



DIRECTORATE-GENERAL FOR EXTERNAL POLICIES
POLICY DEPARTMENT



**RELATIONS BETWEEN
EU & GULF
COOPERATION COUNCIL
(GCC) COUNTRIES**

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**RELATIONS BETWEEN EU & GULF COOPERATION COUNCIL
(GCC) COUNTRIES**

Abstract

Relations between the EU and the Gulf Cooperation Council (GCC) countries have failed to materialize into a deep partnership. After twenty years of talks, the FTA is still not concluded. Although the GCC would benefit most from trade liberalization with the EU, its reluctance to commit to economic reforms reinforcing openness and transparency prevents the negotiations to come to an end. At the same time, France, Germany and UK relations with GCC countries are relatively more developed with high levels of weaponry supply and support on security grounds, albeit non comparable to the American involvement in the region.

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AUTHOR(S):

Dr. Rym AYADI, Senior Research Fellow, CEPS

ADMINISTRATOR RESPONSIBLE:

Pekka HAKALA
Directorate-General for External Policies of the Union
Policy Department
WIB 06 M 073
rue Wiertz 60
B-1047 Brussels

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EXECUTIVE SUMMARY

The Gulf region, comprising of the six Gulf Cooperation Council (GCC) countries, has long been neglected by EU policymakers, who do not manifest a strong political will towards it. The Cooperation Agreement concluded in 1988 provides the basis for cooperation in a wide range of areas and creates the basis for political dialogue. Despite its ambitious framework, the relations did not deepen. More than two decades after its signature, the parties have failed to conclude a free trade agreement (FTA) as foreseen in the Agreement.

Several reasons explain this impasse, including the unwillingness of GCC countries to move from subsidizing their energy industries; their reluctance to open their service sector to foreign competition; the opaqueness of government procurement procedures; and, the dual pricing of gas exports, to name a few.

Regarding their relations with the EU at the multilateral level, GCC countries are mainly interested in having duty-free access to the European markets for their petrochemical and aluminum products. Having implemented customs union agreement in 2009, the Council's members are also interested in technical support for reinforcing their own regional integration process, including the creation of a monetary union.

Despite the weak political will and fatigue in negotiations, several EU member states have actively developed trade and cooperation relations with the GCC countries individually. Most notably, France, Germany and the UK have positioned themselves as military suppliers. France and Germany have also been the advocates of the GCC's role of becoming the third pillar of regional security along with Iran and Iraq.

The prospect of striking deeper relations with the GCC as a regional body does not seem feasible. There are several reasons behind this observation. The weak institutional capacities of the GCC, the lack of human resources necessary for the functioning of an efficient administration, and internal divisions among the GCC states are important weaknesses, hampering the body's credibility and scope of action.

Given the strategic importance of the Gulf region in terms of security and energy supplies, the EU should adopt a hybrid approach consisting in maintaining relations at the multilateral level while simultaneously developing relations with GCC states individually. At the multilateral level, the EU may consider to further support GCC's regional integration. At the bilateral level, given the GCC's inherent divisions, the EU may wish to develop closer relations with the GCC states individually. Such a strategy would anchor the EU more firmly in the region while increasing its leverage in the Middle East politics. With the pivotal role of the GCC countries in the Arab world, such an approach would also allow for complementarities with EU's Mediterranean policy.

1 EU GULF COOPERATION COUNCIL RELATIONS

1.1 EU-GCC Relations at the multilateral level

Table 1. GDP and population data of GCC countries

	GDP per capita (constant 2000 US\$)	Population, total	GDP per capita, PPP (current international \$)
Bahrain	16,967(2008 data)	791,473	34,954 (2008 data)
Oman	10,779(2008 data)	2,845,415	25,303(2008 data)
Kuwait	23,072 (2007 data)	2,794,705	48,363(2007 data)
Saudi Arabia	9,827	25,391,100	23,428
Qatar	29,251(2006 data)	1,409,423	65,205(2006 data)
United Arab Emirates	25,606	4,598,600	57,826

Source: World Development Indicators 2010. Data are for 2009 unless specified

The Gulf Cooperation Council (GCC) countries, which comprises of Bahrain, Kuwait, Oman, Saudi Arabia, Qatar and the United Arab Emirates (UAE), are among the richest in terms of per capita income, reflecting their impressive endowment of hydrocarbons. The driving force behind the GCC as a body has been its members' security concerns. At its creation in 1981, the GCC was built to enhancing regional security threats in the wake of the Iran-Iraq war. Security concerns continue to hold the group together, ranging from the regional instability posed by the polarisation of the region by the Arab-Israeli conflict, the occupation Iraq, and Iran's recent resurgence.

Due to its active engagement in the region, the US has long achieved an influential position, making the Gulf region seen as the "backyard" of US, (Echagüe, 2007). American involvement is largely driven by the need to secure oil supplies at a manageable price. In exchange, the US has been established as the guarantor of regional security against the threats represented by Iran and Iraq for the region. The European concerns, on the other hand, have been chiefly focused on economic interests embedded in the ongoing negotiations of the EU-GCC Free Trade Agreement (FTA) without paying much attention to political factors, such as the Gulf Wars or the growing regional threat posed by Iran. Although the states of the region were an important target of the Euro Arab Dialogue launched in 1974, the initiative collapsed in 1989 without any significant achievement in terms of deepened and comprehensive cooperation.

A framework agreement had been reached in 1983 aiming at freeing and increasing commercial exchanges between the two regions. Its scope was gradually extended over the years and GCC-EU negotiations for a formal Cooperation Agreement were concluded in 1988. The multilateral agreement sought to "promote overall cooperation between equal partners on mutually advantageous terms in all spheres between the two regions and further their economic development, taking into consideration the differences in development of the parties"¹.

The motivation behind the Cooperation Agreement was quite straight forward: GCC countries are important suppliers of energy, export market for the EU, and providers of investment capital, as recently highlighted by the activism of the region's Sovereign Wealth Funds (SWFs) in European financial markets. The Agreement also has a minor political dimension in which the EU sees the GCC grouping as an important actor to promote stability in the region. To achieve this aim, cooperation was established

¹ Quoted from the preamble of the Cooperation Agreement. *Official Journal of the European Communities*, OJ n° L 54/3, 25 February 1989.

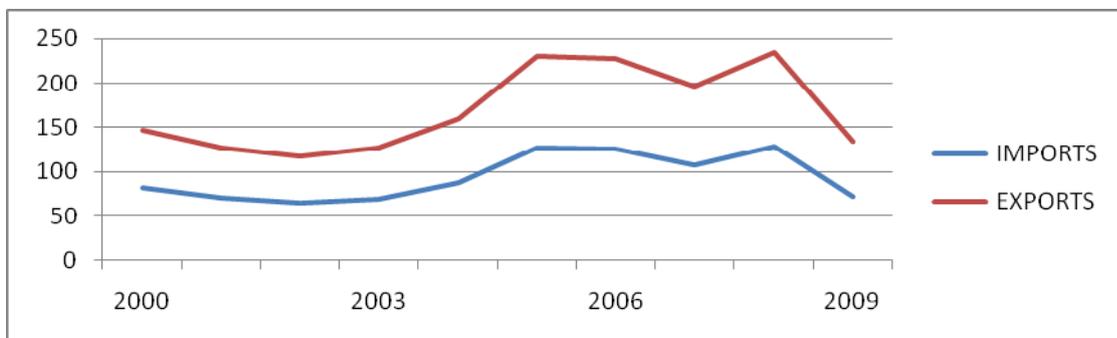
in a wide range of fields: economy and trade, agriculture and fisheries, industry, energy, science and technology, investment and environment.

Despite its ambitious framework, little has been achieved in any of these fields. In fact, the Gulf countries were not included in EU's external cooperation programmes until 2007 when the Council adopted the regulation EC/1934/2006 establishing a financing instrument for cooperation with industrialised and other high income countries and territories (ICHI) for the years 2007-2013. The instrument is allocated a small envelope of €172 million and targets, besides the GCC countries, other industrialised nations, such as Australia, Canada, Japan, United States and others. The fields of intervention of the ICHI are broadly the same as those envisaged in the cooperation agreement².

As regards the political dialogue, the EU-GCC Cooperation Agreement created the Joint Cooperation Council comprising of representatives of both sides who meet at least once a year. The Joint Council's aim is to reach the objectives set in the Cooperation Agreement and to make it operate smoothly. In practice, the bulk of communiqués made by the Joint Cooperation Council have only been political statements on international stability and terrorism on which both parties share the same opinion. In the field of technical cooperation, besides some help in the form of technical assistance provided by the EU to support the regional integration process of the GCC, very little has been achieved (Baabood, 2006).

Outside the scope of the Cooperation Agreement, economy and trade is the most developed field of EU-GCC relations. Up until the second half of 2008, GCC's total trade flows have risen as a consequence of higher oil prices. GCC countries are all now members of the WTO and rank currently the 4th largest export market for the EU, being the main trading partner of GCC countries. Regarding trade in goods, exports from the EU to the GCC accounted for approximately €54bn in 2009, representing 5% of total EU's external trade. In contrast imports to the EU from the GCC account for €21bn, thus resulting in a structural surplus in EU's favour evaluated today at €33bn. Figure 1 depicts the trade relations between the two regions and Table 2 provides the GCC individual countries' trade with the EU for the period 2000-2009

Figure 1. EU imports from and exports to GCC (€ bn)



Source: Eurostat

² The activities covered by the ICHI are: promotion of co-operation, partnership and joint undertakings between economic, academic and scientific actors in the EU and the partner countries; stimulation of bilateral trade, investment flows and economic partnership; promotion of dialogue between political, economic and social actors and NGOs; promotion of people-to-people links, education and training programs, intellectual exchanges and the enhancement of mutual understanding between cultures and civilizations; promotion of co-operative projects in the areas of research, science and technology, energy, transportation and environmental matters; raising awareness about and understanding of the European Union and its operations in partner countries; and, support for specific initiatives, including research work, studies, pilot schemes or joint projects. The midterm evaluation report of the ICHI and its operations is expected to be published by December 2010.

Table 2. GCC countries trade with the EU for the period 2000-2009

EU exports to GCC	In € Billions	As a percentage of exports to the region
Bahrain	12.18	2.57%
Oman	18.67	3.94%
Kuwait	34.92	7.36%
Saudi Arabia	160.49	33.83%
Qatar	37.16	7.83%
United Arab Emirates	210.91	44.46%
	474.34	

EU imports from	In € Billions	As a percentage of imports from the region
Bahrain	5.32	1.96%
Oman	3.83	1.41%
Kuwait	31.05	11.42%
Saudi Arabia	168.13	61.86%
Qatar	14.50	5.34%
United Arab Emirates	48.96	18.01%
	271.79	

Source: Eurostat

EU's imports from the GCC consist mainly of fuel and mining products, accounting for 73% of all goods originating from the GCC states. However, as a result of the diversification of EU's oil supplies, the €15bn. oil from the region represent less than 25% of EU's total crude oil imports. In contrast, oil producing countries formerly belonging to the Soviet Union and North African countries account respectively for 44% and 14% of EU's total oil imports.

As shown in Table 3, EU's exports to the GCC consist mainly of machinery and transport equipment³. In 2009, these exports have accounted for €28bn. representing half of the total exports directed to the region. As a consequence of the crisis, trade between the two regions has decreased since 2008, falling to its 2004 levels. The decrease in EU-GCC trade has been slightly higher than the contraction of EU's trade with the world⁴.

³ This includes among others power generation machinery and equipment, electrical machinery and appliances, parts of, road, air water vehicles, spacecrafts and high technology military equipment. For the complete composition of the nomenclature, see:

<http://unstats.un.org/unsd/cr/registry/regcs.asp?Cl=14&Lg=1&Co=7>

⁴ While the growth rate of EU's total trade with the world has decreased 25% between 2008 and 2009, EU's trade with the GCC has decreased 29% over the same period (own calculations based on WTO and Eurostat data).

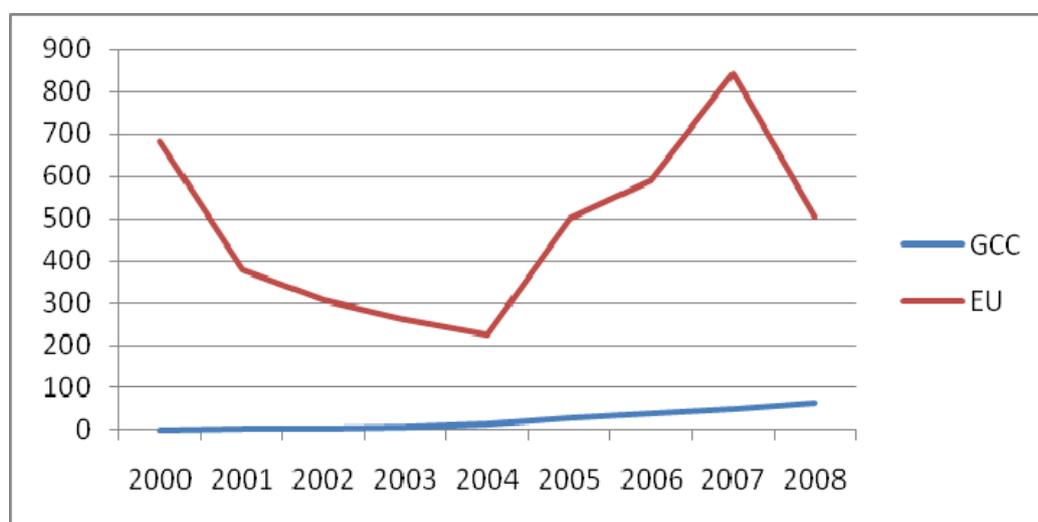
Table 3. EU trade with GCC by product inn 2009 (€ mn)

EU Imports from GCC	Value (€mn)	Share of total (%)	Share of total EU imports (%)
Minerals, fuels, lubricants and related materials	15 337	71,4	5.4
Chemicals and related products	2 068	9.5	2
Manufactured goods classified chiefly by material	1 451	6.7	1.3
EU exports to GCC	Value (€mn)	Share of total (%)	Share of total EU exports (%)
Machinery and transport equipment	28 797	49.9	6.4
Manufactured goods classified chiefly by material	7 589	13.1	5.5
Misc. manufactured articles	7 155	12.4	6.1

Source: DG TRADE

As regards capital flows, since 2007, inflows of foreign direct investment from the EU to the region have declined as a consequence of the crisis. Although recent statistics are not yet available, there is indication that the investment flows are once again on the rise. FDI stocks are high and at par with GCC investments in the EU ranging around €30bn. Figure 2 compares the EU's and GCC's performance in attracting FDI, Figure 3 gives the bilateral flows and stocks of FDI.

Figure 2. FDI inflows to the EU and GCC, global amounts (\$ mn)



Source: UNCTAD FDI statistics database

Figure 3. Bilateral FDI flows and stocks in EU from GCC countries (€bn)


Source: DG TRADE

One issue related to cross border capital flows and out of the scope of EU-GCC relations is the importance of sovereign wealth funds (SWFs). Accumulation of wealth generated by oil exports has allowed GCC states to build vast reserves channelled into SWFs. Between 2002 and 2006, approximately \$100bn of the \$642bn surplus accumulated in these funds was invested into EU countries, especially in the financial sectors. Although these investments are not a new phenomenon, GCC countries' investments have become much more diversified, increasingly likely to acquire management rights. Table 4 shows selected examples of GCC SWF acquisitions in the EU between 2007-2008.

Table 4. Selected examples of GCC SWF acquisitions in EU in 2007-2008

Target	Fund	Value (\$ mn)
OMX (Sweden)	Dubai Investment Financial Corporation)	3551.4
London Stock Exchange	Dubai Investment Financial Corporation)	1648
Alliance Medical United (UK)	Dubai International Capital	1248.7
Mauser (Germany)	Dubai International Capital	1159.8
OMX (Sweden)	Dubai Investment Financial Corporation)	1100.6

Source:Gugler, Chaisse (2009)

The total stocks acquired by GCC's private investors and SWFs in the EU is estimated at more than €400bn, making them among the largest foreign stakeholders in Europe (Hertog, 2007). The GCC SWF's investments accounted for a significant part of the emergency financing made available during the crisis giving them an increased bargaining power.

The degree of financial interdependence that GCC countries have developed over the years with the EU has raised some concern among European policy makers. Of particular importance are the motives behind the funds' investments. For example, none of the Gulf SWFs have adhered to the Santiago

Principles, put forward by the IMF in 2008. Furthermore, Table 5 shows that the funds rank low in terms of overall transparency, based on the index developed by Linaburg and Maduel (LM index)⁵.

Table 5. GCC SWFs' characteristics

Country	Fund name	Assets under management (\$ mn)	Inception	Origin	LM index
UAE – Abu Dhabi	Abu Dhabi Investment Authority	\$627	1976	Oil	3
Saudi Arabia	SAMA Foreign Holdings	\$415	n/a	Oil	2
Kuwait	Kuwait Investment Authority	\$202.80	1953	Oil	6
Qatar	Qatar Investment Authority	\$65	2005	Oil	5
UAE – Dubai	Investment Corporation of Dubai	\$19.60	2006	Oil	4
UAE – Abu Dhabi	Mubadala Development Company	\$13.30	2002	Oil	10
Bahrain	Mumtalakat Holding Company	\$9.10	2006	Oil	8
Oman	State General Reserve Fund	\$8.20	1980	Oil & Gas	1
Saudi Arabia	Public Investment Fund	\$5.30	2008	Oil	3
UAE – Ras Al Khaimah	RAK Investment Authority	\$1.20	2005	Oil	3
Oman	Oman Investment Fund	X	2006	Oil	n/a

Source: Sovereign Wealth Fund Institute

Despite of their importance, EU-GCC relations do not address EU financial linkages with SWFs. The lack of transparency combined with the strategic nature of their investments has put GCC's SWFs under increased public attention. Recipient countries -within the EU chiefly France, Germany and Italy- fear the acquisition by SWFs if strategic assets backed by geopolitical agendas. On the other hand, GCC's SWFs argue they are not driven by such motives and put forward as a proof their past behaviour of quiet investors. But their increasing role in the financial architecture does not allow conceiving the past as a good predictor of their future behaviour. With the steady rise in their investments stock in the EU, their importance will increase, so will their ability to manage increasingly complex portfolios and balance their political risks (Behrent, 2008). In this regard, at the multilateral level, the EU should explicitly address this issue. On the one hand, GCC SWFs complain about discriminatory treatment in the EU. On the other hand, most of them did not adhere to the IMF working group on SWFs. Their discriminatory treatment concerns should be addressed by demanding adherence to the Santiago Principles by GCC's SWFs on an individual basis in exchange of non discriminatory access. At the same time, the EU should push for a deepening of the prerogatives of the IMF working group on SWFs so as to make it binding. One idea to further explore in this regard would be in a first stance to call for the integration of the largest GCCs SWFs, Abu Dhabi Investment Authority (and its branches) and the Saudi Arabia Monetary Agency, into the IMF as it would push them towards more transparency and accountability.

EU-GCC financial linkages are not part of a formal framework within their relations. The high degree of financial interdependence between the two regions gained public attention in the wake of the 2008

⁵ The Linaburg Maduel index has been developed to score SWFs transparency performance. The more information the fund provides, the higher the score. For more information see: <http://www.swfinstitute.org/statistics-research/linaburg-maduell-transparency-index/>

financial crisis. Prior to the crisis, relations focused on trade negotiations: under article 11 of the EU-GCC Cooperation Agreement both parties commit to grant each other the Most Favoured Nation" (MFN) tariff and to enter into negotiations for a free trade agreement (FTA) Talks foreseeing the signature of the FTA started in 1990 and have failed to materialize until today. The FTA is only one layer of the relations perceived in the eyes of the GCC as a preamble for any form of deepened cooperation with the EU in other fields (Youngs, 2009).

Several reasons can be put forward to explain the failure to conclude the FTA after 20 years of negotiations. Initially, the EU's petrochemical lobby forcefully fought against trade liberalization resulting in European governments blocking duty free access for petrochemicals from the Gulf for many years. The reason behind this protectionist stance was that EU's petrochemical procurers argued that the double pricing policy of raw materials by GCC countries constituted an implicit subsidy which would result in dumped imports entering the EU. This policy allowed GCC producers to enjoy input prices 30% lower than export prices, GCC governments arguing this was due to added costs to exports (pipeline transportation, refrigeration, storage and terminal facilities), (Antikiewicz and Momani, 2009). Driven by availability of inputs and economic diversification policies, the petrochemical industry in the GCC is believed to expand massively in the following years. In fact, in the case of ethylene⁶ it is believed that GCC states will account for over 50% of the world's new capacities in that field (PwC, 2004). In addition, within GCC states, Saudi Arabia has the biggest potential in petrochemicals. The national petrochemical firm, SABIC is the regional leader in the industry and the FTA would foster its activity in Europe. For the regional industry in general and for the Saudi petrochemical company in particular, the conclusion of the FTA would result in the rapid acquisition of world class technology potentially challenging EU's competitive advantage and global market power, (PwC, 2004).

The petrochemicals divergence was overcome, when Saudi Arabia joined the WTO. The country managed to convince WTO members that the higher export prices were in fact a result of added costs which put an end to the EU's petrochemical lobby allegations. But several issues continue to block the FTA. The human rights and illegal migrations clauses embedded in the FTA were rejected by GCC states, which advocated that Brussels was bringing issues on the table that had nothing to do with trade (Echagüe, 2007). The refusal from GCC's side to pursue negotiations until they were withdrawn prevents the EU from any attempt at entering into closer partnership while also putting a question mark on the effectiveness of EU's policy based on conditionality. However, according to senior EU diplomats in the region, these issues act as a "smokescreen" hiding the reluctance of countries in the region and in particular of Saudi Arabia to seriously commit to move towards market oriented reforms and leaving aside the heavy subsidization of its energy industry (Youngs, 2009). Negotiations have also failed to go forward due to GCC countries' differentiated pricing of gas exports, lack of transparency in public procurement procedures, and barriers to entry for foreign investors in the services sector.

Despite their reluctance to further commit to the conditions forwarded by the EU, the GCC countries would benefit most from the FTA. Indeed, according to some estimates, following the conclusion of the FTA, GCC countries would benefit from a 3.2% per annum income increase calculated on the basis of their GDP, (PwC, 2004). As GCC economies are to a certain extent different, these gains would not be equally distributed. The potential for expansion enjoyed by the Saudi petrochemical industry coupled to EU's imports from the country would maximize the country's benefits from trade liberalization with the EU. Nevertheless, at the aggregate level, all GCC countries would benefit from the conclusion of the FTA.

The positive effects are to be witnessed not only in the petrochemical sector, but also in the fields of services and investment. Lowering the GCC tariffs as an outcome of the FTA would increase their attractiveness for outward investment by transnational corporations, and not only by EU based multinationals. As they have engaged in a path of economic diversification aimed at reducing their oil

⁶ Ethylene is a petrochemical used as an input for the fabrication of plastics and plastic related manufactured goods.

dependency and the risks of “Dutch disease” syndrome, an increase in services trade and investment would be a supportive factor for the development of the GCC’s economies. With world-class financial centres such as Dubai, Qatar, Bahrain⁷, the FTA would lead to an increase in service-related investments, which would further reinforce their positions and support their knowledge-driven growth. Given the high levels of commercial and financial interdependence between the two regions, the EU could leverage its position by underlining the long term benefits for the GCC stemming from the conclusion of the FTA.

1.2 EU-GCC relations at the bilateral level

While the multilateral cooperation is relatively limited, the EU’s member states rely more on bilateral, state to state contacts with individual GCC states. In the field of bilateral relations, rather than cooperating, member states compete for markets in the region (Baabood and Edwards, 2007).

The primacy of bilateral relations may come at the expense of policy coherence towards the region, undermining efforts to deepen relations. But at the same time, given the differences in the fields of action of the EU and its member states, the dual setting of multilateral and bilateral engagement can reinforce the aggregate influence of the EU in the region.

As the Gulf is rather neglected by EU policy makers, member states’ economic and diplomatic presence in the region is unequally distributed and driven by different individual interests in the GCC countries. Three countries are active in the region: UK, France and to a lesser extent Germany. The following table lists the bilateral agreements in vigor between France, UK and Germany and GCC states. Given the changes the region has undergone after the Gulf War, the table lists the scope of the agreements concluded since the 1990’s as they are more helpful for the understanding of bilateral relations, the motivations behind them, their scope and level of closeness between individual Member States and GCC countries.

⁷ According to the Global Financial Centres Index n°8, as a consequence of the crisis “Dubai no longer figures in the top five financial centres in the next few years but despite the Emirate’s publicised problems, it still holds top position in the Middle East followed by Qatar and Bahrain”.

Country	Bahrain	Kuwait	Oman	Qatar	Saudi Arabia	United Arab Emirates
France	Double taxation (1993) Air services (1995); Investment protection and promotion (2004); Mutual visa exemption (2008)	Double taxation (1994); Joint declaration (2009) to foster cooperation in: Renewable energy climate change mitigation, Air services, Development finance between the Kuwaiti Fund for Arab Economic Development and AFD Institutional cooperation for the management of public finances; New technologies, Cooperation between the Kuwait Investment Authority and the Caisse des Depots et Consignations	Double taxation (1989); Investment protection and promotion (1994)	Double taxation avoidance (1990); Investment promotion and protection (1996); Youth and sports (1996); Tourism (2008); Interior security academy (2008); Mutual visas exemption (2008)	Double taxation avoidance (1991); Investment protection and promotion (2002); Public veterinary health (2002); Bilateral political consultations (2008);	Judicial cooperation (1990); Air services (1991); Investment promotion and protection (1991); Double taxation avoidance (1991); Abu Dhabi museum (2007); Judicial cooperation in penal matters (2007); Pacific use of nuclear resources (2008); "Protocole d'accord" on IPR; Establishment of mathematics and physics classes (2008); Cooperation in diplomatic and Consular representation (2008); Security and defense (2008)
Germany	Investment promotion and protection (2007)	Cooperation in security matters (2007); Investment promotion and protection (1997); Memorandum of understanding in higher education and health (2009)	Air transport (1998); Double taxation (2002); Investment promotion (2010)	Air transport (1996); Investment promotion and protection (1996); Medical research agreement	Cultural cooperation (2006);	Strategic partnership (2004); Political consultations (2008); Air transport (date?); Investment promotion and protection (2008), Double taxation avoidance (2008)
U.K	Drug trafficking (1990); Investment promotion and protection (1991); Air services (1998); Double taxation avoidance (2010)	Double taxation avoidance (1999); Investment promotion and protection (2009);	Embassy premises (1993); Investment promotion and protection (1995); Double taxation avoidance (1998)	Air services (1998); Double taxation avoidance	Drug trafficking (1990); Double taxation avoidance (1993)	Investment promotion (1992); Trade in textiles (1992); Air services (2002); Extradition agreement (2006); Mutual assistance in criminal matters (2006)

Table 6. Member states and Gulf countries bilateral agreements concluded since 1990.

Own compilation. Sources: <http://www.doc.diplomatie.fr/pacte/index.html>; <http://www.fco.gov.uk/en/treaties/search> ; <http://www.auswaertiges-amt.de/diplo/en/LaenderReiseinformationen.jsp>.

Table 6 shows the differences between member states involvement in the region. Overall, Bahrain and Oman are the less targeted countries. Kuwait, Saudi Arabia, and the UAE have received more attention.

As a former colonial power, Britain enjoys closer links with the region and the country has self appointed itself as the “*policeman of the Gulf sea lanes*” regularly carrying anti-piracy and maritime security missions aimed among others at securing Iraqi oil platforms⁸ (Fürtig, 2004). Moreover, it is very active in the field of military cooperation, although no formal agreement has been signed. The series of Al Yamamah deals provide with an example of the high degree of involvement of the UK in the region and more specifically in Saudi Arabia. Under these series of agreements the Saudi government bought from the UK high quantities of military equipment between 1985 and 2006 worth more than £40bn (See Table 6). Although the exact terms of the agreement are not publicly known -raising concerns about transparency in public procurement- it is believed the Saudi government paid part of the deal with oil supplies⁹. In addition to trade in defense equipment, the UK is also intensively involved in training missions and joint exercises conducted in the country. These series of deals have provided more than 30 000 jobs in Saudi Arabia and made the country the 4th largest export market of Britain outside the OECD (Fürtig, 2004).

Although the Gulf region remains under American security umbrella, trade in defense goods with the EU member states is an attempt—to the extent possible—to diversify military supplies.

Table 7 gives some examples of deals between Britain, France, the US and the GCC countries. Although some diversification has taken place, US still remains a major supplier in reaction to growing threats stemming from the Iraqi turmoil, but mostly from the fears rising about Iran’s unclear foreign policy agenda.

Table 7. Examples of security deals between France, Germany, UK and USA with GCC states

Partner countries, date of deal	Goods supplied	Value
UK- Saudi Arabia (1985-2006)	Tornado IDSs, Tornado ADVs, Hawk training aircraft, Pilatus PC-9	£40 bn
France- United Arab Emirates (2008)	Data not available	€12 bn
France- Saudi Arabia (negotiations began in 1996 and were concluded in 2009)	Securisation of Yemeni border (air, land and sea defense systems, electronic fence among others)	€ 2 bn
US- Saudi Arabia (2010)	F-16 jets, upgrade of F-15 jets	\$67.8 bn
US- United Arab Emirates (2010)	Patriot and THAAD missiles, transport aircrafts, unnamed aerial vehicles	\$35.6 bn
US-Oman (2010)	F-16 jets; offshore patrol vessels; air defense systems	\$12.3 bn

Sources: Fürtig (op, cit); Financial Times *Gulf in \$123bn US Arms Spree*, Financial Times, 21st September 2010¹⁰

Despite the absence of colonial links with the region, following the Second Gulf War, France managed to have solid anchors in the GCC countries as it ranked third in military commitments among non Arab participants in the coalition. However, France does not follow exactly the same patterns as Britain in its relations with GCC countries. While the UK is relatively more engaged with Saudi Arabia, France is more involved with the United Arab Emirates, Kuwait and Qatar.

⁸ BBC News, *Naval Warship to Tackle Pirates*, http://news.bbc.co.uk/2/hi/uk_news/england/devon/8278132.stm, published 28th of September 2009 , and BBC News, *HMS Monmouth returns to Plymouth after Gulf Patrols* , published 9th of April 2010 http://news.bbc.co.uk/2/hi/uk_news/england/devon/8611816.stm

⁹ BBC News, *The Company File Arms Sales fuel BAE’s Profits*, published 25th February 1999, <http://news.bbc.co.uk/2/hi/business/285963.stm> , last accessed 27th of September 2010.

¹⁰ Roula Khalaf, James Drummond, *Gulf in \$123bn US Arms Spree*, Financial Times, 21st September 2010

With regards to the Saudi kingdom, the French defense consortium EADS built an air fence system along the Saud-Yemeni border, as is currently engaged in a wider project aimed at securing all the countries borders with a physical fence and virtual barriers comprising of military surveillance technologies and reconnaissance airships¹¹. Given the instability recently witnessed in Yemen, commonly referred to as an Al Qaeda backyard, the Saudi government is willing to stop any external source of instability at its borders. In addition, it is the only country in the region with which relations are structured and formalized at a political level, with an agreement on bilateral political consultations concluded in 2008.

As for the United Arab Emirates, in 2008, French president Sarkozy signed a defense agreement with the country establishing a permanent base in Abu Dhabi albeit very small. The deal that formally set this military base in the Emirate was accompanied by €12bn. arms sales as well as nuclear technology transfers along with a cooperation treaty for the development of pacific nuclear capabilities (Youngs, 2009).

As regards Qatar, half of the military equipment of the Kingdom's armed forces is French and the country has signed an agreement for the training of security forces. French relations with the Gulf, and especially with the Emirates, are not only bound to defense agreements, arms sales and critical technology transfers: the country is very active in other fields.

Paris has concluded a treaty with Kuwait foreseeing among others cooperation in the restructuring of the emirate's public finances and collaboration between the French state investment vehicle Caisse des Dépôts et Consignations and the country's SWF the Kuwait Investment Authority. This shows a clear interest in securing access to external finance in exchange of assistance to one of the country's most challenging issues, the restructuring of public finances. In fact, as an oil dependent economy, long term economic and budgetary sustainability depends on efficient and well crafted management of public finances. On cultural and scientific areas, France's agreement with the UAE has promoted the establishment of its most prestigious universities and higher education institutions in the country among which the Lycée Louis le Grand and the university of La Sorbonne.

Germany's relations follow a different pattern. The country's exports consist mainly of high value-added motor vehicles, electrical machinery and equipment, electrical products, chemicals and energy technology. Germany seems also to be willing to be positioned in the region in security matters as it concluded a cooperation treaty on security with Kuwait as well as a strategic partnership and political consultations agreements with the United Arab Emirates. Despite the country's lack of involvement in military areas during the 1980's and early 1990's, there is a reversal of this trend, with the sales of Alpha Jet Trainers to the region and the agreement to participate in military operations in the Middle East provided they comply with UN resolutions.

If relations at the multilateral level do not succeed in bringing tangible outcomes as is witnessed with the failure to conclude the FTA after 20 years of negotiations, bilateral contacts appear as much more structured, albeit narrower in scope. For example, on economic grounds, all three countries have concluded double taxation treaties as well as agreements on investment protection with GCC countries¹². Hence, member states interested and active in the Gulf especially France, and at the same time pushing for conclusion of negotiations for the FTA during their respective presidencies¹³, manage

¹¹ BBC News, World's Barriers: Saudi Arabia, 5th November 2009, http://news.bbc.co.uk/2/hi/middle_east/8342890.stm, last accessed 27th September 2010

¹² The ministries of foreign affairs of France, Germany and UK display the adherence to international treaties of their respective countries. Information comes from the following websites: France: <http://www.doc.diplomatie.fr/pacte/index.html>. UK: <http://www.fco.gov.uk/en/treaties/search>. For Germany, information was gathered through consultation of GCC states pages of the ministry of foreign affairs: <http://www.auswaertiges-amt.de/diplo/en/LaenderReiseinformationen.jsp>. Germany however, does not have double taxation and investment promotion agreements with Saudi Arabia and Qatar.

¹³ During the French presidency, the conclusion of the EU-GCC FTA was said to be "a priority": Présidence Française du Conseil de l'Union Européenne, *Programme de Travail 1^{er} Juillet – 31 Décembre 2008 : Une Europe qui*

to secure contacts and relations on their own side. Overall, the main picture emerging from the bilateral relations is that where the EU fails to develop relations given its civilian power nature, member states take the lead. This dual setting of EU's engagement in civilian matters and individual Member States' engagement on military grounds is complementary and represents a valuable approach to reinforce Europe's influence in the region.

2 GCC'S INTERESTS, EXPECTATIONS FROM THE EU AND SCOPE FOR A DEEPER PARTNERSHIP

2.1 Interests and expectations at the multilateral level

Abdul Rahman Al-Attiyah, former GCC secretary general in 2002 summarized the region's interests in the EU at the multilateral level: *"GCC countries are a historical partner of Europe. Europe needs us and we need them. We need their technical knowhow. They need our resources. We have a mutual interest"*.

On economic grounds, benefits from free trade and regional integration are the main issues of interest for GCC's cooperation with the EU.

Within the scope of the FTA, the GCC countries would benefit from access to the European market for their petrochemical and aluminum industries, while the EU would only enjoy minor gains (PwC, 2004). Second, the EU's experience in regional integration is a source of inspiration for the region.

Regarding sector specific benefits, petrochemical industries are expected to be winners from an eventual FTA. Petrochemical production in the GCC is expected to increase in the following years due to the proximity to new centers of global demand, a preexisting production capacity, and the availability of low cost feedstock. Preferential market access to the EU would reinforce this trend. At the country level, Saudi Arabia would benefit most from enhanced market access. Moreover, increased exports would likely create jobs in the country for skilled Saudi nationals. (PwC, 2004)

Aluminum is also a strategic sector for GCC producers, who demand duty-free access to the European markets. The region's aluminum industries are expanding, supported by national investment programs and low energy prices. Trade liberalization effects for aluminum have to be assessed on the basis of their short- and long-term benefits. In the short run, profit margins of GCC producers will increase due to tariff reduction, and in the long run, market power of GCC producers will increase. At the country level, United Arab Emirates and Bahrain are the ones most likely to benefit from the FTA.

In addition, direct and indirect benefits at the aggregate level are to be stressed by the EU in its negotiations. First, as regards the direct effects, a lowering of the GCC's common external tariff to a level close to 3% (5% is the actual level) would entail a yearly increase in income estimated at around 3% of GDP per annum. Indirect effects are to be found in the commitments towards openness, the implementation of trade facilitation measures and the adherence to rules based frameworks for trade and investment. Such measures would increase the GCC countries attractiveness as a location for FDI reinforcing their economic diversification policies (Sturm, Strasky, Adolf and Peschel, 2010).

Despite the GCC's reluctance to conclude the FTA, the EU should clearly use these arguments as leverage. Moreover this tariff level should be demanded as it is the one which makes only winners in the region: given that Qatar and Kuwait had already lower tariffs before the entry into force of the GCC customs union, a 3% level would be optimal for all 6 countries.

In a broader perspective, the EU is viewed as a model of successful and deep regional integration¹⁴. Drawing on its own experience the EU can provide valuable technical assistance. Since its constituency,

Agit Pour Répondre aux Défis d'Aujourd'hui,

http://www.eu2008.fr/webdav/site/PFUE/shared/ProgrammePFUE/Programme_FR.pdf

¹⁴ At the multilateral level, *"many GCC citizens still see the EU as a model of regional integration that the GCC should try and emulate"* (Burke and Koch, 2010).

the GCC has put forward its willingness to create a customs and monetary union¹⁵. After several years of slow progress towards the implementation of the former, it finally entered into force in 2009, and talks about a common currency are ongoing.

Although the common currency was expected to enter into force in 2010, the date turned to be unrealistic. Today, prospects about a monetary union in the GCC are gloomier as the United Arab Emirates recently decided to opt out from discussions. Given the benefits of a common currency and the local businesses support¹⁶, it could be possible to see the UAE change their decision.

As a supportive factor to the economic diversification and regional integration processes the creation of a central statistical office for the entire region will carry benefits as it would allow for a close and timely monitoring of economic convergence. The EU can also assist the region in this field. Statistical cooperation already exists in GCC countries; but the creation of a regional statistical office based on Eurostat's model would enhance efficiency gains (Al Mansouri and Dziobek, 2006).

2.2 Interests and expectations at the bilateral level

At the bilateral level, the GCC countries' security concerns are the main determinants of the relations with the EU member states. In the aftermath of the collapse of the Soviet Union and with the emergence of globalization, the Gulf countries expected the emergence of a multi-polar not dominated by the US. Alternatives to American influence were sought, especially among European countries. However, the second Gulf War decisively challenged the perception that the EU could act as a guarantor of the region's security needs, (Fürtig, 2004).

This did not mean that engagement with European countries was dismissed. Gulf countries remain under the US' hard security umbrella but to a certain extent they are able to diversify their military alliances. Although the EU's member states cannot influence decisively events in the region, they remain appealing to the GCC states.

There are several reasons for why the GCC countries remain open to cooperating with the EU's member states on security issues.

First, despite of Washington's commitment to ensure regional security, the US Congress has vetoed arms sales to the GCC countries several times, urging them to find alternative suppliers of weaponry. Many GCC politicians see the American Israeli relationship as too close to expect an US-led approach towards their security interests. The Al Yamamah deal with the UK reported in Table 6 is illustrative (Fürtig, 2004).

Second, Washington based its security approach in the Gulf on the "dual containment policy", consisting in keeping Iran and Iraq in check without considering the option of dialogue and integration of these countries in economic relations. Germany offered an alternative to this option by proposing the "Critical Dialogue" from 1992 to 1997, with the idea that the isolation of Iran would be to the detriment to regional stability, (Struwe, 1998). Although not unanimously accepted by GCC leaders, the dialogue enhanced EU's credibility in the region.

Third, regarding US' involvement in Iraq in 2003, France adopted a critical position, calling for a strict interpretation of the UN resolution 687, which gave preference for sanctions for freeing Iraq from weapons of mass destruction. In this regard, by taking the lead of the group of states against the American intervention, France represented the voice of the countries in the region, (Fürtig, 2004)¹⁷.

¹⁵ There is a marked interest from the GCC in the EU in this regard and consultations between region's officials and ECB staff regularly take place (Jadresic, 2006).

¹⁶ The National, *UAE firms favor GCC monetary union*;

<http://www.thenational.ae/apps/pbcs.dll/article?AID=/20100826/BUSINESS/708269958/1042/rss>, 26th August 2010, last accessed 30th of September 2010.

¹⁷ For example, despite the threat Iraq represented, in 2000 Saudi Arabia called for the opening of a trade route with the country. This was an attempt to integrate Iraq in the region and diminish the value of any bellicose

Among the main European players in the region with Germany's strategic dialogue with the United Arab Emirates, France is the only bilateral treaty on political dialogue concluded with a GCC country.

These examples illustrate why the GCC states are interested in EU member states on security grounds: they can be an alternative to the US for weaponry supplies, and on political grounds they express the GCC states' interest in security architecture different from the American dual containment policies. They thus give some prominence to the region by advocating the GCC states' willingness to become along with Iran and Iraq the third pillar of regional security.

The security architecture¹⁸ of the region has undergone dramatic changes in recent years. The September 2010 arms deal between the US and the Gulf worth \$123bn is illustrative of the fact that the region is mired in an arms race, (Bauer and Hanelt, 2009). The invasion of Iraq and the complete failure of the long pursued dual containment policies, resulted in civil war conditions in Iraq. Meanwhile, fears over Iran's mastering of nuclear military technologies have given way to renewed instability in the region. In addition, the deterioration of Yemen's security and the repeated allegations of Al Qaeda jihadists hiding in the country's tribal areas also push for an increase in security demand, especially from Saudi Arabia.

The arrival of the Obama administration and its support of the Saudi-led Middle East Peace Initiative mark a shift in the overall US Middle East policy and create a framework in which all actors involved in the region seem to agree on the need to create a regional framework of security. EU is not excluded from the process; however, more engagement is necessary for the EU to take a decisive stake in the process of the regional reconfiguration, (Bauer, Hanelt, Koch, 2010).

2.3 GCC's capacities to enter in a deeper partnership with the EU

Given the challenges faced by the Gulf region on economic and security grounds, an important question is whether the GCC as a body is mature enough to enter into a deep partnership that is even more ambitious than the Cooperation Agreement. At the multilateral level, a closer look at the GCC constituency reveals that it is a regional intergovernmental organization lacking supranational institutions and prerogatives. The GCC Secretariat has no independent negotiating competence similar to the European Commission. Thus, in the FTA negotiations, the GCC's Secretariat mandate cannot go beyond a small range of economic issues. In this regard, the failure to conclude the negotiations can be also seen as the outcome of the GCC's weak institutional framework. Moreover, the GCC's president does not have the mandate to speak on behalf of the members of the council. The Council also does not act fully as an independent organ, clearly reflected by the lack of autonomous budget for its functioning.

This has created a situation in which political negotiations are conducted on the bilateral track often through contacts with local ambassadors. It appears also that diplomatic mandates and missions in Gulf countries are held by the same individuals for long periods of time translating into external relations being mostly constructed on the basis of regularity of personal contacts. This is opposed to the EU's practice of leading negotiations on the political track with the Council and the rotation of EU officials. The GCC informal conventions are quite opposite to this trend: the Saudi Deputy Finance Minister always leads negotiations with the European Commission probably reflecting the high interests his country has in petrochemical industries (Echagüe, 2007).

option towards its neighbors. Even Kuwait had a similar position on political grounds by accepting Iraqi participation in the October 2000 Arab summit.

¹⁸ By "security architecture" we mean a balance of power between Iraq, Iran, and the US as guarantor of Gulf states' security. The first change stems from the US invasion of Iraq and the subsequent destabilization, resulting today in civil war conditions. The second change relies in the unclear foreign policy agenda of Iran and fears about its mastering of military nuclear technology. The third major change is Yemen's security deterioration. These three factors are putting a question mark on US' traditional security leadership in the region, altering the previous "balance of power" and triggering a regional arms race in which Saudi Arabia takes the lead as shown by the recent arms deal concluded with the US.

Besides the GCC Secretariat characteristics, the nature of sociopolitical relations in the countries also creates a hurdle in the quest for a deepened partnership. In addition to the lack of institutional capacities at the regional level, at the country level the high degree of patronage and family connections, make it difficult to enter into a more formal framework of relations. This setting results into *“foreign policy revolving around hierarchically structured concentric circles radiating out of the head of state and members of the royal family through the senior members of the political elite towards the bureaucracy with only limited access by business and commercial interests”*. As such, despite of reforms being initiated in the political systems in some Gulf States like Kuwait or Qatar, external relations still contain a high dose of personal contacts (Baabood and Edwards, 2007). In addition to the characteristics inherent to the decision making process, countries in the region lack the human resources necessary for the functioning of an efficient administration (Bauer, Hanelt, Koch, 2010).

Countries in the GCC also fail to behave as a unified block. If we take the example of trade negotiations, opportunistic behaviours have seriously undermined the credibility and commitment of the Secretariat. During several years the EU has postponed the negotiation of the FTA until the GCC implemented effectively a customs union. In 2004, after the US had launched the Broader Middle East and North Africa (BMENA) initiative and the GCC effectively agreed to put in place the long awaited customs union, Bahrain signed with the US a free trade area unilaterally, without consulting the other members of the Council. This has created a *“cacophony of competing and contrasting initiatives bound to generate confusion and stimulate opportunistic behaviour on the part of individual governments in search of petty immediate benefits”* (Luciani and Neugart, 2005). Moreover, the Bahraini and Omani positions were criticized within the GCC itself. As a consequence of the Bahrain-US deal, all countries in the region had to confer the US the MFN tariff, and when the EU decided to re-launch negotiations it asked to be granted exactly the same conditions as the US.

3 POLICY RECOMMENDATIONS

The Gulf region has been rather neglected by European policy makers despite its strategic importance not only in terms of oil supply but also as regards regional stability. GCC countries maintain relations with both the EU and its member states for a variety of interests. At the bilateral level, relations are shaped by security needs. At the multilateral level, economic interests are put forward, despite an apparent inability to conclude the FTA. Given the region’s strategic importance, the FTA should be seen by the EU as a means to anchor geopolitical stability rather than a vehicle for enhancing welfare through trade. Given both regions composition of trade and productive systems, GCC countries are the ones who would mostly benefit from the FTA.

The failure of the FTA to materialize is due to the inability for the GCC countries to act unanimously. Although it would aid all countries, the FTA’s impacts are likely to be different for each country. Given the size of its exports of petrochemical products, Saudi Arabia will most benefit from a free trade agreement with the EU. Meanwhile, the United Arab Emirates export ten times less petrochemicals than their Saudi counterparts to the EU. The recent announcement made by the United Arab Emirates to opt out from the common currency is just another example that raises serious doubts on GCC’s credibility as a compact body.

In this regard, given the institutional weaknesses of the GCC Secretariat and the previous episodes of regional divisions, the EU should change its approach towards the region. The FTA is being negotiated for now 20 years, without being concluded, and the USA have tempted smaller countries with trade deals. In order to secure strategic presence in the region, the EU should adopt a hybrid approach, consisting in maintaining some relations on a multilateral basis while at the same time starting a more substantive approach to the individual countries. With such a hybrid approach, the EU could guarantee its strategic presence in the region while reinforcing competition among the GCC states. EU’s strategic presence in the region lies on securing interests on soft security and economic grounds. On the soft security layer through the multilateral framework of EU-GCC relations the EU can address the regional challenges stemming from the Iraqi turmoil and Yemen’s security deterioration: political radicalization, terrorism, trafficking and piracy to name a few. Bilateral relations would reinforce

multilateral efforts by addressing country specific issues and paving the way for increased political dialogue with GCC states. Moreover, such approach would not only make the EU more present in the region, but would also support the existent initiatives administered by DG DEV targeting Iraq and Yemen. On economic grounds, multilateral relations should push for the conclusion of the FTA while bilateral contacts would secure EU's commercial interests. Such hybrid approach must be seen as a strategy to anchor the EU in the region, make it more visible while insuring continued relations in the event of GCC's Secretariat failure.

To ensure EU's presence in the region, concrete steps should be taken in supporting the regional integration efforts within the GCC. Taking stock of the radical social, cultural and economic differences between the two regions, the EU should devote more resources to the GCC, especially within the European Commission. The instrument for cooperation with industrialised and other high income countries and territories (ICIHI) should be made not only more visible but should also target more GCC countries, especially in the field of training programs which could be used for the training of local administrations. Another good example of use of the ICIHI in the region is the training of local media as this would give the EU the visibility it lacks in the region. In addition, technical assistance in matters related to the regional integration process of the GCC countries should be reinforced within the framework of the cooperation agreement. Last but not least, within such an approach the creation of relations between the EU and each GCC state entails the opening of more European Union's delegations. Until today, there is a single representation operational in Riyadh and it opened only in 2004. To support EU's increased presence in the region through both multilateral and bilateral relations a high level of visibility is essential. Opening of EU's delegations must go hand in hand with a strong communication strategy targeting the region. This strategy should be devised to serve the objectives of raising awareness about EU's achievements in regional integration, presence in the world and EU's programs particularly the ones aimed at increasing people to people contacts. To be efficient such approach must be designed to take into account the socio cultural differences between the two regions and should not be a transposition of similar initiatives targeting other parts of the world.

The EU should also ensure that the integration in the region should not take the form of exporting social and cultural fabric to neighbouring countries. While at the very first sight it could be argued that integration of the Gulf countries in the Euro-Mediterranean relations would be beneficial, the striking differences in the economic structures, the social fabric of both regions make this option unsuitable. Moreover, given the already high presence of the GCC capital in the Mediterranean, the risk of seeing these countries exporting their social fabric in Europe's neighbourhood may undermine the EU's own initiatives.

Policymakers should be aware of the importance of the Gulf beyond its energy supply role and its SWFs. These countries are pivotal in the overall framework of relations between the Arab world and the Middle East. Taking the example of the Mashreq region, the Israeli Palestinian conflict, the Iraqi turmoil and the threat of terrorism, such as in Yemen, might generate negative spillovers to neighbouring countries. Other issues, such as increased intraregional migration flows and political radicalisation are also likely to pose serious challenges to EU's Neighbourhood Policy. Aside from their geographic position, the GCC countries are important because of their strategic role in energy supplies and political and cultural influence in the region. In this regard, a clear position towards the Gulf is necessary. Durable engagement and high level of visibility might act as a leveraging factor in the region fostering EU's international role and position in Middle East politics. By doing so, the EU could also gain importance in the Arab and Muslim world. A closer engagement with the Gulf may very well be an important supportive factor to gain a more important stake in Middle East politics and foreign policy. Most notably, greater involvement of the EU in the Gulf region would substantiate its efforts in the resolution of the Palestinian Israeli conflict. This is especially the case as current tracks envisaged for the creation of a Palestinian State are based on the Arab Peace Initiative brought by Saudi Arabia in 2002.

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