LEGAL ASPECTS OF DOING BUSINESS IN THE MIDDLE EAST

5

INTERNATIONAL BUSINESS SERIES

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Introduction

DENNIS CAMPBELL

Any consideration of the commerce of nations of the Middle East embraces a region consisting of an impressive – and perhaps dismaying – array of disparate political systems, social structures, religions, cultures, economies, and commercial and industrial priorities. This, however, is a region whose nations and people are linked not only by geographic proximity and history, but, as well, by tradition of trading practices and a frequent similarity of resources and aspirations.

There is in much of the region an abundance of particular natural resources, and it is this abundance which initially attracted the interests of international commerce. However, it is in the commonality of the region's aspirations for a more sophisticated economic infrastructure that the future of commercial relations with the area rests. A review of selected countries of the region suggests their potential.

In the following examination, it is useful to distinguish between the oil-rich, such as Saudi Arabia, Kuwait, Iraq, and Libya) and the oil-poor, such as Egypt, Syria and Jordan.

The nations of the Middle East, of course, are vitally interested in the social and economic development of their domestic economies, upon which the welfare of the majority of the population depends. Oil, however, has been increasingly the resource on which depends the development of the economies of both the oil-rich and the oil-poor (through economic aid).

In the oil-rich countries, the oil sector is quite large relative to their non-oil sectors. The oil sectors being nationalized, their foreign exchange proceeds accrue to the respective governments and are employed to support imports or the gathering of foreign assets, or to support economic and military aid to the oil-poor. Until recently, the oil-rich countries enjoyed abundant foreign exchange, which allowed full employment for their labor forces. These countries also could afford to import the technological skills required to achieve a significant productivity.

The ability of the oil-rich to use oil proceeds for domestic development depends on their ability to translate these resources into useful imports. Owing to limitations on that capacity, they have been susceptible to shortages of domestic resources, resulting in internal inflation.

In the oil-poor countries, the export sector cannot be distinguished from the non-export sector. Although export demand depends on the world economy, the supply of exports generally relates on the development of the whole economy. Foreign aid has served the role in the oil-poor countries that oil has served in oil-rich countries.

With insufficient foreign aid, the oil-poor nations can become labor-surplus countries, where capital and import constraints usurp their economic growth. Insufficient foreign aid also can deny the oil-poor the social programs that contribute to the productivity increase, particularly education and training.

ALGERIA

Algeria nationalized major foreign business interests and many private Algerian companies and one-third of the agricultural land after independence. A new investment code in 1982 provided more latitude to private investment with the government setting the extent to which new domestic or foreign private investment will be allowed in a particular development project and the conditions under which such investment must operate. Usually, only foreign private investments involving the formation of joint ventures between foreign firms and Algerian state enterprises are allowed, with the latter retaining a controlling interest.

Thirty per cent of Algeria's population depends directly on agriculture for a living but less than ten per cent of the gross national product (GNP) is generated by this sector. The 'socialist sector' of Algerian agriculture controls one-third of the best land, primarily that abandoned by French owners who left Algeria at the time of independence. This land is organized into worker-managed state farms (*domaines autogérés*). As a first step in the new development plan, some land (mostly in the less arable southern provinces) was redistributed to private owners, and further incentives were being given to private farmers who account for about fifty per cent of farm output.

Algeria produces significant amounts of wheat and barley, wine, olives and olive oil, citrus fruits, and dates. It must import one-third of its food to feed its population, however.

Algerian trade is primarily with Western Europe, Japan, and the United States. Algeria accords most-favored-nation status to all countries. It has special trade arrangements with its neighboring states and the European Communities.

In 1984, Algeria exported an estimated $12.8-billion in goods, almost totally hydrocarbons, and imported $9.8-billion in goods in 1984.

EGYPT

Egypt produced a GNP of approximately $26-billion in 1984. Agriculture and services each provide approximately one-third of the GNP with the remainder resulting from industry, petroleum, mining, electricity, and construction.

Public enterprises are dominant in the industry sector. Virtually all heavy industries are owned by the state. Many private industries have prices controlled by the state or have competition from products which are subsidized by the government. Only thirty-five per cent of industrial production originates in the private sector. Much of agriculture, though nominally private, is regulated through price control, import allocations, and guidelines on production administered through local agricultural cooperatives. Construction, non-financial services, and domestic marketing are primarily private.

The economy is encountering numerous challenges. From 1981 to 1984, oil export revenues decreased as world oil prices declined. Increasing domestic consumption may overtake increases in petroleum production, reducing the quantity of exportable crude. Thus, one of Egypt's major sources of foreign exchange may not be available by the 1990s.

IRAN

The Government indicates that it prefers small-scale trading, farming, and manufacturing. Islam guarantees the right to private ownership, but banks, insurance companies, and the property of certain individuals have been nationalized. The oil and gas, transportation, utilities, mining, metallurgical, and certain construction sectors also have been subjected to close regulation and supervision.

Iran's economy has been disrupted by the war with Iraq. Major business and industrial growth indicators are significantly below the levels which prevailed before the revolution and the war with Iraq.

ISRAEL

Israel's emphasis on development and skilled labor provided force to economic growth rates during the nation's first two decades that often exceeded ten per cent per year. Thus, Israel boasts an industrial and services economy with a per capita income roughly comparable to that in Ireland, Spain, and Greece. The growth rate, however, has slowed in recent years.

The paucity of natural resources, the requirement to absorb immigration, and significant defense requirements have caused Israel to incur a consistent deficit in trade. This is financed through United States Government loans and grants, transfers from international Jewry, German reparation payments, and commercial bank loans. That trade deficit has grown considerably in recent years.

Exports of goods and services were valued at about $10.2-billion in 1982. The principal exports were defense-related items, diamonds, chemicals, and citrus fruits. Import of goods and services were $15.2-billion in 1983.

The United States has been Israel's principal trading partner. Non-defense imports from the United States in 1982 exceeded $1.6-billion, representing approximately twenty per cent of Israel's imports. Machinery, electric equipment, and agricultural products have been Israel's primary imports from the United States. Israel's exports to the United States exceeded $1.2-billion in 1982.

IRAQ

Iraq's gross national product expanded steadily on the basis of increasing world oil prices from 1973 until the Iran-Iraq war. Expenditures on Iraq's 1981–1985 economic development plan were expected to be as high as $75-billion. However, increased military imports and reduced export revenues have resulted in significant reductions in Iraqi investments in such infrastructure projects as power and electricity, transportation, and construction. During the 1970s, the government stressed improving the standard of living by emphasizing education, health and welfare reforms. A continued effort was expected in these sectors with the conclusion of the Iran-Iraq war.

JORDAN

Until the late 1950s, Jordan's economy was accorded little prospect for expansion and development. The country offered little in the way of natural resources, no industry, few hotels for tourists, sparse paved roads and an inadequate agricultural production which relied heavily on limited rainfall.

However, Jordan's economy expanded rapidly in the ten years before the June 1967 war. The war caused severe economic dislocation and it was not until 1972 that Jordan recovered the position it lost following the war. During 1973–1975, the economy achieved a real growth rate in GNP of almost six per cent per year. The 1976–1980 economic plan called for a $2.3-billion investment and a real growth rate of ten per cent per year. Several industrial and mineral extraction projects were constructed or planned, and most targets were met. During 1981–1985, the economy experienced slowdown due in the main to external factors.

KUWAIT

One of the world's wealthiest countries, Kuwait, in 1984 had a per capita gross national product of $13,200. Kuwaitis, who represent forty per cent of the total population, enjoy a relatively greater share of the wealth than expatriates.

Kuwait's wealth is primarily based on its dominant exports of oil and capital. Oil represents eighty-five per cent of the country's merchandise exports and nearly two-thirds of government revenues. Income from foreign investments account for most of the balance of public revenues. The recent downturn in world demand for oil has been the essential reason for recession in Kuwait. Per capita GNP fell from $20,000 in 1980 to $12,700 in 1982. It has since begun a gradual recovery.

LEBANON

Prior to the civil war which began in 1975, Lebanon was the financial and commercial capital of the Middle East. Due to its location, Christian-Muslim population, and mercantile heritage, Lebanon served as a bridge between the West and the Middle East.

The civil war has caused extensive damage to Lebanon's infrastructure. Industry, housing, roads, telecommunications, and water supply systems will require major reconstruction to attain pre-civil war development levels.

Industrial production has been significantly reduced, and agriculture also has been severely damaged.

This service sector, particularly banking, is the most important sector of the Lebanese economy, and the banking industry has maintained a surprising vitality throughout the civil war period.

MOROCCO

The government in the early 1980s placed increasing stress on development of social services and industrialization. However, agriculture remains the dominant factor in the economy, providing most of the domestic food requirements, twenty-five per cent of its foreign exchange, and seventeen per cent of the GNP. Approximately thirty-four per cent of the agricultural land is held by three per cent of the farmers and is devoted to large-scale, export-oriented farm operations. These agribusinesses yield more than eighty-five per cent of commercial production, including nearly all citrus fruit, fresh vegetables, wine, and other agricultural exports. These irrigated areas benefit from substantial government subsidies. The dryland areas, where most of the population is concentrated face drought, inefficient farming methods, and insufficient capital. Most farms are small and family operated, and traditional cultivation methods produce low yields.

SAUDI ARABIA

The world's leading oil exporter, Saudi Arabia, derives more than ninety-nine per cent of its exports by value from oil, and petroleum is the prime source of foreign exchange. Nearly ninety per cent of government revenues come from these exports. Proven reserves are estimated at more than 165-billion barrels, representing of all proven free-world reserves.

Through five-year development plans, the government attempted to utilize petroleum income to transform the undeveloped oil-based economy into a modern industrial state. The country continues to depend on petroleum revenue, but industry and agriculture now provide an increased share of the total economic activity. A shortage of Saudi skilled workers remains the principal obstacle to rapid development, and approximately two million non-Saudis are employed in the economy.

The government's first two development plans in the 1970s emphasized infrastructure – telecommunications, roads, ports, electricity, and water. The total length of paved highways tripled, power generation increased by twenty-eight fold, and capacity of the seaports increased ten-fold. For the period 1980–1985, emphasis was on expansion and diversification of the productive sectors of the economy (primarily industry). The share of infrastructure in development spending remains significant but has declined.

The government encourages private enterprise, and foreign investment, particularly joint ventures with the government and private capital, is encouraged. The private sector has become an important element in the economy, expanding its share in GNP to approximately twenty-five per cent by 1982. Recently, private investment has been in industry, agriculture, banks and construction companies. These investments often have resulted from generous incentives, facilities, and policy support provided by the government.

SYRIA

The country's trade deficit has nearly quadrupled in the past decade. The value of exports has risen significantly in recent years, and imports have followed a similar pattern.

Primary exports include cotton, crude petroleum, and textiles. Major markets are the European Community, communist nations, and other Arab countries.

The principal imports include food, fuels, machinery, transportation equipment, and textiles. Major suppliers are the EC, Eastern Europe, China, the U.S.S.R. and the Arab Common Market and other Arab countries.

With irregular rainfall and limited irrigation, agricultural production is subject to severe fluctuations. Cereals and cotton are the principal crops, but fruit and vegetable production is also important. Cattle, sheep, and poultry amount to approximately thirty-four per cent of agricultural production. The agricultural sector contributed twenty per cent of GNP in the early 1980s.

Extractive industries (mainly petroleum) provide fifty-five per cent of industrial value added; manufacturing, forty-three per cent; and public utilities, two per cent.

SUDAN

The primary resources of the Sudan are agricultural. Although the country is attempting to diversify its cash crops, cotton and cottonseed provide for more than half the export earnings. Sudan also produces eighty per cent of the world's gum arabic supply. Grain sorghum (*dura*) is the main food crop, and wheat is grown for domestic consumption. Livestock production has significant potential, and many animals, particular camels and sheep, are exported to Egypt, Saudi Arabia, and other Arab countries.

An inadequate transportation system and the cost of moving products over great distances are major hindrances to economic development.

TUNISIA

Early economic development efforts focused on the agricultural sector, but that emphasis shifted in the late 1970s to industry and tourism.

Oil from deposits discovered in 1964 were expected to meet domestic consumption over the long term. Sales of high-grade Tunisian petroleum provided approximately thirty-three per cent of export revenues in recent years. Sales of phosphates, Tunisia's only other major natural resource, also accounts for significant export earnings. Tourism is a leading foreign currency earner. Another prime source of foreign currency is textile exports.

France is Tunisia's leading trading partner. Following France are Italy, the Federal Republic of Germany, and the United States.

TURKEY

Turkey achieved a sustained economic development from the mid-1960s through the mid-1970s, attaining annual growth rates in the range of seven per cent. However, the world recession and the return of thousands of Turkish workers also had been employed abroad introduced a long period of economic sluggishness and instability.

Significant steps have been taken since 1980 to combat inflation, reduce debt, and revitalize the economy.

Agriculture represents approximately twenty per cent of the GNP and industry approximately twenty-five per cent. Major exports are tobacco, cotton, textiles, cement, raisins, nuts, leather, glass and ceramics. Prime import include petroleum, pharmaceuticals, dyes, iron, steel, machinery, plastics, rubber, and transport vehicles. Major trading partners are Iraq, West Germany, France, the United Kingdom, Italy, Iran, Libya, Eastern Europe and the U.S.

UNITED ARAB EMIRATES

Before the rise of oil prices in 1973, fishing, herding, and agriculture were dominant in the economy of the country. Thereafter, the economy shifted to one based on petrochemicals.

In the 1980s, government spending was significantly reduced and the pace of investment and construction slowed. Oil remains the essential nature resource and the primary export. The country imports machinery, consumer goods, and food. The main trading partners are Western Europe, Japan and the United States.

Bahrain

M. B. WOOD

CLIMATE FOR FOREIGN BUSINESS

The State of Bahrain is comprised of a group of islands situated almost in the geographic center of the Arabian Gulf some fourteen miles off the eastern coast of Saudi Arabia. Bahrain will soon be linked by a causeway, the construction of which is now underway following the signing of formal contracts earlier last year.

The capital, Manama, is situated in the northeastern tip of the largest island and linked by an existing causeway to the neighboring island of Muharraq containing Bahrain's modern international airport. The vast majority of the population of some 351,000 live in the northern half of the largest island as well as in Muharraq. It is here that one finds the green date gardens and the colourful flowers which have given rise to Bahrain's claims to be the site of the garden of Eden.

Until the Japanese discovery of the cultured pearl in the first quarter of this century, Bahrain's principal export was pearls and although export is no longer a major factor, divers still dive for pearls from the diminishing number of vessels of the pearling fleet. In 1931, the first oil in the Arabian Gulf was discovered in Bahrain and the original well, still producing oil, has become almost a place of pilgrimage to all those connected with oil. Although this oil assured Bahrain of a number of years of comparative prosperity, its production was later to be dwarfed by its neighbors Saudi Arabia, Kuwait and Iraq and now merely serves to meet domestic consumption.

Faced with dwindling oil revenues and the possibility of unemployment for its relatively large and well educated population, the Amir of Bahrain, His Highness Sheikh Isa bin Sulman al Khalifah and his Government under the Prime Minister Sheikh Khalifah bin Sulman al Khalifah determined in the early 1970s to use the country's liberal traditions and excellent communications to make Bahrain the offshore service and financial center for the entire Arabian Gulf region.

Following the withdrawal of the British in 1971, there have been great strides in the development of Bahrain's modern statehood. Comprehensive laws in the areas of companies, agencies, employment, social security and a wide range of other matters have been introduced. In addition to the existing oil refinery, subsequent developments in the industrial sector have led to the construction and substantial extension of a modern aluminum smelter, the building of a dry dock capable of handling the Very Large Crude Carriers which ply the waters of the Gulf and the inauguration of the Associated Petroleum Gases Liquefaction plant. The Government has recently announced further major public works projects and the work on the construction of the causeway may well turn out to be one of the most significant developments in the modern history of Bahrain.

Additionally, in order to stimulate its role as an offshore center, the Bahrain Monetary Agency, the state's central bank, announced in 1975 that it would grant licenses to major international banks to open branches for offshore operations throughout the region. Following this in 1977 was the announcement of investment banking licenses and the granting of permission to non-Bahrainis to form companies in Bahrain to carry on business offshore which would be exempt from the onshore requirement of majority Bahraini participation in the capital share. As of 31 August 1981, sixty-five offshore Banks and nine investment banks were established in Bahrain and sixty-two exempt companies had been formed. Bahrain's complete absence of tax, other than for oil companies, on corporate profits or personal incomes has played a significant role in its successful development as a regional center.

Furthermore, the excellence of Bahrain's telecommunications such as direct dialing and telex that is available to almost all parts of the world and regional and inter-continental air links have been important factors. Gulf Air, the regional carrier has its administrative head quarters in Bahrain and the modern airport is amongst the most efficient in the region. There are flights from there each day to Europe and the Far East as well as numerous flights to the surrounding Gulf States and to Saudi Arabia.

Bahrain is probably one of the most popular destinations in the Arabian Gulf for the visiting business person as well as the resident expatriates. For the former, a large number of deluxe international hotels with full facilities assure a comfortable stay and for the latter, there is now a wide selection of comfortable, modern, fully air-conditioned flats and houses. Many houses are constructed in their own garden compounds which contain swimming pools and tennis courts. Until recently, rents have been comparable with, or lower than other important offshore centers but show signs of soaring as the causeway project makes its impact on the economic infrastructure. There is a large British primary school and other foreign schools have started or are nearing completion. Additionally, there are a number of sports clubs containing swimming, tennis, squash and sailing facilities. The liberal atmosphere in Bahrain encourages the Western style of living which is hindered by restrictions in some other Gulf States.

The Government is firmly committed to encouraging industry, agriculture and tourism thus maintaining Bahrain's importance as an offshore service and financial center for the region. Although no formal commitment can be given, the imposition of personal or corporate income tax is unlikely in the foreseeable future. Increasing numbers of Bahrainis fill top management positions in the civil service, commerce, industry as well as in the international banks and companies established in the state. With the completion of the causeway to Saudia Arabia in 1986, it is expected that this connection to the