The Gulf Divided: The Economic Impacts of the Qatar Crisis

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In a nutshell

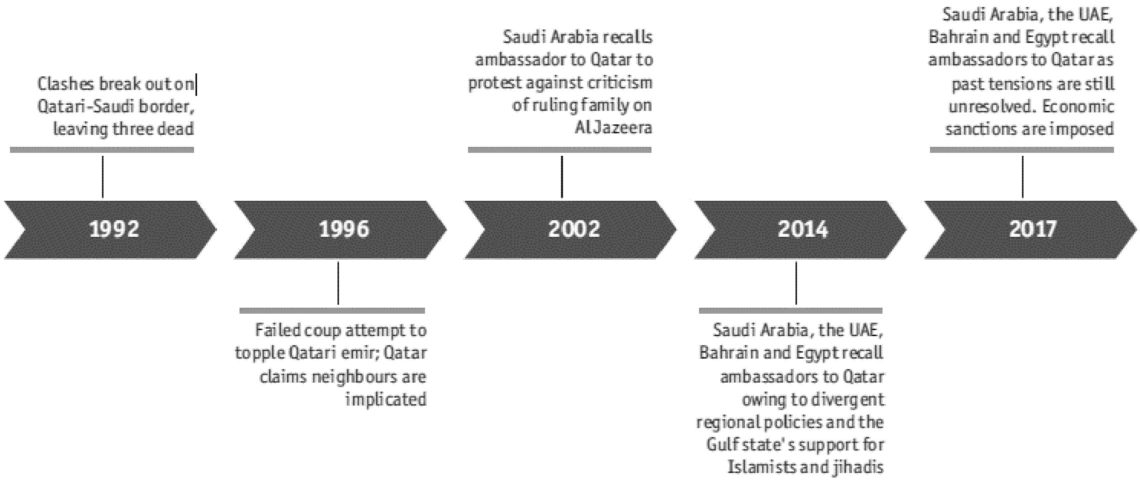
- While the Gulf crisis seems to be de-escalating, it remains unclear yet whether these signs of re-engagement are going to yield to a full restart in links between Qatar and its blockading neighbours.
- This research shows that Qatar diplomatic crisis creates new Gulf with no winners. It has further divided the Arab and Muslim world, and forced small states to make tough choices.
- Post-blockade proves Qatar's remarkable resilience and rapid and efficient adaptation.
- The crisis sped up Qatari plans and strengthened the motivation to take a close attention to self-sufficiency.

Summary

In mid-2017, The quartet of Saudi Arabia, the United Arab Emirates (UAE), Bahrain and Egypt have operated a diplomatic, trade and travel boycott of Qatar. This column reports the results of a recent research on the regional business costs of this blockade. The analysis reveals that while Qatar has been shaken by this crisis, the other countries are not left out, especially Saudi Arabia and the UAE. The causes of this blockade and the strategy put in place by Qatar to resist to Saudi and Emirati dominance have been advanced.

Qatar's crisis with Saudi Arabia and other Gulf neighbors has decades-long roots (see Figure 1). The anti-Qatar bloc has long considered Qatar as too friendly to Iran, too provocative in its backing of Al Jazeera media network, and too supportive of Muslim Brotherhood. Although a variety of issues have been raised against Qatar, the most potent has been the UAE and Saudi Arabia's strong feeling of annoyance over Qatar's support for Islamist movements. In addition, the competition between Qatar and the UAE for the leadership as the region's biggest financial hub. These developments put pressure on the Gulf region as an enduring political and security alliance, which became tangible in a diplomatic crisis that happened in 2014. The collective decision by Saudi Arabia, the UAE, Bahrain and Egypt to cut diplomatic and economic ties with Qatar on 5 June 2017 seems the most recent flare-up in a series of long-running tensions between Qatar its Gulf neighbors. This recent crisis will escalate tensions between the protagonists in the region that is, by nature, very unstable. It has rattled nerves sending shockwaves around the world. It may cost them billions of dollars by slowing trade, investment and economic growth as it struggles with oil price collapse.

Figure 1 : The origins and course of the 2017 Gulf crisis



While special attention has been devoted to the analysis of the effects of economic, macroeconomic and financial uncertainty on international business, rather less attention has been paid to the economic implications of geopolitical risks. The vast majority of these studies indicate that the unstable political scene can have a significant impact on stock markets, portfolio allocation and diversification opportunities. Some recent studies indicate that Qatar crisis have a significant impact on stock markets dependence and risk spillovers (see, inter alia, Al-Maadid 2019 a, b ; Charfeddine and Refai 2019). The contribution of this research is three-fold: first, we compare the conditional volatility process of the stock markets of Qatar and the boycotting countries before and after the blockade. Second, we test whether this Gulf crisis has exacerbated the volatility spillovers across the region. Third, we assess the direction of spillover effects between various markets in an effort to identify the net transmitters or the net receivers of risk spillovers. This would be useful for both portfolio risk managers and designers of policies aimed at safeguarding against increased political uncertainty surrounding the 2017 Gulf crisis.
Our analysis shows that while Qatar has been shaken by this crisis, the other countries are not left out, especially Saudi Arabia and the UAE. All the stock markets become more volatile in response to the blockade, but such volatility does not persist. Our findings also document that the profound political instability over Qatar crisis moderately exacerbate the stock market volatility transmission across Qatar and the boycotting countries. We then identify which from the stock markets is the most potential in exporting volatilities to the other countries during the boycott against Qatar. Before the boycott, two groups of countries are derived: Qatar, Saudi Arabia and the UAE are viewed as volatility transmitters, whereas Bahrain and Egypt are considered as risk receivers. After the crisis, we keep the same groups of countries, though with changing intensity of volatility spillovers.
Overall, our findings suggest that the boycott did not achieve the expected outcome. The fact that Qatar, Saudi Arabia and UAE responded in the same way (with respect the volatility persistence and the directional risk spillovers) to this crisis can be considered as a sign that Qatar "beats" the boycott. Doha

has demonstrated resilience in times of heightened political uncertainty. Despite its economic vulnerability, Qatar has successfully resisted the Saudi-embargo.

How was Qatar able to face a blockade imposed on it by four countries with substantial traditional authority?

Qatar has often been aware of its vulnerability and has managed its business with dexterity (multiplying foreign partners, strengthening the management of gas resources, and pursuing investment mediation) despite the economy's reliance on the hydrocarbon sector. Qatar has retained the crown of world's top exporter of liquefied natural gas in 2017, underpinning Qatari cash flow. The financial reserves at the disposal of the authorities can provide additional support, if needed, the authorities would place a particular emphasis on accelerating structural reforms to ensure that the economy remains internationally competitive and attractive for investment. The diplomatic tensions have served as a catalyst for improving domestic food production and reducing reliance on some countries. In response to the rift, Qatari authorities advanced some structural reforms in an attempt to stimulate the business environment. They plan to set up special economic zones that would help to spur diversification opportunities and encourage foreign direct investments. Overall, if this blockade showed the resilience of Qatar's economy, it also underscores the incapacity of the boycotting countries to put it down.

Why the anti-Qatar quartet failed in its mission?

Saudi Arabia's young leadership vowed to design comprehensive and transformative reforms that include a large range of socio-economic reforms. The latter have already started to address some of the country's long-standing issues including, among others, enabling women to drive and initiating value-added tax. Furthermore, Saudi leadership have undertaken reforms that are indispensable to economic diversification from oil sector like labour market reform, privatisation and opening the market to foreign investors. Even though the Saudi reform plans are vital for the future socio-economic stability of the kingdom, Saudi leadership has faced multiple socio-economic challenges in order to implement economic diversification policies. The Saudi authorities have taken initiatives in an attempt to attract foreign investors such as launching an active privatization programme and easing requirements for foreign institutional investors. Nevertheless, such initiatives did not have the desired impact on attracting more inflows of foreign investment a cornerstone of Saudi vision 2030 plan to diversify the economy away from the great reliance on oil revenues. The kingdom's bid to attract billions worth of investment to build vast city developments has been tarnished by khashoggi affair.

Further reading

Al-Maadid, A., Caporale, GM., Spagnolo, F. and Spagnolo, N. (2019a) "Political Tension and Stock Markets in the Arabian Peninsula." International Journal of Finance and Economics. ISSN: 1076-9307

Al-Maadid, A., Caporale, GM., Spagnolo, F. and Spagnolo, N. (2019 b). "The impact of business and political news on the GCC stock markets." Research in International Business and Finance. ISSN: 0275-5319

Charfeddine, L., and Al Refai, H., (2019) "Political tensions, stock market dependence and volatility spillover: Evidence from the recent intra-GCC crises." North American Journal of Economics and Finance 50, 1010-1032.