

# Gulf States Newsletter

BAHRAIN, IRAN, IRAQ, KUWAIT, OMAN, QATAR, SAUDI ARABIA, UNITED ARAB EMIRATES

● POLITICS ● ECONOMY ● OIL ● FINANCE 16th Year - No. 404 - 11th February 1991

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## POLITICS & DEFENCE

### THE RACE IS ON

Last week, Dick Cheney, the US defence secretary, and Colin Powell, the chairman of the joint chiefs of staff, flew out to Saudi Arabia to consult with General Norman Schwarzkopf, the US commander, about the timing of an allied ground offensive against Iraq. The obvious assumption was that the United States wanted to get the long-awaited attack under way as soon as possible and before the renewed momentum towards peace talks inhibited military action.

### **\*A new shape to the crisis is beginning to emerge which could determine the balance of power in the region\***

A new shape to the crisis is beginning to emerge which could crucially determine the balance of power in the region for the rest of the 1990s. Put briefly, Iraq and the United States, with its allies, now appear to be fighting very different wars.

Saddam Hussein is a political strategist rather than a professional military commander. Where and when he takes the military initiative is determined largely by the political and propaganda impact the action will have, rather than the effect on the overall capability of the opposing forces.

### Baffling

This was clearly demonstrated by the struggle for the Saudi border town of Khafji at the end of last month. The Iraqi forces launched on the offensive, although larger than originally suspected, were definitely inadequate in numbers and quality to make a serious dent in allied defences.

There seems to have been a planned follow-up, if reports of columns of Iraqi tanks moving through Kuwait are anything to go by, and these were apparently halted by allied air strikes.

Nonetheless, it is impossible to believe that Saddam harboured any ambitions of inflicting a serious military defeat on the allied forces.

The wastefulness of the offensive left Western commentators and commanders at a loss for words. In purely military terms, an Iraqi offensive in the eastern sector might make some sense in diverting allied forces away from the more vulnerable western sector through which the Americans and British might aspire to cut off Kuwait from Iraq. But it did not succeed -- and it is hard to think that Saddam Hussein (whatever his bunkered-down mentality) thought it would.

### Resilience

What the attack did show, however, is that after days of intense bombardment, Iraq's forces are still capable of mounting a counter-attack and taking the allies by surprise. After the well-publicised pounding his country and his forces have received, this is precisely the kind of propaganda coup which will attract popular support throughout the Arab world, thereby forcing regimes to rethink their opposition, ambiguity or lukewarm support for Saddam Hussein.

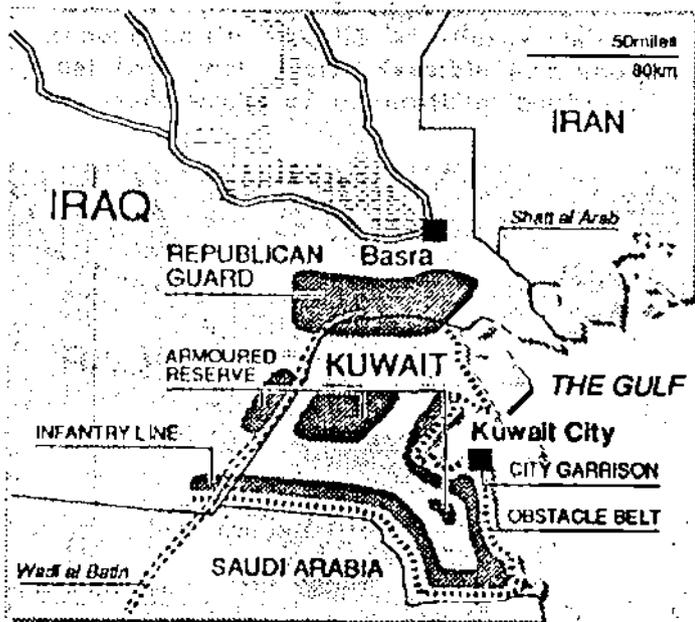
The Khafji attack means Iraq has also made it demonstrably clear that it will not be easily overcome by a ground assault. The forces which undertook the attack were ordinary troops, the bulk of them conscripts, who displayed a high quality of discipline and capability.

One illustration of the seriousness with which the Americans are taking Iraq's defensive capabilities is a recently publicised report by the Strategic Studies Institute of the US Army War College. Drawing on the lessons of the Iran-Iraq war, it states that "if we fight Iraq, we should be prepared to defeat it as quickly as possible, since the Iraqi military has shown it fights well on the defensive. If the Iraqis do not capitulate in the first days of the conflict, we can expect them to 'hedgehog'. They will wrap themselves around Kuwait and force us to

prise them loose -- a hideously expensive prospect in lives as well as in resources".

#### Sheltered

From their press briefings, it seems that the allied commanders are not altogether sure how much damage prolonged aerial bombardment has done to Iraqi material and morale. The air assault, by B-52s at night and F-16 fighter bombers by day, has concentrated on the elite Republican Guard, positioned on the Iraqi-Kuwaiti border. The Pentagon wants the air strikes to weaken the Guards' fighting potential by 30%-50% before exposing allied troops to the high casualties of a ground battle. The US Air Force claims that this goal is still feasible with about two more weeks of unremitting bombing.



*Financial Times*

Some words of doubt, at least, are in order. Allied military sources have shown themselves notably tentative about assessing the amount of damage actually sustained by the Republican Guard after the bombardment. Tucked into well-prepared shelters built since last August when Iraq moved into Kuwait, its forces may well emerge in far better condition than the US and British air forces imagine.

The performance at the battle for Khafji of the less highly-regarded troops on the front line should also give cause for concern. They seem quite prepared to take

the military initiative and -- if that is anything to go by -- will be just as difficult to dislodge. In the face of such circumstances, the words of the Army War College report take on a grisly ring. If the less-trained and equipped troops in the front line will exact heavy casualties, what will happen when the battered allied troops come up against the Republican Guard?

#### Conundrum

The allied forces now find themselves in a quandary. Seeking to reduce casualties on the ground if the land war takes place, they are intent on pulverising Iraq's defences as much and as quickly as possible before they go onto the offensive. But to be militarily satisfactory, this may take more time than is politically feasible.

The United States, which provides the bulk of the ground forces which will actually attack Kuwait, may therefore be rushed into a land offensive for which it does not feel ready. There is a growing atmosphere of crisis in Washington. No wonder Dick Cheney and Colin Powell have been despatched to the Middle East to see how soon the offensive can be started.

**"Tehran has become the gathering point for diplomats concerning a negotiated settlement before the battle begins"**

Their problem is that the pace of political developments threatens to overtake the speed with which the allied forces can move onto the offensive. Tehran has become the gathering point for diplomats sounding one another out concerning a negotiated solution before the battle begins (see page 9). Recent visitors include Francois Scheer, the secretary-general of the French Foreign Ministry, Sid Ahmed Ghazali, the Algerian foreign minister and an inveterate Middle East mediator, Iraq's deputy prime minister, Saadoun Hammadi, and the Kuwaiti foreign minister, Sheikh Sabah al Ahmed.

This is where Saddam Hussein could politically outflank the American-led alliance. After demonstrating his virility

at Khafji, he can back down with minimum loss of face and portray himself as a new Arab hero. "Saddam Hussein can compromise at any point", comments Robert Hunter, a former Middle East director for the National Security Council in the United States. "Once he gets something that makes him look like Nasser, that may be enough to allow him to withdraw and save face. The question is whether the battle of Khafji is big enough of whether he will launch another, bigger attack."

#### Face to face

Transparently, the majority view within the US administration is that Iraq must be cut down to size, preferably by effecting the removal of Saddam Hussein and the annihilation of his chemical, biological and nuclear weapons capability. But there is evidently a body of opinion, concentrated largely in the State Department, which takes a longer-term view of the repercussions which will result from a major incursion into Iraqi territory.

Last month's joint statement by James Baker, the US secretary of state, and the visiting Soviet foreign minister, Aleksandr Bessmertnykh, was downplayed by the White House, but it seemed to imply that there are forces within the administration which are prepared to contemplate negotiated settlement with Saddam Hussein.

After insisting on Iraqi withdrawal from Kuwait, the joint Soviet-US statement went on to say that "the ministers agreed that establishing enduring stability and peace in the region after the conflict, on the basis of effective security arrangements will be a high priority of our two governments..In addition, dealing with the causes of instability and the sources of conflict, including the Arab-Israeli conflict, will be especially important."

#### Compromise

Two critical battles are taking place right now. One is the anti-Iraq coalition's attempt to beat Saddam Hussein into submission. The other, quieter struggle is going on inside Washington and around the diplomatic corridors of the outside world. This is being waged by the foreign powers -- notably France and the Soviet

### **"While his military machine may be surviving, his civilian and administrative infrastructure is suffering badly"**

Union -- which believe that Iraq can be brought to the negotiating table if only such a table is put in place.

Why should Saddam negotiate while his armed forces maintain the capability of inflicting heavy (and politically unsupportable) casualties on the American forces? The principal reason is that, while his military machine may be surviving the allied onslaught better than expected, his civilian and administrative infrastructure is suffering badly. While the army holds the front line, internal command and control -- vital to Saddam's iron rule over all sections of Iraqi society -- is increasingly threatened. It is now quite clear that the United States is seeking to destroy the basis of Saddam's economic survival, and thereby bring about his downfall.

#### Martyr syndrome

Forget the idea that Saddam Hussein is willing to die fighting in order to go down in history as a glorious martyr. Throughout his entire career he has displayed a remarkably tenacious ruthlessness in the acquisition of power; the personality cult is just so much window-dressing.

### **"He must be starting to recognise that the coherence of his domestic support may begin to fall apart"**

He knows he can give the allied forces a far bloodier fight than they had reckoned upon. He must also be starting to recognise that the coherence of his domestic support may begin to fall apart. Hence the importance of keeping open the negotiating loophole through Tehran.

If he suddenly decides that the time has come to do a deal by agreeing to pull out of Kuwait (as the Baker-Bessmertnykh

statement seems to offer), US military plans will be frozen and the excruciating process of trying to organise a Middle East peace conference will begin. There will then be no allied offensive against Iraq under the guise of the liberation of Kuwait; Saddam will still be in power; Iraq will retain much of its military capability; and Israel, faced with a new diplomatic tussle over Palestine, will no doubt feel free to attack Iraq on its own.

It is in order to prevent this grim scenario becoming a reality that President Bush is now so anxious to implement the military option against Iraq and get the job done.

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## IN BRIEF

### General

\* THE UNITED STATES AND ITS ALLIES MAY SEEK TO MAINTAIN sanctions against Iraq after the war ends in order to deal with problems of compensation and war crimes. Robert Gates, the deputy national security adviser to President Bush, said at the beginning of the month that sanctions might be retained until questions were resolved about compensation relating to oil spills and decisions had been made on whether there might be war crimes trials. He stressed, however, that these decisions were dependent on the progress of the war and the "post-war situation" -- which, he said, "makes it prudent to wait after it's concluded before deciding what steps to take with respect with sanctions".

Robert Gates is chairing an inter-agency review of post-war US policy in the region. He announced that the United States was developing ideas which it intended to discuss with its partners in the anti-Iraq coalition about security structures and arms control in the region. Subsequently, James Baker, the secretary of state, declared that the United States might be interested in cooperating with Iran in a post-crisis security arrangement. He also stated that the United States was prepared to assist in the post-war reconstruction of Iraq.

\* GENERAL MIKHAIL MOISEYEV, THE CHIEF OF THE SOVIET GENERAL staff, has denied that Moscow is supplying the United States with secret information about the supply of arms it has provided to Baghdad. Western press reports have claimed that the Soviet Union has passed intelligence reports onto the Pentagon. General Moiseyev said that releasing such secret information would be a breach of the Soviet Union's friendship treaty with Iraq.

Moiseyev's statement was the latest in a series of indications that Moscow is now keen to disassociate itself publicly from US military actions in the Gulf. Over the past few weeks, the Soviet press has carried numerous commentaries criticising the US decision to attack Baghdad so soon after the 15 January deadline set by the UN Security Council for an Iraqi withdrawal from Kuwait. For example, Marshal Sergei Akhromeyev, the chief military adviser to President Gorbachev and a former chief of staff, denounced the United States in an interview, saying that Washington had failed to give economic sanctions sufficient time to work.

Aleksandr Bessmertnykh, the foreign minister, also made it clear during talks in Washington that the United States was in danger of overstepping the original intentions of the United Nations resolutions. A joint statement with James Baker, the US secretary of state, included a reference to post-crisis talks on the Palestinian issue, apparently inserted at the insistence of the Soviet envoy.

\* LIEUTENANT GENERAL CHARLES W BROWN HAS BEEN APPOINTED AS the president and chairman of the board of directors of the American-Arab Affairs Council. Now retired from active service in the US army, General Brown's most recent staff assignments have included assistant deputy chief of staff for logistics with the US army in Europe and a similar post with the Department of the Army in Washington. In 1984, General Brown became involved in providing military assistance to allied and friendly countries. For the last three years prior to his retirement, he served as director of the Defense Security Assistance Agency.

## Iraq

\* SOUTH AFRICA'S ARMSCOR, THE STATE-OWNED WEAPONS COMPANY, was reportedly supplying Iraq with 155mm artillery shells up until December of last year in defiance of the UN trade embargo. Baghdad is said to have bought Armcor's entire 1990 production run and paid in gold through Zambia. Military observers in the region say that the South African-manufactured artillery has proved superior in range and accuracy to guns deployed by the United States and its allies.

## Saudi Arabia

\* THE KINGDOM HAS PLEDGED TO GIVE THE UNITED STATES \$13.5BN in cash towards the costs incurred by the US military in the first three months of 1991. Riyadh is already providing local services to the United States and other allied countries free of charge. Kuwait has promised to donate a similar sum.

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## ECONOMY & TRADE

### KUWAIT PLANS FOR RECONSTRUCTION

Construction opportunities in post-war Kuwait could bring a boom worth \$30bn to foreign contractors. A draft plan for the rebuilding of the country and its infrastructure has already been drawn up by a team of experts led by the head of Kuwait's National Housing Authority, Ibrahim al Shaheen.

Previous suggestions put the minimum postwar reconstruction bill at no less than \$20bn, and other sources claim that another \$10bn will be necessary to cover damage incurred since hostilities broke out on 17 January.

**"Construction in post-war Kuwait could bring a boom worth \$30 bn"**

The draft is reported to be in the final stages of preparation and is expected to be presented to the Kuwaiti minister for finance, Sheikh Ali Khalifa al Sabah, when full details are to be released.

### Comprehensive

However, it is already understood that the plan is fully comprehensive, covering everything from basic infrastructural services, human resources and a socio-economic strategy for the future, to housing, hospitals and the oil industry. The draft apparently predicts that the return of exiled Kuwaitis following liberation could take up to six months, and that the first priority will be to bring back public utility services to working order, followed by urgent restructuring work on living accommodation.

The US Army Corps of Engineers (USACE) is expected shortly to announce a request for interest from contractors willing to carry out emergency reconstruction work. USACE signed a \$45m contract in January with the Washington office of the Kuwait Emergency Reconstruction Programme. Under the contract, USACE will provide initial planning, assistance and contracting for goods and services related solely to emergency reconstruction. Organisation of the long-term rebuilding effort will come later.

**"Ports and the airport have been singled out for special attention by the draft plan"**

### Damage assessment

Before the conflict to liberate Kuwait began, damage to the domestic sector was not thought to be have been that great -- apartments and villas had been stripped rather than totally destroyed. Similarly, before the US-led attack began, the damage done to roads, bridges and communications by the Iraqis was not generally considered to be particularly severe.

Ports and the international airport, however, have been singled out for special attention by the draft plan as it expects that both will require major reconstruction and extensions. All the mechanical handling equipment at the ports of Shuwaikh and

Shuabia has been removed, and so as a matter of urgency the ports will have to be restored if the construction equipment, which will be needed to rebuild the country, is to be unloaded.

Among the earliest casualties of the August invasion were hospitals and health centres. It is suggested that about \$2bn will be needed to restore these to fully functional order, although as with the housing situation, so far most hospitals seem to have been stripped rather than structurally damaged.

#### Oil and communications

One sector which will almost certainly have to be completely overhauled is telecommunications. Prior to the invasion, Kuwait was in the final stages of completing a major telecommunications development. It more than likely that this work will have to be repeated.

There has also been extensive damage done to the oil and petrochemical industries, and virtually all industrial machinery which it was possible to move out of Kuwait has been taken away. All kinds of generators, compressors and drilling rigs have made the journey northwards. Initially, an estimated \$600m-\$700m of movable equipment will be needed for the industry, although the cost of replacing whole refineries will be substantially higher.

### **"The question is: Who will get the plum contracts?"**

#### Competition

Mohammed Abdul Moshen al Kharafi, chairman of the National Bank of Kuwait, has said that the bank will organise the funding of the reconstruction, but the question on many observers' lips is: "Who will get the plum contracts?"

For example, a row has already broken out over who will implement the reconstruction masterplan. Three leading US companies -- Bechtel, Ralph M Parsons Co and Brown and Root -- have been competing from the start, and early indications suggest that these three companies are likely to get a major share of the action.

There has been anger among British companies, however, who appear to have been frozen out of plans despite Britain's active military support in the liberation effort. Recently, some British companies have begun to team up with US contractors to form joint ventures which will bid for post-war reconstruction work.

For example, Trafalgar House, the construction, property, shipping and hotels group, and Acer, the consulting engineers, have agreed in principle to work with Kaiser, the US engineering group, to pursue contracts to reconnect water supplies. Cleveland Bridge Middle East, a steel engineering subsidiary of Trafalgar House, is understood to have been talking to Bechtel.

### IN BRIEF

#### Bahrain

\* GULF AIR IS TO CUT STAFF AND MAKE TEMPORARY LAYOFFS because of the contraction in business since the outbreak of the Kuwait conflict. The cuts will affect up to 400 non-operational staff around the world. Of Gulf Air's global workforce of 5,173 people, 3,913 are employed in Bahrain, of whom 2,100 are Gulf nationals. Expatriate staff include 1,100 cabin crew members, 300 pilots, at least 100 engineers and more than 200 ground service and catering staff. Some expatriate staff will be offered extended leave or termination of their contracts. According to a Gulf Air spokesman, the company has decided to retain all Gulf national employees irrespective of their jobs. Of the 1,060 staff at the company's foreign offices and installations, only 100 are Gulf nationals. By the end of January, Gulf Air was the only airline still operating out of Bahrain, but even then with only six daily flights to Bombay and Karachi.

(Continued on Page 11)

## CENTREPIECE

### MEDIATION BY DEFAULT

Last week, President Ali Akbar Rafsanjani of Iran offered to mediate between Iraq and the United States in order to help end the Gulf war. His peace initiative is probably the most important -- and certainly the most intriguing -- since the Gulf crisis began last August. There are reasons to believe that it may just succeed (see page 2), and if it does there are important implications for the post-war balance of power in the Gulf.

First, however, it is worth asking why Rafsanjani has chosen this rather unpropitious moment to suggest a personal meeting with Saddam Hussein for the "sake of regional peace and security" while neither Iraq nor the United States show the slightest intention of suspending hostilities.

Rafsanjani made his proposal to Saadoun Hammadi, the Iraqi deputy prime minister who was on a visit to Tehran last week. The Iranian president commented afterwards that Hammadi had shown "no flexibility" on the question of an Iraqi pullout from Kuwait, which must be the starting point for any peace negotiations.

Meanwhile, in Washington, Rafsanjani's intervention was brushed aside by the Bush administration. The White House spokesman said dismissively that Iran was not directly involved in the conflict, while Dick Cheney, the defence secretary, declared firmly that he expected the only likely resolution of the conflict would come on the battlefield. He then left for Saudi Arabia with Colin Powell, the chairman of the joint chiefs of staff, to decide the precise moment for launching a ground attack on Iraqi forces in Kuwait.

### Discouraging

The only person openly to welcome the Rafsanjani initiative was the UN secretary-general, Javier Perez de Cuellar, who said he thought Iran was "in a good position to produce a formula which could put an end to the present situation". But even Perez de Cuellar is

out of favour in Iraq, having been the victim of personal abuse from Baghdad last month after his own mediation efforts.

Yet despite what must have been the expected response from the combatants to yet another of a long line of so far futile peace initiatives, Tehran has eagerly played host to a number of visiting dignitaries, including the Kuwaiti, Turkish, Algerian and Yemeni foreign ministers (not to speak of Hammadi) and the secretary-general of the French foreign ministry.

### **"Tehran is becoming the natural focus for mediation"**

### Pressure

This reveals two things. First, having alone among the regional powers so adamantly stressed its neutrality, Tehran is becoming the natural focus for mediation. Hence the number of peace-minded emissaries beating their way to its doors.

Second (and crucially important for the outcome of its efforts), Rafsanjani is being forced by domestic political pressures and apprehension about Iran's security in the post-crisis region to take more vigorous action than just appearing as an innocent neutral.

The war over Kuwait has placed Rafsanjani's regime in a dilemma and caused considerable political confusion. On the one hand is the urge to get involved now that the opportunity to deliver a blow to the "Great Satan" has presented itself. The other option is to stand aside and exploit the crisis for all that it is worth, emerging from the debris of everybody else's war intact, powerful and perceptively reasonable (in the West as well as the Arab Gulf).

It is too easy from the outside to divide Iranian politicians neatly into two classes of "extremists" and "moderates" according

to the position for which they opt. Certainly, there are radicals who have recently called unequivocally for Iran to join Iraq in a *jihad* against the United States on the ground that the Western presence in the Gulf is a greater danger to Iran than Iraq's invasion of Kuwait.

#### Ambiguity

Predictably, this argument has been put forward vociferously by Ali Akbar Mohtashemi, the interior minister sacked by Rafsanjani when he took power in 1989, and who has since become the standard-bearer of the radicals, as well as by Ahmed Khomeini, the son of the late Imam, who is trying to preserve -- and trade upon -- whatever he can of his father's revolutionary legacy.

However, other leading figures usually identified with the political "left" in Iran appear to have been trying to straddle the fence. Mehdi Karrubi, the radical Speaker of the majlis who succeeded Rafsanjani, has talked almost in the same breath about *jihad* and a peace plan, which would involve a simultaneous withdrawal of Iraqi forces from Kuwait and Western forces from the Gulf, an Islamic peace-keeping force and international negotiations on all Middle East problems (which, of course, means the Palestine issue).

Ayatollah Ali Khamenei has been equally ambiguous. In recent speeches he has also referred to the possibility of a *jihad*, accusing the Western powers of being "prepared to murder for the sake of oil". A Muslim nation, the official Iranian news agency reported him as saying, has been "subjected to direct crimes by Western arrogance". But Khamenei has been just as critical of Saddam Hussein, whom he claims is fighting for "wrong, secular and unholy motives".

#### Religion

His phraseology is indicative of how Iran's moderates see the problems of the Gulf. Rafsanjani has explicitly refused to assist Iraq in its fight against the Americans and their allies ("suicide", he called it), but he is under no illusion that a crushing US-led military victory of the kind the Bush administration now

seems to envisage will be hugely detrimental to Iranian interests.

### **"Especially unappealing to the Tehran moderates are Saddam Hussein's attempts to portray the conflict as a holy war"**

Especially unappealing to the Tehran moderates are Saddam Hussein's attempts to portray the conflict as a holy war against the West. The Iraqi leader has of late become notably concerned with religion, harping on -- provocatively if untruthfully -- about Western occupation of Islamic shrines in Saudi Arabia and implying that the United States (and, even worse, its Arab allies) are attacking the Muslim religion.

Oddly, for a regime that once preached Islamic revolution throughout the Gulf, this distinctly worries the present leadership in Tehran. Iraq's annexation of Kuwait has long since ceased to be a purely inter-Arab political matter. Rafsanjani and his friends at home fear that they may be dragged into another Gulf war by popular sentiment which has been aroused by Saddam's almost messianic appeals.

#### Inheritance

Rafsanjani is now paying the cost of the years of militant fundamentalism of the Khomeini era. It is understandably afraid that public opinion, wilfully inflamed in the past to accept massive human losses during the war with Iraq, may now respond to Saddam Hussein's espousal of a *jihad* against the United States.

### **"The argument is about how to deal with the United States and the West in a post-crisis Gulf"**

The division between Iran's "pragmatists" and the "radicals" is not really about whether they should or should not support Iraq. Rather, it is an argument about how to deal with the United States and the West in a post-crisis Gulf.

**"As they see it, the biggest danger is becoming swept by religious enthusiasm into a confrontation with the United States"**

Judging by their statements, Rafsanjani and his allies in Tehran believe that the Gulf conflict is not primarily a holy war between Islam and blasphemy but a political war about oil and power. As they see it, the biggest danger is becoming swept by religious enthusiasm into a confrontation with the United States which ultimately can only ensure a long-term American military presence in the region. Hence the constant emphasis by Tehran on the withdrawal of all foreign forces from the Gulf and the creation of a local security pact.

Buffer zone

Perhaps paradoxically, having fought its own eight-year long Gulf war, the Iranian leadership has no desire to see Iraq dismembered. From Tehran's, and a lot of other people's, point of view it is becoming increasingly clear that Washington's long-range aim is the destruction of Saddam Hussein's regime.

Saddam's disappearance would cause no tears in Iran. But if such a highly personalised regime were to be destroyed, there would be a considerable danger of Iraq simply falling apart in the ensuing chaos. The upheaval could well be exploited by Turkey (which has always retained a claim on Iraq's oil-rich north), by Syria, and by the Kurds. If such a disintegration became a reality, Iran would be forced to intervene on its own behalf -- presumably under the pretext of protecting the Iraqi Shia population in the south of the country -- but in doing so would also revive Arab Gulf and American fears of fundamentalist Islamic expansionism.

Caution

It is not surprising, therefore, that Rafsanjani is trying to tread cautiously. On the one hand, a massive blow to Iraq's military machine would remove the biggest local threat to Iran's security. On the other hand, if the anti-Iraqi allied forces in Saudi Arabia actually invade Iraq, or

if the war spills over into other areas, Iran will risk becoming entangled in a regional conflict it neither wants nor can afford.

Rafsanjani's narrow room for political manoeuvre at home was demonstrated at the end of last month when Assadollah Bayat, a radical deputy Speaker of the majlis, declared that Iran would abandon its neutrality to fight alongside Iraq if Israel were to be "stupid enough to respond to Iraqi missile attacks".

Haven

Then there is the curious affair of the Iraqi combat aircraft which suddenly landed in Iran at the end of January. Quite what more than 100 Iraqi planes were doing flying to Iran has not been (may never be) satisfactorily explained. The best guess is that Saddam Hussein wanted them out of the country for the duration of the war in order to preserve some of his military potential for the post-crisis period.

For the time being, Iran swears that the Iraqi aircraft will be impounded for so long as the crisis lasts. Ali Akbar Velayati, the foreign minister, was widely quoted by the Iranian press as vocally criticising Iraq's Saadoun Hammadi during his visit to Tehran for dumping the planes in Iran.

**"Rafsanjani and his supporters are determined to avoid Iran being drawn into the conflict"**

This would indicate that Rafsanjani and his supporters (of whom Velayati is one of the most prominent) are determined to avoid being drawn into the conflict over Kuwait. But the fact that several waves of Iraqi aircraft were allowed into Iranian airspace without being attacked and then permitted to land lends credence to the theory that some kind of understanding had been drawn up before the outbreak of hostilities, though it may have been interpreted differently by the two sides.

Saadoun Hammadi is reported to have asked that the fugitive aircraft be returned and been turned down,

bolstering the suspicion that Iraq really thought it was taking advantage of free parking space. The problem for Rafsanjani now is that, as Assadollah Bayat hinted, Iran may be sucked into a wider war and Iraq will be able to reclaim its aircraft or fly them from Iranian bases.

**"He has a lot to lose by being dragged into the war and much to gain by diplomatic manoeuvre"**

Opportunity

Small wonder, then that the regime has been embarrassed by the arrival of the Iraqi aircraft. Iran has as much interest as the United States in seeing Iraq humbled, but it also wants it left intact and desperately hopes to keep itself out of the war. Whether all that can be accomplished, given the bellicosity of President Bush, remains to be seen. But the fear that it may not be feasible -- and that Iran's radicals could give the crucial push into the combat arena -- explains Rafsanjani's conversion from hands-off neutrality to active mediation.

He has a lot to lose by being dragged into war, and much to gain by diplomatic manoeuvre. One Iranian official was quoted earlier this month as saying that all the diplomatic activity in Tehran of late provided the country with a "unique opportunity" to play a crucial role in shaping the future of the region. A thoroughly bruised Iraq, Arab Gulf countries aware of their vulnerability but suspicious of the long-term implications of a permanent American military presence, and post-war disarray throughout the Arab world would give Iran the chance to play the part of the region's pre-eminent power.

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*(Economy & Trade  
continued from Page 7)*

**\* THE GULF INDUSTRIAL INVESTMENT COMPANY, WHICH MANAGES**

Bahrain's iron production plant, ceased production in mid-January for "security reasons". The company was due to close temporarily in February to allow maintenance work to be carried out, but this has been brought forward because of the Gulf conflict. GIIC expects the plant to begin operations again by the end of this month, but it is expected that its output will be well below its capacity of 12,000 tonnes per day of iron ore pellets. The company says that it has been badly affected by higher shipping premiums and the departure of about 40% of its expatriate workforce.

Iran

**\* IRAN WILL BUILD A 1,000 MW POWER PLANT WITH CANADIAN cooperation in the south-eastern province of Kerman, according to the managing director of the state-owned Tavanir Power Company. An agreement has already been signed for the manufacture of power plant equipment under Canadian licence in Iran and the new venture was decided upon during a visit to Iran of a trade delegation from Ontario. Tavanir recently announced agreements for the construction of two power plants in Khorassan by the Soviet Union (Gulf States Newsletter, 28 January 1991).**

**\* IRAN HOPES TO BECOME GERMANY'S LARGEST TRADE PARTNER IN THE Middle East, according to Mohammed Hadi Nejad-Hosseinian, the minister for heavy industries. Speaking on a visit to Bonn, he addressed a conference of more than 100 German industrialists, urging them to take part in joint ventures in Iran. The minister stressed that there were no restrictions on trade and no controls on exports in Iran, adding that the government was trying to "reduce red tape and other bureaucratic obstacles".**

Nejad-Hosseinian also discussed technology transfer and the expansion of

economic and industrial cooperation with the German economy minister, Jurgen Mollemann and the minister of research and technology, Heinz Reisenhuber. After the meetings, it was reported that German companies had agreed to help Iran upgrade the value of its domestic products and establish new export-oriented production lines. Germany was also believed to have promised to provide necessary credits for bilateral trade exchanges, participate in industrial projects in Iran through joint investments or barter trade, and establish joint companies to implement major industrial projects with the aim of training Iranian workers, technicians and engineers in Germany.

**\* THE MINES AND METALS MINISTRY AND DUBAI'S INTERNATIONAL**

Development Corporation (IDC) have formed the joint venture Al Mahdi Aluminium Corporation to build a \$1.4bn aluminium smelter at Bandar Abbas. This is the first post-revolution joint venture scheme with a foreign company. The Dubai Aluminium Company (Dubal) will supply the technology and financing will be arranged through Lloyds Bank of Britain. The initial agreement to set up a smelter was signed almost exactly a year ago, providing for IDC to take a 40% share in the venture. The Dubai-based company is an international partnership led by the local Al Tajir International and including George Wimpey of Britain and the Swiss-based Marc Rich and Company and Cardel Investments. IDC is also involved in promoting and developing Iran's recently established Qeshm island free trade zone off Bandar Abbas. Construction of the aluminium smelter is due to start later this year for completion in 1994.

**\* IRAN IS CALLING ON THE INTERNATIONAL COMMUNITY FOR**

help and compensation for losses resulting from the Gulf war. It is concerned that its economic plight is being ignored while increased aid is being pledged to countries such as Egypt, Jordan, Israel and Turkey. Mohammed Hossein Adeli, the governor of the Central Bank, said in an interview with the official Iranian news agency that "if

a fund is going to be established to pay for damages resulting from the crisis, it should include all suffering countries without discrimination". Adeli said that he regretted aid appeared to be extended only to states friendly towards the West.

The Central Bank governor said that Iran's trade with the Arab Gulf states, which he put at around \$1bn a year, had been affected by the diminished purchasing power of its partners because of the crisis. (IMF statistics estimate the two-way trade between Iran and the whole Middle East at around \$600m, but the balance may be made up by the lucrative black market.)

Adeli said that Iran's defence expenditure had increased "in view of the need for vigilance and precautions". He also referred to the growing number of refugees entering Iran. "No foreign country or organisation is helping Iran with the settlement of Kuwaiti refugees and their expenses", he declared.

Observers say that Adeli's remarks can be taken as a signal that the government would welcome help from the rest of the world, despite the opposition of hardliners who feel that aid might pose a threat to the country's independence and freedom of action.

**\* THE CENTRAL BANK, BANK MARKAZI HAS LIFTED MOST FOREIGN**

exchange restrictions in an effort to boost export industries and pave the way for foreign investors. A partial devaluation of the rial has resulted from the move, which was announced on 20 January.

Exporters, travellers and foreign business people are now able to change their currency at a floating free market rate initially set at \$1 = IR 1,330. Markezi's governor claims this will transform Tehran from being the world's most expensive city for foreign business people, to one of the cheapest.

The official rate of nearly \$1 = IR 70 is, however, being maintained for the import of essential goods. As an incentive, a competitive rate, improved from \$1 = IR 800 to \$1 = 600, is still being offered to importers of industrial raw materials and machinery.

Since President Rafsanjani took power in 1989, the government has slowly

been moving towards a unified foreign exchange rate system. It is believed to be aiming at a single rate of \$1 = 600-800 which would amount to a 90% devaluation of the rial.

\* CUBA HAS SIGNED A PRELIMINARY AGREEMENT WITH THE MINISTRY of Agriculture to help develop a major sugar cane complex in Haft Tappeh in the south of Iran. Cuba will help set up the mills and sugar by-products plants in association with other international investors, according to the memorandum of understanding. The agreement was signed after a visit to Havana of the agriculture minister, Issa Kalantari. He was attending the second session of the joint Iranian-Cuban economic commission. The agreement also covers the creation of agricultural and industrial research centres specialising in sugar production. A team of 18 Cuban experts is to visit Iran to advise on all areas of sugar cane cultivation and processing of by-products such as animal feed.

The complex at Haft Tappeh is being rebuilt and considerably expanded at a cost of more than \$7bn. It will have seven sugar cane plants, seven livestock feed units, a compressed wood unit and a livestock protein unit. Iran and Cuba are also reported to have examined the possibility of supplying Iranian crude oil to a Cuban refinery with a yearly capacity of 3m tonnes.

#### Iraq

\* ATTEMPTS BY IRAQI AIRWAYS (IA) TO FLY TEN PASSENGER AIRCRAFT out of Iraq to save them from bombing raids were reported by Reuters on 18 January. The plans were disclosed by Tunisia, which reportedly told the UN's sanctions committee of Iraq's requests for overflight and landing permission.

The aircraft were bound for Algeria, Morocco, Tunisia and Mauritania. Two IA aircraft did land in Mauritania which led to reports that with them were Saddam Hussein's family and senior government officials. Washington and Mauritania have since discredited the reports.

#### Kuwait

\* THE KUWAIT FOREIGN TRADING, CONTRACTING & INVESTMENT

company (KFTCIC) is to arrange a \$1bn credit line for the Soviet Union's Vneshekonombank (Bank of Foreign Economic Affairs). The agreement follows a \$300m loan signed by KFTCIC with the same bank in May 1990. KFTCIC's chairman said the loan reflects the excellent relations between the two countries.

#### Oman

\* THE GOVERNMENT IS CONSIDERING PLANS TO ALLOW FOREIGN investors, including expatriates living in Oman, to buy stock in local companies, according to reports in the daily Muscat Times. According to the director-general of the Muscat securities market, trading since the stock market opened in May 1989 has exceeded expectations, with the volume of trading 150% higher than forecast for year one, and already 60% higher in the second year two.

#### Saudi Arabia

\* BUSINESS CONTINUES AS USUAL IN THE EASTERN PROVINCE, according to the deputy governor, Prince Fahd bin Salman bin Abdul Aziz. In an interview with "Voice of America", he said that despite the war conditions in all cities, towns and villages of the province was normal. He claimed that residents of the region "be they citizens or expatriates enjoy very high morale".

Other reports, however, suggest that expatriate workers and their dependents are continuing to leave the Eastern province, although local officials are reported as saying that the pace of departures has eased off. The most extensive departure rate is among Japanese workers of whom only around 40% were estimated to be still in the province at the end of January.

#### UAE

\* PRODUCTION OF HOT METAL BY THE DUBAI ALUMINIUM COMPANY (Dubal) has risen by 40% to 240,000 tonnes a year following the commissioning of the company's new potline. According to Sheikh Hamdan bin Rashid al Maktoum, the UAE minister of finance and industry and Dubal's chairman, the company had

increased annual production from an initial level of around 170,000 tonnes. Nearly all aluminium sales from the plant now consist of premium products, he stated. In addition, the plant is now providing 26.8m gallons of desalinated water to Dubai daily.

The minister reported that Japan was the company's largest single customer, accounting for two-thirds of last year's sales, followed by Taiwan (10%), Thailand (6%), the local UAE market (5%) and South Korea (4%). Sheikh Hamdan added that special efforts were being made to tap the European market, "despite the adverse effects of the European Community's import tariff restrictions".

\* \* \* \* \*

## OIL & ENERGY

### General

\* SADEK BOUSSENA, THE PRESIDENT OF OPEC, HAS CALLED FOR A ceasefire in the Gulf, saying that the sooner the war was over the quicker the organisation could get back on its feet. "There are risks to Opec", he said in Algeria (where he is minister of mines and industry), "but at the same time I have not heard anyone say the organisation should not exist afterwards." He stressed that "all of our efforts must be to achieve a ceasefire. The faster [the war] ends the faster we [in Opec] will be able to settle our problems".

Boussena claimed that oil had played a vital role in the motivation of the alliance currently opposing Iraq in the Gulf conflict. "The United States has between 10 and 12 years of oil production", he claimed. "Maybe it considers that it needs to be reassured about access to these resources that are strategic and vital for decades to come."

The Opec president declined to predict future levels of world oil prices, saying that supply and demand had become irrelevant and psychological factors relating to the war had taken over. "We are still in a situation of uncertainty. It is enough for the oil installations of one

country in the region to be hit or destroyed for a new increase in prices. [However] I do not exclude other factors leading to a reduction in prices."

Two weeks ago, Boussena said he blamed the Paris-based International Energy Agency (IEA) for deliberately manipulating the oil markets to attain a lower oil price. In expressing concern about the sudden fall in oil prices, he stressed that it did not augur well for either the industrialised nations or the petroleum producing countries. He stated that the IEA, which had until now "refused to contribute to any market stabilisation action, has now acted resolutely in a war perspective". He explained that "this has become abundantly clear in light of the fact that the emergency procedure for oil-sharing between the agency's member countries is supposed to be implemented when a physical shortage, equivalent to 7% of supplies, occurs". But according to the IEA itself, he said, the shortage had not reached that level.

"The least one can say is that there is a contradiction in this approach", he added. "But this is not surprising when one knows that even information sources related to important market parameters, such as production, demand and stocks, are controlled by a very few centres and can easily be manipulated."

### Iran

\* PRESIDENT RAFSANJANI SAID LAST WEEK THAT THE GULF CRISIS HAD neither affected Iran's oil exports nor the price of the country's crude. "Fortunately we managed to draw up our budget before its scheduled time this year, and based on this year's performance we made sure that the five-year development plan remains feasible", he said.

\* THE OIL MINISTRY IS CHARTERING TANKERS FOR A POSSIBLE SHUTTLE service from the main crude export terminal at Kharg island to Lavan island in the central Gulf. Foreign tankers, except those from Japan, were still calling at Kharg a week after fighting began in the Gulf but The Iranian Oil Company,

NIOC, is reportedly expecting disruption in the future. The National Iranian Tanker Company, NITC, is also maintaining its floating stocks of 30-40 million barrels outside the Gulf, which it will use in emergencies and to take advantage of any sudden price increases. The stocks have been built up since 2 August.

#### Qatar

\* A CONSORTIUM LED BY THE SHARJAH-BASED CRESCENT Petroleum has received a letter of intent to construct a 1,600km natural gas pipeline which will link Qatar with Pakistan, according to reports in the Gulf press. Quoting Pakistan's minister of petroleum and mineral resources, Ali Khan, during a visit to the UAE, the reports said that the project will cost an estimated \$3bn.

#### Saudi Arabia

\* REPORTS THAT THE KINGDOM PLANS TO CUT OIL PRODUCTION by 30% because of the war have been denied by Gulf oil sources, who say production is being maintained and only fluctuates because of transport difficulties. The reports, originating on 21 January, said Saudi Arabia planned to cut production from 8.5m b/d to 6m b/d. This was a precaution against possible Iraqi attacks and the oilfields closest to Kuwait were to be closed. Any resulting shortfall could be made up from stocks released by International Energy States, the reports added. Gulf oil sources say the reports of production cuts are "absolutely not true" and that changes in production were only caused by two factors other than the transport problems: the shutdown of Khafji field after artillery attacks and variations in Saudi Aramco's output.

\* THE SAUDI BASIC INDUSTRIES CORPORATION (SABIC) HAS announced that it will continue all manufacturing and marketing operations, despite the outbreak of hostilities in the region. Sabic's vice-chairman and managing director, Ibrahim Ibn Salameh,

said at the end of last month that Sabic customers were being served through product distribution points located around the world. However, the company faces some shipping problems because companies have been reluctant to enter the Gulf since the war began.

\* FAR EASTERN PURCHASERS OF SAUDI CRUDE CLAIM TO HAVE BEEN assured they will be compensated for any losses of crude caused by the war. They say Saudi Aramco has told them it will replace any cargo lost because of damage to tankers. Iran and Qatar have have introduced tanker shuttle services to transport crude to the lower Gulf, but Saudi Aramco has not yet done likewise.

#### Yemen

\* GOVERNMENT OIL REVENUES WILL TOTAL SOME \$437m IN 1991, according to Oil and Minerals Ministry sources. This is based on the assumption that the oil will average \$22 per barrel. The ministry says the government's share of production will average at about 119,000 b/d, of which 65,000 b/d will be refined for local consumption and 54,000 b/d will be for export.

\* \* \* \* \*

## BANKING & FINANCE

### IN BRIEF

#### General

\* THE GULF FINANCIAL CRISIS COORDINATION GROUP (GFCCG), of Gulf states and industrialised countries providing economic assistance to countries hurt by UN sanctions against Iraq is scheduled to meet this month in Washington. Although officials have not revealed the agenda, it is believed that the United States is urging the group to pledge additional sums to the \$13.4bn already promised in the first round of fund-raising. Most of this has already

ben promised to Egypt, Jordan and Turkey. The meeting will also decide on where to allocate the undisbursed \$3bn promised in the first round. Syria and Morocco have been nominated as potential recipients. GFCCG fund-raising is separate from the call for finance made by the United States and Britain to help cover the military costs of their intervention in the Gulf.

#### Bahrain

\* NET INCOME OF THE BAHRAIN-BASED INVESTCORP IN 1990 stood at \$66m, an increase of 28% over 1989 and 44% compared with 1988, according to the bank's annual report. It said that return on shareholders' funds last year was 30%, return on paid-in capital was 66% and return on average assets was 7.5%. Summing up its success since it was established, the report said that "eight years ago our shareholders contributed \$50m in capital to start up Investcorp. Four years later, they injected an additional \$50m in equity. Through net income generated during the period, this \$100m has grown to \$341m, of which \$90m was paid back to shareholders in cash dividends, \$5m was allocated for charitable contributions and \$243m remains as total shareholders' funds as of 31 December 1990".

#### Saudi Arabia

\* THE SAUDI-BRITISH BANK HAS ANNOUNCED A 56.1% INCREASE IN profits to SR192.1m (\$51.2m) in 1990. It is the bank's second year of profits after

reversing a loss of SR239.3m (\$64m) in 1988. Saudi British Bank says that the crisis in the Gulf "has led to unsettled market conditions over the past six months, but that has not so far impacted negatively on the bank's profitability. The bank will continue with its plans of steady growth in its businesses and upgrading of services."

Customer deposits recovered after falling because of withdrawals in reaction to Iraq's invasion of Kuwait in August. Deposits fell to SR9.143m (\$2.438m) at the end of September from SR9.808bn (\$2.651m) at the end of June. By the end of the year, however, they had increased again to SR10.179bn (\$2.714bn), higher than their mid-year level and 21.5% up on the end of 1989.

Total assets rose by 16.2% to SR14.6bn (\$3.9bn), while shareholders' funds increased by 17.2% to SR839.2m (\$223.8m). The bank made provisions against doubtful loans of SR25.4m (\$6.8m) in 1990, slightly less than the previous year's SR25.7m (\$6.9m).

\* PREDICTIONS OF A POSSIBLE RUN ON DEPOSITS IN LOCAL BANKS after the outbreak of war have thus far failed to materialise. Bankers said that the sector was very quiet with no noticeable rise in withdrawals. Following the Iraqi invasion of Kuwait, almost 11% of all private deposits were withdrawn, with most being removed in the first 10 days after 2 August.

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