

# KUWAIT

Richard Johns

How are the oil-rich states of the Middle East faring today, since their petro-dollar boom set in after 1973. The case of Kuwait was examined in a recent *London Financial Times* survey by its Middle East Editor, Richard Johns.

Kuwait is embarking upon its 18th year as a fully independent entity under a strong leader who commands the respect and loyalty, not only of the ruling Sabah family, but also the privileged Kuwaiti citizenry, whose position as the richest people on earth in terms of per capita income was recently confirmed again.

## Firm new hand at helm

Adjusting to a less frenetic pace of life with the slowdown in the rate of economic activity compared with the boom of 1975 and 1976, Kuwaitis are not bracing themselves for any dramatic changes. Continuity of policy at home and abroad will be the order of the day. The new Emir has effectively been running the State's affairs for many years now. His strong commitment to Kuwait's development will ensure steady growth for the next decade which is likely to see also Kuwait's financial surplus decline still further from the extraordinary level reached two years ago — though no diminution of its accumulated foreign assets now estimated to be worth more than \$25 billion.

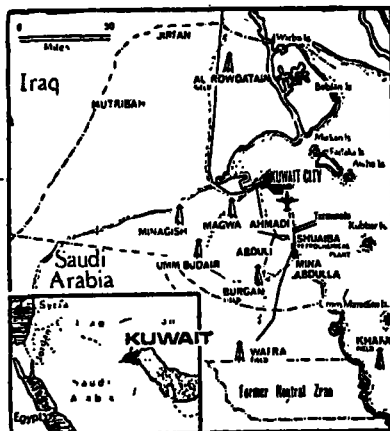
On the domestic front Sheikh Jaber al Ahmed will be faced with the need for a decision on constitutional change and the question of what mechanism, if any, should be established for popular participation in the legislative process, at least, consultation. Already he has promised specifically, if somewhat obscurely, consolidation of "our genuine democracy through popular participation". Internal security, that over the past year has been maintained effectively, if discreetly, may be tightened — especially with Sheikh Saad al Abdullah, the new Crown Prince, who was formerly Minister of the

*'Its fiscal surplus will decline as expenditure catches up with revenue and the real value of its oil income falls'*

Interior. His Premier also. Liked for his compassionate open-handedness, he has always taken a tough line with trouble-makers. Externally, Sheikh Jaber al Ahmed's accession could mean Kuwait, which is deeply concerned about the divisions within the Arab world over Egypt's peace initiative and its possible repercussions at home where the Palestinian minority is so large, being more assertive in trying to restore unity.

## Simplified

It is commonly said that the essence of the unique Kuwait system is an alliance between the ruling family and the leaders of the mer-



chant community who, like most of the citizenry, showed little or no concern when the factious National Assembly was dissolved in 1976. It was at their pleading that the Government interceded late last year to alleviate the losses of speculators in the share market in a typically paternalistic move, the wisdom of which is questioned by some of Kuwait's young technocrats.

Apart from the merchant community, there are other important factors in the Kuwaiti socio-political equation which is complex enough in itself quite apart from the presence of almost as many Arab expatriates as Kuwaitis in the State. On the one hand, there are the tribal elements whose support is important and has notably

been cultivated by the new Emir in the past by well-conceived matrimonial policy. On the other hand, there is the technocratic element produced by several decades of education and affluence which has made Kuwait into one of the most civilised centres of the Arab world. By design the tribal element was more heavily represented in the National Assembly but the technocratic one also made its voice heard — not the least through the handful of "Arab nationalist" deputies. Whatever his thinking or intentions it may be significant that the Emir consulted four former Speakers of the old National Assembly before finally appointing Sheikh Saad Abdullah Premier as well as Crown Prince.

## Unhappy

Jealous of its wealth and privileges Kuwait has still not come to terms with its expatriate Arab inhabitants, only a few dozen of whom have been granted citizenship of the second-class variety. They are unhappy about the way in which they are treated and, justifiably, by the fact that they are paid less for doing the same work (usually much better) than Kuwaitis who are not only their masters but landlords as well. Fifty per cent or more of indigenous families are reckoned to receive an income from property, mainly at the expense of the foreigners who serve them. Over the years, in an attempt to correct the demographic imbalance, Kuwait has recruited citizens from the itinerant bedouins of the region. The time has come for it to extend on a generous scale similar rights to other Arabs who have struck deep roots in the State, a fact that some intelligent Kuwaitis are showing signs of appreciating.

Conscious of its wealth but physically weak and vulnerable, Kuwait suffers from the tensions within the Arab world and is acutely concerned about the current disarray caused by President Sadat's initiative in negotiating directly with Israel. Implicitly, the Government

approved of the bold move in the hope that it might bring a lasting settlement and, consequently, a more comfortable environment for Kuwait. But it was offended by Egypt's lack of prior consultation, not the least with its aid donors, and deplored the hostile reaction created by the unilateral action. For the indefinite future Kuwait will continue to tread a delicate path between the conservative and radical forces of the Arab world, spending liberally on aid in the process. No other member of this diverse family of nations has a bigger vested interest in its unity.

#### THE ECONOMY

##### A gentler pace of growth

In line with its oil production and revenues, Kuwait's economic activity and growth has slackened to a more comfortable and accommodating level. While the Government views philosophically the decline of its financial surplus, it can only be relieved that the boom of a year ago, which reached its artificial peak last year with a mad frenzy of stock market and real estate speculation, has subsided.

In (mid-February) there were only two vessels unloading at the port whereas at the end of 1976, waiting times ran for months as capacity was over-burdened by congestion elsewhere as well as by Kuwait's own mounting demand for imports.

With its relatively well developed infrastructure and human resources Kuwait was better able to stand the strains from the escalation in oil prices and the resulting exponential growth in expenditure. But it felt, though not as badly as Saudi Arabia and Iran, severely stretched and now is recovering its breath.

Having had their expectations aroused by the 1975-76 bonanza and excessive profits realised during it Kuwait's merchants may be complaining — some of them misleadingly talking of recessions and "crying their eyes out over a 5 per cent reduction in turnover", as one commercial banker put it. Apart from the huge expansion of domestic business, Kuwaiti businessmen were able to profit from the economic explosion in the region as a whole to the extent that probably up to 20 per cent of goods imported in 1975-76 were re-exported.

Statistics from Kuwait's main trading partners point to a decline

KUWAITI BUDGET (KD)				
	1977-78		1976-77	
		% of total		% of total
Allocations for reserves:				
(a) Reserve Fund for				
Future Generations	227,272,190	10.00	217,192,680	10.00
(b) State general reserve	7,449,710	0.33	632,734,120	29.13
(c) KFAED	50,000,000	2.20	50,000,000	2.30
Sub-total	284,721,900	12.53	899,926,800	41.43
Ordinary expenditure	1,511,000,000	66.48	929,000,000	42.78
Development expenditure	392,000,000	17.25	263,000,000	12.11
Acquisition of property	85,000,000	3.74	80,000,000	3.68
Total	2,272,721,900	100.00	2,171,926,800	100.00

in the rate of increase for imports to about 35 per cent last year — compared with 40 per cent in 1976 and 55 per cent in 1975. Investments are high and the market is sluggish. For the community as a whole, however, the slowdown can only be a relief, not the least with the reduction of inflation to an annual rate of about 20 per cent.

More dramatic and traumatic was the bursting of the inflated bubble of the over-inflated stock and real estate markets 12 months ago. In this respect the most revealing statistics of all come from the Central Bank. Last year expansion of credit was down to a 26 per cent rise from the breathtaking 82 per cent recorded in 1976. The difference was accounted for by speculation frenzy, according to Mr. Hamza Abbas Hussein, Governor of the Central Bank who says the modest increase in advances in 1977 would have been wholly to finance the "productive" sector — which in Kuwaiti terminology includes trade.

##### Intervened

Real estate valuations are now down 15—20 per cent from the end-1976 peak. Bigger losses were made on the stock market where the fall was 25 per cent. Finally, the Government intervened by undertaking to purchase from investors shares at the lowest price quoted between October 1 and December 17 through the Kuwait Foreign Trade and Contracting Company (which is 80 per cent owned by the State). So far this paternalistic gesture is reckoned to have cost the State KD 125 m. or more.

"That was man-made inflation and totally unrealistic", says Mr. Abdelatif al Mahad, chief of the

Kuwait Fund for Arab Economic Development (among many other important posts) and one of the State's leading economic brains. Like some others in influential positions, including Sheikh Ali Khalif al Sabah, the new Minister of Oil, he questions the wisdom of the Government in helping the speculators who burnt their fingers. In the meantime it is business back to normal and on a more stabilised basis — but on a "higher plateau" than in 1974, as Mr. Hamad put it. Better developed, Kuwait suffered less of a jolt than many of its neighbours when the money gushed in 1973-74. Yet, despite the State's continuing fiscal surplus, the scale of Kuwait's development programme and its capacity for absorbing revenues is generally ignored by the Western forecasters.

The slump in real estate and share values, which were large by the criteria of businessmen who believe that they cannot fail to make a profit that would amaze the best organised multinational company, will have had a sobering effect. For less privileged Kuwaitis and the expatriates upon whom they depend — if one can presume to rationalise on their behalf — there is still too much liquidity in the market for comfort. Kuwait, like Saudi Arabia, suffers from a lack of any real co-ordination of fiscal and monetary policies to restrain inflationary pressures. In the last analysis it could be cynically said that the pattern is set by the merchants' drive for profits and their alliance with the ruling hierarchy at the expense of any longer-term strategy.

For the record, last year the increase in money supply (cur-

rency in circulation plus demand deposits) declined to 24 per cent compared with the 35 per cent level of 1976. Yet monetary growth is almost completely dictated by Government disbursements of money, as the Governor of the Central Bank emphasises — pinpointing the essential nature of the Kuwaiti economy.

Kuwait's business community is still essentially a mercantile one, with origins long predating production of oil but fed and enriched over the past three decades by the State's disbursements of oil revenue that still generate the greater part of economic activity (though to a much lesser extent than in the United Arab Emirates or Qatar).

Despite the considerable diversification and sophistication achieved, the economy remains dominated by oil, which provides some 95 per cent of the State's revenue and 75 per cent of its foreign exchange earnings — as well as 70 per cent of GDP (according to the last official calculation for fiscal 1975-76). It has always been conscious policy to distribute as much of the surplus wealth to the citizens—not the least through the long-established land acquisition programme — while also building up an investment portfolio as an alternative source of income.

Foreign assets accumulated by the Kuwait Government from its unspent revenue and invested abroad rose from the equivalent of rather less than \$4 bn. at the end

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of 1973, when oil prices were tripled almost overnight, to \$18.3 bn. at the end of 1976. That was after aid disbursements worth \$2.1 bn. in the three-year period and excluding the foreign exchange reserves held by the Central Bank as currency cover and to finance imports. The total undeclared sum is now thought to be in the region of \$25 bn. Unquestionably Kuwait, like Saudi Arabia, will remain a surplus producer for the foreseeable future, but will also surprise forecasters by its ability to spend its revenue over the next few years.

In its own way Kuwait, like the other members of OPEC, has seen a shift in its financial for-

tones, though it has not gone into deficit. In the course of its extended 15-month fiscal year up until the end of June, 1976, the Government officially recorded a budgetary surplus of KD 2.92 bn. (the equivalent of \$10.42 bn. at the present rate of exchange). In the 12-month fiscal year 1976-77 which followed, the excess of revenue totalling KD2.46 bn. (\$8.91 bn) over expenditure of KD1.4 bn. amounted to KD1.32 bn. (\$4.7 bn.), again at the current rate, according to officially published figures.

Kuwait tends to underestimate revenue, either for cautionary or presentational reasons (perhaps a mixture of both). Actual receipts for 1976-77 were 13 per cent higher than the forecasts. As it is, the revenue is conservatively put at KD2.27 bn. (\$8.10 bn.) though in practice it is likely to be higher.

#### Allocations

For the current fiscal year allocations for ordinary spending, development and property acquisitions are up by no less than 57 per cent. Even after allowing for inflation, however, the increase is more apparent than real in that the budget is more comprehensive than its predecessors, including for instance, the big projects programme of the Kuwait Oil Company for the first time. At the same time it does not cover Kuwait's \$700m. contribution to the Gulf Organisation for the Development of Egypt and the OPEC special fund, which were fully disbursed over calendar year 1977 and drawn from the State General Reserve.

As it is, after the transfer of another KD50 m. to the capital of the Kuwait Fund for Arab Economic Development, the fiscal surplus projected is down to KD234.7 m. (\$838 m.) Mr. Abdel-Rahman al Attiqi, Minister of Finance, is confident that the sum set aside for capital will be spent "to a great extent". Sheikh Ali Khakifa al Sabah, speaking in his capacity as Under-Secretary of the Department before his new appointment, predicts that in the final outcome there will be only \$900 m. — \$1 bn. to transfer to the reserves. This would compare with a surplus for investment of KD1 bn., or about \$3.5 bn. in 1976-77.

Meanwhile, it is believed that actual income from the oil sector including gas, will be more in the region of \$9 bn. rather than the

\$7.6 bn. envisaged in the budget. (Investment income is likely to be running at a rate of \$2 bn. annually now—but is ploughed back into the accumulating reserve assets). Overall, however, the financial statistics reflect the way in which the gap between revenue and expenditure has closed, as oil production has stagnated, world-wide inflation has continued and purchasing power has declined. Last year the Central Bank calculated the State's loss from the depreciation of the dollar alone at over 5.4 per cent.

In comparison with its Arab neighbours Kuwait is at a much more advanced stage of development. It is not generally appreciated, however, just how big the scale of its spending on projects will be over the next two decades. Kuwait's draft five year 1977-81 plan embraces a capital expenditure programme of nearly KD 5 bn. Government projects already in hand include the vast programme for housing construction (costing over KD1 bn). expansion of electricity generating and water desalination capacity (KD 350m.), the extension of the motorway system around Kuwait city and the LPG plant now nearing completion (up to KD 350m.) as well as a considerable investment in recreational facilities, hospitals, schools, telecommunications and ports.

Despite its surprising absorptive capacity, the preoccupation with finding reliable and profitable outlets for investment in the Arab world, apart from the big multilateral projects, for both State-owned and private capital goes on. "We are working on it but it takes time", says Mr. Attiqi, who has been the foremost protagonist of deploying funds for productive purposes elsewhere in the Arab world. The Government's biggest involvement is in the troubled Kennan sugar project in Sudan where, says Mr. Attiqi, "progress has not been as fast or easy as we hoped". He is reasonably happy about the joint investment companies formed elsewhere, but has complained of lack of suitable projects generally and the restrictions imposed in various countries.

Kuwait's investments in other Arab countries, together with loans to them, the World Bank and the IMF and its capital contributions to multilateral funds and organisations make up a significant part of

**BALANCE OF PAYMENTS**  
(K.Dm.) 1975

Description	1975		1976	
	Debit	Credit	provisional Debit	Credit
1 - Goods and services (net):		2,016		2,194
Trade balance		1,695		1,758
Exports and re-exports (fob)		2,459		2,828
of which: Oil and gas exports		(2,289)		(2,615)
Imports (cif)	764		1,070	
Non-monetary gold	32	2	34	2
Services (net)		351		468
Freight and insurance	—	14	—	17
Other transportation	33	100	35	128
Travel	55	24	67	30
Investment income	38	372	36	477
Government	(—)	173	(—)	(255)
Financial institutions	(12)	(72)	(20)	(82)
Other private	(26)	(127)	(16)	(140)
Other government (not classified)	37	7	50	9
Other private+	7	4	10	5
2 - Private transfers:	80	—	92	—
3 - Total current account (1+2):		1,936		2,102
4 - Non-monetary capital and official transfers (net)*		789	1,249	
Official transfers	228		59	
Direct investment	47		117	
Government	(20)		(85)	
Kuwait Fund	(6)		(17)	
Other investment institutions	(21)		(15)	
Loans (net)	11		35	
Kuwait Fund	(22)	(7)	(49)	(6)
Other investment institutions	(12)	(16)	(36)	(44)
Other non-monetary capital	288		425	
Oil sector		(58)	(221)	
Government	(185)		(132)	
Kuwait Fund	(91)		(5)	
Investment institutions	(32)		(17)	
Specialised banks	(38)		(50)	
Other private	215		613	
5 - Commercial Banks (net):	27			94
Liabilities	—	26	—	155
Assets	53	—	61	—
Total (3+4+5)		1,120		947
6 - Reserves and related items (net):	1,120		947	
Central Bank of Kuwait (assets)	92		63	
Monetary gold	(6)	(—)	(20)	(—)
Reserve position in IMF	(112)	(—)	(48)	(—)
Other assets	(—)	(26)	(—)	(5)
Ministry Finance**	1,028		884	

\* Debit items are increases in assets or decreases in liabilities; credit items are decreases in assets or increases in liabilities.

+ Residual item, reflecting partly errors and omissions, but mostly outflow of private capital.

\*\* Estimate for 1975 based on available information for the period March 31, 1975, to January 31, 1976, and for 1976 based on available data for January 31 to December 31, 1976.

the State's foreign assets. In 1976, 50 per cent of the total accumulated was transferred to the Reserve Fund for Future Generations established under a law which also declared that in future 10 per cent of oil revenue should be ploughed into it. Kuwait's better class long-term assets worth over \$9 bn. were shifted to it. Overall the total \$25 bn. or so deployed abroad by the Ministry of Finance is divided about equally between equities and money market instruments, with 2 per cent of it in real estate.

**Decline**

In respect of its cash balances of \$3—4 bn. Kuwait is concerned about the decline of the dollar's value, but it is not so much concerned about its longer-term investment. Mr. Attiqi says, "We have a good diversification and a good spread". Sheikh Ali Khalifa al Sabah says that it is not a question of reducing the existing amount of dollar assets—rather shifting the direction of new investment slightly where this is possible. The Government accepts that a large proportion of its as-

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sets must inevitably be in the U.S. (which accounts for 60 per cent of the equity market worldwide). Moreover, it appreciates that nowhere else can it obtain the same optimum combination of growth and yield.

Over the past five years the average rate of return from the U.S. was 9 per cent on stocks and shares and 6—7 per cent from real estate. Even as its fiscal surplus declines, Kuwait rests assured that its giant nest egg will go on growing inexorably if only from income ploughed back into the fund. For their part the rich merchants have their own immense fortunes abroad that compensate them for fluctuations in the local market.

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