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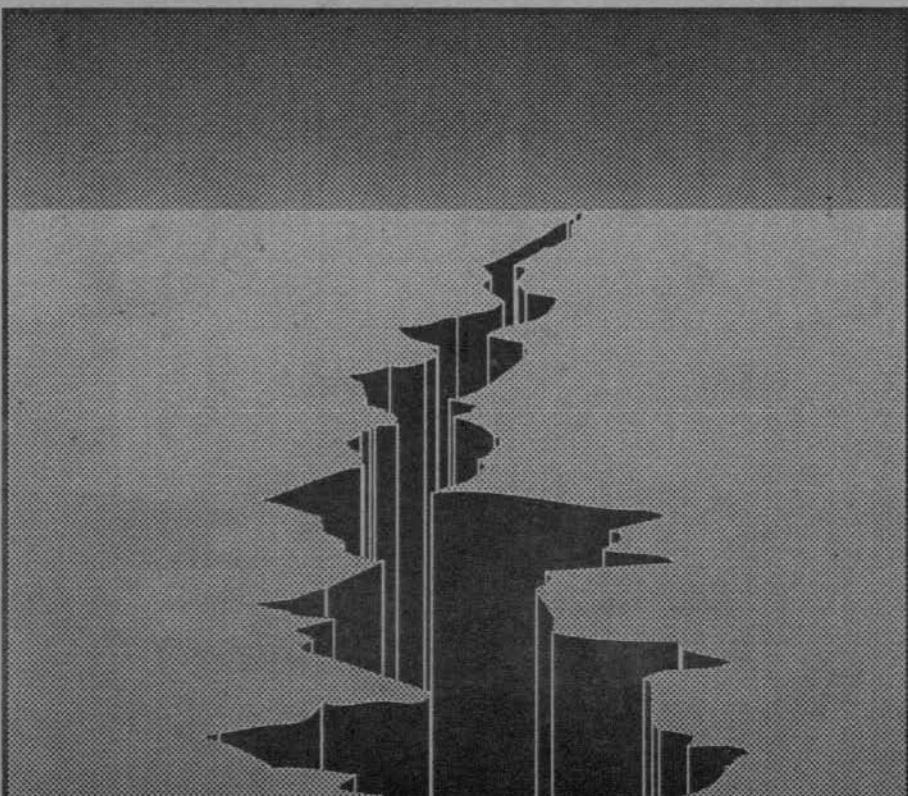

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THE GULF CRISIS
AND THE WORLD ECONOMY

by

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Introduction

Let me begin this second anniversary lecture of the Nigerian-French Insurance Company, under the auspices of the Nigeria-French Chamber of Commerce and Industry, by expressing my sincere appeciation to the Chairman of the Company, Chief (Dr) C. O. Ogunbanjo, OFR and to the members of the Board of Directors for their invitation. I gather that this annual lecture series was launched last year by Monsieur Antoine Merieux, Financial Adviser on West-African Sub-Region to the Government of the Republic of France. He spoke appropriately on the Debt Problems in Africa

I say appropriately because, as you are all no doubt aware, I have for some time now been arguing that unless and until Africa's three economic and financial albatrosses - the excruciating debt burden, the collapse of the commodity markets and prices and reverse flows of resources - are removed from its neck, the continent's socio-economic crisis will persist and the standard of living of its people will continue to fall. These three factors have contributed in a very large measure to the woeful economic performance of the economies of the majority of our countries. They are the principal exogenous factors which must be addressed if African economies are to resume the process of recovery and development and if the decade of the 1990s is not, like that of the 1980s, to become a lost decade.

However, let me hasten to add that there are equally important endogenous factors that have to be also urgently addressed as they are no less inhibitive of the development process. They contribute as much, if not more, to the persistence and pervasiveness of the socio-economic crisis as the exogenous factors. These are poor economic management, the lack of public accountability, the inadequate economic and political empowerment of the people, the absence of social and economic justice, the marginalization of the people in the political and development process resulting in a pervasive lack of democracy and corruption. Unless these externally-generated problems are addressed most urgently, resolving the internally-generated factors will not by itself lead to recovery and a sustainable process of development and transformation. Conversely, any attempt to address the endogenous factors which is not complemented by imaginative and bold efforts to address the debt, commodity and resource flow problems will be an exercise in futility at least in the short- and

medium-term. There is therefore, a need for simultaneous action at both the domestic and external fronts.

As the saying goes, it never rains but pours. Africa, in addition to all its problems, has now to cope with the socio-economic consequences of the Gulf Crisis which has culminated in the Gulf War currently raging with all its ferocity and destructive consequences. Both the crisis and the war have had and are having a particularly disruptive impact on the ailing and fragile African economies. But, above all, the impact of the crisis is global. There is no corner of the earth that has not been affected and will not be affected for months and years to come. The fallout is likely to linger around for quite a while after all hostilities would have ended.

The Gulf Crisis and the Gulf War are unfortunate for our world and its economy for four principal reasons. Benjamin Franklin once said that there never was a good war - a sentiment recently echoed by Pope John Paul when he said that "war cannot be an instrument for solving problems." The result of all wars are men and women and children and the aged killed, maimed or made insane by horror; property destroyed; and, the environment degraded with the inevitable acceleration of the desertification process. While we can all agree that there is no good war, many among us would argue that sometimes a bad peace can be worse than war itself. Nevertheless, it is unfortunate and indeed very sad and tragic that even during this last decade of a century that has been saturated with war, we are not spared of it.

This Gulf War is unfortunate for another and second reason. Until the annexation of Kuwait by Iraq on August 2, 1990, the world was floating in the belief that all threats of war have finally disappeared and that we were entering an era of peace and indeed that there would be substantial peace dividends arising from savings made from disarmament and the closure and the redirection of the armaments industries which can be invested to make our world more humane and more just by helping the growing population of the impoverished in the industrialized rich countries and the poor countries of the world, among which African countries are the poorest. Euphoria was in the air as it was assumed by one and all that the unification of the two Germanies, the growing cooperation between Eastern and Western Europe and the growing talk of a common European house had finally brought World War II to an end and has heralded the dawn of a new era. But how short-lived has our optimism

turned out to be! How sobering that soon after the ending of the cold war, fighting men are back on the battlefield. War, instead of becoming a shameful anachronism, is once again a bitter reality.

In retrospect, our optimism has, as usual, arisen from our Euro-centrism. In the world in which we live today, events in Europe and North America are overwhelmingly dominant. They are more often than not globalized and universalized. Others are regarded as secondary or irrelevant or both. This is the only rational explanation we can provide for the euphoria of universal peace followed so closely and so shortly by the agonies of a new war. When the remarkable development in Eastern Europe including the pulling down of the Berlin wall in the late 1988 and early 1989 took place, it was hailed as an amazing turnabout not for Europe alone but for the world as a whole. It was agreed by one and all that a new era had indeed dawned. We had forgotten the other problematic parts of the world whose problems arose from the consequences of World War II just as the division of Europe into East and West and the division of Germany were the consequences of that war.

The situation in the Middle East was soon treated as secondary. Yet no one can deny today that in addition to the immediate cause of the Gulf War (the annexation of Kuwait), **Operation Desert Storm** is a consequence of problems descending from World War II and, some may argue, from the collapse of the Ottoman Empire. War is a political event - it is an eruption of violence in a continuum of politics. As the Gulf conflict unfolds, we are compelled to learn to live with the knowledge that the future of the Middle East and the lives of its peoples are being determined by the actions of the Iraqi and the Coalition forces led by the United States. Just as World War II dominated the entire youthful experience of a generation, the Gulf War may have a decisive impact on a new generation not just of the people of the Middle East but of our world as a whole.

The fourth reason why the Gulf Crisis is unfortunate is that it is taking place at a time when there is economic recession in the making. With the world already drifting towards recession, the economic disruption caused by the war is bad for everybody. It had been hoped by the OECD in its mid-1990 Economic Outlook that the world economy could avoid a recession in 1991 largely as a result of continued robust growth in Japan and Germany. But Europe's economy caught cold in August when oil

prices jumped after Iraq had invaded Kuwait. European economists have now come to the view that unless the war would end soon, Europe's economic slow-down might deepen rather than be reversed. Should the war last longer, many economists say that even Germany's robust economic growth might not save Europe from recession.

In the United States, business activity has been falling in most parts of the country in the weeks leading up to the Gulf War. The decline in interest rates has done so little to halt the slow-down. According to a survey by the US Federal Reserve published on 23 January 1991, "despite continued export growth and manufacturing orders, employment and shipments have weakened and construction is still slowing in most places."[1] Recession in Europe coupled with recession in North America will, as sure as night follows day, lead to a global turndown in the world economy.

The genesis of the crisis and the international response

Though war is still raging with all its savagery and destructive power, though we have moved from **Operation Desert Shield** to **Operation Desert Storm** and though the end is not yet in sight, we must begin to analyze its socio-economic impact on the world in general and on Africa in particular. First, we will need to review the impact on the international economy, including the African economy, during the crisis period i.e. between August 2, 1990 and January 15, 1991. In other words, from the invasion and annexation of Kuwait by Iraq to the outbreak of the war at the end of the January 15 1991 deadline imposed by the Security Council of the United Nations for the withdrawal of Iraq from Kuwait. Second, we will undertake an analysis of the evolving economic and financial impact of the war as it rages on. Finally, we will look at likely developments in the international economy in the post-Gulf War period. In undertaking all these analyses, we must perforce take full cognisance of the political impact which will inevitably affect and decisively influence the course of development in the world economy. But as a background to all these, we must commence our analysis by providing a short review of the genesis of the crisis, the world response thereto and

[1]New York Times, January 24, 1991, pp D1 and 16.

the underlying causes of the failure of diplomacy and dialogue which led inevitably to war.

In doing all these, we must, of course, realize that we are dealing with a complex and evolving situation full of uncertainties, risks and dangers. The end result of the forces that have been unleashed are unpredictable. Only a prophet can fortell the end and fortunately or unfortunately we do not have the gift of prophesy. The only thing that is predictable is that as a result of this Gulf War, nothing will ever be the same again.

Let me start with the genesis of the crisis and the international response thereto. I did suggest earlier that we need to put it into proper historical context if we are to develop appropriate and realistic solutions to its remote causes. The annexation of Kuwait by Iraq is only the latest unfortunate manifestation of a much more fundamental and deep-rooted problem that has its roots in the collapse of the Ottoman Empire. It is also a legacy of the Second World War. We must understand this history if we are to search for an enduring solution to the crisis without which political and economic instability that has become the order of the day in the Middle East will persist and intensify.

The struggle which Britain had with France and Germany for political and economic hegemony over India made her determined, in the nineteenth century, to control the route to India. The British thus ensured that every possible Arabian staging post to India was safely in the hands of a friendly local ruler - guided naturally by a minder from the imperial government in Whitehall. This policy led to de facto if not de jure British protection in Aden, Oman, Kuwait and several other tiny Gulf States. And when the German Kaiser in the early years of the twentieth century planned a German railway to India, the British thwarted the attempt by using the 1919 dismemberment of the Ottoman empire to set up a friendly local ruler as king of a new country, Iraq. The Hashemite monarchy which was installed in 1921 was overthrown in 1958.

In response to unceasing agitation, British rule had been terminated in Iraq in 1932 when the country became the first Arab state to enter the League of Nations. In 1961, Kuwait cut its formal link with Britain by declaring its independence. However, six days after independence, Iraqi troops were reported moving in to occupy it. This first attempt by Iraq to

annex Kuwait was aborted by the British. The British troops which had been sent to ward off the invasion were later withdrawn from Kuwait when Arab nations undertook to guarantee the independence of the country. Fortunately, Iraq accepted it as a member of the Arab League in 1963.

Until the invasion of Kuwait in August 1990, Arab countries had at least abided by the vital rule of accepting each other's independent existence and by so doing had accepted "the patchwork of states sewn together from the cut cloth of the Ottoman empire"[2] Unfortunately, annexing Kuwait broke that rule. Although relations between regimes in the Middle East have always been tense and borders have always been brittle, the annexation of one state by another not only enhances the dangers of disintegration but also is not in conformity with the Charter of the United Nations which, among other things, guarantees the political independence of all its member states.

Because of the opposition to the annexation of any member state by another, the reactions of the international community were swift, strong and firm. The starting point to the annexation was when on July 18, 1990 Iraq accused Kuwait of stealing its oil. One week later it moved its troops to the frontier of Kuwait and on August 2 it carried out the invasion.

The UN Security Council's response was immediate. On the very day of the invasion, the Security Council passed a condemnatory resolution (Resolution 660) which also called for immediate, unconditional withdrawal and the intensive negotiations for resolution of differences between the two countries. On August 6, the Council passed its second resolution (No. 661) which, because of lack of compliance with the earlier one, imposed wide-ranging sanctions. Rather than complying with either or both of these resolutions, Iraq defiantly annexed Kuwait on August 8, thus aggravating the crisis. In response, the Security Council further adopted Resolution 662 which declared that Iraq's annexation of Kuwait had no legal validity and called for international recognition of that fact. On August 10, Arab Heads of State voted 12-8 to condemn the invasion.

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[2] The Economist, 19-25 January 1991, Vol. 318, No. 7690; p. 14.

Meanwhile, American troops had begun to arrive in Saudi Arabia. Their task, according to President George Bush, was to defend that country although later it was expanded to driving Iraq out of Kuwait. The Arab Summit also decided to send a Pan-Arab force to defend Saudi Arabia. As the days passed by, the crisis escalated. By the end of the year, 12 Security Council resolutions had been adopted - all culminating in Resolution 678 of 29 November which set January 15, 1991 as the deadline for Iraq's withdrawal from Kuwait. The adoption of that resolution moved the world inexorably close to war. Unless dialogue and diplomacy prevailed and triumphed during the forty-seven days before the deadline, war became an inevitability.

From crisis to war

In December 1989 and January 1990, the world was filled with euphoria; the Soviet Union and Eastern Europe were going through fundamental changes; the Cold War had yielded place to growing cooperation between the West and the East; arms reduction by the two major powers was progressing slowly but surely. It looked as if a new world political order, in which war would become an anachronism, was in the making. Exactly a year later (December 1990 and January 1991) not only was there no talk about anything else but war but by 17 January the world was actually at war.

Peace - total peace - has once again become a twilight. It has once again eluded the millions of people throughout the world who have been yearning for long for true peace and for a new world political order. Between August 2, 1990 and January 17, 1991 the world moved inexorably to war. Diplomacy failed completely to resolve the crisis as it had done in 1939. Instead of dialogue there were accusations and counter accusations. Instead of conciliation there was brinkmanship. The result is that war rather than negotiations and diplomacy became the only alternative with sanctions putting in the required pressure.

It is always the case that when governments and their leaders stand on high principles compromise becomes impossible. One of such principles which was supported strongly by the Security Council is that aggressors cannot be rewarded, that international law is sacred and that as we enter a potential new world order, the United Nations should, in the absence of the usual East/West intransigence and Third World anti-Western rhetoric,

not miss the historic opportunity of acting in the way it is supposed to act by countering aggression. As US Secretary of State, James Baker, puts it, "we are living in one of those rare, transforming moments of history, an era full of promise". In such a circumstance, aggression must not be allowed to go unpunished.

It is therefore clear from these high principles that sanctions were seen as a soft, slow and ineffectual alternative - as it were, a kind of non-alternative alternative. But the question must be asked - as it will certainly be asked again and again when the history of the Gulf Crisis is written - would sanctions have worked? Could they have saved us from the cataclysm of the Gulf War?

We will never be able to answer this question definitively - at least not for now, but an article by Gary G. Hufbauer and Kimberly A. Elliot in the New York Times of 14 January 1991 provides a pointer as well as some tentative and indicative answers. They assert as follows in the opening paragraph of the article:

> *"Proponents of a military solution to the Kuwaiti crisis have asserted repeatedly that there is no proof that sanctions will work. Only war, they say, guarantees that Iraq will get out of Kuwait, and soon. But there is abundant proof that sanctions can work - a recent report by the Central Intelligence Agency notwithstanding - and there is considerable evidence they can do so within the next 12 months."*[3]

The authors who are experts on economic sanctions and have together with Jeffrey J. Schott co-authored a book entitled Economic Sanctions Reconsidered, tested their conclusion on the effectiveness of the sanctions imposed against Iraq by constructing a computer model that analyses the factors that contribute to successful sanctions. These are, **inter alia,** lost trade and economic output. The model was then asked to predict the likelihood that sanctions would succeed. In the words of the authors,

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[3]Gary C. Hufbauer & Kimberly A. Elliot, "Sanctions Will Bite - and Soon", New York Times, 14 January 1991.

"Since the estimated cost to Iraq - 48 per cent of the gross national product - is so far beyond that observed in other cases, the initial results placed the probability of success at nearly 100 per cent. Even when the model is adjusted to account for Mr Hussein's exceptionally tyrannical control, and the estimated cost is say, halved to 24 per cent of GNP, the probability of success remains above 85 per cent. ...The evidence suggests that sanctions will begin to bite sometime in the spring or early summer, with a high probability of forcing Iraq from Kuwait as early as the fall."[4]

As Hufbauer and Elliot rightly concluded, while war may resolve a crisis more quickly than sanctions, it does have unpredictable side effects. Therefore, the imponderables of sanctions and the costs of waiting must be weighed against the imponderables of war including the loss of lives and property.

There were also high political and moral principles which from Saddam Hussein's point of view made war inevitable. The explicit aim of the Baathist (the ruling party) ideology on which the Iraqi regime is founded is to sweep away "artificial" borders and unite the Middle East. By so doing, Saddam Hussein has revived the dynamic of secular Arab nationalism, which has at its core the goals of Arab political unity.

One of the distinctive features of the Middle East - Arab and non-Arab - is the degree to which frontiers are regarded as irrelevant. Arab nationalists say that the frontiers of the region are artificial creations and therefore temporary. To a large extent this is true. Neither the frontiers of Kuwait nor for that matter those of Iraq are natural. They were both created by administrative decisions taken by colonial authorities - the British. However, this is not unique or peculiar to the Middle East. Most of the frontiers in Europe and Africa are equally arbitrary and equally recent. What is uniquely Middle East is not that the frontiers are arbitrary, but rather, whether or not the delimitation of states should be respected at all.

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[4]Ibid.

As one writer put it recently, *"what is distinctive about the Middle East is the refusal of states to accept this delimitation. Interference in the internal affairs of other states is more pervasive in the region than anywhere else. Indeed, it follows from the logic of Arab nationalism that frontiers merely divide a political community that should be united."*[6] But this having been said, two points need to be made. The argument that the annexation of Kuwait is the overcoming of the colonial legacy of division cannot hold since most of Kuwait was never part of the Vilayat of Basra - the forerunner of Iraq. Secondly, if Kuwait is an artificial political entity, created by colonialism, so too is Iraq.

There are two other issues of high principles that Iraq has put forward: redistribution of oil wealth and liberation of Palestine. Saddam Hussein's call for equal distribution of oil revenues is partly an apparent attempt to resolve the fact that most Arab oil is found in countries with small populations and partly due to the virtual collapse of the Iraqi economy as a result of the war against Iran. Indeed, at the Arab League Summit which took place in Baghdad on May 28, 1990, he accused some unnamed countries of keeping the price of oil too low through over production and of making "economic war" against Iraq. Two months later, Iraqi Foreign Minister, Tariq Aziz claimed that Kuwait has stolen Iraq oil worth $2.4 billion. Iraq also "wrote off" about $10.00 billion worth of loans made to it by Kuwait during the Iran/Iraq war.

On August 12, Saddam Hussein subsequently expanded the scope of his high principles by linking the demand for his withdrawal from Kuwait under Security Council Resolution 660 with the demand for the withdrawal of Israel from Arab territories. As is well known, Israel's occupation of the West Bank and Gaza has continued for twenty-three years against the wishes of their inhabitants and the overwhelming majority of the member states of the United Nations. Linkage therefore sounded a matter of high principles. But the international community while still adhering to its condemnation of the occupation of the occupied territories by Israel did not think that linkage was called for within the

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[5]The Crisis of the Arab World; The False Answers of Saddam Hussein.

context of the annexation of Kuwait by Iraq. Rather it would appear that it felt that linkage was the surest way to make both problems insoluble.[6]

Thus Iraq's four issues of high principles are: (i) unification; (ii) redistribution of oil wealth; (iii) liberation of Palestine; and, (iv) resistance to imperialism. On the part of the UN Security Council and the allied powers led by the US, the issues of high principles are (i) the rule of law; (ii) countering aggression; (iii) strengthening the effectiveness of the United Nations to be the peace-keeper of the world; and, (iv) oil.

The oil as an issue has generally been more implicit than explicit. Western leaders have refrained directly from putting it on the table. But there is no doubt in anybody's mind that it is very much an issue. As Robert Samuelson puts it in an article in **NewsWeek** of January 21, 1991, *"we have not sent nearly 400,000 Americans to the Persian Gulf to defend crude at $18 a barrel. They are there to keep Saddam Hussein from controlling two-thirds of global oil reserves and from using that control to blackmail the industrial world... What we are doing is maintaining access to the oil on which the world depends."*[7]

The **Economist** even puts it more directly in one of its lead articles on January 12, 1991 when it says:

> *"Ever since Iraq invaded Kuwait, good-natured people have felt queasy about fighting merely for the sake of oil. They should reconsider that "merely".*
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> *"Oil is not just any commodity, it is the fuel on which almost every country's hopes for growth and prosperity rest and will continue to rest until they embrace nuclear power or some technology not yet invented. The war is not being fought for the oil companies or to keep oil "cheap" - no war came after the oil shocks of 1973 and 1979 - but to keep the hands of a*

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[6]The Economist, Vol. 318, No. 7689, January 12, 1991; p. 12.

[7]Robert J. Samuelson, "The Grounds for War" NewsWeek, January 21, 1991, p.43.

ruthless blackmailer off the windpipe of the world economy. With Kuwait, Mr Hussein already controls 19 per cent of the world's oil; with Saudi Arabia he would have 44 per cent. Mr Hussein says openly that he needed to control Kuwait in order to control the price of oil, in order to pay for his war machine, in order to ... This is an impossible position for the world to accept, and no shame attaches to acknowledging the vital self-interest at stake. It would be shameful to conceal it"[8]

The immediate impact of the crisis on the international economy

It is clear from our review and analysis so far that the Gulf Crisis is at once local, regional and global. Right from the start, it captured the attention of the world as no other crisis has done and since war broke out on 17 January, everyone has been involved in it. In no other war has the entire humanity been so involved since World War II ended.

Not surprisingly therefore, the crisis has affected the world economy with a bang right from the first day. The impact during the first five-and-a-half months has been particularly significant on (i) the oil market; (ii) world trade; (iii) commodity prices; and, (iv) the global macro-economic outlook for 1991 and beyond. Let us look at these albeit briefly seriatim.

(i) Changes in the oil market: Before August 1990, oil prices were fluctuating markedly. At the start of the year it was \$18.70 but by 6 July it had fallen to \$13.40. By the time of the invasion, the price was close to US\$20.00 as a result of an earlier agreement by OPEC to increase the target price from \$18 to \$21 a barrel. The effect of the invasion of Kuwait and the implementation of the sanctions under Security Council Resolution 661 was a 50 per cent increase in prices from \$20 to \$30 per barrel of crude by mid-September and a doubling of prices to \$40 by early October. Thus as a result of these price escalations, the price of oil averaged \$24.30 a barrel in 1990, that is, a third more than the average price in 1989. To make up for the deficits in supplies from Kuwait and

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[8]**The Economist**, "Don't save this face", Vol. 318, No. 7689, January 12, 1991, p. 12.

Iraq, many OPEC and non-OPEC oil producing countries increased their production of crude oil. While oil exporters gained, oil importers lost. It was a zero sum game in which a price change of only $1 per barrel maintained over the course of one year implies a reallocation of resources between exporters and importers of around $9 billion per year.

(ii) <u>World Trade</u>: Before the emergence of the Gulf Crisis, world trade was expected to grow by about 6.5 per cent in 1990 as against the 7.0 per cent rate achieved in 1989. However, due to the crisis, the growth rate in world trade in 1990 is now estimated at 5.6 per cent as import demand in both the industrial and low- and middle-income countries slackened in response to weaker economic activity due largely to the prevailing uncertainty about the outcome of the crisis and whether it would lead to war. Given the debt constraint of some of the oil exporters (Indonesia, Nigeria and Venezuela), the stimulus provided by the extra earnings was insufficient to offset the deceleration in world trade.

(iii) <u>Commodity Prices</u>: Increases in oil prices have two types of impact on the prices of other commodities. First, there is the direct effect - or what economists call the price effect - which operates through an increase in the cost of inputs and is price-increasing in nature. Second, there is the indirect effect or the income effect - which is price depressing in nature. The latter i.e. the price-depressing income effect - appeared to have been dominant in the latter part of 1990 in the commodity market. Thus, the World Bank index of 33 non-oil commodities is estimated to have declined by about 6.5 per cent in nominal terms or by about 12 per cent in real terms last year.

(iv) <u>Global Macro-Economic Outlook for 1991 and Beyond:</u> The Gulf Crisis accentuated the economic gloom that was becoming increasingly discernible during the first half of 1990. As already indicated, a downswing in the economies of North America and Europe had been widely expected in 1990. The advent of the Gulf Crisis aggravated whatever gathering signs and indications there were of a coming recession in these economies. There is now no doubt that these economies (and because of their dominance, the entire international economy) are now in recession even in spite of the war.

But the impact of the Gulf Crisis before the war has varied from region to region as it has from country to country. It is particularly

intense in its severity as far as the frontline countries of Turkey, Jordan, Syria, Lebanon and Egypt are concerned.

In the Asia and Pacific region, apart from the impact arising from the rise in the price of oil, the immediate effects of the crisis have been (i) large-scale repatriation of Asian workers; (ii) the concomitant decline in workers' remittances; (iii) the decline in exports and imports; and, (iv) the decline in official development assistance and foreign direct investment flows from Iraq and Kuwait and possibly other Gulf states.

According to an ESCAP study,[9] there were 3.260 million Asian migrant workers in the Middle East in 1988. Pakistan, India and the Philippines topped the list with 850,000, 800,000 and 730,000 respectively. They were followed by Bangladesh (250,000), Thailand (230,000), Sri Lanka (180,000) and Indonesia (150,000). There were 70,000 migrant workers from the Republic of Korea. 538,000 of this migrant population in the Middle East (nearly 17.0 per cent of the total) were in Iraq and Kuwait by July 1990. Remittances to these countries from their nationals working in the Middle East averaged $8.5 billion annually. While no separate comprehensive data are available with regard to the exact volume of remittances emanating from Kuwait and Iraq, they have been estimated to be an average of between $1.7 and $2.0 billion annually. Definitely, all of this would have been lost to these Asian countries with the repatriation of the migrant workers and remittances coming from other Middle East countries would also have been considerably reduced if they have not completely evaporated.

India, the Philippines and Japan depend on Iraq and Kuwait for 20, 12 and 10 per cent respectively of their petroleum imports. With regard to exports, the largest exporters from Asia to the Gulf area are the Republic of Korea ($2.5 billion) and China ($2.1 billion) annually. In terms of the proportion of total exports in 1988, Sri Lanka ranks highest (17.9 per cent), followed by India (13.8 per cent) and Pakistan (11.1 per cent). Although Bangladesh's exports to the Middle East were less than 5.8 per cent, about a third (31.73 per) of such exports were destined to

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[9]Economic and Social Commission for Asia and the Pacific (ESCAP) - Economic Impact of the Gulf Crisis on the Developing ESCAP Region: A Preliminary Analysis

Iraq and Kuwait. The exports of India and Sri Lanka to the Middle East were also highly concentrated in Iraq and Kuwait, accounting for 20.5 and 21.8 per cent respectively. Thus, a significant proportion of the exports of South Asian countries are highly vulnerable to the events in the Gulf.[10]

Among the frontline countries, Sudan relies on Iraq and Kuwait for 68 per cent of petroleum imports and Turkey 62 per cent. 11.7 per cent of Turkey's total export value during 1987 was with both countries. Jordan, Lebanon, Syria and Yemen together have 6.4 per cent of their export trade with them also.

As far as Africa is concerned, I have already indicated in my Preliminary Assessment of the Performance of the African Economy in 1990 and Prospects for 1991 that "the deep changes in the world economic situation by the Gulf Crisis have had the effects of constraining the level of demand for Africa's exports and raising the price of its non-oil imports... thus redounding adversely on productive capacity and export earnings".[11] But the impact while generally unfavourable, particularly as far as African oil-importing countries are concerned, has had some positive effect for the oil-exporting countries.

African oil-exporters produced some 267 million tons of oil in 1989, of which nearly 200 million tons were exported. At spot prices, these exports were roughly valued at $26.5 billion. In 1990, on the basis of first semester results and of the quotas set by OPEC, production could reach 283 million tons, and exports 208 million tons. Given an estimated average price of US$24.40 a barrel, revenues could increase to US$37.1 billion for the year or 40 per cent more than in 1989. In relation to 1989 GDP, this represents nearly a 5 per cent gain.

Such a windfall, largely unforeseen by anyone, not even the African oil exporters themselves, most of whom had predicted their 1990 budget estimates on very low oil prices of around US$15, has created great opportunities. The pressure on the balance of payments, particularly strong in countries such as Nigeria and Algeria, eased considerably in

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[10]Ibid Paragraph 18, p. 8.

[11]Published on 14 January 1991 by the United Nations, p.8.

1990 while payment of debt service became much easier. In place of the cut-backs on imports, the impact of the windfall was such that imports of badly-needed capital goods and intermediate inputs were easily paid for. However, the situation was not uniformly good, even for the African oil exporting countries, and some of them were likely to experience negative rather than positive balance of payments in 1990.

Although oil-importing African countries are marginal consumers of oil, their oil bill is significant enough relative to their total exports and general financial resources. At one to two barrels per head per year, their oil consumption is very low indeed; but oil is vital to their transport and industrial sectors. In 1989, they imported an estimated value of US$7.0 billion of fuels, roughly the equivalent of 1 million barrels per day. Given the price increase in 1990, their total oil bill could amount to US$9.3 billion, i.e. 32 per cent more and an extra cost equivalent to 2 per cent of GDP.

Among the most severely affected are undoubtedly the 29 least developed countries. Without coal and/or gas exploitation and an underdeveloped hydro-electric power generating potential, these countries depend very highly on oil as a primary source of energy which implies that they would have had to pay larger amounts of scarce foreign exchange. An aggravating factor is that the eleven land-locked LDCs in Africa lack refinery facilities and depend almost exclusively on imported refined oil products. As primary-commodity-dependent economies, the African LDCs are expected to suffer a severe loss in export earnings as the crisis leads to a world recession.

African LDCs are also the most aid dependent group among developing countries. If a world recession results from the Gulf crisis, export credits and other related flows of official development finance as well as foreign private direct investment could be severely affected as a result of the adjustment in donors' aid packages and the wait-and-see attitude of foreign private investors.

North African countries have been particularly affected by the Gulf Crisis. Trade and tourism have been severely affected. Egypt has additionally suffered from the lower traffic in the Suez Canal and the loss of export markets in Kuwait and Iraq. As I said in my end-of-year preliminary assessment of the performance of the African economy in

1990, the total losses sustained on all this account is estimated for Egypt to have reached some $3.6 billion compared with $1.5 billion accruing to it as additional oil revenue. To this must also be added the cost of $4.7 billion in the resettling of the 600,000 migrant workers returning to Egypt from both countries.[12]

The evolving economic and financial impact of the war

So much for the immediate impact of the crisis. The ongoing war has added new dimensions in terms of its impact on the global economy as well as in terms of the financial burdens of prosecuting it. Since the war is still raging, its full effect cannot be accurately assessed. We can only review how the situation is evolving. Later we shall undertake a prognostic analysis of its medium- and long-term impact.

As The Economist puts it recently *"only a fool could fail to be alarmed by this gathering of opportunities for catastrophe. Apart from the loss of life and limb, the Gulf war does indeed pose a risk for a global slump... Wars cause inflationary booms when they persistently raise the demand for workers and goods beyond the capacity of economies to supply them. The war in the Gulf is being fought with soldiers and weapons that already exist; on any plausible assessment it will stop long before the armies (on the allied side, at least) start to drain additional resources from their economies."*[13]

As we have indicated repeatedly, even without the Gulf crisis and war this year was not going to be an easy year for the world economy. *"Financial systems especially in America are choking on bad debts; banks have failed and industry is caught in a "credit crunch". The Uruguay round of trade-reform talks has been suspended, and governments seem more willing than ever to embrace protectionism. Political and economic reform in the Soviet Union is disappearing*

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[12]Adebayo Adedeji - A Preliminary Assessment of the Perfor-mance of the African Economy in 1990 and Prospects for 1991; p. 11.

[13]The Economist, "The Economic Pull"; pp.15-16 - Vol. 318 No. 7690, January 1991.

under the backs of advancing tanks. Reform elsewhere in Eastern Europe and in much of Latin America remains vulnerable to shocks from abroad. Now two huge armies are fighting a destructive war in one of the world's economic nerve centres".[14]

The three immediate impact of the war are (i) the huge and rapidly escalating cost of the war; (ii) the depression of oil price; and, (iii) the rapid downward turn of the world economy.

The costs of the war are already huge and are mounting daily. The pre-war military costs to the US are estimated at $10 billion and the war itself is expected to cost some $50 billion. Burden sharing has however relieved the United States of a large proportion of the costs. In the pre-war period, the Gulf States provided between $5 billion and $6 billion with Japan contributing an additional $2 billion. Since the war commenced, it is estimated that the costs have amounted to $36 billion so far. Of these, $13.5 billion have been contributed each by Saudi Arabia and Kuwait, with Japan pledging to contribute $9 billion.[15]

The United Kingdom is the second major partner in the military operations. A sum of $936 million has already been added to UK 1990/91 defence budget and this is expected to rise to about $2 billion. Britain which was slow to pursue the policy of burden sharing by approaching other countries to help with its war effort has so far received or been promised $590 million - $392 million from Saudi Arabia, $50 million from Japan and $40 million from Germany.

The US has also set up a Gulf Crisis Financial Co-ordination Group of 25 countries to monitor the needs of frontline states - Egypt, Turkey and Jordan. About $13.5 billion was committed for both 1990 and 1991 for these countries but mainly for Egypt and Turkey as Saudi Arabia and other Gulf States have shown a lot of reluctance to support Jordan in view of what is considered its pro-Iraq attitude in the crisis.

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[14]Ibid, p. 15.

[15]The figures quoted are from the Financial Times (London) of 29 January 1991 - Who is sharing the Gulf burden; p. 16.

Thus while the US is the leader of the international coalition, it has reduced its direct burden of the financing of the war on the ground that it is acting on behalf of the international community. This is a reverse of what the US has done in past wars when it not only financed its own contribution but also helped the efforts of close allies. But, of course, the US is now financially weaker. It has a chronic budgetary problem. Were it to finance the war entirely from its own resources, it would have severely strained its economy and aggravated its budget deficit. .

Since the war began, the escalation in the price of oil has been reversed. Oil prices have continued to fall since the beginning of the year. Even in spite of the fact that supplies are more than adequate to meet demand, the International Energy Agency (IEA) has decided to release 2.5 million barrels of oil a day from strategic stocks. Quite understandably, members of OPEC believe that they are being poorly rewarded for quaranteeing adequate oil supplies to the West to compensate for the absence of crude from Iraq and Kuwait. They fear that this oil is being stockpiled by industrial nations whose stocks are already at a nine-year high, and will flood back into the market after the war, sending oil prices sharply lower. If the IEA maintains this policy for long and OPEC producing countries continue to pump more oil, an oil glut may be seen in the second quarter of the year and price may fall to as low as $10-$15 a barrel.

With the escalating financial costs of the war and the collapse in oil prices and the likelihood that the war may be more prolonged than was originally anticipated, the current recession will deepen, standards of living will fall in most countries, unemployment will rise and government finances ruined. Indeed, there is a doomsday scenario which holds that one of the consequences of the war may be a very severe global depression.

In such circumstances, one shudders to think of the impact on developing countries generally and Sub-Saharan African countries in particular. The collapse of commodity markets will become more severe, export earnings will dwindle to a fraction of 1990 level and the human costs will become unbearable. It is said that when two elephants are fighting, it is the grass that suffers. Even when they make love, the grass still suffers all the same. African countries, particularly the least developed countries, thus face very difficult days and months ahead particularly as no special assistance programme has been put forward by

the donor community to help the fragile and crisis-ridden African economies.

Post-gulf war world

Let us conclude this lecture by focussing our attention for a few moments on the world we will live in after the Gulf War. Regardless of the outcome, it is going to be a much different world from the one before January 17, 1991. Charles Krauthammer in a very thoughful essay on "How the War Can Change America" which appeared in the Time magazine of January 28, 1991[16] says that *"war is an exercise in surprise and the real surprise of this one may be that it was not about Kuwait, not about Iraq, not even about the future of the Middle East, however much all of these will be shaped by the outcome. It may turn out to have been a war about America... Except for a revolution, nothing changes a country more than war... A new post-gulf America will emerge, its self-image, sense of history, even its political discourse transformed... A post-gulf America might see its economic problems in perspective: not as a metaphor for corruption and decline, not as an indictment of a society's health and vitality, not as a crisis of the soul but simply as an economic problem - a product of mistaken policies and misaligned resources. A post-gulf America might even see itself in perspective as the planet's dominant power, afflicted with problems but able nonetheless, by prodigious acts of will, to turn history. Of course, if the war turns out badly, this new American self-image will turn into a desert mirage. And a historic opportunity for the self-transformation of America will have been missed. Even if the war does turn out well, the post-war euphoria will eventually fade too. But it will leave something behind: renewed America, self-confident and assured. That was the legacy of the last good war, World War II, a legacy lost in the jungles of Vietnam."*

Quite understandably, Charles Krauthammer's prognostication about the impact of the war is focussed exclusively on the US - it is American-centred. But then the United States is, as we have already stated, the

[16]Time magazine, page 56.

leader of the Coalition Forces apart from being the most dominant nation in the world political, military and economic order. The leadership role of the United States in post-gulf war ear will be specially crucial.

There is also an Arab-centred perspective of the post-gulf war world in the Middle East. For the Arab world, the crisis marks a decisive moment , however the war resolves itself. The Arab states have been divided strongly in the past: after the 1962 revolution in Yemen, and after Sadat's visit to Israel in 1977. But the current division gives the appearance of being deeper than any previous one. The Iraqi attack on Kuwait and its subsequent annexation and its military attack against Saudi Arabia will not heal very quickly after the war. Arab disunity is likely to become a legacy of the conflict for many a year. While Iraq's fate clearly demonstrates that militarism is not an alternative to political modernization, the war's longest reverberation may be from the fact of Arab participation in the studied punishment of an Arab nation particularly as it looks as if this is a coalition of rulers and regimes, not of people. If the war goes on to the bitter end, then the polarization between the government and their people may become more pronounced. In this connection, one cannot but agree with Adrian Hamilton, who in his article, "Getting the West out of the Gulf", in the Observer (London) of 27 January 1991 argued that if the war is to usher in a new era rather than try and preserve the old, *"the first principle must be a withdrawal of Western presence; the second must be a willingness to countenance political change in the region; and, the third, and most important, must be that it is a peace that is allowed to flourish of its own accord."*[17]

If the hostilities were brief, if the United States were perceived as decisive and successful, if the coalition held firm and if the scenes on Arab television of American military might bashing an Arab country could be minimized, the legacy of the war might be less horrendous. As Alfred Leroy Atherton Jr., former US Ambassador to Egypt and former Assistant Secretary of State for the Near East and South Asia correctly argued, *"should the war not go as quickly and surgically as planned, there is a great risk that deep-rooted Arab historical memories and resentment of Western domination, symbolized today by the United*

[17]The Observer (London), page 20.

States, could fan the backlash into a fire storm that would turn the inevitable US military success into a Pyrrhic victory."[18]

Thus, our post-gulf war world economy will depend inter-alia on how long the war lasts, in what circumstances and how the issue of high principles that brought it about in the first instance are settled. But whatever happens, nothing will remain the same. If there is widespread political instability, social and economic instability will inevitably follow. And given the strategic economic importance of the Gulf, this will affect the entire global economy generally and those of the Third World in particular.

The economic prospects of post-gulf war world have been made even dimmer by the worst oil spillage the world has ever seen. This will be in addition to the environmental impact of the presence of 500,000 troops in the desert that may lead to more frequent sand and dust storm because of the disturbance in the surface of the desert. Scientists have predicted that between one million and two million birds would die as a result of the Gulf oil spillage. One of the most fragile of all marine eco-systems has thus been disrupted for years. There are also fears that numerous oil well fires could lead to colder temperatures and other climatic changes. The assumption is that soot would rise into the stratosphere and linger, blocking some sunlight and lowering surface temperatures. Such an outcome in Kuwait could affect the growing season in countries like Iran, Afghanistan and northern India which are in the path of the prevailing winds from Kuwait.

As for Africa, the post-gulf war period presents the continent with a new set of challenges in addition to those relating to the relaunching of the development process. The events in the Gulf and their socio-economic and political implications are worthy of urgent consideration not only at the economic level but also at the political plane. At the economic level, there is need to revisit the energy issue, which seems to have been unduly neglected since the early 1980s. There is need for redoubling efforts to remove this recurrent constraints on development. For that, we need to go beyond the traditional questions of diversification of energy resources to designing an overall regional energy strategy as a part of an overall

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[18]Herald Tribune, 17 January 1991; p. 8.

strategic plan for the African region. Above all, Africa must draw necessary lessons from the ongoing crisis. It should raise itself up to the challenges of the new geopolitical set-up that will emerge after the Gulf war, if it is to avoid further marginalization both economically and politically.

Two questions arise from all these dim prospects. The first is what kind of world will exist by the year 2000? What kind of legacy will the twenty-first century inherit from this excessively troubled twentieth century? The second question is: can our world ever escape the path of mutual injury and self-destruction? I leave it to you to answer both questions. But as we ponder on them perhaps we should, like Prophet Jeremiah, ask of our God and our Maker during this season of Lent which will soon be followed by the month of Ramadan:

"Why hast thou smitten us
And there is no healing for us?
We looked for peace but no good came,
And for the time of healing and behold terror."[19]

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[19]Jeremiah 14:19.