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What difference will Ronald Reagan make?

Despite the gloom in the Middle East, he will probably be better than Carter

Syria's Assad stores up a troubled future

After a turbulent year he is back on top, but for how long?

The mini-OPECs make their first appearance

OPEC cancels one conference after another as its members regroup

Iraq is trying to pretend that business goes on as usual despite the war with Iran (2). President Assad weathers the storm in Syria but builds up trouble for the future (3). In the fighting in the Gulf, Iraq is slowly beginning to prevail (5). What difference will Ronald Reagan make to US Middle East policy? (6), but he will certainly face difficulties with military strategy (7). Here comes the mini-OPECs (8). Are Egypt and Saudi Arabia making up? (8).

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IRAQ AND IRAN

"Business as usual", but firms find the going hard

Iraq at least is trying to put a brave face on the disruption caused by the war with Iran. But while the fighting continues it is becoming increasingly difficult for companies on either side to go on working because of shortages. Which means that as soon as the fighting dies down, both countries will make a major effort to resume oil supplies to pay for reconstruction.

Last week the fortnight-long Baghdad International Fair was scheduled to open, even though Iraq is still at war and the capital is subject to sporadic Iranian aerial attacks. Although the public were barred from the trade fair, the fact that it is taking place at all testifies to the government's determination to proceed with economic development as if nothing else is happening. It also provided a test case for foreign companies which want to continue doing business after the war. All companies are in something of a dilemma, caught between wanting to pull out during the conflict and conscious of the importance of staying in Iraq's good books by showing willingness despite the dangers and difficulties.

And difficulties there certainly are. None of the foreign workers pulled out of Iraq during the first days of the fighting have returned, and weekly announcements are made of further contracted foreign companies running down their operations in Iraq (not so much because of the danger as the difficulty of getting adequate supplies). President Saddam Hussein has tried to allay fears about rising costs by issuing a decree providing for the formation of a special committee to examine the "abnormal conditions" caused by the war, and set compensation terms and amend fixed price contracts. On the other hand, companies pulling out will be viewed with disfavour in the future.

One of the most serious effects of the fighting with Iran has been to give a sharp upwards push to price, and this is putting a severe squeeze on companies which have secured large civil engineering contracts by submitting bids that allow for only very narrow profit margins.

What of the future? Iraqi officials point confidently to massive gold and foreign exchange reserves (estimated to be in the region of $20 billion) as a guarantee that – war and the oil cut-off notwithstanding – Iraq can go on a long time importing at last year's rate of $5.5 billion without recourse to external financing. But obviously there will be considerable pressure to resume the oil-generated cash flow as quickly as possible. Most foreign estimates presume that Iraq's damaged export terminals and pumping facilities can be repaired within a few months of the cessation of hostilities; the oil fields themselves do not appear to have suffered (*MEN 20 October 1980*).

The outlook for Iran is a lot less promising, though the few foreign companies still working there are anxious as well to prove willing. Mitsui has constantly reiterated that despite yet another cessation of activity at the plagued Bandar Khomeini petrochemical plant it will not use the new interruption (and the damage to the project) as an excuse to pull out. But with far smaller reserves – and a good proportion of those still frozen by the United States – Iran will be even more eager to get oil moving once the fighting has died down.

Once the conflict dies down, Iraq could probably get about 700,000 b/d out through the trans-Turkey pipeline (of which 100,000 b/d is offloaded by Turkey). If the Syrians allow it in

This is the last issue of the *Middle East Newsletter* in its current form. Starting next issue, the *Middle East Newsletter* will appear in three separate fortnightly parts to provide extended coverage of the region. Still under the general title *Middle East Newsletters*, these will cover *Saudi Arabia* (a development of our existing *Saudi Arabia Newsletter*), *Egypt/North Africa* (an expanded version of our *Egypt Newsletter* now taking in Libya, Tunisia, Algeria and Morocco) and a completely new publication covering the *Gulf States* (Iraq, Iran, Kuwait, Bahrain, Qatar, the UAE and Oman). We hope that by devoting considerably more space to events in the Middle East we will provide our subscribers with a more thorough and extensive picture of economic, financial and political developments.

present conditions of very strained relations, another 500,000 b/d can be taken through Banias. But that means even if Iraq can resume pre-war production at 3.4 million b/d, with the closure of the Gulf terminals over 2 million b/d will be stuck – and more if Syria chooses to be obstreperous. Without alternative export facilities, Iran depends entirely on its Gulf terminals for export (running at about 700,000 b/d before the war).

It could, therefore, be several months after the re-establishment of peace before oil exports are resumed on any scale by either side. And it will take a long time before Iraq is sending out the 3.4 million b/d it was exporting before the war. On the other hand, both countries will be desperately eager to resume exports as quickly as they can (and at as great a volume as possible, which could signify the first Iranian effort to stop the slide in oil exports) because they will have to pay for reconstruction over and above already planned current and development expenditure.

Where will the money go? In Iraq's case, first and foremost to make up the army's losses. That can be expected because Saddam Hussein must appease his armed forces if he wants to survive a somewhat inglorious military campaign which he has identified as his own. And if he does not survive, his military successors will waste no time in making up the damage. The same may not apply to Iran, because the clerical element is still very fearful of a powerful army and can argue that the brunt of the fighting was done by revolutionary guards equipped with light weapons rather than ultra-expensive tanks and aircraft (where were the F-14s?). On the other hand, President Bani Sadr has tried to identify Iran's defence with himself, and might be open to rebuilding a smaller and more cohesive army after the shock of the Iraqi attack on Iranian territory.

For both sides, the big economic priority will be reconstruction of the oil industry, simply because that alone earns the hard currency to pay for everything else. Only then comes spending on industrial and infrastructural projects, which can be expected to slow down in both countries. In Iraq, the slowdown should be only temporary, and followed by an acceleration to erase the feeling of setback after the war. In Iran, however, it is uncertain just who would be inclined to carry out the reconstruction after this latest lesson in why not to do business with the Iranians. More than ever, Iran will feel the pinch on its hard currency, and that could lead to barter deals with the Soviet bloc for oil in exchange for hardware.■

SYRIA

Beneath the surface calm lurks trouble for the future

Outwardly Syria looks calmer than it has done for a long time. President Assad has successfully broken the back of the Moslem Brotherhood, but his forthright repression may prove in the long run to be fatally costly. None of the underlying problems of his regime have been solved by this year's violence which has weakened the regime's chances of surviving further disturbances.

The sheer extent of the brutality employed by President Hafez Assad in Syria to ensure his survival is only now becoming apparent abroad. Recent reports from the country indicate that victims of the regime's repression may be measured not in hundreds but thousands since the massive clampdown was ordered earlier this year. On occasions this has taken the form of full-scale military operations – such as the house-by-house "cleansing" of the northern city of Aleppo in April and again in August and the assault on the rebellious town of Jisr al-Shughur further south where helicopter gunships were employed.

As a result of firm action, Hafez Assad and his associates have survived a major threat to the regime, chiefly from the fundamentalist Moslem Brotherhood. At one time there were serious doubts as to whether he would come through (*MEN 7 April 1980*), especially as the middle classes and professionals tried to take advantage of the growing turbulence to express their own opposition. The seriousness of the threat can be judged by the fact that arrests and killings of suspected Moslem Brothers are still going on as reports of attacks on army patrols filter through. Judged by past evidence, the incidents which do get reported are only a small proportion of the ones which actually take place.

But if President Assad has restored himself, he has only done so at a considerable price which may ultimately prove fatal to his regime. Most obviously, by abandoning his normally shrewd act of balancing political pressure groups off against one another and permitting just enough political and economic leeway to release tensions, Assad has entrusted his stability in the future entirely to the use of force. The experience of the last few months has left a gloomy and oppressive atmosphere in Syria beneath the surface calm with a host of bitter opponents vowing revenge. In casting aside his reliance on stealth and compromise in one of the Middle East's more factional and sectarian countries, Assad has moved onto unsteady ground.

The cost of doing so is likely to be heavy. As Assad mops up what is left of the active opposition, it may seem rather premature to talk of new threats to the regime. But his tactics of this year have not only stored up resentments which are bound to resurface eventually. They have also demonstrated the regime's unwillingness to tackle the very abuses which have fuelled the revolt. If Assad has to face the same degree of opposition in the next few years, he is much less likely to survive than this time.

Much of Assad's problems derive from the very means with which he has lasted as long as he has (he seized power in 1970). Syria has an unrivalled history of coups in the Middle East, and although the Baath party has held power since 1963 it is a faction-ridden group itself. Assad has remained on top because he deliberately set out to create a firm and loyal power base, but this has been shown to contain the seeds of its own weakness. He has relied partly on the exclusive and secretive Alawite sect (a heretical branch of Shiite Islam) which is much resented by the Sunni majority in the country from whom the Moslem Brotherhood spring, and he has extended his support by the creation of a privileged group of army officers, party functionaries, government bureaucrats and favoured businessmen who have taken full advantage of their position.

Syria's socialist and centralized economic structure has proved an ideal environment for this privileged group to use the government machine for personal enrichment, and officially tolerated corruption on a vast scale has been the bane of the regime for years. In 1977 and 1979 mounting public criticism prompted the authorities to institute anti-corruption campaigns, which (if they demonstrated the regime's consciousness of the problem) were entirely ineffective because the culprits themselves were ultimately in charge of the purges. After 1973 Syria embarked on an unprecedented economic boom which opened up new opportunities for graft. Now that recession has set in, corruption is simply resented all the more.

The purist Moslem Brothers chose as their targets supporters of the regime, many of whom were members of the Alawite sect. Since they took to assassination and bombings in 1976, nearly 400 of Assad's supporters have died. It was an attempt on Assad's own life this spring which unleashed the regime's single-minded repression. What the severity of the (still-continuing) campaign against the Brotherhood has undeniably revealed is the strength of its organization and the broadness of disillusionment with the regime. The middle classes (as represented by the now dissolved professional organizations) are certainly no lovers of Islamic zealotry, but at the height of the disturbances they came out tellingly against President Assad with demands for the dissolution of the Baath party, the cancellation of relations which the Socialist bloc, the restoration of parliamentary democracy and the guaranteeing of personal liberties.

Apart from "daily incidents" involving sporadic clashes with the remnants of the Brotherhood, Syria is now quiet if sullen. But President Assad is clearly conscious of his isolation both at home and abroad (hence the unlikely and largely abortive "union" with Colonel Kaddafi's Libya and the treaty of friendship with the Soviet Union). To make his prospects worse, he cannot count on an improvement in the dire economic climate. His alliance with Moscow will deter the Gulf oil producers (already worried about Soviet ambitions in the Middle East and South Asia) from continuing to provide all their pledged $1.5 billion in annual aid. Nor has Kaddafi come up with any cash. Economic growth has slumped from a yearly 10% to 4%, the trade deficit is likely to double this year and foreign exchange reserves are dangerously low. Although he minimum wage has been raised, it is still pitifully low. The government simply cannot afford to pay more, but unofficial estimates of inflation are in the region of 20%. None of which adds up to the recipe for social peace which the regime so desperately needs in the aftermath of this harrowing year.

On the credit side, Assad can count on the docility of the middle classes so long as they are making money. And for the time being the battered Brotherhood will be no more than a rather violent nuisance. But Assad's relations with the rest of the Arab World now vary almost entirely from the poor to the downright dreadful.■

WAR

Iraq thinks it's winning but this isn't the end

Iraq's armed forces are beginning at long last to prevail on the battlefield against Iran as the slogging match takes its toll. Fuel and spare part shortages are beginning to tell on the Iranian side, and there is a note of desperation in official announcements. However, a cessation of fighting will not lead to peaceful negotiations but be a prelude to a war of attrition.

Iraq's armed forces apparently sense that the balance of fighting on the Iranian front has swung decisively their way in recent days. Iran has consistently reported successful counterattacks against the invaders, but subsequent news from the front tends to support the view that Iraq is pressing slowly but inexorably forward. For all intent and purpose Abadan has fallen and fighting now appears to be taking place along the road eastward into Iran towards Mahshahr. That would indicate an Iraqi strategy of pushing further into Khuzestan in order to bring Iran to the negotiating table *(MEN 3 November 1980).*

But there have also been reports of fighting in areas far further north which have hitherto been relatively untouched. There are some indications that Iraq is pushing towards Kermanshah, directly east of Baghdad, on the assumption that the Iranians have denuded the more northerly frontiers to maintain their defences around Dezful and in Khuzestan. Again, the Iraqi strategy is not so much to occupy extensive areas of the country as to demonstrate its ability to occupy key points and persuade the Iranians that their only recourse is to talk.

For the first time, too, Iran seems to be flinching under the steady if unspectacular advance of the Iraqi ground forces. Last week, Iran's Supreme Defence Council in Khuzestan announced that it was seeking clarification of "ambiguities" in the five-point peace plan put forward on behalf of the non-aligned nations by Cuban Foreign Minister Isidoro Malmierca. This is hardly tentamount to Iran sueing for peace, but it does indicate a degree of anxiety at least among those close to the front.

There is no guarantee that any such feelings are shared back in Tehran. But even there recent declarations by deputies in the Majlis point to an awareness of the gravity of the situation. Undeniably, the war is being brought home to the man in the street far from the front line: last week, for instance, saw the announcement by the Economic Mobilization Headquarters of increases in the price of gasoline for private citizens.

So how difficult is Iran's position? Most military analysts are confident that there will be nothing like a major Iraqi breakthrough, partly because the Iranian front is falling back rather than disintegrating, and partly because deep armoured penetration has not been the Iraqi strategy so far. But the Iranian armed forces are unquestionably feeling the pinch of a shortage of spare parts and fuel. Because of the lack of aircraft fuel, transport flights are apparently being kept to a minimum, and the same constraint applies to a lesser degree to land transportation. Even Iranian artillery is replying with decreasing frequency to Iraqi bombardment.

Especially hard hit is the air force. Iranian air activity has declined noticeably in recent weeks – not only because fuel is in short supply but because there are not enough tyres to go round (a Phantom F-4 fighter works its way through a set of undercarriage tyres every five or six sorties). The Phantoms have not engaged in aerial combat because (according to US assessments based on AWACS observation) their sophisticated onboard identification system is not working sufficiently to prevent them shooting down friendly aircraft in the skies. And although the F-14 Tomcat has now been seen in the sky, it has not used its Phoenix missiles. Indeed, it is a reflection on the general state of the fighting that most of the aircraft casualties on both sides have been the result of simple anti-aircraft artillery.

There also appears to be a serious deterioration in Iranian regular army morale, according to some Western sources recently reported to be in contact with the Iranians. The regular army units are understood to have been undermined by the government's attitude that they are on the same operational basis as the revolutionary guards.

Although no-one (least of all the Iraqis) totally discounts the possibility that the Iranians could manage to mount some kind of counter-offensive, it is generally believed that lack of organization, poor relations between the regular army and the revolutionary guards, shortage of fuel and lack of spare parts have all effectively consigned the Iranian forces to a holding posture. On the other hand, the Iraqis are playing a careful game, aware that even as the battle at last swings decisively their way on the ground it would be foolhardy to press ahead too far and spread resources too thinly.

There are signs, therefore, that Iran's logistical problems are leading to a decrease in fighting, and that the Iraqis will take advantage of this not to push ahead with any major new offensive, but rather maintain their pressure in the hope that Iran will signal its willingness to negotiate. It will take a long time for negotiations on the hostages to lead to resumption of US arms to Iran; nor will Soviet supplies of jet fuel or airlifted Libyan ammunition and explosives be sufficient to restore the balance. But if the conflict does wind down, there is every likelihood it will be resumed (perhaps on a smaller scale) once Iran has caught its breath. Far from Iraq's "victory" leading smoothly to a settlement of the dispute around the nagotiating table, a ceasefire will merely be a prelude to the kind of rumbling war of attrition which followed Egypt's defeat by Israel in 1967 for several years.■

UNITED STATES

Will Reagan make much difference in the Middle East?

The election of Ronald Reagan as the United States' next President was greeted in the Arab World with either fear or foreboding. Certainly his campaign rhetoric offers little comfort to Arab leaders. But the policy changes he is likely to make (on Camp David or US exports) are hardly retrogressive, while in other areas (military involvement) he will pursue the Carter line.

Most Arab leaders who did care something one way or the other (which is to say those with a pro-American tilt) were hoping for the re-election of Jimmy Carter as American President earlier this month. In President Sadat's case this was a commitment to the architect of the Camp David process; for everyone else it was a case of better the inept President you know than the rather rhetorically frightening challenger you do not. In the event, they got Ronald Reagan. Sadat delivered a speech which sounded less like a congratulation to the incoming President than a requiem for the outgoing incumbent. But otherwise the disappointed Middle Eastern Carter supporters tried to put a brave face on the result. Will the outcome make any real difference?

As far as the Middle East is concerned, Reagan's most outstanding characteristic is his pro-Israeli leanings and horror of the PLO. Even after his election he found time to denounce the PLO as a "terrorist organization", a constantly reiterated statement which must be music to Israeli ears. Arab forebodings have been increased by the marked Zionist sympathies of many of his campaign foreign advisory staff (two of them, Edward Luttwak and Uri Raanan, are Israeli citizens).

That, plus his rejection of Camp David ("we don't intend to mandate or dictate a settlement to promote peace in the Middle East") looks bad news for Sadat. But the outcome may yet prove advantageous for Egypt and the Arab moderates.

First, Reagan and whatever turns out to be his team will have to undergo that traditional and inevitable process of presidential "education" about the Middle East whereby campaign rhetoric gives way to a more nuanced approach to the Arab-Israeli conflict. President Reagan will have many more pressing problems on his agenda when he assumes office on 20 January, and even the most optimistic Middle East hands do not expect the full weight of the administration's attention to turn to the Palestinian autonomy question before June. By that time it should be learning fast.

Second, Reagan's rejection of the Camp David process is hardly a disastrous omen. Camp David has already proven to be a lamentable impasse which requires for extrication someone less committed to its success than Carter. Reagan has made it plain that he wants to bring in a wider circle of negotiating parties (his eye is specifically on Jordan). And while the sceptics may well be right in thinking that any new initiative is unlikely to get much farther than the old one, at least it will introduce some fresh thinking in time for the Begin government's expected demise next year.

All in all, the outlook is not all that rosy for Israel. First indications are that Reagan is not picking a heavily pro-Israeli team of advisers. Some members of his transition team have noted Israeli sympathies (Senator Henry Jackson and former Senator Richard Stone among the Democrats he has picked). But others were reared in the tough (if unattractive) school of Nixon-Kissinger realpolitik. The real proof must obviously await the selection of the cabinet and White House staff.

In the Congress, meanwhile, there are definite signs that the new batch of influential Senate leaders may be less susceptible to the Zionist lobby. The new Republican Senate majority leader, Howard Baker, is less pro-Israel than the outgoing Democrat Robert Byrd. Mark Hatfield, the new chairman of the Appropriations Committee, earlier this year recommended a cut of $150 million in aid to Israel. But most important will be the chairman of the Senate Foreign Relations Committee. Of the two leading contenders, Senator Charles Percy is considered likely to be much more amenable to Administration pressure on Israel than his predecessor Senator Frank Church. He is also thought to be sympathetic towards Saudi views. Even his rival, arch-conservative Jesse Helms, would be far from a thoroughgoing Israel supporter.

Reagan has also sent a frisson of nervousness through some of his more faint-hearted allies by his frequent hints of willingness to use military force. But although he undoubtedly favours heavy defence spending, even his more extreme campaign pronouncements do not seem to foreshadow military adventurism. In contrast with the early President Carter, he is likely to respond much more aggressively to anything he may perceive as a threat to American interests abroad. But in doing so he will merely be following the path that President Carter had himself begun to tread with the formation of the Rapid Deployment Force *(see box)*.

Businessmen, meanwhile, can only welcome the Reagan victory. A Republican-dominated Senate will be in two minds about the World Bank and the International Monetary Fund. On the one hand, a Reagan Administration and a conservative Senate will be tempted to tie political strings to contributions for international financial institutions. On the other hand, they will both be more responsive to pressure from US corporations to release funds for such institutions because it will enable developing countries to buy more US goods.

More important will be the Administration's and Congress' view of the Export-Import Bank. The Carter Administration's failure to provide adequate concessionary finance to US exporters (typified by Carter's refusal to increase Eximbank's fiscal 1981 allocation above $5 billion) is – in the eyes of the business community – seriously hampering US export efforts. Carter effectively controls the 1981 budget, so there will be relatively little that Reagan can do until the beginning of fiscal 1982 next October. But he could well lean towards active support for exports, and will certainly be encouraged to do so by the favourite to take over the Senate Banking Committee, Senator Jake Garn, who is a major supporter of Eximbank's role in furthering the export effort of US corporations.■

Big ambitions, smaller resources

What will be the shape of President Ronald Reagan's military policy in the Middle East? Presumably neither he nor his advisers knows as yet, but some pretty shrewd guesses can be made. The Republican candidate's apparent enthusiasm for speaking loudly and wielding a big stick abroad will not be a reversal of President Carter's careful non-intervention but a continuation of his more forward Rapid Deployment Force strategy.

Any changes are likely to arise because Reagan does not consider Carter is doing enough. As presently conceived – and slowly taking shape – the RDF consists of several merchant ships loaded with supplies for an expanded Marine division at Diego Garcia in the Indian Ocean, base facilities in Oman, Kenya and Somalia, the stationing of a fleet in the Indian Ocean, and periodic exercises in Egypt *(see page 8)*. Many Reagan-watchers think that the new Administration will go further than mere facilities and seek outright bases in the area.

But Reagan's big problem will be finding the resources to beef up his Mideast presence. A bigger naval force in the Indian Ocean means stripping the Seventh Fleet in the Pacific just as the Soviets get stronger there. Furthermore, it has generally been envisaged that a Middle East intervention capacity would rely to a considerable extent on US forces now in Western Europe. Unfortunately, the West Germans and the British simply are not prepared to increase their own defence spending to take up the slack.

OIL

Here come the mini-OPECS

The Iraqi-Iranian conflict has taken a severe if often indirect toll of OPEC's always fragile unity. Already several major OPEC conferences have gone by the board, including the 20th anniversary summit scheduled for Baghdad at the beginning of this month, a finance ministers' meeting in Quito and an oil ministers' consultative meeting in Vienna. A large cloud hangs over the next scheduled regular oil ministers' conference in Bali, Indonesia next month (especially as the Iraqis have made a prisoner of war out of Iran's new Oil Minister). At the end of the day, OPEC is no more than its conferences. Once these start getting cancelled, the future of the organization looks increasingly insubstantial.

In its two decades of existence, OPEC has known plenty of divisiveness. For all the organization's commitment to commonality of purpose, each member has jealously guarded its right to define its own production (and of late pricing) policy. Tellingly enough, Saudi Arabia has been the most insistent advocate of OPEC unity and at the same time the most prepared to flout majority wishes on output levels and prices (the first quarter of 1977 and the two years since the Iranian revolution are obvious cases).

Until this summer, however, OPEC has survived as a formidable alliance if not exactly as the cartel publicized by the Western industrialized nations. But what is happening now portends something rather different. The Arab Gulf producers have ganged together with greater or lesser enthusiasm to compensate for the Iraqi-Iranian shortfall on their account. This has been done under Saudi prompting chiefly as a result of a secret meeting in Taef in October. As far as is known at present, the additional output promised by Saudi Arabia, Kuwait, Qatar and the UAE for the last quarter will be adjusted according to specific market conditions and directed to those countries which have suffered worst from the cut-off from Iraq and Iran rather than poured indiscriminately onto the international market. But the fact remains that the rest of OPEC was not consulted at all.

To add to the enmity between Iraq and Iran (it is almost impossible to see representatives of the two sides sitting down round a conference table), this and the Saudi call for American help has led to a disruption of relations between Libya and Saudi Arabia. Meanwhile, Libya and other African OPEC producers (Algeria, Nigeria and Gabon) have had their own meeting in Algiers where they decided – once again on their account – to help African countries caught short by the Gulf conflict. No actual pricing decisions were taken because it was an informal meeting, but the four producers are certainly keeping a close watch on the evolution of the spot market. They definitely envisage a concerted increase in their benchmark prices from \$37 to \$40 a barrel – and ruled out extra production as a means of helping their importing neighbours *(see page 11)*.

At the same time another informal OPEC subgroup made its first nebulous appearance at a meeting of economic experts of the Islamic Conference in Ankara. Here Moslem members of OPEC pledged to give other Moslem states priority in exports of crude oil within the framework of a projected Islamic economic bloc. Given the venue of the meeting, it is not difficult to conclude that these reassuring words were chiefly directed to chronically oil-short Turkey, but the wider implication is that a new forum of oil decision-making within OPEC may emerge. None of this is necessarily a prelude to the disintegration of OPEC, but so long as OPEC meetings are put off coordination among the oil exporters will increasingly fall into the hands of regional or religious groupings. Now watch out for a Latin American oil forum. ■

SAUDI ARABIA AND EGYPT

Now will you play the game?

For the past few months there have been more than one false start to a Saudi-Egyptian rapprochement, but the Gulf conflict may prove to be the vital element in bringing the two countries together again. *MEN* learns from Cairo that Egypt and Saudi Arabia have effectively buried their differences, but for the moment neither side can work out how to reveal the fact without undue embarrassment.

Earlier in the summer the climate seemed ripe for a coming together *(MEN 30 June 1980)*. The passing of the deadline for Palestinian autonomy talks stalled the Camp David peace process altogether, giving President Sadat a chance to alter course graciously. In the hope that once the American presidential election was over, Washington would provide a new impetus by putting pressure on Israel, Sadat unfortunately gave no indication of disavowing any elements of his past policy. So nothing concrete happened.

Now that President Carter has been voted out, the shape of future Egyptian-Israeli negotiations is hard to tell. Certainly, the slow process of normalization of relations is continuing (a new trade exchange agreement has been signed), but Egypt is still dragging its feet and – by implication – keeping its options open. Intriguingly, these seem to include the maintenance of secret but very definite contacts with Saudi Arabia.

Saudi Arabia's implicit acceptance of the United States' ultimate role in protecting Gulf security (as expressed in the request for American aerial radar surveillance aircraft shortly after the Iraqi-Iranian war broke out) brings the kingdom much closer into line with Egypt's far more enthusiastic wooing of Washington's military might. Repeated US military exercises in Egypt culminated this month in the arrival of a training force at the projected US base at Ras Banas on the Red Sea and the despatch of 1,400 combat troops and a squadron of A-7 ground attack aircraft for exercises at Cairo West air base. Since the beginning of the year, Sadat has openly made Egypt available for the role of Washington's most important advance base for intervention in the Middle East. With the United States' jumping off point suitably (but not too distantly) removed from the Gulf, Saudi Arabia can benefit from a notional US defence umbrella (*see above*) while not having to suffer the ignominy of American troops actually based in the Gulf region.

The Saudis have been keen in recent months to encourage a rapprochement with President Sadat. And the Egyptians are discreetly responding. Egyptian emissaries turned up in the kingdom last month – ostensibly on pilgrimage to Mecca – and Sadat has stopped his vitriolic attacks on the Saudi royal family. Also last month US chairman of the joint chiefs of staff General David Jones visited Saudi Arabia and Egypt and is understood to have told the Egyptians that Saudi Arabia was now ready to cooperate in the protection of its oil fields.

The big stumbling block, of course, is Sadat's peace initiative with Israel. Depending on what President Reagan does, Sadat is unlikely to cut the tenuous links he has established with Israel (now he is waiting for the advent of the Labour party to power in next year's Israeli elections). And as the Egyptians see it, the job of restoring relations is really up to the Saudis since it was they who broke off in the aftermath of the Egyptian-Israeli treaty last year.

A formal announcement of renwed friendship is hence highly unlikely. Instead, what will happen is a steady but low-key intensification of cooperation between Saudi Arabia and Egypt (particularly in the security sphere). Much as they hate to swallow President Sadat's policy towards Israel, the Saudi rulers are far more frightened about their vulnerability (real or feared) in the Gulf. With the Arab World in unprecedented disarray, Saudi Arabia's traditional policy of trying to maintain some form of Arab consensus lies in ruins. Searching for like-minded friends, it has little option but to throw in its lot quietly with President Sadat. ■

Business fortnight

Trade and economy

● The Gulf conflict is affecting **Bahrain's exports** to the combatants. Orders totalling an estimated $4 million placed with Bahrain Aluminium Company have been held up to both Iraq and Iran. Balco is the marketing agent for Aluminium Bahrain which hopes to make deliveries to Iraq's aluminium rolling mill, extrusion and cable complex through Kuwait. No deliveries have been made to Iran since fighting broke out in September.

● On the other hand, the Gulf conflict has had little effect on orders at the **Arab Shipbuilding and Repair Yard** (ASRY) in Bahrain. Although company officials are reported as saying that high war-risk insurance premiums may deter some potential customers from entering the Gulf, forward orders are still good with five VLCC's booked in before the end of the year. Since oil tankers are continuing to load in the Gulf, ASRY expects to weather the crisis comfortably, and it is hoped to draw extra business eventually from the ships currently trapped in the Shatt al-Arab because of the Iran-Iraq war.

● More companies operating in **Iraq** are halting work as a result of disruption from the conflict. The latest companies to suspend work are Brazil's ESUSA and Constructora Alfredo Mathias building hotels and Mendes Junior Construtora building the Baghdad-Hussaibah railway.

● **Jordan and Iraq** have confirmed their closer economic ties with a cooperation agreement signed at the beginning of the month in Amman. Collaboration in transport, supply, construction materials and transit have been decided upon. The agreement calls for increased use to be made by Iraq of Jordan's Aqaba port (*MEN 20 October 1980*), confirms plans for the recently formed Iraqi-Jordanian Land Transport Company, and promises study of a rail link between Aqaba and Iraq.

● The Western embargo of direct trade with Iran seems to be proving handsomely profitable to **Dubai** as a transit centre. Goods valued at more than $2.6 billion were imported through Dubai in the first half of 1980 according to statistics published by the central accounts department. This represents a 32% increase over the corresponding period of 1979.

● Agreement has now been reached on the scheduled increase for **Suez Canal rates**. An average increase of 30% is understood to have been made, effective from next January. Details of the increase are in the hands of the International Chamber of Shipping.

● Speculation abounds that **EgyptAir**, the state-owned airline, may be dismantled in favour of private sector operation under auspices of the ruling National Democratic party. EgyptAir's board was dismissed earlier this year, and the new proposals are said to be provoked by lack of sanctions against unsatisfactory employees while low wages are damaging efficiency. According to the reports, EgyptAir would take a 50% share in the new operating company which would take over the most effective portions of the company (with the most competent staff being paid competitive wages).

● **Egypt's balance of payments** has made a remarkable recovery in the past year despite the Arab boycott, according to the recently published Central Bank report submitted to the People's Assembly. The current account deficit declined to only $E11.2 million ($16.2 million) in the first six months of 1980 compared to $E557 million in the corresponding period of 1979. Exports are also rising faster than imports: in the six month period oil revenues reached £E859 million compared to £E306 million last year, workers remittances from the rest of the Arab World rose from £E683 million to £E936 million, Suez Canal revenues grew by 25% to £E230 million and tourist revenues by 16% to £E200 million. With foreign aid at $2 billion a year added into the current account balance, Egypt has more money than it needs to cover daily needs for the first time in more than a decade.

● **Egypt and Israel** have signed a memorandum of understanding to improve land-borne trade exchanges. Goods will henceforth be transferred from truck to truck at a Sinai border post since Egyptian law forbids foreign commercial vehicles from operating in Egyptian territory. There have been problems hitherto in clearing merchandise from Israel to Egypt which it is hoped the new arrangements will overcome. Egyptian orders for Israeli agricultural equipment are in the pipeline, while Israel is reportedly interested in Egyptian cotton seed, textiles, onions and chemicals, as well as the oil supplies sold under the terms of the Egyptian-Israeli treaty.

● Instituto Biochemico Italiano of Milan has formed a joint venture **pharmaceuticals company in Egypt** with Misr International Bank and the Egyptian government to be known as Advanced Biochemical Industries (ABI). The company is capitalized at $1.4 million and will produce pharmaceuticals, fine chemicals and cosmetics, eventually supplying Egypt's needs for synthetic penicillins. Other private pharmaceutical companies producing in Egypt are West Germany's Hoechst, Pfizer and Squibb of the United States and Swiss Pharma of Switzerland.

● **Israel's trade union** confederation, the Histadrut, is threatening selective industrial action in response to a Bank of Israel forecast that the annual rate of inflation will soon rise to 160%. The impetus for the threatened strike action was the government's decision this week to increase the price of fuel by 25%. The Bank of Israel expects that last quarter 1980 inflation will run at an equivalent annual rate of 160%, compared with 90%, 150% and 125% in the first three quarters respectively. Inflation last year was 111.5%.

● Israel is planning to invite representatives of Latin American countries to Israel to study the purchase of the **Kfir combat aircraft**. Previously Ecuador had shown interest in buying the plane, but like other potential export orders this was blocked by the United States which supplies the General Electric J-79 engine. In a significant policy change just before the election, President Carter gave permission to Israel to offer the plane for sale to Mexico, Venezuela and Colombia.

● **Kuwait** is going into the desalination business on its account instead of depending on purchases of equipment from abroad. The Finance Ministry and four semi-public financial institutions have incorporated the Kuwait Company for Manufacturing Seawater Desalination Units. It plans to sign an agreement before the end of the year to buy technology from a foreign company. In the running for the contract are understood to be Japan's Ishikawajima Harima Heavy Industries and Britain's Weir Westgarth. Both firms are currently in the bidding for supply and installation of 12 six million gallon-per-day units at Doha West power station along with another Japanese consortium (Mitsui, Sasakura and Mitsubishi) and an Italian group consisting of Ansaldo, Nuovo Reggiane and Tonolli.

● **Saudia**, the Saudi national airline, has recorded major increases in turnover and losses for 1979, according to its recently issued annual report. Operating revenue rose to 3.2 billion riyals ($962 million), which was a quarter up on 1978, but expenditure rose by more than 25% to 3.4 billion riyals ($1.03 billion). The consequent gross operating loss was 237 million riyals ($71.3 million), up 50% on the previous year.

● Bids are being evaluated for four construction contracts to be let before the end of the year in the $2.4 billion **Vocational Training** and Training Centre Construction programme in Saudi Arabia. Each contract entails building a training centre and a housing complex at Abha, Hasa, Al-Qasim and Riyadh. Lowest contractor for the Riyadh contract is Nam Kwang Construction of South Korea ($72.2 million). South Korea's Chin Hung International submitted the lowest bid for the Hasa contract ($37.6 million), while front-runners on the other contracts are local companies (Bahreth Organization at $42.1 million for Abha and Al-Rashid and Al-Omran at $46 million for Al-Qasim).

● Reports that the joint venture between LM Ericsson of Sweden and Philips of the Netherlands is expected to win a third extension to the **Saudi telephone expansion programme** have been dismissed by Philips as pure speculation. The two companies won an extension contract last year, but no decisions have yet been made on almost $500 million in extension work envisaged under the plan.

● Wescon Nederland and JGC Corporation of Japan are carrying out a feasibility study for an **ethanol plant in south Sudan**. According to Japanese reports the plant will produce 120,000 litres of ethyl alcohol (ehtanol) from 2,000 tons of sugar-cane waste a day. The project may involve planting sugar cane on 12,000 hectares of land, and (although Wescon says no specific plans have been drawn up) the company says it is interested in a complete agricultural project. Cost estimates vary between Japanese reports of $142 million and Wescon's approximate $70 million.

Oil and minerals

● **Western countries** can readily achieve the cuts in oil imports and consumption they aim to make in the next decade (even though goals set for increased non-oil energy use appear "very far out of reach"), according to a study by Chase Econometrics. The study by the Chase Manhattan Bank subsidiary argues that reduced oil imports can be reconciled with slower-than-planned non-oil energy expansion because of the gloomy international economic climate. The seven-nation Venice summit last June pledged support for the IEA's plan to cut member's oil imports to about 22.5 million b/d by 1985 (compared to this year's target of 24 million b/d). Chase feels that this could be cut to 19.2 million b/d. The report is based on the assumption that major Western economies will grow by only 2.7% annually during the 1980s with total energy requirements rising by 1.5% a year.

● Oil Ministers of **OPEC's four African members** – Algeria, Libya, Nigeria and Gabon – have announced after a meeting in Algiers that they intend to divert part of their output to African countries hurt by the loss of exports from Iraq and Iran due to the Gulf war. Production will not be increased nor output cuts (estimated at 9%) restored, but relief supplies will be found by renegotiation or non-renewal of existing contracts.

● Following agreement with Abu Dhabi to take an extra 50,000 b/d of crude to help make up the Iraqi shortfall (*MEN 3 November 1980*), **France** is to receive 120,000 b/d of additional crude from Saudi Arabia under a three-month contract signed with Petromin. The oil will be delivered to CFP-Total and Elf-Aquitaine in addition to 260,000 b/d delivered under a three-year contract signed in December 1978. Saudi Arabia has also agreed to supply an extra 20,000 b/d to Petrobras of Brazil. Saudi Arabia has said it will use its additional output to help countries most affected by the war, and these are reported to include Brazil, Turkey, France, Japan, Italy, Spain, Greece, Yugoslavia, India, Pakistan, Morocco and Somalia. There are unconfirmed reports of additional suppy contracts having been arranged for Japan (40,000 b/d) and Pakistan.

● The **Netherlands** is reported to be seeking an extra 100,000 b/d in oil supplies from Saudi Arabia under a direct government-to-government deal. This will constitute an important policy change from reliance on Royal Dutch Shell and the spot market.

● International firms have been invited to prequalify for the modernization and expansion of **Kuwait's Mina Abdullah refinery**. Industry sources say the contract may be similar to or even exceed the $500-$700 million contract recently awarded to Japan's JGC Corporation for modernization of the Mina al-Ahmadi refinery.

● **Libya** is expected to renew its oil supply contract to Spain's Hispanoil on much more stringent terms. The current 1975 agreement (which expires at the end of this year) provided for deliveries – at 100,000 b/d this year – to be paid for at a price equivalent of 65% of the prevailing level, with the remainder considered at the end of the year as a dollar loan at 1.5% below LIBOR. The 1980 loan component is expected to be about $250 million. Libya is understood to feel that the terms are far too generous in the climate of the 1980s, and (worried about supply security) Spain will not be in much of a position to bargain.

● The contract to build a 50,000 b/d refinery at Umm Said in **Qatar** has gone to Technip of France with a final bid of $138 million (beating JGC and Chiyoda Engineering of Japan). The refinery will be completed in two and a half years and be built next to the existing Umm Said plant. Technip is already working in Qatar on the ethylene plant at Umm Said. The new refinery is expected to meet local demand for refined petroleum products until 1995.

● Saudi entreprenuer **Sulaiman Olayan** has been elected to the board of directors of Mobil. The move is seen as a gesture by the American oil company towards building up its involvement in the Saudi oil industry with the imminent takeover of Aramco (in which it is a junior partner with Exxon, Socal and Texaco). Olayan is already a major shareholder in First Chicago Corporation.

Banking and finance

● The fourth meeting of the **Consultative Group for the Development of Egypt** (sponsored by the World Bank) will take place in January in Cairo. According to *Al-Ahram*, the transfer of the meeting (originally scheduled for Paris) was in response to Egypt's improving balance of payments postion (*see above*). The World Bank is also setting up a Cairo branch and raising aid in 1980 to $500 million as compared to $400 million last year.

● **France** has agreed to commit 625 million francs in soft loans to Egypt. A quarter of these will be in the form of government aid at 3% interest, with the rest in export credits at 7.5% interest. The new protocol brings French concessionary aid to 1.1 billion francs this year. About a third of the finance is earmarked for new projects, including the Cairo metro and Damietta port expansion.

● Financial problems have forced Bank Melli of Iran and the Industrial and Mining Development Bank Iran to sell their 25% shares in Egypt's top development bank **Misr Iran Development Bank** (MIDB). Last year the bank's capital was doubled from $20 milion and it was the Iranian banks' failure to meet the second instalment of the capital increase that forced the sale. MIDB's chief executive, Fuad Sultan, said he had received requests from a number of prime purchasers to take up the shares.

● Heavy speculation in the **Arab International Insurance Company's** (AIIC) share issue prevented the Bahrain Commerce Ministry allowing the issue to go ahead until the very end of October. AIIC (an exempt company which under Bahraini regulations is not required to have a controlling Bahraini interest but enjoys tax advantages) offered 2.5 million shares at a face value of $1 apiece out of an issued caital of $6 million eventually allotted shares on a basis of 1.47 per 1,000 applied for – indicating that the issue was 680 times oversubscribed. The ministry was initially suspicious that applications had been duplicated, and delayed authorization after the closure of the two month subscription period.■

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