

## ***Economic Challenges and Outlook for the Petrochemical Industries in the GCC Countries***

I gives me pleasure to be among you today, in response to the invitation of the High Organizing Committee for this Fifth Conference of the Petrochemical Industries and Chemical Fertilizers in the GCC Countries.

It goes without saying that the importance of this conference stems from the fact that these industries provide a main introduction for industrial development in the GCC countries, along with the opportunity for broadening their investment basis and achieving the qualitative and quantitative enhancement of their industrial production. This is particularly so, since all factors conducive to the success of these industries are available in the GCC countries, namely large national hydrocarbon resources, capitals, and the proximity to Asian importers of hydrocarbon products. Thanks to these positive factors, the petrochemical industry in the GCC countries has achieved a considerable development in a relatively short period of time by world standards.

Careful consideration of this subject reveals that the furtherance of the success achieved by the petrochemical industry and chemical fertilizers in the GCC countries does not rely solely on technical and technological aspects but is also influenced by aspects of international economy and trade. I shall, therefore, deal with these aspects in my address today.

Firstly, I would like to point out that by following up on the development of the petrochemical industries and chemical fertilizers in the GCC countries against the backdrop of relevant world changes, numerous lessons could be learned about the factors that have a significant bearing on these industries. By doing so, it will be possible to plan the development of these industries in the region on a sound basis. Following the discovery in the seventies of the possibility of using natural gas as a feed stock for these industries, most GCC countries focused their efforts on using this element of their natural hydrocarbon resources in establishing the petrochemical industries as a nucleus for their industrial production. During the eighties, the expansion of these industries in the GCC countries was the main factor behind the growth in the value added by their industrial sector to their total gross domestic product (GDP), which reached an annual average of 7.8% during that decade. According to latest available estimates, the value added by the GCC petrochemical industries to the total GDP of these countries reached \$ 8.9 billion in 1995, i.e. a ratio of 4.1%. During that year, the petrochemical industries in these countries contributed \$ 17 billion or 52% of the total value added by the manufacturing industry sector to the total GDP. Available estimates for that year put the total annual production of the petrochemical industry in the GCC at 13 million tons.

However, this success achieved by the petrochemical industry has also been the result of its confrontation of the challenges, which beset its early development during the eighties, namely the then worldwide decline in the prices of basic petrochemicals and the application by some major industrial countries of protective measures with regard to their crude oil and petroleum products imports.

**We cannot affirm that these challenges have vanished and will not reappear in any other form within the context of the radical changes witnessed nowadays in industrial and trade relations. Therefore, the extent of the current and expected success of the GCC petrochemical industry remains a function of the successful interaction of these countries with the emerging world conditions and their appropriate handling of any further changes. In my speech before you today, I shall address these aspects in some detail from the perspective of our present economic situation in the GCC in general and our current industrial and trade position with regard to petrochemical industries and chemical fertilizers in particular.**

The world economy has entered into a new phase, following numerous and diverse changes since the end of the eighties, such as the gradual disappearance of the bipolarity which had characterized the international relations between two main rival camps throughout forty years, and the start of an era of multipolarity in the technological and economic areas, exemplified in three main blocs: the United States of America, Canada and Mexico within “NAFTA”, the European Union (EU), and the Asian Tigers along with Japan, Australia and the United States of America, with the Asian Pacific Economic Cooperation” (APEC).

The emergence of these new international blocs was expected to entail further interaction and competition among them. Hence, their international economic relations had to be coordinated through an international regulatory process based on an enhanced role of the Group of Seven (G7), an expansion of the role of the Bretton Woods Organizations, namely the International Monetary Fund and the World Bank, as well as the establishment of the World Trade Organization (WTO). This organization was established for the purpose of implementing the GATT decisions regarding the liberalization of multilateral international trade, providing a forum for multilateral trade discussions, managing procedural aspects concerning the settlement of international trade disputes, along with reviewing and following up the national trade policies of member countries.

116 countries signed the GATT agreement which concluded with the Uruguay round, and whose recommendations were endorsed in April 1994, in

*Marrakech*, Morocco. The number of signatories to the Agreement reached 122 in 1995, among which were Kuwait, Bahrain and Qatar from the GCC.

For the GCC countries, whose influence as producers and exporters of crude oil and petroleum products is internationally recognized, the results of the final round of the GATT discussions in 1994 provided the means for further enhancing their current dialogue and relationship with the international economic blocs, particularly with those importing oil and petrochemical products from them. According to the latest available estimates, the ratio of petrochemical exports to total gross exports and to total non-oil exports in the GCC countries was 18% and 58% respectively in 1994. Furthermore, although the GCC countries account for only 3% of the total annual world petrochemical production, they hold a much larger share of the world exports of certain petrochemical products. For example, according to available estimates for 1994, while the petrochemical exports of the GCC countries accounted for 8% of the world trade in these products, their methanol exports exceeded 28% of the total world figure.

***Expected positive effects on the petrochemical industries in the GCC countries as a result of GATT implementation:***

The results of the Uruguay round are expected to have positive effects with regard to the oil and petrochemical exports and industries in the GCC countries, as follows:

1. The liberalization of trade and world markets is expected to bolster economic growth worldwide, thereby increasing the world demand for crude oil and petrochemical products. This is owed to the direct relationship between economic growth and the demand for both energy and petroleum products. Furthermore, the reduction in customs tariffs on other non-oil imports is anticipated to have indirect positive economic effects, such as increasing the actual income of importing countries, which will in turn increase their demand for oil and petrochemical exports.
2. The executive framework reached by the United States of America, Europe and Canada in 1991 within the GATT agreement provides for a reduction of the customs tariffs applied to chemical products, including petrochemicals. This will contribute to boosting the markets for the GCC countries petrochemical exports. This reduction in customs tariffs will take place gradually over a period of five to fifteen years, depending on the percentage of tariff charged, so as to bring this tariff to zero for feed stocks such as ethylene, 5.5% for intermediates such as methanol, and 6.5% as a maximum for final products such as polyethylene.

Worthy of note is that the GCC countries can cater for any increase in demand for their petrochemical products, which may result from the positive effects expected from the GATT implementation as well as the prevalence of favourable factors in the markets situated near to the GCC countries. In fact, available data for 1994 show that the current aggregate petrochemical production of the GCC countries represents only 21% of their total capacities.

Yet, the gains anticipated in the GCC oil and petrochemical industries from the implementation of the last round of GATT discussions may be restrained by factors, which are among the expected post-Agreement challenges in these industries, for example:

1. The erosion of the Generalized System of Preferences, which exempts from customs duties the petroleum product exports of the GCC countries to European markets.
2. The attempt by some importers of petrochemical products to impose indirect restrictions on these imports, so as to protect their national counterparts, which may be unable to withstand foreign competition. An example is the attempt by the EU to levy a carbon tax under the pretext of environmental protection, thereby imposing an additional -though indirect - taxation burden.
3. It is noted that the major industrial countries endorsing the Agreement were initially keen not to include oil in it, so as to have the latitude to impose restrictions or taxes on oil and petrochemical imports, as they deemed appropriate. However, they then chose the indirect approach of levying an "Excise Tax" on refined products rather than imposing custom duties.

**Although these challenges are relatively common, some other aspects of relevance to the Agreement may require prudent and careful consideration from the GCC countries. The importance of these particular aspects lies in the significance of their possible repercussions on the national regulations and procedures adopted by these countries in the process of developing their domestic industrial investments, particularly with regard to the petrochemical industry and chemical fertilizers. The most significant of these aspects can be illustrated in the following:**

1. The GATT principles provide for the equal treatment of resident foreign companies and national companies. This means that foreign companies operating in the GCC countries can, by virtue of this Agreement, hold more than 50% equity in national oil companies. This may conflict with the vital interests of these countries.

2. The GATT regulations regarding international trade take precedence over the corresponding national legislations that derive from the state sovereignty. This means that in the event of conflicting stipulations, national legislations should be adjusted in line with the terms of the Agreement.
3. The GATT principles oppose subsidization and compensation measures, as well as preferential treatment, undertaken by some countries in support of their national industries. The application of such GATT principles may have negative repercussions on the petrochemical industries in some GCC countries where these industries are currently subsidized.

***Future Outlook and Joint GCC Action for Coexistence with the New Order:***

What I have mentioned demonstrates that the actual challenge likely to be encountered by the petrochemical industries in the GCC countries in the process of coexisting with the new world trade order resides above all in being able to effectively stand up to international competition. Far from remaining outside the confines of the region, international competition is likely to make its way into these countries and compete with national industries here. Under such circumstances, the true success of these countries on the international level will lie in maintaining their current competitiveness while achieving higher profitability. This can be realized by undertaking the following essential responsibilities:

***First:*** Establishing national and regional bodies capable of negotiating with the WTO, so as to safeguard the interests of the region.

***Second:*** Upgrading the quality of industrialization in the GCC countries in general, and equipping industries there to stand up to international competition under these emerging global circumstances. This could be achieved through exporting quality products, enhancing productivity, and cutting production costs so as to attain a higher level of competitiveness. Although the refined products industries and the exploitation of natural gas constitute the basis of industrial production in the GCC countries, petrochemicals and chemical fertilizers are considered the industries of the future in the region and, as such, are given priority in the allocation of investments earmarked for industrial development.

***Third:*** Broadening the financing basis of the petrochemical projects in the GCC countries by developing the region's financial markets and enhancing their role, along with attracting private regional and

international investment in these projects. This approach is dictated by the economies of scale and vertical integration principles, which require that the petrochemical projects be capital intensive, so as to ensure their competitiveness in the world markets.

Worthy of note is that these projects have always been fully owned and managed by the governments in the region. However, the recently witnessed enhancement of the private sector's role in the Gulf economies and the endeavor to expand this role to become a main contribution to these industries is based on the growing financing role of the banking and financial sector there. Therefore, the success of the petrochemical industries in the GCC countries, along with the subsequent establishment of downstream industries, are expected to reflect positively on the banking and financial sector in the region, particularly by providing this sector with the opportunity to exercise its financing role in the channeling of national savings to these projects. This will further enhance capital productivity and rationalize the investment of financial resources in the region.

**Fourth:** Giving due consideration to research and development programs and the establishment in the Arabian Gulf region of scientific centers specialized in the petrochemical industry and chemical fertilizers, so as to support the horizontal transfer of technology and pave the way for vertical technology transfer in the region. The petrochemical industry, as we know, is one relying on sophisticated technology in its establishment and presence in the world markets. It is important here to point out that should the world be on the downturn of an economic cycle, intensive and accelerated expansion in petrochemical production capacities worldwide may result into a market glut. Under these circumstances, the only surviving petrochemical industries will be those relying on state-of-the-art technologies, which reduce basic production costs, thereby ensuring their competitiveness in an oversupplied world market.

**Fifth:** Attaching particular importance to organizational and support aspects in the establishment and commissioning of petrochemical industries, particularly with regard to the accounting, administration and marketing frameworks. In addition to being a main element in the success of any production project, these frameworks assume particular significance in the manufacturing industries, especially where there is fierce worldwide competition, which is particularly the case for the petrochemical industries in the GCC countries. It is, therefore, necessary to upgrade the components of these frameworks in the Gulf petrochemical projects, such as by offering specialized

training programs to the administrative cadres in this area, conducting applied research in petrochemical marketing and applying the findings of such research at the regional level. This will pave the way to an improved status for the Gulf petrochemical industry in the next century, along with securing its success on the international scene.

**Sixth:** Bearing in mind as we approach the twenty-first century that future conditions will inevitably bring about a close inter-relatedness of world markets. Survival in these markets shall be contingent upon a strong presence. This illustrates the necessity for further coordination, integration, as well as increased cooperation among the GCC countries in order to stand up to the new international trade challenges and effectually withstand competition.

**In conclusion, I also wish to address a topic of increasing importance to the GCC countries, namely the employment of national manpower in these countries, since this is an area where the petrochemical and chemical fertilizers industries can make a contribution.**

Since the petrochemical industry is the starting point of a long and varied chain of downstream industries, it provides an opportunity for expanding the private sector role and firmly establishing it within privatization policies as a main element of economic reform in the GCC countries. This active role of the private sector in the GCC petrochemical industry will have important results in terms of providing employment opportunities for the increasing numbers of nationals entering the labour market. In fact, the GCC countries' population structure shows that large numbers of young citizens will be entering the labour market in the coming few years. This necessitates generating sufficient employment opportunities to accommodate them. For example, the ratio of citizens aged between 15 and 24 to total population in the GCC countries is increasing steadily over the years. According to latest available ESCWA estimates, by year 2000 the number of citizens in the above age bracket will reach 21% in the State of Kuwait (from 17.3% in 1990), 13.7% in Qatar (from 10.7% in 1990), and 15.8% in the United Arab Emirates (from 10.2% in 1990).

Undoubtedly, the expected effective role of the petrochemical industries in absorbing a portion of the national manpower in the GCC countries will contribute to alleviating the burden on their general budgets. Furthermore, by taking up work in this field, these young nationals will acquire the scientific and technologic training necessary to meet the need for qualified national technical cadres in the region. In this regard, particular importance should be assigned to providing adequate training and educational services, as well as to supporting the training function of those GCC institutions, which specialize in qualifying engineers and technicians in the petrochemical industries. If it is true that petrochemical industries bear promising investment opportunities, it is

also correct that the investment in national human resources is one, which bears the highest return. Such an investment is in keeping with a country's obligations towards the new generations and represents its most important and solemn duty.

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