



Excursion: The Prospects for a Common Currency in the Gulf Cooperation Council

During their December 2001 summit in Muscat, Oman, the GCC heads of state agreed on the introduction of a common currency by 2010. Following the example of the Euro, the decision also comprised a stability pact that limits budget deficits, inflation rates and public debt in the respective countries. To profit from European experiences, the European Central Bank (ECB) was asked to advise in the process.

The introduction of a common GCC- currency is anticipated to be easier than that of the Euro, as GCC economies already show substantial structural and financial similarities, such as oil and gas being their main export products (i.e. in Kuwait 93% of total exports) and the peg of most GCC currencies to the US-Dollar. Exchange rates and, therefore, transaction costs would be cancelled within a single currency system, leading to growth in intra-regional trade. This is of significant importance as trade among the GCC-countries makes up only about 1% of their total trade.

Moreover, the introduction of a common currency is a political indicator that supports the growing economic power of GCC states and that could strengthen region-specific financial sectors, such as Islamic Banking. Compared to their total share of economic power in the Muslim world, the GCC countries' importance in this sector remains relatively low. A new currency could bind investment in Shariah-compliant funds to the Gulf region.

Still, despite expected advantages, problems are ahead. GCC inflation rates, especially in the past two years, considerably exceeded those designed by the stability pact. This is due to the growth-oriented economic policy of most GCC member states. There is a trade-off between compliance to stability rules and two-digit economic growth.

In addition, the stability criteria, as opposed to the example of Europe, are not binding. The decision of joining the new currency does not rely on compliance to the criteria; it has already been taken politically.

As most of the GCC currencies are currently pegged to the US-Dollar, some analyst claim that there already is a de-facto common currency, because exchange rate fluctuations between GCC currencies remain naturally low. This also includes the Kuwaiti Dinar, which was recently released from its exclusive peg to the Dollar in favour of a basket of currencies, which will, nevertheless, be dominated by up to 70% by the US-Dollar.





After Oman's withdrawal from the time table, an introduction of a common currency by 2010 seems unrealistic. "We will defer the introduction of a single currency until we have a common market we are satisfied with", Sultan Bin Nasser Al Suwaidi, the UAE's central bank governor pointed out.

With the delayed introduction of a single currency, the GC might face the problem of diminishing similarities between its respective member states. Some countries such as Oman, Bahrain and, for the UAE, Dubai might not be exporting commodities at that time, leading to growing structural economic disparities in the GCC.

By Clemens Recker

