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GSN

Companies & People

KUWAIT: Al-Sabahs Take On Editor In Pre-election Spat

By launching a public prosecutor's investigation into pungent criticisms of the ruling **Al-Sabah** family, the government has given fresh publicity to *Al-Watan* Editor **Mohammed Abdelqader Al-Jassem**'s attacks. Jassem has promised to make his trial a public forum for debate over freedom of expression. Open criticism of the Al-Sabahs is commonplace, with widespread frustration at the sluggish tone of national leadership, and complaints of a lack of vision and even corruption aired frequently *(GSN 705/8; 704/8)*. The Jassem affair has brought such frustrations centre stage in the run-up to the 5 July National Assembly election.

The timing is particularly sensitive, with individual Al-Sabahs backing different parliamentarians to build personal support for the future. Meanwhile, some candidates are said to be mobilising voter support through personal favours. Jassem suggested votes could cost as much as KD3,000. Islamist candidate **Mohammed Al-Juwaihel** was banned for offering this sum to potential voters in an advertisement. The *Al-Watan* Editor really stepped beyond conventional bounds by directly attacking the royal

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Across The Region

Saudi Arabia will throw its weight behind the Roadmap plan for Middle Eastern peace, with compromises even on such hot issues as Jerusalem. Geopolitics, Page 3

Bahrain's King Hamad attended MidEast summit talks as a representative of the new, more democratic Gulf, as well as being Arab League President. Page 4

The Bush Administration feels more comfortable about Saudi Arabia's role in tackling the terrorist money chain, but that does not mean the issue will go away. *GSN* examines the law suits now under way. Page 4

Plans by UK and UAE firms to establish a naval joint venture signal that bilateral defence ties are finally on an even keel and highlight ADSB's ambitions. Page 6

Abu Dhabi Crown Prince Sheikh Khalifa's visit to London was an important event in UAE domestic politics. Page 20

Amidst resurgent street protests in Iran, there are signs that hardline clerics may be prepared to compromise with President Khatami over two crucial reform bills. Page 7

The Saudi security forces have acted against the ultra-radical underground after stinging criticism of Interior Minister Prince Nayef's handling of the Riyadh suicide bombings. Page 7

India has signed security agreements and is providing important military support for Iran. Page 9

Iraq represents a huge new market for insurers, but *GSN*'s soundings suggest insufficient provision of political risk cover could act as a brake on reconstruction and foreign direct investment. Page 11

The US Ex-Im Bank and UK's ECGD set out their Iraqi cover positions. Exporters want more still. Page 12

Qatar Airways has led international carriers back into Iraq. Page 13

IMF Managing Director Horst Köhler gave strong support for GCC currency union, but his officials have attached a long 'to do' list of measures that must be implemented. Page 13

Two years ago, hopes were high for the Saudi gas initiative. Perspective, Page 2

GSN's Analysis

A decision that Syria should take seven years to implement economic reforms highlighted contradictions facing reformers, who talk a good transformation but have proved unable to push through key liberalisations. *GSN* has started a Syria *Risk Management Report*, to be updated every five issues. Given Syria's difficult external relations, domestic policy problems and patchy economic outlook, we have assigned a D/4 Risk Grade.
Risk Management Report, Page 15

With Saudi Arabia's international relations strained by Islamist undercurrents and the gas initiative's failure, we maintain our cautious C/2- Risk Grade.
Risk Management Report, Page 14

There is talk of female emancipation again in Kuwait, but it is unclear that a majority in the new National Assembly will agree – and votes for women may have to be forced through from above if Emir Sheikh Jaber really wants to give women the vote.
GSN View, Page 2

India has emerged as a key source of military assistance for Iran, while the Islamic Republic is emerging as a major energy source for India. Despite reports of a WMD standoff, India can balance its growing US and Iranian relations.
Centrepiece, Page 8

MIDDLE EAST ENERGY

Saudi reformists talked the talk, but opening up downstream energy projects proved just too much for conservative opinion to stand. GSN's soundings suggest the authorities will now opt for an alternative plan involving a higher degree of local content. Page 16

Kuwait is pushing its $7bn northern oilfields development, hoping to make up lost ground while parliamentarians fight out the election. Page 17

Russia believes it can keep its Saddam-era oil contracts, but the jury is out. Page 18

OPEC agreed to do nothing at its Doha meeting, while markets waited on the expected Iraqi crude tender. Page 18

MEE Pointers on an Omani IWPP, Qatari GTL and LNG, Iranian oilfields and a Saudi at OFID. Page 16

GSN View

Is it possible to be a modern, outward-looking society, with aspirations to regional leadership that are largely rooted in a track record of transparency and political freedom, and yet to deny women the vote? That is the question Kuwait's Sunni Islamist and conservative tribal members of Parliament have to ask themselves about an issue that will not go away at a time of reform in Qatar and Bahrain, debate about democracy in Iraq and increased US pressure on all Arabian states to modernise their political structures.

Kuwaiti conservatives have blocked attempts by Emir Sheikh Jaber Al-Ahmed Al-Sabah, to introduce women's full political rights through legislation in the National Assembly. They now face the prospect that the Head of State may introduce these rights by decree, during the interval between the 4 June dissolution of the Ninth Assembly and the 5 July election by some 126,000 male nationals of a new 50-seat legislature – the subject of heated speculation in recent weeks. The government has already proposed a new Municipality Law that would bring women into politics at the local level.

If Sheikh Jaber does exploit the pre-election window to impose reform from above, the opponents of women's suffrage could kick up a storm when the Tenth National Assembly returns. In the combative atmosphere of the elegant National Assembly building, who knows how events might turn out?

This issue has now gone beyond a matter of domestic Kuwaiti politics. For 12 years after the Iraqi invasion Kuwait stagnated. The threatening presence next door of Saddam Hussein's regime acted as a physical and psychological block on Kuwait's development, suffocating any prospect that it might recover its earlier role as an intellectual, diplomatic and financial hub for the Gulf. That block has been removed by the US/UK overthrow of Saddam Hussein's regime. Although the condition of Iraq itself remains unstable and uncertain, there is no doubt that Kuwait has, in a real sense, been set free to revive its self confidence and ambitions. Indeed, a hint of the new mood can already be detected in Kuwait's rapid emergence as a provider of aid, emergency oil fire control and high-tech medical support for Iraqis.

Already Kuwait has many of the assets that foreign governments and international investors look for in a modern leadership state: financial strength and transparency, government accountable to the people's elected representatives, media and intellectual freedom, academic institutions and a high-tech infrastructure.

Central to this appeal is Kuwait's self-presentation as the Gulf's oldest democracy. It is a strong image – albeit one that is undermined by the refusal to allow women to vote or stand for office. Also problematic is the nature of Kuwaiti electioneering, currently the subject of heated claim and counter claim in the Emirate.

The absence of female political rights plays up to every clichéd prejudice touted by outsiders to Arabia. Indeed, at a time when women are voting freely in Bahrain, Qatar, Oman and Iran, it leaves Kuwait "behind the curve" in Gulf terms. Emir Sheikh Jaber, reformist members of his family and wider Kuwaiti society – not to mention local feminist groups – understand this. But it is unclear that a majority in the new Tenth National Assembly will agree, given the weight of conservative elements thrown up by elections in Kuwait.

If female emancipation, expected in the 1962 Constitution, is to happen, it may have to be forced through from above, so the wider world can see that Kuwaiti women have the same political rights as Kuwaiti men.

Perspective: Two Years Ago

The long-term prospect of buying into the World's biggest oil reserves played a critical role in persuading global oil majors to battle for investment contracts in Saudi Arabia's nascent gas sector. For all the bullish talk of company chairmen and chief executives, the three gas development packages as apparently structured would appear a far less attractive investment were it not for companies' determination to gain a foothold in the Saudi energy industry.

This being Saudi Arabia, even international company grandees, as well as their expert advisers, are short on details on how the eventual projects will be structured. Whatever the eventual rates of return, the chairman and CEOs of eight leading companies who on 3 July signed preparatory agreements for three projects with an estimated combined initial investment of $25bn knew they were taking part in an historic event *(GSN 653/16)*.

The contracts have been years in the making – at least since Crown Prince Abdallah Bin Abdelaziz's September 1998 meeting with the heads of seven US majors at Saudi Ambassador Prince Bandar Bin Sultan's home in Virginia, in an event which signalled his modernisation push to global business. The so-called Gas Initiatives Projects (GIP) has since been seen as the standard bearer for Crown Prince Abdallah's "liberalisation" *(GSN 659/5)*…

US major ExxonMobil seems to be the big winner, but also takes on the biggest commitment in what industry analysts have described as "a jump into the unknown". The leading role played by US firms confirms that America Inc will continue to play a dominant role in Saudi business, whatever the Saudi leadership think about Washington's pro-Israel policies in the Middle East, and despite popular pressures to reduce the Al-Saud's trans-Atlantic links.

Gulf States Newsletter, Vol. 25, No. 663, 11 June 2001

Saudis Could Accept Roadmap Compromise

Saudi Arabia is expected to throw real weight behind the "Roadmap" plan for Middle Eastern peace over coming months – but very much in a behind-the-scenes role, pressuring Arab radicals into line, rather than holding centre stage.

Despite their own highly public assertion of the importance of Jerusalem – an issue for which the Roadmap provides no pre-set answer – those close to the government believe Riyadh is "essentially sanguine" about the new **US**-led peace strategy.

Crown Prince Abdallah Bin Abdelaziz (CPA) and his close advisers believe the benefits for wider regional development that would flow from an **Israel/Palestine** settlement ultimately outweigh concerns about specific details of the final deal. As CPA's circular to Arab leaders this spring made clear, they feel the conflict is diverting attention away from pressing domestic reform issues within Saudi Arabia and other Arab states.

There is a growing perception that President **George W Bush** is serious about promoting peace, as was apparent from his sponsorship of the Aqaba and Sharm El Sheikh meetings, which brought together Israeli Prime Minister **Ariel Sharon** and the new Palestinian Premier **Mahmoud Abbas (Abu Mazen)** in , along with key allies including **Jordan's King Abdallah II**, **Egypt**'s President **Hosni Mubarak** and **Bahrain**'s **King Hamad Bin Isa Al-Khalifa** *(see box)*.

This marks a major shift from the situation when CPA visited Bush at his Crawford, Texas, ranch on 25 April 2002, and found a leader who – unlike his father **George HW Bush** – apparently had no conception of the Arab-Israeli dispute and its consequences. He had been warned: soon after becoming President, Bush Jnr had told Ambassador **Prince Bandar Bin Sultan Bin Abdelaziz** he had no intention of "aggressively" pursuing Middle East peace, unlike his predecessor **Bill Clinton** and, indeed, Secretary of State **Colin Powell**. Key Administration figures, such as Vice President **Dick Cheney**, seriously under-estimated Saudi anger over the issue.

Following **Saddam Hussein**'s fall in **Iraq**, views are converging – as Bush suggested would happen in a private communication to CPA last January. The Roadmap proposals are not fundamentally incompatible with the Arab peace offer launched with such fanfare by CPA at the Beirut summit.

But while they are ready to contemplate an ultimate settlement with Israel, the Saudis and other leading Arab moderates are not interested in extending "halfway house" goodwill gestures to Sharon's government. **Qatari**-style trade and diplomatic contacts are not on offer. Riyadh sources told *GSN* that recent Arab endorsements for the Beirut "all-or-nothing" peace offer were designed to make it clear to Washington and the Israelis that no such friendly overtures would be offered this side of a final settlement.

However, this predictable response should not detract from Riyadh's flexibility over the shape of that eventual Israel/Palestine treaty. The Saudis are taking a particularly close interest in two issues – the Palestinian right of return and the fate of Jerusalem. But they are also realistic about what can be hoped for.

The message received by Western governments is that Riyadh accepts it will be physically impossible for most of the millions of Palestinian families to return to the homes they had to leave in 1948 and afterwards. What Saudi Arabia regards as essential is some form of official compensation and recognition that the families were wrongly forced out.

The Jerusalem question

More surprising is the apparent Saudi willingness to support a compromise over Jerusalem – which, if implemented, would not go down well with many Saudis. Al-Qods is the third holiest city in Islam; the official Saudi policy statement on the peace process states plainly: "The question of Jerusalem, in the view of the Kingdom of Saudi Arabia, represents the very essence of the Palestinian cause and the core of the Arab-Israeli dispute. The future of the whole peace process depends on the way in which this question is dealt with."

But senior Saudi officials have made clear in private Riyadh's belief that there is a way for the Palestinians and Israelis to share Jerusalem, if both sides are prepared to think creatively. The Saudis see the city's fate not as a matter of religious principle but one of practical politics for the Palestinians; they are willing to back whatever position the Palestinians ultimately take – perhaps even if this meant some form of shared sovereignty over the historic area of the holy sites.

Riyadh is firmly behind Abu Mazen, the new Palestinian Prime Minister now engaged in the peace process. ***Palestinian Authority*** President **Yasser Arafat** is distrusted, not least because of the history of corruption that has seen the disappearance of so much Saudi aid meant for Palestinian public services and welfare.

Saudi Arabia is coming under a degree of pressure from the USA, but primarily over the control of funding for Palestinian welfare organisations – although, despite the claims of the

Bahrain's King Hamad Struts A Global Stage

Bahrain's **King Hamad Bin Isa Al-Khalifa** was an unfamiliar figure at the Sharm El-Sheikh summit between **US** President **George W Bush** and Arab leaders more familiar with the proceedings. All the other attendees – **Egypt**'s President **Hosni Mubarak**, **Jordan**'s **King Abdallah II**, **Palestinian** Premier **Mahmoud Abbas (Abu Mazen)** and **Saudi Crown Prince Abdallah Bin Abdelaziz** – have been prominently associated with recent efforts to revive the Middle East peace process. But the US State Department which, in partnership with the host, Egypt, made all the arrangements for the Sharm meeting, appears to have had a dual purpose in seeing the Bahraini monarch attend – as well as recognising his current role as President of the ***League of Arab States***.

The presence of a leader with no direct strategic interest in the **Israel**/Palestine crisis was intended to signal wider Arab support for the Roadmap peace initiative, especially from the pro-Western but also pro-Palestinian states of the Gulf. King Hamad's attendance demonstrated a readiness to remain closely associated with the USA, despite the public rift over the invasion of **Iraq**. The Bahraini monarch – who had already accepted official American designation as a major non-***NATO*** ally and continues to host the main permanent base of the US Fifth Fleet – is one of the few Arab leaders who appears to have no qualms about being viewed as solidly pro-American.

With Washington looking to create a more democratic Arab world, King Hamad is a ruler who has understood the need to start devolving power to legislative institutions – even though his opposition critics say this process should move further and faster than is now apparent, while conservative foot-draggers within the ruling Al-Khalifa family believe he has already conceded too much ground. For King Hamad, the invitation to Sharm sent out a useful message to opposition critics and regime conservatives about the continuing strength of Washington's support for his phased approach to democratisation. Bahrain is now frequently cited by senior US officials as an example of the sort of reform model they would like other Arab allies to emulate.

neo-conservative right, the Bush Administration does not believe the Saudis are deliberately funding ***Hamas***' militant activities.

The US Treasury and ***Federal Bureau of Investigation (FBI)*** accept that, particularly this year, there has been a dramatic tightening up in the control of financial flows from Saudi charities to the Palestinians and international Islamic causes *(see below)*. There is an acceptance that no system can be foolproof but that auditing and money transfer controls are now more effective.

However, Washington remains concerned that some money, particularly from the Saudi public, destined for Palestinian welfare activities is ending up supporting armed Hamas activity. Ordinary Saudi charity givers do not distinguish between pure welfare organisations such as the ***Saudi Red Crescent*** and those that are also engaged in political or armed activity such as Hamas.

The plight of ordinary Palestinians – highlighted in the coverage by ***Al-Jazeera Satellite Channel*** and other Arab television stations – arouses deep popular sympathy among ordinary Saudis. A three-day fundraising "telethon" in April 2002 raised a staggering $109m for Palestinian victims, with **Princess Johara Bint Ibrahim Al-Ibrahim**, wife of **King Fahd**, personally contributing $0.8m. Some government money is thought to have been given to the telethon appeal.

Yet when welfare money reaches the Occupied Territories there is no rigorous system for ensuring it does not, directly or indirectly, support the militants. The families of suicide bombers receive the same welfare compensation as those of innocent Palestinians shot in the street by the Israelis or crushed by Israeli army bulldozers. This does not play well in Washington.

Saudi Legal Hot Potato

Speaking at the G8 summit in Evian, **France**, where he was a rare invitee, **Crown Prince Abdallah** sought to reassure Western governments that Saudi Arabia was committed to fighting terrorism and terrorist funding, asserting that "we have tightened control on donations so that they will not leak into the hands of suspect parties."

CPA said Saudi Arabia was "enacting legislation stipulating that donations going out of the country be channelled through a single authority, which will work in accordance with regulations ensuring total transparency and clarity."

Such moves mean the **Bush** Administration, Treasury, ***FBI*** and other officials say they now feel comfortable about Saudi Arabia's role in tackling the terrorist money chain. But it does not mean the issue will go away, with lawsuits in the **USA** targeting leading Saudis from Deputy Prime Minister, Defence and Aviation Minister **Prince Sultan Bin Abdelaziz** downwards.

High-profile lawyers at Mount Pleasant, South Carolina-based ***Motley Rice*** – led by senior partner **Ron Motley** in a team that includes French intelligence expert **Jean-Charles Brisard** – have launched a lawsuit on behalf of the families of the 11 September victims. Some 2,760 relatives are now represented, and a total 37 defendants named.

This claim focuses "on wealthy Saudi individuals, banks, corporations, and Islamic charities implicated in the financing of the terrorist organisation ***Al-Qaeda***." It is brought in the individual names of the 9/11 victims' immediate family members. Its case "will rest on the premise that those who finance the terrorist organisations are liable for the damages done by them," according to Motley Rice, which cut its teeth on products liability litigation against the asbestos and tobacco industries and ***Firestone***.

The litigants – named as ***9/11 Families United To Bankrupt Terrorism*** at a Washington address – have started actions in the United States District Court for the District of Columbia, Civil Division against some of the Kingdom's most illustrious names, as well as Al-Qaeda luminaries such as **Osama Bin Laden**, **Ayman Al-Zawahiri** and **Abu Musab Al-Zarqawi**.

Also listed are a number of Saudis already blacklisted by the USA, including Jeddah-based businessman **Yassin Abdallah Al-Qadi**.

Those cited in legal notices published in the *International Herald Tribune* and *Al-Qods Al-Arabi* also include ***Al Baraka Investment and Development Corporation***, ***Faisal Islamic Bank***, ***National Commercial Bank*** – despite its wide-ranging reforms and removal from the board of the **Bin Mahfouz** family (some of whose members are also cited) – ***Saudi Bin Ladin Group*** (and other individual Bin Ladens and family companies) and the **Al-Rajhi** family and companies.

Also named is ***Delta Oil Company***, in the 1990s a Saudi partner in ***Unocal***'s plan to build a gas pipeline from **Turkmenistan** to **Pakistan** via **Afghanistan**. Delta is now involved in **Azerbaijan** via its ***Delta Hess*** venture with ***Amerada Hess***. It is controlled by the **Al-Amoudi** family, headed by **Mohammed Hussein Al-Amoudi**.

Lawyers ring the golden chain

Others named in the very diverse group include **Yousef Jameel**, whose family ***Abdul Latif Jameel Group*** is a major player in the motor trade, oil and construction. Jameel's is one of those names found on computer disk at the **Bosnian** headquarters of the ***Benevolence International Foundation*** during a 2002 raid in Sarajevo, which yielded up the names of Saudi billionaires, producing the now infamous "Golden Chain" list of wealthy donors who might contribute to Islamic causes. It did not say who actually donated.

Jameel apparently made charitable donations to help Bosnian Muslims channelled through the ***Saudi Red Crescent (SRC)***. The 9/11 Families suit names the SRC among its defendants.

In response to such actions senior Saudis are spending big on legal talent. Among those most in the public eye, the ***Bin Ladin Group*** is represented by ***Jones Day***, ***Al-Rajhi Banking Group*** by ***White & Case***, **Khaled Bin Mahfouz** by ***Ropes & Grey***, Al-Amoudi by ***Akin Gump***, and ***Nimir Petroleum*** by ***Fulbright & Jaworski***.

Baker Botts filed a motion on behalf of Prince Sultan attacking the 9/11 lawsuit as a "broadside indictment of Saudi government, religion and culture". Prince Sultan and other royal family members such as Ambassador to the **UK Prince Turki Al-Faisal** were named in earlier reports of actions, but were not listed in the 9/11 Families' Complaint launched on 25 March in Washington.

The Houston-based Baker Botts – whose star partner is former Secretary of State **James Baker III** and whose ex-employees include US Ambassador to Saudi Arabia **Robert Jordan**, a former lawyer to George W Bush – argued that Prince Sultan was immune from US legal action as he was number three in the Kingdom and should be dismissed from the case altogether.

But the Baker Botts team also showed the extent to which senior Saudis had financed questionable Islamic charities. Documents presented to the court showed that on behalf of the Saudi government Prince Sultan had approved regular payments to the ***International Islamic Relief Organisation (IIRO)*** and ***World Assembly of Muslim Youth***, Saudi-based groups that have come under intense scrutiny since 9/11.

By claiming Sultan's conduct was official policy and then introducing affidavits to back it up, Motley claimed the defence had opened the way for "discovery" (pre-trial proceedings) that might eventually lead to the Kingdom of Saudi Arabia itself being named as a defendant.

According to the Baker Botts brief: "Surely the plaintiffs do not contend that an American court can or should pass judgment on the religious beliefs or practices of Saudi Arabia or determine whether its government is 'anti-American'."

The answer to this question could further unsettle US/Saudi relations. While the Bush Administration is being widely criticised with playing fast and loose with civil liberties in the name of post-9/11 security, it is highly unlikely to step into a separation of powers minefield by openly trying to influence Judge **James Robertson**, whose court must hear the case.

Meanwhile those in the US Administration who feel particularly uncomfortable about the Saudis and their charities have been disposed to help Motley and his crew.

IRAQ: Royal Return?

Harried by the speed at which radical Shiites have filled the political vacuum left by the ***Baath Party*** in parts of Iraq, and dispiritied by in-fighting among its supposed local allies, is the US-led Interim Administration having new thoughts about a restoration of monarchy in Iraq? What seemed like a flight of fancy when **Jordan**'s Prince **Hassan Bin Talal** attended a July 2002 opposition meeting has become an outside bet as the Coalition struggles to find a workable constitution (*GSN 691/5*). **Sherif Ali bin Hussein** said many of the right things to Coalition onlookers and his apparent tribal following as he returned on 10 June. One to watch.

Jassem Versus Kuwait's Rulers

Continued from Page 1

family in a newspaper column and in public remarks at a media forum. He claimed that associates of First Deputy Prime Minister **Sheikh Sabah Al-Ahmed Al-Sabah** – the *de facto* head of government – could say whatever they wanted without fear of prosecution.

Jassem also attacked the proposed new copyright law and accused the high-flying Information Minister and Acting Oil Minister **Sheikh Ahmed Al-Fahd** of possessing "a tyrannical mode of thinking". Sheikh Ahmed is a shrewd political operator who has balanced his modern government contacts by cultivating ties in traditional tribal circles; his popularity is enhanced by the fact that his revered father, **Sheikh Fahd**, died resisting the **Iraqi** invaders at the Dasman Palace, in 1990. But even though the Minister is not seen as the most liberal of the younger Al-Sabah generation, Jassem's attack on him stands out for its ferocious tone, even in Kuwait's traditionally open (by Gulf standards) environment.

British Coup In UAE As VT Signs For Naval JV

In the week that **Abu Dhabi Crown Prince Sheikh Khalifa Bin Zayed Al-Nahayan** visited Tony Blair and the British royal family, the announcement that the UK and UAE planned to establish a naval joint venture signalled that more than three decades after independence, defence ties were on an even keel. The joint venture plans of ***VT Group*** (formerly ***Vosper Thornycroft***) also underlined the wider return to form of the British naval construction industry.

British contractors have long argued that Abu Dhabi's traditional defence partner **France** and, more recently, the **USA** have muscled UK Ltd out of defence contracts. One oft cited reason for this is **President Sheikh Zayed Bin Nahayan**'s tendency not to buy British due to disputes dating back to the independence period – although these claims can be overstated.

When the UK has been competitive there have been contracts, as in the ***UAE Technical Training Project/UK***, which operates out of East Sussex.

For some time diplomats have been saying that outstanding issues have been settled and "several irons are in the fire" for defence contractors. VT's project to invest in facilities for the joint production of naval vessels with ***Abu Dhabi Ship Building (ADSB)*** company was one of them.

The proposed joint venture will focus on the production of fast naval boats and coastal defence vessels, with a potential production facility in the UAE to promote sales in ***Gulf Co-operation Council (GCC)*** states. VT already has a project in **Oman** and is competing for a contract in **Kuwait**.

Export sales director **Peter Stirk** said the joint venture with Abu Dhabi would manufacture glass reinforced plastic (GRP) coast guard naval vessels. These fast patrol vessels are 37 metres long and meant for coastal defence.

The project is part of an ambitious strategy pursued by the Musaffah-based shipbuilder, which has seen a number of partnerships including with **Sweden**'s ***SwedeShip*** *(GSN 679/6)* and France's ***Constructions Mécaniques de Normandie***.

ADSB Chairman **Abdallah Nasser Bin Huwaileel Al-Mansouri** has evolved a strategy based on expanding into construction of vessels using advanced technologies – such VT's advanced composite materials.

"Land has already been set aside and designs are complete for the further expansion of facilities to provide for the construction of composite vessels for military and para-military customers," Mansouri said earlier this year.

VT is farming into ADSB's ambition to capture regional market share and participating in one of the Gulf's most technologically advanced shipyards.

Public/private sort of partnership

In March, ADSB became the 25th public company to be officially listed on the ***Abu Dhabi Securities Market (ADSM)***. But following a decision made in Q4 02, the Abu Dhabi government has also increased its stake in ADSB, to 50%, having bought the 30% equity previously held by US shipbuilder ***Newport News Shipbuilding (NNS)***.

Some 1,000 UAE nationals hold the remaining 50%. ADSB was first set up in 1996 with NNS through the ***UAE Offsets Group (UOG)***.

The changes in equity stakes are significant for two reasons: the increase in government ownership reinforces the already close relationship between ADSB and the government of Abu Dhabi; and it allows the government to consider offering some shares to other international technology partners to bring further strategic and marketing advantages to the company. Abu Dhabi sees ADSB as a facility that will establish the UAE as a major regional supplier in the defence industry. In June 2002, a $50m expansion facility was commissioned, which increased ADSB's ship-lifting capacity to 2,000 tonnes and the shipyard's total area to 175,000 m^3 from 50,000m^3 at its inception.

The expanded facility is capable of handling vessels of up to 85 metres long. There are three ship repair dry berths, a 70-metre quay wall for new ship construction, outfitting and testing facilities and two 2,720 m^3 construction halls.

ADSB's customers include the ***UAE Navy***, the ***UAE Coast Guard***, the naval forces of **Qatar** and **Yemen**, ***Abu Dhabi National Oil Company*** and its subsidiaries. The shipbuilder has contracts for around two-dozen vessels, including large naval landing craft, high-speed troop carriers and a sophisticated commercial dredger.

But what ADSB really wants is for the formal signing of the estimated Dh2bn Baynunah project contract to build six 70-metre naval Corvettes for the ***UAE Armed Forces***. This would hopefully lift revenues and profits at the high-profile but loss-making company. It posted a net loss of Dh26.6 million for 2002.

In March, ADSB was advised that contract documents for Baynunah were finally considered complete and acceptable to the UAE government. Signing is due soon.

ADSB is also waiting decisions by the navies of Oman and Qatar to bids submitted for refits for their naval vessels.

IRAN: Signs Of Compromise, Street Protests Resume

Amidst resurgent street protest led by student groups – encouraged by satellite TV broadcasts from exile groups in the **USA** – there are signs that hardline clerics on the Guardian Council (GC) may be prepared to compromise with President **Mohammad Khatami** and his supporters over two crucial reform bills already approved by the Majlis. A month of intense political activity beckons, with the exiled opposition – cheered on from the sidelines by Washington hawks and 'Young Shah' **Reza Pahlavi of Iran** *(GSN 710/9; 704/12)*.

Parliamentary sources have indicated that the GC – whose formal task is to ensure legislation to complies with the Islamic Republic's constitution – may be willing to surrender its right to veto candidates for elected office. This is the central provision of Khatami's new election law.

Talks also appeared to be under way to find a compromise over the bill to reassert the President's role as a defender of constitutional principles. This would allow the President to block judicial verdicts he deemed unconstitutional and refer them for final decision to a panel of judges who would examine whether the defendants' rights had been violated. Such a move would take Iran back to values espoused by the 1970s' framers of a Constitution, in which executive power has since been usurped by clerical politicians invoking the primacy of the *Velyat e-Faqih* system of religious rule.

Winning the GC round on this issue could prove exceptionally difficult. Conservatives have used their prerogatives to fight back against the popularly elected Khatami and reformist parliamentarians, and would be loath to give up this weapon. Last week, the GC rejected both bills outright, and appeared to have Rahbar (Supreme Leader) Ayatollah Ali Khamenei's backing.

However, there are rumours that key conservative power brokers are considering letting even the bill covering presidential prerogatives to pass eventually, as they expect Iran's next President to be one of their number, rather than a reformist. A deal could be in the making: Khamenei and Khatami have sometimes shown a readiness to compromise in the interests of maintaining stability and national survival. Such an understanding could be behind the apparent moves towards a new compromise, reported by several sources including MP **Mohsen Tarkasvand**.

Domestic political games-playing accepted, a compromise on reform now might also reflect a recognition that repression in Iran plays into the hands of US neo-conservatives seeking grounds to justify assertive action against Tehran. The hawks' assertion that Iranian opposition groups should receive more support to consolidate building popular resistance to the clerical leadership, received some confirmation when on 10 June students, police and heavies from the ***Basij*** and ***Ansar e-Hizbollah*** lined up against each other in Tehran. These forces could clash again in the weeks leading up to the July anniversary of the 1999 unrest.

Tehran is also closely watching the ***European Union***, which is using tougher than usual language over issues like weapons of mass destruction. Positive signals from Tehran will make states like **Germany** and the **UK** feel much more comfortable arguing the case for continued constructive engagement.

SAUDI ARABIA: Prince Nayef Gets 'On Message'

After weeks of criticism of Interior Minister Prince Nayef Bin Abdelaziz's handling of the 12 May Riyadh suicide bombings and other incidents, the security forces have acted against the ultra-radical underground *(GSN 711/6, 710/3)*. The authorities have clamped down on suspected dissident and terrorist networks in the Kingdom – including clerics – and called in markers abroad, with **Sudan** rounding up 17 Saudis and a **Palestinian** linked to ***Al-Qaeda***. Saudi security personnel flew to Khartoum to help Sudanese officials interrogate the militants, who were alleged to have been training in West Kordofan.

According to one Western source, "someone had a word with Nayef and since then he's been very much on message." Intense investigations, roadblocks and other activity followed. At a roadblock incident in Hail, one of the two suspects was killed and found to be carrying an Eid Al-Fitr greeting from **Osama Bin Laden**. Two policemen were killed in this incident. The dead man has not been identified, but was described by radical Islamists in an Internet posting as one the "Ulema of the Jihad".

Most of the 12 May bombers are believed to have been captured, although a couple may have escaped to **Pakistan**, whose Head of State General **Pervez Musharraf** visited Saudi Arabia on 11 June. The Pakistani authorities are believed to be rounding up suspects demanded by the Saudis. Meanwhile in Medina, ten Saudis and two **Moroccans** linked to the attacks were arrested. Three (non-Saudi) Arab women were also rounded up. The suspects were said to be followers of the late Buraidah-based extreme Islamist **Hammoud Bin Oqla Al-Shuaibi**. Opposition groups have complained about the arrest of clerics including **Sheikh Abdelkarim Al-Humayid**.

In a move to counter radical thinking – which officials said had nothing to do with the 12 May events, but was anyway well timed – the Ministry of Islamic Affairs sacked 353 Imams and sent 1,357 mosque officials for retraining.

Meanwhile those of a reformist bent around **Crown Prince Abdallah** – including the vocal **Prince Talal Bin Abdelaziz** – have been calling for accelerated political and economic change. Prince Talal wants the Majlis Al-Shura to be given a legislative role. Washington remains confident that, despite frequent opposition claims that he lacks real power or inclination to act, CPA is still making progress in his efforts to nudge the Kingdom towards more representative government. Sources observed that recent months had seen the active exploration of a host of possibilities, such as filling some Majlis Al-Shura seats by election or holding elections for local government posts.

Recognising that CPA is not King, and that he has to build a consensus for change within a conservative public and ruling family, the Americans are reluctant to exert overly harsh public pressure for change. The **USA** has signalled it is satisfied with the turn of events, notably with unusually positive words from the ***Federal Bureau of Investigation***'s **Robert Mueller**.

However, for now Western embassies have not changed their security advice. There have been indications of plans for further attacks, notably in Jeddah. Western governments are looking for further initiatives – with the **UK** negotiating a deal based on an appeal for clemency to release the Britons held since early 2001 for their alleged involvement in a series of car bombs. A formula is needed to save Prince Nayef's face over the affair.

Yemeni link

High level talks in Riyadh and a bilateral anti-terrorism agreement point to closer relations with Yemen since the border dispute was settled, but it also comes as the Saudi authorities have been claiming that arms and ordnance used by underground groups have been entering the Kingdom from Yemen. This issue featured large during Yemeni Interior Minister Major-General **Rashad Mohammed Al-Alimi** and Legal Affairs Minister **Rashad Ahmed Al-Rasas**'s 8-9 June talks in Riyadh. The Yemeni ministers also signed an agreement with Prince Nayef on organising border authorities.

Centrepiece: India-Iran Relations

Indians Look To Best Of Both Worlds

Some in the **USA** have looked on with increasing irritation as Iran has forged closer relations with India, which has emerged as one of the Islamic Republic's primary sources of conventional military assistance. Reports of nuclear assistance have suggested a new weapons of mass destruction standoff.

But contrary to reports that US concern at Indian nuclear assistance to Iran could lead to a new crisis between Washington and New Delhi, India's careful efforts to cultivate closer relations with the USA and the Islamic Republic should allow it to negotiate a tricky diplomatic path in which WMD need not be an issue. This was the message presented by India's National Security Advisor **Shri Brajesh Mishra** during recent visits to Tehran and Washington.

India will carefully define the limits of its defence co-operation, and will not provide any destabilising technologies to Iran whose supply would threaten access to the new generation of US technology transfers that India craves.

The consensus in Washington is that India's Iranian links are unlikely to upset New Delhi's long-term strategy of building closer ties with the USA. Hawks may not see it that way, and New Delhi should brace itself for more turbulence over its growing security relationship with Tehran, but India should be able to live with this.

Some form of alliance between India and Iran is natural given the compatibility of their views on national security, long-held concerns over a unipolar world and US involvement in regional politics, and consistent stress on non-alignment. Shared concerns over **Pakistan** and Sunni fundamentalism in **Afghanistan** give focus to active co-operation, enshrined in an intelligence-sharing and counter-terrorism agreement *(see below)*.

Meanwhile business is booming via joint diplomatic, energy, trade and defence activities.

Relations between the two states have burgeoned since 1993, when Prime Minister **Atal Bihari Vajpayee** became the first Indian premier to visit Iran. Since then, Vajpayee has kept up a high level of bilateral visits and engaged in an increasingly broad range of joint projects. Many of the likely fields of co-operation highlighted by *GSN* following Vajpayee's April 2001 visit have been translated into concrete initiatives *(GSN 661/4)*.

Energy is a critical factor, as India turns to gas to meet rising demand in its energy balance. It is widely assumed that India will rely on Iran for a major share of its natural gas requirements, with domestic demand set to top 100bn m^3 by 2010.

India also represents a growing market for Iranian oil; it buys approximately 100,000 barrels per day, worth some $1bn/yr. According to energy analysts at the Washington-based ***Center for Strategic and International Studies (CSIS)***, India will need to source an estimated 78% of its oil overseas by 2025.

Gas fuels industry boom

According to CSIS analysis, gas import dependency, currently put at 53%, will rise to 91% by 2025. Iran will provide a significant part of this total, satisfying 6.9bn m^3 of demand with delivery of 5m t/yr of liquefied natural gas over 25 years. Within nine months, New Delhi and Tehran are expected to sign a gas sale and purchase agreement, with deliveries beginning under Phases 11 and 12 of the South Pars development and from six fields in Assaluyeh in 2008.

The deal will include a number of associated joint ventures, which were discussed in Tehran on 11-13 May at the first meeting of the Indo-Iranian Joint Steering Committee on Hydrocarbon Issues. Indian firms will be offered exclusive equity partnership in the construction of a 6m t/yr, two-train LNG export terminal in Iran.

Following Tehran's refusal to sweeten the LNG deal with oil swaps, Indian oil firms such as ***ONGC Videsh*** will be offered subsidised buy-back equity involvement in oil exploration in Iran.

Gas Authority of India Ltd (GAIL) will provide technical consultancy to support the development of a major compressed natural gas (CNG) urban transportation system in Tehran.

Pipeline politics

The issue of how Iranian gas will reach India remains unresolved. Other markets may be more attractive than India for LNG, while Iran's maritime export capacity and terminals remain less advanced than rival LNG suppliers in **Qatar** and **Oman**, who might prove more attractive options for India. Iran's strength lies in pipeline options, ideally an overland route via Pakistan which would cost an estimated $2.5bn-3bn to construct over three years, and would deliver natural gas at a price of approximately $2.20/Btu.

This option has its supporters – including Pakistan, which anticipates roughly $500m/yr of transit fees ($12.5bn over 25 years). Islamabad points out that despite numerous armed clashes with India, the 1960 Indus River water sharing agreement has never been broken by either side.

Ultimately however, India is unlikely to grant Pakistan turnkey control of a major revenue flow, even with foreign involvement in the project, and is thus continuing to investigate the possibility of an undersea pipeline. This option has been pushed by specialist contractors, including **Italy**'s ***Saipem*** and ***Snamprogetti***.

Feasibility studies envisage a twin pipeline of up to 1,600km costing some $4bn-5bn. Pipeline capacity would leave space for major increases in deliveries, providing a planned annual capacity of 20.4bn m^3, equivalent to 15m tonnes of LNG. Import terminals would need to be constructed on the Indian coast, either at Dahej in Gujarat or Trombay in Maharastra state. Deliveries would cost approximately $3/Btu.

As well as cost concerns, these ambitious plans have been dogged by serious snags at the survey stage. Due in Q1 03, the initial survey of pipeline routes may not be available until Q4 04, according to GAIL Chairman **Proshanto Banerjee**.

There have been other problems: negotiations between the Iranian and Omani governments on pipeline routing have stalled. The governments otherwise claim a good relationship. **UK**-based ***Gardline Surveys***' *Ocean Voyager* survey ship sank on 10 July 2002 and other delays were caused by heavy monsoon conditions. Gardline – hired by GAIL and ***National Iranian Oil Company (NIOC)*** – also reportedly suffered slow payments, which delayed the handover of initial results.

Gardline also cited technical reasons for delays in the surveying phase; two pieces of equipment were unavailable because the US supplier could not provide them under the *Iran-Libya Sanctions Act (ILSA)* and other equipment proved unsuitable at the depths required, which exceed 3,000m at some points – well beyond the previous deepest laid pipeline which sits 2,150m under water.

Sectors With Potential

The Indian government continues to look closely for new markets. The following sectors signal the scope of New Delhi's interests:

- **Energy:** Supply of coal handling system like coal crushers and coal conveyor associated items; cooling water pipes, valves (casting items); coated pipes for sea water system; industrial liquids for steam (coal-based) power plants; package boilers for different process plants, water treatment plants; and engineering services for gas turbine and combined cycle power plants
- **Textiles:** Renovation of machinery and plant; financial investment and technical co-operation.
- **Railways:** Indian railway companies ***Ircon*** and ***Rites*** expect to become involved in major railway development projects; training and consultancy.
- **Wheat:** Initial attempts by Indian companies to supply wheat have not succeeded, mainly due to concern among some Iranian officials that wheat in India was infected with Karnal Bunt disease.
- **Agriculture:** High capacity tractors of 250 horsepower; water pumps; irrigation systems based on under-pressure irrigation.
- **Food processing:** Establishment of small-scale industries, particularly food processing units such as apple juice, dehydrated onion, dried tomato, tomato paste, snacks, etc; sorting and grading machinery for raisin and pistachio; shrimp cultivation; packaging.
- **Chemical:** Potash and phosphate fertilisers and pesticides to Iran's ***Agriculture Support Service Company (ASSC)***, affiliated to Ministry of Agriculture and Jihad.

Common views on the North-South corridor

Iran and India are partners in a number of trade-related ventures, including three trilateral coalitions to develop a north-south corridor providing an export route for goods originating in the former Soviet Union.

These started with the Trilateral Transit Agreement between Iran, India and **Turkmenistan**. Thereafter, India, Iran and the **Russian Federation** formed another trilateral bloc – with some **Belorussian** and **Kazakh** involvement – to develop Bandar Abbas as an economic transit route for goods aimed at the European market.

Most recently, India, Iran and Afghanistan signed a memorandum of understanding aimed at developing transit routes linking India to Iran's Gulf ports. Iran agreed to reduce transit taxes by 90% and warehousing and porterage charges by 50%. The three countries will also develop a joint trade policy and hold exclusive trade exhibitions.

Most importantly, transportation infrastructure will be developed. A 200km road will be developed to improve links between Zaranj in Iran and Delaram in Afghanistan. The $70m project will be undertaken by Indian construction companies, who will also upgrade Iran's Chabahar port. This should help to improve India's negative balance of trade, which stands at over $1bn (mostly oil).

Few other steps on trade have been taken since April 2001, when the two countries signed a *Bilateral Protection and Promotion of Investment and Avoidance of Double Taxation Agreement*, and India extended a $200m line of credit to Iran.

Conventional Military Programmes: Significant Synergies

India and **Iran** have highly compatible world views on national security, which has led to rapidly expanding ties in the fields of defence and security. Both countries have long-held concerns over a unipolar world and **US** involvement in regional politics, and both have consistently stressed non-alignment, non-interference in sovereign affairs, and self-reliance in military development. Shared concerns over **Pakistan** and Sunni Islamic fundamentalism in **Afghanistan** provide a tangible focus for active co-operation.

Both seek to minimise Pakistan's influence and military capability with actions short of war; both closely monitor Islamic militants and Pakistani influence in Afghanistan. This was reflected in an intelligence-sharing and counter-terrorism agreement signed in February.

Both countries share a fundamentally pragmatic and realistic security outlook which places international norms second to national security.

India has carefully sought to avoid involvement in Iran's weapons of mass destruction programmes. Although **Germany**'s federal intelligence service, the ***Bundesnachrichtendienst (BND)***, highlighted the role of Indian chemicals companies in both Iran and Iraq's chemical weapons programmes as late as 1994-96, the US government has not accused India of chemical weapons assistance since 2000 and has never provided solid data on nuclear-related collusion. The USA instead recognises Pakistan and **North Korea** as Iran's principal partners in unconventional weapons development.

Number one for assistance

India is instead set to develop as Iran's primary source of conventional military assistance. As *GSN* noted two years ago, defence co-operation had the potential to transform the Iranian military, providing 'breakout' from containment and a means of indirectly accessing high-quality upgrades and modernisation programmes for its **Russia**n equipment *(GSN 661/4)*. India is in many ways the blueprint for Iranian military modernisation and is a number of steps ahead. Both states plan to build their future capabilities around key Russian exports such as the Su-27 (and in India's case, the highly advanced Su-30) aircraft, the Kilo submarine and advanced Russian air defence missiles such as the S-300PMU (***NATO*** designation SA-10) family.

Iran requires a number of fleet replacements and a period of supplier stability and India may represent the reliable one-stop shop it requires, offering equipment, maintenance, training and upgrades. Recent months have seen high tempo military-to-military contacts, including meetings between all senior military leaders on both sides – from presidential to service chief levels – and visits to Iran by high-level delegations from India's ***Research and Development Organisation (RADO)*** and naval shipyards.

Recent bilateral agreements, pushed through to completion at the highest levels during President **Mohammad Khatami**'s visit to India in January, involved an Iranian offer of contingency support and anchorage for Indian naval forces in the event of a war between India and Pakistan. India agreed to extend a range of technical assistance and training opportunities to the Iranian armed forces.

Naval exercises

India and Iran will hold their first bilateral naval exercises later this year, when Iran sends two combat ships plus replenishment and logistics vessels to participate in India's Western Fleet exercises off Mumbai

This symbolic gesture will open the way for trilateral Indian-Iranian-**Omani** naval exercises, and is backed by more tangible examples of Indian security assistance, which include Indian modification of Iranian Kilo-class submarines for warmer waters, Indian expansion of Iranian naval repair facilities at Chahbahar, supply of patrol boat and submarine simulators, and training at Indian Navy bases in Mumbai and Vishakapatnam.

The Iranian Air Force will benefit from the stationing of technicians from ***Hindustan Aeronautical Ltd (HAL)*** at Iranian MiG-29 maintenance centers in Tabriz, indicating the likelihood of future upgrades of the MiG-29 fleet. India will sell Iran the Konkurs anti-tank missile and assist Iran to upgrade its T-72 tanks, other armoured vehicles and artillery.

A foot in each camp

Despite these ties – which alarm US decision-makers already gauging the difficulty of militarily threatening Iran – India will place definite limits on defence co-operation, avoiding the supply of destabilising technologies.

One reason for this is New Delhi's growing defence ties with the USA and **Israel**, which are reversing decades of exclusion for cutting-edge Western military technology. Provision of US aircraft engines and artillery-locating radar are just the beginning, and have been accompanied by a busy schedule of military exercises since May 2001. Major high-tech transfers to Iran would impact negatively on US technology transfers to India.

Improved relations began in the late days of the **Clinton** Administration, when the White House reversed a long-standing policy by condemning Pakistan for cross-border incursions in the Kargil war of 1999. Clinton-era visits and criticism of Pakistan's military leadership were followed by a complete break with past policy under the **Bush** Administration, which repealed nuclear-related sanctions on India, condemned Pakistani support for militant groups (now designated as terrorist groups by the US State Department), and took a hands-off approach to Kashmir.

India, in turn, only issued muted criticism of Washington's pull-out of the anti-ballistic missile treaty and military operation in **Iraq**. These moves were indicators of a new pragmatic approach embraced by National Security Advisor **Shri Brajesh Mishra** and Foreign Minister **Jashwant Singh**, whose leadership of the foreign policy elite is likely to see India cautiously embrace Iran in a sustainable and long-term relationship, without risking US censure for short-term gain. Mishra has in past weeks been to Washington and Tehran, for talks with his counterparts **Condaleezza Rice** and **Hasan Rohani**.

Mishra on 8 May addressed the ***American Jewish Committee***'s annual dinner in Washington, in recognition of the AJC's "contribution to promoting US-India relations and India-**Israel** relations". He observed that India hoped to host an official visit from Israeli Prime Minister **Ariel Sharon** soon and saw "worrying signs of a regrouping of Taliban elements in southern and south-eastern **Afghanistan**". There was no mention of India's Iran link.

Insurers Wary Of Iraqi Political Risk Market

Iraq represents a huge new market, with intensive reconstruction, upgrading, and eventually fresh construction work for at least the next 20 years, involving all the major sectors of the economy and civil society. This massive effort will generate a big market for insurance products.

GSN's initial market soundings suggest that insufficient provision of insurance products could develop into a potential brake on near-term reconstruction and longer term foreign direct investment in Iraq – despite the recent surge in export credit agency (ECA) cover *(GSN 711/17)*.

Policies covering political violence will remain hard to come by, expensive and reliant on government support for contractors operating inside Iraq. For potential investors, provision of other forms of political risk insurance may deter early market entry, while the lack of sovereign authority and a body of law prevent underwriters from developing policies.

Funding for reconstruction activity will initially originate from international financial institutions and Iraq's slowly expanding government revenues.

Private sector funding through privatisation will take longer to develop – very much longer than some **US** hawks will think acceptable, despite the bullish noises coming from the senior Coalition Advisor to the Ministry of Industry and Minerals **Tim Carney**, who sees a raft of privatisations within one year. Privatisation is the favoured option of several of Defence Secretary **Donald Rumsfeld**'s advisors, including former Secretary of the Army **Martin Hoffmann** and the ***American Enterprise Institute*** team.

It is unlikely the US government will directly control funding beyond the initial, relatively modest emergency reconstruction. The ***US Agency for International Development (USAID)*** projects under way involve a maximum spend of $2.4bn, a small percentage of the expected reconstruction total. With a genuinely international reconstruction effort, a wide range of global risk mitigation specialists can be expected to participate – but not just yet.

Risk profile

For foreign operators inside Iraq, the primary risks throughout the immediate occupation/ reconstruction period and beyond will relate to political violence. The key sources of political violence are likely to originate from Sunni Arab tribal and urban activists (motivated by a mix of tribal, nationalist and ***Baathist*** grievances towards the foreign presence); organised or street level criminal activity; and foreign terrorist groups operating under the cover of lawlessness in Iraq.

The Shiite and Kurdish communities have displayed fewer propensities for violence against foreign interests than the Sunni Arab community and this is likely to remain the case.

The foreign operators at highest risk will thus include those operating in the Sunni Arab areas covering an arc from the west to the north-east of Baghdad. High-risk areas include Fallujah, Baghdad suburbs like Haditha, and Kirkuk's Hawijah suburb.

The rule of law will be established in intensively patrolled urban areas before lower priority rural locations, suggesting greater risks to unescorted foreigners working in remote locations, such as oil pipelines and highways. Although an increasingly heavy Coalition presence is likely until a new government is established, Iraq will retain a mid- to high level of political violence throughout the decade. At best it will reach the risk profile of **Egypt**, but it could be a **Yemen**. There will thus be a strong and sustained demand to write political violence cover throughout the next decade.

The market will not cede systemic advantages to US companies. In the USAID contracts – an important but relatively small proportion of future orders – the US government used a waiver stating that any companies from "the free world" (that is, not under US sanctions or designated state sponsors of terror) could bid for subcontracts. ***Bechtel*** controls the largest USAID project and has stressed its willingness to outsource subcontracts to international bidders *(GSN 711/20)*. They are likely to use a broad range of insurance providers.

As increasing numbers of international development and funding bodies become involved, non-US insurance companies will access other opportunities as clients from their traditional markets move in.

Political violence policies will normalise as concern about unusual war-related risks decrease. The lack of third party insurance coverage dealing with chemical, biological, radiological, and nuclear (CBRN) weapons release (plus land and sea mines, and unexploded ordnance) led to a 17 April US presidential Executive Order indemnifying Bechtel and (with some discretion) its subcontractors from exposure to third party claims of these types.

Early insurance for other forms of cover threatened exceptionally heavy costs – requiring $1m premiums to secure $5m cover – due to the uncertainty involved in complex war scenarios.

Even as a pattern of data becomes available,

Bringing Ex-Im Bank Back On-cover

Ironically, given the **USA**'s leading role in remaking **Iraq**, the Export-Import Bank of the USA is not yet back on-cover. However, this could change – and may even generate a new international controversy if the US export credit agency's return is underwritten by advance sales of Iraqi hydrocarbons. There are technical reasons why Ex-Im Bank cannot return to Iraq, including a mountain of unreconciled debt and conditions in the ECA's constitution which cannot be met in prevailing circumstances. In testimony to Congress, Ex-Im Bank President and Chairman **Philip Merrill** said "programmatic constraints" on Ex-Im Bank, which included the need for a "reasonable assurance of repayment" for every credit, meant it was not the first ECA to go back into Iraq.

To overcome these constraints, Merrill said Ex-Im Bank "was actively considering mechanisms that would allow [it] to support US exports to Iraq sooner rather than later, including taking the credit risk of companies and banks in third countries – such as **Turkey**, **Jordan** and **Kuwait** – that may be involved in obtaining US goods and services for reconstruction efforts". The US ECA had established an internal task force "to address the legal and credit concerns that currently impede our ability to offer trade finance programmes in Iraq". Ex-Im Bank was "co-ordinating closely with the other [US ***Trade Promotion Co-ordinating Committee***] TPCC member agencies, as well as the US exporting community".

According to Commerce Secretary **Don Evans**, TPCC members will play a "significant" role in Iraq's reconstruction, including Ex-Im Bank, the ***Overseas Private Investment Corporation (OPIC)*** and the ***Trade and Development Administration (TDA)***. Evans said TDA believed it could provide up to $2.5m in FY2003 in grant funding for technical assistance and feasibility studies for Iraq, while OPIC was considering using existing finance, insurance and funding programmes to help provide liquidity to the financial sector and insure businesses and contractors. Unlike in **Afghanistan** – where a 1950s accord remained valid – OPIC lacks a pre-existing bilateral agreement with Iraq, slowing its allocation of cover.

US companies want high levels of cover, delivered quickly – and business lobbies are pushing the **Bush** Administration to consider more innovative financing mechanisms. One scheme being promoted by the ***Coalition for Employment Through Exports (CEE)*** – a big business grouping whose members include Iraq reconstruction principals ***Bechtel*** and ***Halliburton*** – is based on arrangements set up in 1993 for Ex-Im Bank to finance **Russian** purchases of US goods to rebuild oil and gas facilities. This facility was secured against Russian oil and gas revenues which were deposited in an escrow account; it has since financed more than $1bn in US sales with no losses reported by Ex-Im Bank. The CEE believes its scheme might generate $3bn-4bn/yr for projects – a price well worth the cost of the approbation a scheme exploiting advanced sales of Iraqi oil and gas to underwrite US contracts would generate among the occupation's many critics worldwide. In comments to Congress, Merrill said the idea had "real merit". Indeed, "it's one of the priorities the bank is looking at as a way to support US exports to Iraq."

ECGD's Cover Position

The **UK**'s Export Credits Guarantee Department has pointed out that it has not yet formally restored cover for Iraq ***(GSN 711/17)***. It said "the government is committed to supporting UK companies wishing to take part in the reconstruction of Iraq. With that in mind, the government is monitoring the situation closely and the potential for restoring normal ECGD cover to Iraq as soon as the risk environment justifies this." Analysts expect ECGD to provide an initial £300m cover, probably before finalising a bilateral debt deal, as was also the case with **Iran**.

underwriters remain leery of issuing risk assessments under conditions of such complexity. An underwriter at market leader ***American International Group (AIG)*** told *GSN*, "the situation is too unpredictable, any faction could decide to let off a bomb at any time."

AIG, ***Chubb***, and **French**-owned ***Unistrat*** analysts canvassed by *GSN* expected the ***US Overseas Private Investment Corporation (OPIC)*** to rapidly develop political violence policies, "taking on the lion's share of exposure on political violence issues," said one underwriter.

An OPIC insurance specialist told *GSN*, "there has been a lot of buzz within OPIC about Iraq, and we expect to see policies emerging as soon as 90 days time."

An AIG analyst concluded: "Underwriters will focus on their traditional markets, competing to produce reasonably priced general third party liability insurance." This will include automobile insurance, employee and foreign national compensation and medical evacuation insurance, plus first party property insurance for contractors' equipment in theatre.

That old sovereignty problem

The lack of an internationally recognised sovereign government prevents the underwriting of other forms of political risk insurance.

This problem was underlined by the USA's recent decision to scale back expectations about the speed at which an Iraqi government would develop. In general terms, however, the plan remains to establish a consultative assembly in 2003-04, hold elections in 2004, and return Iraq to sovereign control in 2005.

Meanwhile the end of sanctions has been technically resolved, but is still being digested by government, multilateral and private institutions. Underwriters have been unable to write policies for Iraq since the imposition of ***United Nations*** sanctions in 1990, and are only slowly beginning to approach the issue.

Sanctions technically ended with UN Resolution 1483, freeing up most international insurance providers to write policies.

In the USA, the end of sanctions also needs to be accompanied by the end of Iraq's status as a "state sponsor of terrorism". A recent Presidential statement to Congress indicated the beginning of this process, but it will take some time for this change to filter through into normalised US commercial and export practices – indicating a window of opportunity for non-US companies.

A more long-term problem remains the issue of Iraqi debt. Quantifying the debt will take many months, followed by a period of reconciliation that could be prolonged. Until the debt is resolved, risk assessments concerning payment conditions will be very difficult to resolve.

Given Iraq's long-term potential, a wide range of governments and international financing institutions are moving rapidly to extend financing to foreign companies dealing with Iraq.

One senior US Treasury official told *GSN* the Administration was already in close contact with 30 major US and non-US banks over financing developments. ECAs are moving faster than expected to open up new lines of credit: **Japan**'s ***Nippon Export and Insurance Company (NEXI)*** extended new cover on 19 May in an example of the unusual speed at which ECAs are moving.

NEXI is typically hesitant to enter markets with unresolved debts – a major factor in Iraq – but did so without hesitation to get Japanese companies on the inside track when they complained that political risk insurance cover was not available.

Although varying degrees of foreign investment and privatisation will take some time to develop, there will eventually be a large market in Iraq for the full range of political risk insurance products.

Other major ECAs gearing up for business include the **UK**'s ***Export Credits Guarantee Department*** *(see box)* and **Italy**'s ***Sace*** (with a new €1bn cover ceiling).

CURRENCY ISSUES

Another issue in future contract decisions will be currency hedging. But for now, the Civilian Administration and its US Treasury advisors have yet to work out quite what currency regime the new Iraq should follow.

Indeed, ***Central Bank of Iraq*** has been ordered to resume printing ID250 notes, bearing **Saddam Hussein**'s head to satisfy local demand. The IR10,000 notes so far used to pay civil servants – when US dollars have not been used – are unpopular. On 9 June, Acting Central Bank Governor **Faleh Salman** was forced to confront an angry crowd, telling them IR250 notes would soon be available at bank branches throughout Iraq.

It is likely that Saddam's face will remain on Iraq's currency until a national government is appointed – and can authorise a new design.

Swiss Worry About Money Laundering – In Iran

Financial transparency failures in Iran are emerging as a major concern for potential Swiss investors, as Finance Minister **Tahmasb Mazaheri** discovered during a business promotion visit to Zurich. While Mazaheri focused on selling the virtues of Iran's reformed investment regime and the prospects opened up by privatisation and equal treatment rules for foreign companies, his audience posed some uncomfortable questions. Competition from the lively informal economy was inevitably a concern, but it was financial sector issues and particularly money laundering that raised the most worry among Swiss institutions.

Zurich analysts believe money laundering could account for as much as 20% of all financial activity in the Islamic Republic. They want greater co-operation with the Swiss authorities to try and curb this traffic. A specialist commission of Iran's Majlis (Parliament) has been examining a bill to counter money-laundering.

However, Mazaheri's audience was encouraged by the current wave of economic reform. The Minister – who will be visiting the **UK** at the end of June – indicated that the names of parastatals destined for privatisation would be released soon. Sectors such as water and power, agriculture, petrochemicals, textiles and vehicle manufacture are being opened up to foreign companies, and investors will be offered incentives to establish operations in deprived regions and to make Iran their Middle East headquarters.

Swiss Economics Minister **Joseph Deiss** (a former foreign minister) visited Tehran last November. The two governments have reached double taxation and bilateral trade agreements. But Swiss business continues to raise concerns over issues that trouble Western investors, including the ban on foreigners doing business directly through the ***Tehran Stock Exchange***. The high level of tax on corporate earnings (60% in some cases) is another cause for complaint, although the government has said it may be cut to 20-25%, to encourage businesses to operate legitimately within the official fiscal regime.

Swiss pharmaceuticals group ***Laboratoire Roche*** complained its pharmaceuticals were being smuggled out of Iran and sold at half price in neighbouring countries. But discounted sales are a challenge to the big drugs companies world-wide and perhaps Roche should not be surprised at what is happening, given the high level of regional demand, and the low level of personal spending power, particularly in countries such as **Afghanistan**.

Airlines Return To Iraq

Qatar Airways underlined its ambitions when on 10 June it became the first airline to operate commercial services to Iraq – ahead of regional rival ***Emirates***, which plans a regular commercial service to Baghdad, as do several other airlines including ***British Airways*** and ***Lufthansa***.

The **Qatari** carrier has launched a twice-weekly service between Doha and Basra (on Tuesdays and Fridays). Those waiting for Baghdad International Airport's civilian services to resume must wait until July at least.

IMF Backs GCC Single Currency

IMF Managing Director **Horst Köhler**, visiting Doha for roundtable talks with Gulf Co-operation Council finance ministers and central bank governors, has publicly endorsed the region's plans to create a single currency. Köhler reminded governments of the need for reform efforts to create jobs and reduce oil dependence, observing that "undoubtedly, increased regional integration culminating in an efficient monetary union will help in this process."

But IMF Middle East experts have also posed some awkward questions about the detail of the currency plans, attaching a stern "to do list" of reforms that Arabian countries will have to implement if they are to make the proposed new arrangement work to their best advantage.

At a semi-official level, IMF officials argue that the GCC states should look beyond their natural **US** dollar orientation and take account of Europe's economic significance and its recent experience of monetary unification.

GSN will analyse the Gulf currency question in issue 713, to be published on 26 June.

Risk Management Report — Saudi Arabia

GSN Risk Grade — C/2-: International relations strained by Islamist undercurrents, gas failure

Political And Social Development

Overview: The May terrorist attacks in Riyadh underlined the Kingdom's increasingly complex political and social crisis. Previous attempts to play down the Kingdom's radical Islam problem have led to criticisms from the West that more could have been done to prevent the attacks. Against a background of growing poverty and unemployment, conservative/liberal rivalries within the ruling Al-Saud family are under the spotlight. One longstanding issue looks likely to have been resolved with the withdrawal of US forces from the country.

Government: A government reshuffled in mid-April brought in a few modernisers, but sent out few other positive signals; no Shiite cabinet minister was named as Crown Prince Abdallah Bin Abdelaziz (CPA) avoided antagonising Wahhabi opinion. New faces included Hijazi businessman Abdallah Bin Ahmed Zainal; several ministries were restructured, with water added to electricity and industry grouped with commerce. CPA's Charter for Arab Reform could launch internal reforms; the prospect of elections has been mooted first at municipal level, followed by the 120-member Majlis Al-Shura. Al-Saud divisions, however, continue to act as a brake on reforms.

Internal security: The 12 May Riyadh suicide bombings left 35 dead. Western intelligence and increasingly governments feel the Saudis could have done more to crack-down on terrorist cells within the Kingdom. In late May/early June the authorities responded with arrests to counter the US claim that Al-Qaeda is a "real and persistent threat" in the Kingdom. Jihadi support is believed to be particularly strong in the far north, the south-west and conservative parts of Najd. Interior Minister Prince Nayef Bin Abdelaziz has come under flack after years of trying to blend hardline policing with the promotion of Islamist policies to co-opt opposition.

External relations: Relations with the USA were further complicated by the 12 May bombings, even though US forces are withdrawing from the Kingdom. The Riyadh attacks have prompted the UK to become more vocal about the cases of UK citizens held in the Kingdom after a series of car bombs that were blamed on alcohol smuggling turf wars. Saudi is taking a keen interest in the Palestinian-Israeli 'road map', with the possibility of recognising Israel a as reward for peace.

Economic Outlook

Overview: A positive growth outlook is forecast for 2003 – estimates vary at 3.3%-4.5% – but masks serious problems. Despite high oil prices, finances remain strained, with debt estimated at $168bn. Unemployment pressures remain unchecked – at over 30% – while population growth is 4-4.4%. Meanwhile, the Gas Projects Initiative (GPI) looks dead after the cancellation of the ExxonMobil-led Core Venture One.

Unemployment: According to the Saudi Monetary Agency unemployment has reached 31.7%. Sama has recommended a review of the sponsorship system and increased Saudi-isation. The Interior Ministry plans to limit foreign residents to 20% of the indigenous population within ten years, with any one nationality limited to one-tenth of the total. There are around 6m-7m foreign workers alongside 17m Saudi nationals.

Finances: The FY03 budget, based on $17.5/bbl oil, envisages a $10.4bn deficit, but Riyadh Bank estimates that if average oil production of 8.5m bbls is maintained and prices averaged $22/b, then a $4bn surplus is possible. If prices do not hold up the government will borrow. Total 2003 revenue is projected at $45.3bn, with expenditure at $55.7bn. According to Riyadh Bank, development projects will require financing of SR2.4trn by 2020, including SR525bn for infrastructure, SR435bn for electricity, SR345bn for petrochemicals and SR330 for water.

Liberalisation: The government renewed its bid to join the World Trade Organisation ahead of its attendance of a G8 meeting on 1 June. The authorities are understood to be keen to reach agreement on a number of hurdles to WTO entry including a prohibition of trade in certain commodities such as alcohol and pork products. The Supreme Economic Council has announced plans to open more sectors to foreign investment. These include some telecoms services (including IT-related areas, but not GSM and fixed-line services), insurance, educational services and publishing. Some sectors, including insurance, will require new laws before they are declared open. Saudi Telecom was listed on the SSE in January and an IPO for National Commercial Bank has been mooted. The Shura Consultative Council has passed a law that would reduce the tax of foreign companies' profits to 25% from 45%. Approval is still awaited from the government.

SAUDI ARABIA: Key Projects

Gas Projects Initiative: Prospect look bleak after the authorities cancelled talks with the ExxonMobil-led consortium for the $15bn Core Venture One South Ghawar project (with Shell, BP and Phillips Petroleum) after "final terms" were refused. The $5bn Core Venture Two Red Sea project, also led by ExxonMobil (with Marathon and Occidental), had previously been postponed. With Saudi Aramco (backed by Al-Saud conservatives) privately opposing the IOC influx, the prospects for the Shell-led Core Venture Three (partners ConocoPhillips, TotalFinaElf) may be equally bleak. The projects look likely to be broken up into smaller component parts. with heavy local investment instead

Butanediol plant: Kvaerner E&C was awarded the EPC contract for Saudi International Petrochemical Company's Jubail facility, to be completed in 2005 to produce 75,000 t/yr of butanediol, 5,000 t/yr of gammabutyrolactone and 5,000 t/yr of tetrahydrofuran.

Power sector: Request for proposals for the first independent water and power projects are expected in Q3 03, starting with the 700MW Shuqaiq plant and the 2,000MW Shouaiba plant. IWPPs at Ras al-Zour and Jubail will follow. HSBC is financial adviser. Saudi Aramco is expecting bids by end June for four IPPs totalling 800MW. Crédit Agricole Indosuez and Banque Saudi Fransi are arranging the $200m financing for Saudi Petrochemical Company's IPP, being developed by CMS Energy with National Power Company. Financial close is anticipated in late June.

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.

SAUDI ARABIA: Selected Economic Indicators

($ billion)

	1999	2000	2001	2002
Nominal GDP	161.0	188.4	186.2	182.8
Nominal GDP growth rate (%)	10.4	17.1	-1.2	-0.5
Real GDP growth rate (%)	-0.8	4.9	1.2	0.7
Current account	0.4	15.6	14.5	10.5
Central gov. domestic debt	44.4	43.8	45.6	48.8
as % of GDP	119.0	87.0	90.0	95.0
Oil price Saudi avge ($/bbl)	17.45	27.0	21.5	21.8
Official Foreign Assets	69.4	73.5	82.6	78.5
Cost of living (% change)	-1.2	-1.0	-0.8	-0.4

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

Syria Risk Management Report

GSN Risk Grade — D/4: Assad squeezed by old guard and USA, bureaucracy stifles economy

Political And Social Development

Overview: President Bashar Al-Assad, a quiet operator known to his small, modernising circle as "Dr Bashar", is battling to overcome a reactionary Arab Baath Socialist Party establishment in an effort to push through genuine reforms. This has so far yielded only limited results, with reformists often reduced to structuring policies that by-pass traditional Baathist institutions to effect change. While the business class who often suffered under his late father, Hafez Al-Assad, feels more confident, Syria's economy remains stifled by bureaucracy. The human rights situation has improved, but arbitrary actions by a variety of mukhabarats and Baath Party grandees remain a problem. Islamic sentiment is strong at family level, even though political Islamism remains underground – its fate since the spectacular and bloody crushing of the 1982 Islamist uprising in Hamma.

The US threat: Dr Bashar has courted US investment, and after the 11 September 2001 attacks provided useful intelligence on Al-Qaeda and other Islamist groups which was appreciated by Washington. But domestic political pressures mean Assad must publicly hold to traditional Syrian Baathist ideas. He is caught between his father's legacy and a personal impulse to modernise, as became painfully apparent in mid-April, when President George W Bush said the USA believed Syria had chemical weapons. Foreign Ministry spokeswoman Busaina Shaaban (who some see as a future minister) said Damascus was only looking for peace, but Washington wants much more, as Secretary of State Colin Powell subsequently told Assad.

Middle East peace: Much depends on how Syria responds to the US-led peace process and whether a new proxy conflict ensues involving Hizbollah in Lebanon. Israeli Prime Minister Ariel Sharon has been positioning himself as "a man of peace", but that would not stop a new offensive against Hizbollah and radical Palestinian groups operating in what Israeli military intelligence calls its "northern arena". According to US Deputy Secretary of State Richard Armitage, "Hizbollah may be the A-team of terrorists… They have a blood debt to us." Stopping that blood debt being paid out will be a key issue in international diplomacy this year, notably for France and for the UK; Britain has made Syria a focus for its policy of "constructive engagement".

Economic outlook

With the regime divided by factional, communal and ideological rivalries, an early June cabinet decision that Syria should take seven years to implement economic reforms agreed in Q1 02 highlighted the contradictions facing Syrian reformers, who talk a good transformation but have proved unable to push through many key liberalisations. At the same meeting, the government decided to revitalise efforts to join to the World Trade Organisation and EU Euro-Mediterranean Partnership. Meanwhile the economic outlook has taken a marked turn for the worse with Saddam Hussein's fall in Baghdad; although for long a rival, Syria had been pumping around 200,000 b/d of Iraqi crude, substituting this for local crude in domestic consumption and exporting the surplus.

Liberalisation: Reformists in Assad's regime are pushing ahead with projects that might improve the investment environment, from oil exploration and production (E&P) contracts to plans for IT parks and other technology initiatives in zones away from traditional Baathist influence. Modernisation of the main commercial ports at Tartous and Latakia includes a European Investment Bank (EIB)-funded project at Tartous to develop passenger traffic, as well as cargo, reflecting Syria's tourism ambitions *(see below)*. Assad's informal advisors include businessmen, and he has placed some liberals in government, such as Economy and Trade Minister Ghassan Al-Rifai (who returned home in a December 2001 reshuffle after nearly three decades with the World Bank), his old mentor Higher Education Minister Hassan Risheh and Communications Minister Mohammed Bashir Al-Munajid. Banking reforms are under way, but so uneven is the nature of reform that the best hopes of an investment boom come from big name Arab investors, who include Saudi billionaire Prince Alwaleed Bin Talal Bin Abdelaziz.

Electricity generation: Syria plans to install some 3,000MW of new capacity by 2010 but there is little interest in Public Establishment for Electricity Generation and Transmission (PEEGT)'s plans for two major power plant projects – and there is a distinct lack of international appetite for Syrian project risk (see below). More worrying still is the distribution network's poor condition, with one-quarter of generated capacity estimated to be lost.

HUMAYDI RELEASED: Syria's friends welcomed the recent release of Al-Hayat's bureau chief Ibrahim Humaydi, but charges still hang over Humaydi, who may be suffering from a very Syrian disease as one branch of government (represented by General Security chief Bahjat Sulaiman) clashes with another. Players include Military Intelligence chief General Ghazi Kanaan, whose Deputy Assef Shawkat is married to hardline presidential sister Boushra Al-Assad). Figures like Humaydi are pawns in elite in-fighting.

SYRIA: Economic Indicators

($m unless stated)

	1999	2000	2001	2002	2003f
GDP	15,600	17,300	18,400	18,900	19,500
Growth (%)*	-2.0	2.5	1.7	1.8	2.3
Population (m)	15.9	16.3	16.7	17.1	17.5
Inflation (%)*	-2.1	-0.6	0.4	0.9	1.6
Imports*	3,600	3,700	4,300	4,500	4,600
Exports*	3,800	5,100	5,000	5,800	4,900
Current account/GDP (%)	0.6	5.8	1.2	3.4	-0.9
Capital investment**	36.0	59.0	122.4	–	–

f Forecast.

Sources: Syrian government; Coface, Guide Risque Pays; Investment Bureau of Syria**.*

SYRIA: Key Projects

Oil E&P: Oil Minister Ibrahim Haddad in January announced contracts giving exploration Block 2 to Shell (already a major player in Syria), Block 17 to Canadian minnow Stratic Energy, Block 22 to HBS International's Egyptian arm, Block 24 to IPR International and ONGC Videsh (India), and Block 26 to Ocean Energy. Development contracts were placed for the Audeh (Dublin International Petroleum), Tishreen (Russia's Zarubezhneft) and Kubayba (China National Petroleum Corporation) fields. On 26 May, Block 26 was confirmed as a Devon Energy (80%)/Gulfsands Petroleum (20%) venture following Devon's Ocean takeover.

Power upgrade: The 100MW upgrade of Tishreen power station was blocked after the two preferred bidders submitted offers far above what state PEEGT could afford. Plans for the 125MW Nasirieyh power station were abandoned in 2002 when there was only one bid. New tender documents are due.

Transmission upgrade: The EIB and Arab donors have committed some $265m to expand and upgrade the network by 2005. This should boost Syria's prospects of participating in a future region-wide electricity grid with Egypt, Jordan and Turkey.

Tartous port development: The EIB on 23 May announced a €50m ($59m) loan to modernise and develop Tartous port, rehabilitating one quay and the main breakwater, dredging, and building two new quays to handle additional traffic, including passenger and cargo terminals.

MIDDLE EAST ENERGY

POLICY, RISK AND PROJECTS IN THE GULF AND LEVANT

OMAN: New IWPP

The government and advisors ***SG Corporate & Investment Bank*** have invited expressions of interest to develop an IWPP at Sohar, continuing the drive to raise generation capacity using private finance. The approximate 500MW/30m g/d plant is scheduled onstream in mid-2006, to be linked to the North Oman grid. Expressions of interest were due by 13 June.

QATAR: Ivanhoe out of GTL

Canada's Ivanhoe Energy has announced the termination of its negotiations for a gas-to-liquids project in Qatar, using technology owned by ***Syntroleum Corporation***.

Qatargas, ExxonMobil 'still to finalise' UK LNG site

Qatar Petroleum and ExxonMobil are still evaluating possible UK locations for an LNG terminal, Qatargas's Vice Chairman and Managing Director **Faisal Al-Suwaidi** told ***Dow Jones Newswires***. Gas will be produced by Qatargas II at Ras Laffan. The likely spot is South Hook, at Milford Haven, Wales, where ***Petroplus Tankstorage*** is also planning an LNG terminal.

IRAN: Oilfield developments

Two oilfield developments costed at around $2bn each are in the offing, Oil Minister **Bijan Namdar Zanganeh** said during the 11 June OPEC meeting. Contracts for Azadegan could be signed with a **Japanese** consortium by early July, to produce 300,000 b/d. Iran has shortlisted ***BP*** and ***Total*** for a 100,000 b/d extension to output at Bangestan.

OFID: Saudi appointment

The OPEC Fund for International Development has appointed **Suleiman Jasir Al-Herbish** as its director for the next five years. Herbish is thus no longer Saudi Arabia's nominee for OPEC Secretary-general. In the running are **Iran**'s **Hadi Aejad-Husseinian** and the incumbent **Alvaro Silva Calderon** of **Venezuela**.

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Saudi Gas Initiatives: A Death Foretold

Saudi reformists and their cheerleaders talked the talk, but opening up downstream projects and upstream gas proved just too much for conservative opinion in the Kingdom. *GSN*'s soundings suggest the authorities will now opt for an alternative plan involving a higher degree of local content.

Oil Minister **Ali Al-Naimi**'s formal scrapping of the $15bn South Ghawar Core Venture confirmed the unspoken consensus among gas initiatives project participants over the past year: that the GIP's basic structure was fundamentally flawed and no amount of browbeating could persuade international oil companies (IOCs) to commit to it without promises of better access to reserves and improved internal rates of return.

The death knell was sounded in a letter from Naimi to CV1 leader ***ExxonMobil*** on 5 June to the effect that the MoU signed three years ago would be terminated by 15 June. This leaves just the ***Royal Dutch/Shell***-led CV3 in Shaybah on the life support machine – though that too is expected to be annulled in due course.

Yet *GSN*'s soundings suggest the untimely demise of this particular Saudi mega-project does not signal the end of the Kingdom's efforts to drive power, water and petrochemicals expansion via the exploitation of untapped gas reserves.

According to a Riyadh-based legal adviser involved in one of the GIPs, the Saudis are now likely to evolve a more suitable model to exploit their gas – in which the Saudi component will be much more prominent. "My guess is that it will be re-examined and retendered in a different format," the lawyer told *GSN*. "For example, ***Saudi Aramco*** might retain the upstream portions and let private companies, predominantly Saudi-owned, get involved in the downstream, power, water and petrochems."

Industry sources indicated the new business model would be more attuned to the economic realities of post-9/11, post-**Saddam** Saudi Arabia. Increasingly, local developers are forming consortia to put together big ticket projects, notably in the petrochemicals sector. The old 'Saudi mega project model', typified by ***Saudi Basic Industries Corporation (Sabic)***, which would invite a foreign major in to develop a key venture on a 50/50 basis, is being ditched in favour of projects backed by local investors.

These include ***National Polypropylene Company***, which plans a polypropylene (PP) plant at Jubail.

Another private concern, ***Saudi Polyolefins Company***, is backing a PP plant to come on stream by year-end. Such companies typically comprise significant investment from Saudi-owned trading houses.

New power and water model

A new model is also likely to emerge in the power and water sectors, the key driver of the GIP from the outset. Subdued international investor appetite for Saudi project risk post-9/11 and post-Riyadh bombings, could be compensated for by greater willingness of Saudi investors to risk their capital inside the Kingdom.

Groups of local investors could put up most of the capital for an independent power project (IPP), with the possibility of a foreign partner coming in, even if only in a technical capacity. More Saudi industrial groups are likely to bid for projects in conjunction with Aramco.

Senior Aramco chiefs recently mooted changes to the regulation of the gas sector, in which the state energy company would retain its dominant position in exploration but might work with foreign partners in joint ventures. Industry sources told *GSN* that foreign companies might be employed as drilling contractors in service contracts, rather than being offered equity gas.

Whether the ExxonMobils and Shells will ever again be in striking distance of the prized Saudi upstream is a moot point. Analysts predict that some of the lower rung IOCs will line up for retendered projects – which are unlikely to bear any resemblance to the original core ventures with bits and pieces of the original plant fragmented into smaller pieces.

"Companies like ***Occidental*** will want to do a small one, ***Conoco*** might be on for a small project, but it's not going to be enough to whet the appetites of an ExxonMobil or Shell – and these are basically the companies that the Saudis want," said **Fadel Gheit**, senior energy analyst at US securities house ***Fahnestock & Company***.

IOCs would subsidise Saudi goals

But insiders downplay suggestions that the Saudi government is desperate to lure in the oil majors.

There was an obvious geostrategic imperative behind the Saudi authorities' invitation of the IOCs into the Kingdom; their presence was in part designed to underwrite international confidence in the Al-Saud regime itself – as was reflected in the leading role played by **Crown Prince Abdallah Bin Abdelaziz** and Foreign Minister **Prince Saud Al-Faisal**. There was an apparently compelling economic argument – especially during a period of low oil prices – with the authorities seeking IOC investment that would prove a relatively cheap way of harnessing foreign capital to source new power, water and petrochemicals capacity, while also creating job opportunities for the burgeoning reserve army of the Saudi unemployed.

But taken in the Saudi context, there was an obvious mismatch between this project and what the IOCs wanted – a promise of access to upstream reserves and a high return on their invested capital – that condemned the model to failure from its inception. Aramco leaders, typified by Naimi, consistently argued that IOCs' demands for rates of return in the mid- to late teens could not be countenanced, not least because few IOCs could expect such returns on downstream projects elsewhere. They were essentially seeking returns typical of upstream projects, where 20% margins are common. But Riyadh was never intending to let the IOCs into the upstream

The failure to strike a deal with the majors is still a bitter disappointment to the authorities, but is not a fatal blow to the Kingdom's long-term ambitions to unleash its gas potential. "Quite how the project moves forward is difficult to say at this stage, but somehow or other it will move forward," said **Michael Hamilton**, Senior Manager of Project and Trade Finance at Saudi-based ***Arabian Petroleum Investment Corporation (Apicorp)***. "They're not going to put it aside and shelve it – it's a matter of finding the right parties to go forward with, whether foreigners or Saudis."

Big fish to fry

With the burgeoning US oil protectorate of Iraq expected to be opened up to IOCs at some point in the near future and signs of a revival in the $7bn Project **Kuwait**, the majors may in any case have other upstream fish to fry in the region.

Neither is the GIP's demise a body blow to the majors. Many of these same companies are already heavily active in the Kingdom. ExxonMobil is the biggest foreign investor in the Kingdom with some $5bn of investments, while ***ChevronTexaco*** has a major petrochemicals project. "Money is money – it doesn't have to be in assets under the ground," said the lawyer.

Saudi pique at the IOCs' reticence is palpable. According to one Saudi banker, they will never get a deal this good again. But CPA's willingness to let the GIP die of natural causes suggests the Al-Saud hierarchy is relaxed about the consequences of allowing such a high-profile initiative fall by the wayside, whatever the ramifications for the Kingdom's international image.

But the GIP's demise does mark a watershed in the Saudi way of doing things. Insiders say the old-style command economy approach to major projects – "Roll it out and people will do it, just because we're Aramco," as the Riyadh lawyer put it – has run its course. Whatever emerges will be an entirely different kettle of fish

KUWAIT: Northern Fields Opening Gets Under Way

While **Saudi Arabia** has let its big hydrocarbons investment die, the Kuwaiti government is looking to advance its $7bn Project Kuwait northern oilfield opening during the summer parliamentary recess, circumventing potentially difficult political opposition to the scheme.

Kuwait Petroleum Corporation (KPC) is understood to have released a draft operating services agreement and a development plan to prequalified operators in June, on which their responses have been invited by 18 August – traditionally a “down” period in the Gulf.

A diplomatic source confirmed to *GSN* that the government is anxious to push Project Kuwait in the summer as a means of avoiding it being held up in the National Assembly, for which elections are due on 5 July.

Nine majors including ***ChevronTexaco***, ***ExxonMobil***, ***ConocoPhillips*** (in their pre-merger forms), ***BP***, ***Total***, ***Eni*** and ***Royal Dutch/Shell*** have been prequalified as operators and 17 as non-operators.

Project Kuwait calls for upgrading production capacity at five northern fields near the **Iraqi** border, boosting capacity from 450,000 b/d to 900,000 b/d within a ten-year timeframe.

Once IOCs have offered feedback on the draft agreement, KPC will then spend about a month sounding out companies on the plans and then insert amendments. The resulting documents will then form the basis for putative deals.

Any such deals would need parliamentary sanction, but the government is clearly hoping to use the summer period to make Project Kuwait a *fait accompli*.

The government signalled its intention to push through the project at the start of the year, but the ousting of **Saddam Hussein**’s regime in Iraq has given renewed impetus to the country’s upstream opening. “Many Kuwaitis believe what happens in Iraq, rather than the National Assembly, will shape the country’s future,” said the diplomat.

Analysts said parliamentary opposition to Project Kuwait was not necessarily a matter of principle against all foreign investment in the upstream, but concerns over the precise formula for their involvement. KPC and government officials have spent much of the year studying other countries’ production sharing models, with **Norway**’s understood to have been examined particularly closely.

IRAQ: Russians Dig In For Assets

Russia’s diplomatic offensive, designed to win guarantees from the **US** administration that its firms will enjoy a level playing field with coalition members in the looming competition for Iraqi hydrocarbons, has yet to bear fruit.

Foreign Minister **Igor Ivanov** claimed in early June that Washington had given it firm assurances that there would be no discrimination against Russian companies, but analysts said this fell far short of the kind of cast-iron guarantee sought by Russian oil companies – notably ***Lukoil***, which is hoping to shore up it $3.7bn West Qurna contract signed in 1997 with – and subsequently reneged on by – **Saddam Hussein**’s regime.

At their early June meeting in St Petersburg, President **George W Bush** told President **Vladmir Putin** that it was up to the Iraqi people to decide on the sensitive issue of oil contracts – a form of words that is unlikely to instil confidence in Russian oil chiefs.

“It’s easier for the US not to say whether it can guarantee equal treatment, as at some point it could provide an excuse for them not to fulfil commitments,” said **Gennady Krassovsky**, an energy analyst at the Moscow-based ***Alfa Bank***.

But the Russian-backed ***UN*** Security Council resolution lifting sanctions against Iraq may yet come to the Russians’ rescue. According to UN envoys’ interpretation of the resolution’s terms, long-term oil contracts cannot be negotiated until a permanent, internally recognised Iraqi government has been installed.

Russian firms fear the US-dominated Interim Authority is more likely to discriminate against them than a putative independent Iraqi regime.

Lukoil is confident it can reclaim the West Qurna concession, which is expected to have production capacity of up to 600,000 b/d when the field comes on stream. However, Baghdad’s decision to pull the plug on the MoU in December 2002, for not having begun field development work, may damage its claim significantly.

Lukoil’s reluctance to begin work was prompted by its unwillingness to flagrantly flout sanctions against Iraq.

In one of the Baathist regime’s last concession awards, Russia’s ***Stroitransgaz*** was granted a contract in January to develop Block 4 in Iraq’s Western Desert.

OPEC Quotas, Iraqi Sales

As *GSN* went to press, OPEC ministers met to discuss production and prices – and, as expected, to postpone a decision on Iraq’s possible new quota. OPEC meets again on 31 July and then in September. **Qatari** Energy Minister and OPEC President **Abdallah Bin Hamad Al-Attiyah** said OPEC was in touch with Iraq, but its readmission depended on an internationally recognised government being put in place.

Also apparently delayed was Iraq’s much anticipated re-entry onto global oil markets, set for 11 June, with ***State Oil Marketing Organisation (SOMO)*** inviting bids for some 10m bbls of Kirkuk (8m bbls) and Basra (2m bbls) light crude in the first free sale of Iraqi crude since 1990.

According to *Platts*, demand was such that some bids were not in by the 10 June deadline. SOMO had said it would be more selective towards clients, giving preference to refiners over traders.

International Energy Agency chief **Claude Mandil** said he expected full pre-war production back within a month. According to the US-appointed head of the oil sector **Thamer Ghadhban**, production should reach 1.5m b/d by mid-June, despite delays in resuming the war-damaged pipeline system.

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Sheikh Khalifa Comes Into The Limelight With London Trip

LONDON—Abu Dhabi's **Crown Prince Sheikh Khalifa Bin Zayed Al-Nahayan** has taken a significant step forward into the international limelight with a highly public visit to the **UK**. Tea with **Queen Elizabeth II** and a Downing Street photo-call after talks with Prime Minister **Tony Blair** were clearly designed to consolidate Sheikh Khalifa's international profile as the head of day-to-day government in the **United Arab Emirates** – of which he will be the next President. The visit also brought a rare defence deal for the UK.

Much-loved head of state President **Sheikh Zayed Bin Sultan Al-Nahayan** remains the national figurehead and a lively participant in Emirati public life. Ruler since 1966, he sets the tone of UAE foreign policy – as with his very vocal sympathy for the **Palestinians** and a clear public distance from the UK/**US** line on **Iraq**. But Sheikh Zayed does not travel much these days and for the past few years he has entrusted the Crown Prince, born in 1949, with management of most routine government matters, including the big spending decisions. Sheikh Khalifa is Chairman of the ***Supreme Petroleum Council (SPC)***, which monitors ***Abu Dhabi National Oil Company (Adnoc)***, and of ***Abu Dhabi Investment Authority***. Yet it is only recently that Sheikh Khalifa has begun to take a prominent role in international affairs, depicted in the local media receiving foreign dignitaries on his own and making policy statements. The sons by Sheikh Zayed's high-profile wife, Abu Dhabi's 'First Lady' **Sheikha Fatima Bint Mubarak**, have enjoyed a higher profile *(GSN 698/7)*.

The London trip represents a considerable step forward in this process, with Sheikh Khalifa stepping forward to act as the public voice of the UAE in a major western capital. The Foreign and Commonwealth Office press relations team made a point of circulating the media with an invitation to the photocall.

Sheikh Khalifa's presence was extremely useful to the British, showing that, despite the bruises caused by the Iraq affair, the UK retains some firm friends in the Arab world. The Abu Dhabi Crown Prince helpfully lauded Blair's role in promoting the new "roadmap" peace initiative for **Israel**/Palestine and reiterated Emirati condemnation of terrorism. "Islam is a religion of tolerance, and it denounces these acts and abhors bigotry, violence and terrorism," said Sheikh Khalifa.

The visit by a leading Abu Dhabi figure helps to maintain balance in UK-Emirati relations, which have always been characterised by the strong ties to Dubai's ruling **Al-Maktoums**. **Dubai Crown Prince Sheikh Mohammed Bin Rashid** is more or less an honorary member of the British aristocracy, and a dominant player in the racing industry.

Besides meeting Blair, Sheikh Khalifa – who was accompanied by Foreign Minister **Rashid Abdallah** and his half brother, Armed Forces Chief-of-staff **Sheikh Mohammed Bin Zayed** – also held talks with Foreign Secretary **Jack Straw** and lunched with Prince Andrew, Duke of York, who has a business promotional role as the UK's Special Representative for Trade and Investment. Although British companies are solidly established in Abu Dhabi, they face strong competition, while the defence sector has traditionally been dominated by **France** and the USA.

This added frisson to the announcement that the UK and UAE planned to establish facilities for the joint production of naval vessels. The project, bringing together ***Abu Dhabi Ship Building*** with ***VT Group*** to promote sales in ***Gulf Co-operation Council (GCC)*** states, comes after years when British contractors have complained they lose out to France, the USA and other competitors – in part a legacy of antagonisms going back to the period when Sheikh Zayed was left to steer the UAE towards independence in difficult circumstances *(see page 6)*.

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