider of humanitarian aid to Iraq. Now, the UAE will want its voice to be heard in shaping post-Saddam Iraq. There are signs of a gradual democratisation in a society where wealth oils a high degree of consensus, but the Emirates' rulers will dominate for the foreseeable future.

Security: The UAE remains one of the region's safest countries despite increased travel warnings from countries such as the USA, UK and Australia in the run-up to war. There has been no major public anti-American backlash (although product boycotts are in vogue), while the authorities have worked hard since 9/11 to combat terrorist financing and remain attractive to investors. With the September World Bank/IMF meetings looming large in the minds of the Al-Makhtoums, Dubai has undertaken a big crackdown on crime and links to radical Islamist cells, Gulf smugglers and Indian mafia dons. The ongoing four-month amnesty for illegal immigrants is a convenient way to get rid of unwanted elements; the authorities have promised to come down hard on those who do not take up the amnesty.

Government: The UAE is behind other Gulf countries in pushing forward democratisation reforms. Women have yet to be included in the 40-member Federal National Council – an appointed advisory body that is the UAE's nearest thing to a parliament. This was despite promising noises from UAE President Sheikh Zayed Bin Sultan Al-Nahayan's influential wife Sheikhha Fatima Bint Mubarak, and the rulers of Sharjah and Ras Al-Khaimah. RAK has announced plans for its FNC members to be elected, while Dubai – following a lead set by Sharjah – has set up an advisory Dubai Executive Council, chaired by powerful Dubai Crown Prince and UAE Defence Minister General Sheikh Mohammed Bin Rashid Al-Makhtoum.

External factors: Relations with Western countries remain close, but the UAE will continue to lobby behind the scenes about the urgency of tackling the Palestinian situation. Diplomatic tension with Iran over disputed islands has not impacted on a growing commercial relationship. Relations with fellow GCC members are strong.

Economic Outlook

Overview: A generally favourable macro performance has been undermined by a deteriorating fiscal position, according to an IMF Article IV report – the first the UAE has allowed to be published (in the run-up to the upcoming Dubai IMF/World Bank Annual Meetings). Big-ticket projects are pressing ahead despite a minor slump caused by the war in Iraq. The Dubai real estate market, cornerstone of Al-Makhtoum strategy, is holding up well. Real GDP growth for 2003 is forecast at 2.8%-3.1%, with inflation around 1.5%. The UAE can pump 2.138m b/d under the present OPEC quotas, and more if needed.

Finances: The IMF says the consolidated fiscal balance registered a 9% of GDP deficit in 2002 as spending was not reined in to reflect reduced oil earnings caused by OPEC quotas. Abu Dhabi accounts for the majority of the UAE's oil revenue earnings and underwrites other emirates during periods of stress. Dubai's planned Dh1.5bn (\$408m) five-year bond issue to help finance the IMF/World Bank Meetings in September is still awaited; substantial investor interest is reported for a bond that would boost the Dubai Financial Market. In a rare IPO, the state-owned Commercial Bank of Dubai listed on 1 April, bringing to 13 the number of DFM-listed firms, of which five are banks, plus one bond and four open-ended funds. The IMF commended the banking sector's strength, profitability, supervision and capitalisation, but foreign banks say the UAE is over-banked.

Privatisation: Progress has been slow beyond independent water and power projects (IWPPs). Telecoms company Etisalat is traded on the DFM, but is still majority state-owned. Oil firm Zadco, Abu Dhabi's electricity transmission system and Emirates Post may be part-privatised.

Investment: The UAE is a WTO member. Foreign investors can hold 100% of companies in the free zones and 49% elsewhere. Sharjah is a manufacturing hub for SMEs, as are the FTZs. The Dubai Economic Council was created in March to help further boost private investment. There have been problems with Saudi Arabia over implementation of the GCC Customs Union, effective from 1 January. The UAE has accused Saudi customs of levying 12% tariffs on some shipments and has threatened to impose retaliatory tariffs against Saudi imports.

UAE: Key Projects

SHUWEIHAT IWPP: Abu Dhabi's \$1.6bn 1,500MW Shuweihat S1 power and desalination project is to start 2004 under a contract where the US' CMS Energy and UK's International Power have a 20-year O&M deal.

AL-TAWEEELAH A1 IWPP: The \$1.5bn Al-Taweelah A1 power and water plant is being developed by TotalFinaElf and Tractebel.

UMM AL-NAR IWPP: A developer to take a 40% stake in the project near Abu Dhabi City was expected to be selected as GSN went to press (see MEE).

OTHER POWER AND WATER SCHEMES: 700MW Jebel Ali L power and 70m g/d desal plant (due onstream 2005); phase two work on Fujairah's Qidfa power/desal project expected 2003; expansion of Abu Dhabi's Mirfa plant planned, possibly as an IWPP (Fichtner is technical consultant).

DOLPHIN ENERGY: \$3.5bn project to import Qatari gas is progressing. Partners are Occidental, TotalFinaElf and UAE Offsets Group. Omani gas will supply Fujairah plant from Q4 03 until Dolphin gas comes onstream in 2006.

AJMAN BOT WASTEWATER: Work has started on \$140m financing for \$450m integrated wastewater project, including a \$77.5m 14-year club loan.

GCC GRID: Electricité de France was awarded a consultancy contract for phase II work (UAE-Oman link) in January. Completion of link expected 2005/06.

JEBEL ALI PORT: Dubai Ports Authority announced a \$1.1bn expansion plan. Capacity will be expanded over four phases to an eventual 22m teu/yr.

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 by 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.

UAE: Selected Economic Indicators

	1998	1999	2000	2001	2002f
GDP growth (%)	-6.2	10.1	20.4	-4.0	3.5
GDP per capita (\$)	16,991	17,668	20,300	19,945	19,600
Population (million)	2.78	2.94	3.25	3.39	3.50
Exports/re-exports (\$ bn)	30.4	35.1	43.3	38.5	40.0
Imports (\$ bn)	28.9	30.8	32.0	33.5	35.4
Trade balance (\$ bn)	1.5	4.3	11.3	5.0	4.6
Oil production (million bpd)	2.3	2.1	2.3	2.1	2.2
Crude oil exports	34.6	45.4	70.1	56.0	56.0

f = Forecast.

Source: Central Bank of UAE, Local authorities, Ministry of Planning.

GSN Risk Grade — D/3: Election sideshow with emotions running high, investment low

Political and Social Development

Overview: President Ali Abdallah Saleh's relationship with the USA is under the spotlight ahead of parliamentary elections on 27 April. Anger at the USA has become even more vocal with the war in Iraq; government and parliament have been united in their vocal opposition with Foreign Minister Abu Bakr Al-Kurbi calling for the activation of the Arab League Joint Defence pact, which defines an attack against a League member as an attack against all Arab countries.

Elections: Campaigning has begun for parliamentary elections on 27 April. The war in Iraq has been blamed for a reduction in candidates; 1,707 (including 13 women) are standing for the 301 seats compared to over 5,000 in the 1997 ballot. All parties have publicly agreed not to use or sanction violence during the campaign; 2001 municipal elections witnessed fighting between some political groups and allegations of corruption. The election is being monitored by local and international groups. The biggest battle will be between Saleh's General Peoples' Congress (GPC) and the Islamist Al-Islah party, which has a loose alliance with the Socialist party, which controlled South Yemen before unification and boycotted the 1997 ballot. Terrorism and the government's relationship with the USA are burning issues. The GPC holds 224 seats and Al-Islah 63.

Security: Tribal violence and general lawlessness persist, although security has been tightened since the war in Iraq started. Yemen saw passionate protests against the war; one in late March left two people dead. Iraq is an old ally but the authorities reportedly detained a number of Yemenis who were attempting to leave the country to help resist the Coalition. A number of Iraqis who were believed to have been plotting attacks against US/UK interests have been arrested.

External factors: The USA has provided significant funds and expertise for security, reflecting Saleh's readiness to act against "terrorism". Yemen is keen to maintain an improved relationship with Saudi Arabia. In March, three Yemeni journalists were handed four-month suspended sentences for writing articles judged to be harmful to Yemeni-Saudi relations. Yemen has joined some secondary Gulf Co-operation Council consultation groups as a prelude to full membership.

Economic Outlook

Overview: World Bank estimates suggest 42% of the population is living under the poverty line. Even so, Yemen has a creditable payments record, a low debt service ratio and has used its oil revenues carefully. Unemployment is estimated at over 25% and a downward trend for oil output is not good news. GDP growth of 4.1% was recorded for 2002. The government anticipates real growth of 3.2% for 2003.

Development: An IMF Poverty Reduction Strategy Paper for 2003-05 underlines the need for structural and governance reforms. YR293.6bn has been allocated for development and service projects in 2003, of which YR106.9bn is expected to come from foreign sources. Donors pledged \$2.3bn over three years in October. Qatar initialled a \$90m loan in March.

Finances: The 2003 budget is based on a \$21/bbl oil price, and envisages a YR64.1bn deficit, with spending of YR668.4bn and revenues of YR604.3bn (YR207.4bn oil export revenues). Parliament approved an anti-money laundering law in March; penalties include five-year jail sentences, confiscation of funds and fines equivalent to the amounts laundered. A Central Bank of Yemen committee will supervise the law's implementation. Yemenis have been linked to Al-Qaeda funding. Total external debt was \$4.95bn at end-2002, compared to \$4.87bn at end-2001. Forex reserves were \$4.29bn, 20% up on 2001.

Oil: The government says 130 offshore oil wells are planned for drilling in 2003, when total output is targeted at 500,000 b/d. However, a World Bank study forecast that output could decline to 198,000 b/d by 2008 unless more work is undertaken. Oil exploration has increased since production-sharing agreement terms became more favourable. Settlement of the Saudi border has opened potential exploration zones along the fringes of the Rub Al-Khali (Empty Quarter).

Liberalisation: The EU has granted €7m technical assistance to help Yemen prepare for World Trade Organisation membership, but much work has still to be done before this becomes reality. Yemen's latest IMF Article IV assessment pressed for budget reform, reduced energy subsidies, a clearer public spending focus, poverty reduction and efforts to cut the non-oil deficit. Reforms to the civil service and judiciary, tax system and customs service are planned.

AL-QAEDA HUNT: The authorities were severely embarrassed after ten suspects connected with the October 2000 *USS Cole* bombing escaped from custody in early April, prompting a massive manhunt. The men include key *Cole* suspect Jamal Al-Badawi. Local sources suggested the fugitives might try to reach Al-Qaeda strongholds in the northern Shabwa province. Their escape followed the recent capture of a number of Al-Qaeda suspects including Fawaz Al-Rabeei, wanted for questioning by the USA.

Yemen: Selected Economic Indicators

	1999	2000	2001e	2002p
Real GDP growth (%)	3.7	5.1	3.3	4.1
Real non-oil GDP	2.9	4.7	4.0	5.0
Consumer price inflation (%)	8.0	10.9	11.9	15.8
Yemeni crude price (\$/b)	18.7	28.2	23.0	23.1
Public revenue and grants*	29.8	41.7	38.5	36.2
Public expenditure*	30.0	33.2	35.7	35.7
Public finance balance*	-0.2	8.5	2.8	0.4
Current account*	2.8	14.1	6.8	4.0
External public debt*	—	54	56	54
Reserves (months of imports)*	6.0	12.3	14.8	15.1

e = estimate p = projection *percentage of GDP
Sources: IMF, Yemeni authorities

Yemen: Key Projects

ADEN PORT: Managed by 49% shareholder Port of Singapore Authority, Aden's \$580m container terminal and transshipment hub competes against Oman's Salalah and the UAE's Khor Fakkan and Fujairah ports as a regional gateway for East Africa and the Gulf, avoiding the Straits of Hormuz. Container throughput reached 380,000teu in 2001 but the *Limburg* attack has hit business with throughput down and a reported 3,000 jobs lost since October. The government has reportedly offered financial guarantees of up to \$150m against acts of terrorism in its waters.

HYDROCARBONS: Established operators include Nexen and TransGlobe Energy Corporation (both Canada), Occidental and Hunt Oil (USA). TransGlobe announced the successful An Nagyah 3 well on block S1 in March; a further appraisal well is planned. UK-based Capital Oil & Gas signed E&P agreements for blocks 37 and 39 in January. TotalFinaElf has a long-planned LNG project, but risk mitigation questions persist even if markets can be found. The government plans a \$280m Hadramaut refinery.

IPP: US Delma Power plans to develop a \$300m 400MW gas/diesel independent power plant near Marib; feedstock announcement awaited. \$400m IPP between Aden and Mukalla is under study.

OTHER POWER PROJECTS: Contract awards also awaited for 60MW Sanaa South and 60MW Aden Al-Arish power plants. Bids are expected in June for a 200km 400kV Marib-Sanaa transmission link and supply/installation of total 300MW capacity gas turbines for a plant in Marib.

MIDDLE EAST ENERGY

POLICY, RISK AND PROJECTS IN THE GULF AND LEVANT

Does Goodbye Mean Farewell For Fleeing Power Developers?

With global power developers pulling out of emerging markets as quickly as they piled in during the 1990s, regional authorities looking to accelerate ambitious generation expansion plans now find an increasingly barren field to choose from.

Major US and European developers are reining in their foreign operations in the wake of domestic pressure on the bottom line, shackling prospects even in those areas where demand is holding up strongest like the Middle East. The bitter irony for capacity-strapped countries is that this developer flight is coinciding with a remarkably strong demand growth profile throughout the region.

The *World Energy Council* estimates Middle East electricity demand growth at 6-7%/yr, some four percentage points above the global average. That growth is underpinned by a renewed push towards regulatory reform that makes Middle East project risk appear increasingly attractive to the few big players left with sufficient appetite for the game.

Fixed-price power purchase agreements (PPAs) and quick timeframes established in benchmark markets like Abu Dhabi ought to make the region a top draw for developers with regional experience, notably the US "big three" of *AES Corporation*, *CMS Energy* and *PSEG Global*.

"The Middle East is still prepared to go for long-term offtake agreements which you

won't find anywhere else," acknowledged CMS' regional chief **Ron Heyselaar**.

But the priorities of having to put their own houses in order mean only a handful of European operators, such as the UK's *International Power (IP)* and French champion *TotalFinaElf (TFE)*, are left in the game.

IP and TFE were the only two bidders last November on the 1,500MW independent water and power project (IWPP) at Umm Al-Nar, sponsored by *Abu Dhabi Water and Electricity Authority (Adwea)* – a project that in headier times would have seen a queue of developers knocking at the door.

Not that the few existing bidders are complaining. At Umm Al-Nar project sponsor IP, Regional Director **Ranald Spiers** argued that departees were unlikely to find a red carpet reception should they seek to return to the Middle East power market at a later juncture. "It's not easy to come back in this region. You're pretty much blacklisted if you leave," he said.

The developers' problems are standard MBA material: stagnant global economic growth impinging on industrial activity, filtering down to weaker overall demand for power generation.

MEE Pointers

IRAQ: Oil decisions

Oil fires are all but out, but defining the shape of the new Iraqi oil industry remains one of the interim administration's toughest tasks (*GSN 707/15*). Among those said to be lined up for a key role is former *State Oil Marketing Organisation (Somo)* official **Fadhil Othman**. Washington is talking to Othman, now an advisor to Qatar's Oil Ministry, and a few others, including **Ramzi Salman** and **Mohammed Ali Zainy**, about becoming oil minister – once an interim government is in place. Former *Shell Oil* chief executive **Phillip Carroll** is the most widely cited candidate to head the planned oil policy advisory board, possibly backed by Zainy (*GSN 707/2*).

Meanwhile *Lukoil* is "actively defending" its West Qurna-2 project, the Russian giant's **Vagit Alekperov** said on 14 April, amid widespread reports of horsetrading over reconstruction contracts and other agreements with the USA. Alekperov confirmed that recoverable reserves were "close to 7bn barrels", the project would "yield about \$20bn for the company and \$16bn for the Russian government within 13 years", and he put development spending at \$6bn.

SYRIA: Iraq effect confirmed

There were no surprises when US Secretary of Defence **Donald Rumsfeld** confirmed the Iraq-Syria pipeline shutdown. State oil marketer *Sytrol* had already announced major cutbacks in exports – which were around 200,000 b/d above the normal Syrian export/consumption balance. In May, Syria expects to export only around 14 80,000t cargoes, down from 23 in March.

LEBANON: EDL cuts losses

Electricité du Liban lost only about \$60m in 2002, a considerable improvement, mainly due to better revenue collection – a critical indicator if EDL is finally to be privatised. The government plans to sell 40% of EDL's assets by end-June.

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The US market is now saddled with significant overcapacity, attributed by some to overzealous deregulation, while power pooling has had the effect of driving prices down even further. Add in *Enron's* implosion, 9/11 and the California energy crisis, and the picture for the Americans appears particularly bleak.

Power developer debt is now regarded as high risk by ratings agencies, making cheap capital increasingly hard to access. According to *Standard & Poor's*, credit quality in the utilities and competitive energy sector will remain under pressure throughout this year.

CMS, PSEG AREN'T BIDDING

For the big developers, the only strategy available is to return to brass tacks, concentrating on the domestic US market. CMS is maintaining its Gulf-based interests at the 1,500MW Shuwaihat IWPP in Abu Dhabi and is continuing talks with *Saudi Arabian* petrochemical group *Sadaf* over a planned 200MW captive power plant at Jubail.

However, CMS says it is not bidding for any new work in the region – and in this it is not alone.

“Hardly any American companies are doing anything in power now,” said Heyselaar. *Williams* was looking at a few things but then they got hit by the banks and that was cut short. But even the Europeans are scratching their heads a bit.”

PSEG Global said it was not bidding for any new private power plants outside the USA.

AES IS SAVED BY THE IDB

AES is in the midst of a fire sale of assets aimed at recouping the company some \$1bn in cash, but most of its Middle East interests – including the Barka independent power plant in *Oman* and the Ras Laffan IPP in *Qatar* – will stay in place.

The company's *Dubai*-based affiliate *AES Oasis* has recently completed the sale of a 32% stake to the *Islamic Development Bank Infrastructure Fund*, which should boost its ability to bid for new work such as Abu Dhabi's planned IWPP at Mirfa and an IWPP at Sohar in *Oman* (*GSN 707/22*). Like CMS, AES had put a moratorium on bidding for any new Middle East projects. But with the *Islamic Development Bank* on board as a major shareholder – contributing a welcome \$150m – it might be in a better position to pitch for projects.

EUROPEANS, JAPANESE STILL JUST IN THE HUNT

AES' bailout by the IDB looks to be an exception, with even the European heavyweights feeling the pinch.

Belgium-based *Tractebel* withdrew from a 450MW IPP at Al-Samra in *Jordan* late last year. It blamed this on the decision of its French parent, *Suez Group*, to undergo a major corporate restructuring. It also pulled out of the running for the Umm Al-Nar IWPP, as did *Italy's Enelpower*.

Some *Japanese* developers are still in the frame, with *Mitsui* and *Tokyo Electric Power Company*

UAE: Umm Al-Nar Financing Progress Veiled

Participants in the syndicated debt financing for the \$1.5bn Umm Al-Nar independent water and power project were unwilling to comment on the deal as *GSN* went to press. *Gulf International Bank* and *Bank of Tokyo Mitsubishi*, two of the lead arranger group, were unwilling to field questions on their progress in recruiting newcomers to the banking group.

Developer *International Power* also declined to field questions on the transaction, in which *First Gulf Bank* has reportedly assumed a \$75m portion of the debt, joining *ING Bank*, *Sumitomo Mitsui Banking Corporation* and *West LB* at this level. Reports also said that the lead arranger group, which includes *HSBC*, has been augmented by *National Bank of Abu Dhabi* and may grow to include *Royal Bank of Scotland*.

International Power and *Japanese* partners *Tokyo Electric Power Company* and *Mitsui* are taking a 40% stake in the project company and increasing capacity at the existing site by 1,500MW and up to 25m g/d of new desalination capacity.

lining up behind IP in one of the consortia bidding for Umm Al-Nar.

Mitsui and fellow *Japanese* groups *Mitsubishi Heavy Industries* and *JGC Corporation* are also taking part in the beauty contest for *Saudi Aramco's* planned slate of “captive” IPPs.

But the *Japanese* have their own problems to deal with. Like the *Americans*, they've got to get their house in order before they venture outside.

BETTER TERMS STILL MAY BE NEEDED

Regional power authorities should still encounter enough interest to ensure most projects will receive a realistic competitive bidding round. But the absence of top-tier developers will invariably leave its mark on deals.

Industry executives say sponsors might have to offer improved terms if they are to attract competition to privately financed projects. For example, BOT pioneer *Adwea* might find it will have to bump up the 13% internal rate of return established on previous IWPPs.

Lukewarm developer interest could also prompt some sponsors to tear up BOT deals and go back to traditional engineering, procurement and construction (EPC) models.

But the real losers could be the traditional private power laggards such as *Saudi Arabia*. The Kingdom has failed to establish a single IPP in the more than six years since *Oman* floated its first private power plant at Al-Manah, hamstrung by bureaucratic delays and indecision over the path of regulatory reform.

SAUDI ARABIA LOOKS FOR PROJECTS

With the larger developers now largely sitting out Middle East projects, *Saudi Electricity Company* could find it has missed the private power boat, particularly with the natural gas initiative, in which power projects were to have played a major part of the three core ventures, seemingly stalled.

Riyadh is not yet giving up the fight. *Saudi Aramco's* planned list of “inside the fence” IPPs

might set a useful template for wider private power provision. Three bidding groups are in the running for the four 140MW-240MW plants at Ras Tanura, Juaimah, Uthmaniyah and Shedgum, led by IP, **Mitsubishi Corporation** and the local **Al-Zamil Group**. The client aims to award the four power plants in one contract with a 20-year energy conversion agreement. The winning bidder will own 100% of the IPPs.

Aramco's decision to go ahead with an Abu Dhabi lookalike package, albeit on captive plants, has raised dampened spirits.

According to IP's Spiers, "The important thing is that it's an IPP and it's being bid, as the biggest risk for us in the region is that there's not enough bidders or that the governments concerned will go down a different route such as EPC."

IP and the other bidding groups for the Aramco plants – who include Mitsui, **Korea Electric Power Company** and the French-based **L'Air Liquide** – appear well placed to mop up a lot of the other business in the region.

ADWEA'S MIRFA EXPANSION

The next big regional project limbering up for this autumn is Adwea's expansion of the Mirfa power and water desalination plant to 1,500 MW and 100m gallons/day. There remains a good chance that Adwea's disappointing encounter on Umm Al-Nar will cause it to ditch the BOT model for the time being – or at least scale back the size of the expansion.

But this is unlikely to temper long-term plans for private power expansion throughout the region. Regional authorities are being urged to keep up the momentum behind power sector reform, despite developer flight.

Some are holding up the baton of reform. Jordan is expected to persevere with the private model for Al-Samra, in spite of Tractebel's eleventh hour withdrawal. In the meantime, authorities will have to get used to a reduced cast list.

QATAR: Oryx GTL Draws Out Syndication But Funds In Place

General syndication for Qatar's \$1.1bn Oryx GTL scheme has yet to be fully tied up, with no definitive date for closure on the ambitious gas-to-liquids project, *GSN* learns.

ANZ Investment Bank, **Commercial Bank of Qatar**, **Doha Bank** and **First Gulf Bank** have made total commitments of \$80m, and several other banks remain interested in the deal, whose closing time was originally cited as end-March.

A source close to the financing stressed that "Oryx is already a done deal".

The project's sponsors – a joint venture of **Qatar Petroleum (QP)** and **Sasol** of South Africa – received their first draw-down from the underwriting banks in March. He said that the small general syndication "is a low key affair, and

the sponsors don't feel compelled by any time-limits." The source added that the end-January signing by 15 lead arrangers of a \$700m loan to the sponsors "was the icing on the cake," avoiding any possible problems caused by the imminence of a war in Iraq.

"The arrangers are all in at a level below their maximum holds, so if the new banks need any more time, there is no reason not to give it to them," he said.

Other financiers that have been mentioned in conjunction with the scheme include **Union National Bank**, **Die Norddeutsche Landesbank** and **Export Development Canada**.

Technip-Coflexip's \$765m contract with Oryx GTL for the design and construction of a GTL complex in Qatar came into force on 21 March. Production of GTL is slated to begin by Q4 2005.

Insurers Note Iraqi War Fallout

The impact of the war in Iraq for the wider Middle East region has been more limited than some predicted, according to trade risk insurers canvassed by *GSN*.

At one of London's leading private sector political risk insurers, a senior executive said his company had for some weeks ceased to provide cover for **Syria** and **Turkey**, given the proximity of these two countries to hostilities. However, risk cover on **Egypt** and **Iran** had continued to be available throughout March and April.

Another London-based underwriter said that cover against *force majeure* events – occurrences involving large scale violence – was stopped for many Middle East countries in late 2002, as the likelihood of hostilities increased. "We have decided to wait one month to see how things pan out," he said, as the war in Iraq was winding down.

"We are more conservative in general about the region, and have been holding off to some extent, but are still insuring regular business such as Turkish letters of credit," *GSN* was told by a New York-based underwriter. He predicted his company's cover stance would widen "when some level of stability returns, and the violence is winding down. At the moment we see continuing problems in the area."

Among official export credit agencies, the UK's **Export Credits Guarantee Department** said it had "factored the conflict in Iraq into its risk assessments for other countries in the region, but has not considered it necessary to change cover policy."

A leading European ECA told *GSN* its policy depended on the country involved. According to a senior official: "We are studying a structured transaction in Iran, but in some other markets we would have to wait to see how developments pan out. For major projects in more stable countries such as **Oman** and **Qatar** we are very willing to provide lots of cover."

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