

# A REVIEW OF THE FINANCIAL MARKETS IN THE GCC

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## ABSTRACT

*With the advent of globalization, which necessitated economic and financial development across the globe, the notion of setting the rules and regulations that would govern ethical domestic and international dealings became a foremost priority to many nations. Be it an employment contract, an entrepreneurial venture, or a global-scale stock market transaction, clarity, integrity and transparency are constructs that have nowadays become highly delineated and sought.*

*The Gulf Cooperation Council (GCC) countries provide a concrete example of nations that have perceived the significance of regulating their market affairs. This can be seen in their almost-uniform call for the creation of Financial Markets in interest of further promoting privatization in a time where traditional reliance on the oil sector proved – like all things – transient.*

## INTRODUCTION

This paper presents a cross comparison of four GCC Financial Markets – Kuwait, Qatar, Bahrain, and United Arab Emirates, namely Dubai. A brief recount of the Judicial System prevalent in each of the four countries is presented and an introduction to the regulating Investment Authority – or its equivalent – in each country. Further, the concept of privatization shall be explored as relevant, followed by an introduction to the Financial Market and its regulations as applicable across the countries in question. The fundamental notions of transparency and integrity shall be presented accordingly, followed by a comparison of the most prominent findings and the conclusion.

**State of Kuwait Judicial System** In Kuwait, the legal system “is an amalgam of British common law, French civil law, Islamic legal principles, and Egyptian law” (Pogar – Kuwait: Judiciary, 2004). Judiciary in Kuwait consists of three levels, the first of which is the Courts of First Instance that “handle civil, commercial, personal status and penal matters separately” on which sanctions on wrongdoings “by less than three years of imprisonment or fines of less than 250 Kuwaiti dinars cannot be appealed to a higher level court [whereas] commercial and civil judgments involving fines less than 1000 dinars are final.” Subsequent to that come the Courts of Appeal, which serve “as both the intermediate and final court” (Pogar – Kuwait: Judiciary, 2004). Then, at the final level comes the Court of Cassation serving as the final court of appeal.

**Kuwait Investment Authority (KIA)** The mounting amount of allocated investment funds has led to the development of the Kuwait Investment Authority (KIA) in interest of “improving the quality of investment operations and processes [consequently,] Law 47/1982 was issued establishing KIA as an independent legal entity operating under the auspices of the Ministry of Finance” (Kuwait Investment Authority, 1996). As a substitute to the Ministry of Finance, “KIA is authorized to develop and manage the General Reserve, and the assets of the Future Generations Fund as well as any other funds entrusted to it by the Minister of Finance” (Kuwait Investment Authority, 1996). KIA aims to continue with the investment of the Future Generations Fund assets and the General Reserve Funds in the usual most appropriate manner where the generated income is eventually “to be used to implement state economic and social policies for local development on the one hand and regional and international cooperation on the other” (Kuwait Investment Authority, 1996).

**Privatization** The aspect of privatization is greatly emphasized in the ongoing practices of the KIA in its continuous attempts at developing “national financial systems” through “training

nationals in various investment fields” (Kuwait Investment Authority, 1996). **Kuwait Stock Exchange: An Introduction** Established in 1977, the Kuwait Stock Exchange (KSE) was the “twelfth largest stock exchange” prior to the Iraqi invasion in 1990 because of which it had to halt its operations and reopen in 1992 (Kuwait Information Office – USA, 2002). However, it “recovered strongly after it adopted an automated trading system in 1995 [and became] the most active market in the Arab World” with “77 listed companies in 2002” (Kuwait Information Office – USA, 2002; Pogar – Kuwait: Financial Management, 2004).

In 2000, *Law No 20/2000 – Foreign Participation in Kuwaiti Companies Listed on the Kuwait Stock Exchange* – was enacted to permit “overseas investors to participate in the Kuwait Stock Exchange through ownership of shares of Kuwaiti shareholding companies” (AsiaLaw Profiles 2002: Middle East- Kuwait, 2001). This law was passed to further regulate share cross-trading amongst the Kuwait Stock Exchange and its neighboring Bahraini, Egyptian, and Lebanese Stock Markets which took place in 1998. In May 1999, Kuwait and Jordan “signed a memorandum of understanding that permitted cross-listing on their respective Stock Exchanges” (Pogar – Kuwait: Financial Management, 2004). “Trading on the bourse had been restricted to Kuwaitis and nationals of the GCC states. Foreigners could own Kuwaiti stocks only through mutual funds” (Kuwait Information Office – USA, 2002).

**Kuwait Stock Exchange: Foremost Regulations** In terms of rules and regulations governing the Kuwait Stock Exchange, it is important to note that the Kuwait Stock Exchange Committee is the authorized body that sets forth all such regulations.

**Transparency & Integrity** In August 1996, the Kuwaiti Government passed Law 25 in which it “require[d] full transparency and accountability in all government contracts in excess of one hundred thousand dinars (approximately \$300,000) in value... [as well as] a stipulation by the contracting party as to whether it has paid or will pay a commission of any kind to a disclosed or concealed intermediary.” Furthermore, this “law imposes an obligation on both the payer and the payee to disclose in a separate declaration, the amount of the commission, the type of currency, and the place and manner of the commission.” Failure to do so will result in “sanctions for non-disclosure or misinformation [which] range from civil and criminal penalties equal to the value of the payment to imprisonment” (Ali & Partners, 2004).

On the Transparency International’s 2003 Corruption Perception Index, Kuwait ranked fourth among Arab countries and 35th out of 133 countries worldwide with a score of 5.3 on a scale from 1 to 10, where 10 represents no corruption” (Pogar – Kuwait: Financial Management, 2004).

**State of Qatar Judicial System** The legal system in Qatar focuses on following Shari’a principles “although it has been influenced by the Egyptian legal traditions.” While the judicial structure is composed of Shari’a and Civil Courts, “those two systems are unified in a single structure” and judiciary in Qatar is made up of three levels (Pogar – Qatar: Judiciary, 2004). The first of which are the Courts of Justice and the Shari’a Courts of First Instance where the former “are empowered to hear civil, criminal, and commercial matters” and the latter are dedicated to dealing with “cases involving personal status” (Pogar – Qatar: Judiciary, 2004). Depending on the nature of the case, “decisions rendered in these courts may be appealed” either to the Appeal Court of Justice or the Shari’a Court of Appeal. The third level in the judicial system, the decision of which is deemed final, is the Court of Cassation that includes “one chamber for Shari’a cases and one to serve as the appellate court for Court of Justice appeals” (Pogar – Qatar: Judiciary, 2004).

**Central Bank & Doha Securities Market** Qatar does not have an Investment Authority that would regulate the financial procedures in the country from a single body but rather encompasses two key players, Qatar Central Bank (QCB) and Doha Securities Market (DSM) that take hold of these responsibilities.

**Privatization** Arising from the fact that the government of Qatar viewed privatization as an essential basis that would “reduce pressure on the budget,” the process of privatization came into effect in 1998.

Doha Securities Market: An Introduction Law 13/ 2000 was enacted in October 2000 to confer “upon foreign investors privileges, benefits and protection.” This law allows “foreign investors to invest in ‘all national economy sectors’ except banking, insurance, commercial agencies and trading in real estate” (The Law Offices of Sultan M. Al Abdulla Advocates & Legal Consultants, 2001).

In the Doha Securities Market, “GCC nationals can own up to 25% of the shares of any traded company, and other foreigners can only participate in the market by means of local mutual funds”(Pogar – Qatar: Financial Management, 2004). Moreover, “The Council of Ministers approved on 29 May 2002 the Law of Investment Funds draft allowing non-Qataris to invest in all listed companies”(Ministry of Foreign Affairs, 2001). Recently, as reported by Gulf News “Qatar has issued regulations for the establishment of mutual funds that will allow foreigners to invest in the Doha Securities Market for the first time... Only banks and securities firms with three years or more of experience in the local market will be able to set up mutual funds” (Cooper, 2004).

Doha Securities Market: Foremost Regulations Under article 3 of section 2 – Market Formation – of Unit 1, the Securities Market Committee is the authorized body that sets forth the regulations governing company share listing, stock trade transactions and stock ownership requirements.

Transparency & Integrity Upon the inauguration of the Doha Securities Market, Hussain Al-Abdullah – Director – advised that the “key success factors of the [Doha Securities Market] will be integrity, liquidity, efficiency, and transparency” (Stock Market Director Addresses ABC Qatar, 1997).

Qatar is ranked third in the Arab World on the Transparency International’s Corruption Perception Index with a worldwide score of 5.6 (Transparency International’s Corruption Perception Index, 2003).

Kingdom of Bahrain Judicial System The Bahraini legal system is “a mixed system based on British Common Law models and Sunni and Shi’a Shari’a traditions [; however,] the Constitution declares that Shari’a is [the] principal source of law” (Pogar – Bahrain: Judiciary, 2004).

The Judiciary in Bahrain is the authorized body “empowered to review the constitutionality of laws.” Essentially, the judicial system is divided into two main branches – the Civil Law Courts and the Shari’a Law Courts. The Civil Law Courts reserve the authority to resolve all “commercial, civil, and criminal cases, and all cases involving disputes related to the personal status of non-Muslims.” (Pogar – Bahrain: Judiciary, 2004).

The Economic Development Board of Bahrain The Economic Development Board (EDB) of Bahrain is “an autonomous semi-private agency [that] was established by Amiri Decree in April 2000, and is chaired by the Crown Prince.” The EDB devises and monitors the economic development strategy of Bahrain. This semi-private agency aspires to attract Foreign Direct Investment to Bahrain and has “identified six main economic clusters which capitalize on Bahrain’s competitive advantages and present significant investment opportunities.”

Privatization “Privatization of some state-owned industries and economic diversification with the aim of providing more jobs for Bahraini nationals” is considered one of the main priorities of the EDB (Pogar – Bahrain: Financial Management, 2004). **Bahrain Stock Exchange: An Introduction** In 1957, the National Bank of Bahrain became the first public shareholding company in Bahrain. During the late 1970s and early 1980s, Bahrain realized there was a growing need for a regulated stock market; therefore, the Government, in collaboration with the International Finance Corporation “prepared a feasibility study highlighting the importance of establishing an official stock market in Bahrain.” This study resulted in establishing the Bahrain Stock Exchange (BSE), which commenced operations in June 1989, under Amiri Decree No. 4 (Bahrain Stock Exchange, 2004). In addition to serving as a regular stock exchange, the BSE acts as a securities regulator and undertakes supervision of the capital market.

**Transparency & Integrity** Bahrain has been renowned for its “solid international reputation for low occurrence of corruption. It ranks in the top quarter of all countries worldwide on Transparency International’s Corruption Perception Index, with a CPI of 6.1 on a scale from 1 to 10...” which ranks it second in the Arab World after Oman (Pogar – Bahrain: Financial Management, 2004).

The United Arab Emirates Judicial System “The Constitution, first written in 1971 and reaffirmed several times since then, declares Shari’a to be a principle source for law in the United Arab Emirates.” Other sources that might influence the UAE legal system include Common Law and Egyptian legal traditions (Pogar – UAE: Judiciary, 2004). Civil matters are usually dealt with by the “federal judiciary structure of UAE, although two emirates, Dubai and Ras Al Khaimah, remain outside of this structure.” The first-level or so-called “lowest courts in the system are the Courts of First Instance” and are located in each of the emirates. Beyond the Courts of First Instance, the UAE judiciary system houses a “two-tiered appellate system.” This system encompasses the “Federal Appeal Court, located in each of the emirates, and the highest court in the structure, the Court of Cassation.” Separate criminal and Shari’a courts are also part of the UAE judiciary system. “While the criminal courts have a separate appeal system, cases heard in the Shari’a Courts of First Instance may be appealed to the Civil Courts of Appeal and the Court of Cassation in Abu Dhabi” (Pogar – UAE: Judiciary, 2004).

**Dubai Development & Investment Authority** The Dubai Development and Investment Authority (DDIA) is a “Government Authority entrusted with catalyzing the growth and development of Dubai’s economy by attracting corporate and private investors to the UAE and by facilitating the growth of leading local businesses and encouraging local entrepreneurs” (Dubai Development & Investment Authority, 2004).

**Dubai International Financial Center** The instigation of the Dubai International Financial Center (DIFC), one of the milestones delivered by the DDIA and Dubai Government, aims at facilitating the transformation of Dubai into a key financial hub since the Center serves as a liaising point accounting for the trade time gap imposed by other international financial centers.

**Privatization** The UAE Federal Government encourages diversification and privatization of the economy.

**Dubai Financial Market: An Introduction** The Dubai Financial Market (DFM), an internationally-recognized market espoused by the DDIA and Dubai Government, formally commenced operations in June 2000.

**Dubai Financial Market: Foremost Regulations** The Dubai Financial Market essentially bases its rules and regulations on the policies espoused by the United Arab Emirates Stocks and Commodities Authority (ESCA). (Emirates Freezones.com, 2004).

**Transparency & Integrity** The ESCA sets specific rules that ascertain that investors are protected at all times, and that guarantee the reliability of the “interaction between supply and demand which allows for the natural setting of prices” In terms of The Transparency International’s Corruption Perception Index in 2003, the UAE ranked fifth among Arab countries and 37th out of 133 countries Worldwide with a score of 5.2

## CROSS COMPARISON OF THE FOUR GCC MARKETS

It is evident that the countries in question display shared principles and undergo, to a certain extent, similar functions. Specifically, all four countries’ judiciary systems include three levels and apply Shari’a law in cases involving personal status. Moreover, each country appears to have gained a certain amount of financial market experience, although fairly limited, given the relative novelty of its operations. Additionally, the concept of privatization has been greatly emphasized and applied in all four countries.

In a time characterized by globalization and openness to trade, it becomes imperative to combine efforts in the GCC region in order to effectively respond to the challenging business environment.

### **CONCLUSION**

This research document has briefly looked into the judicial systems of four main GCC countries – Kuwait, Qatar, Bahrain, and the United Arab Emirates. As noted, all four countries rely mainly on Shari'a Law as a basis upon which the local legal system is built. In addition to the national judicial system, these countries have set forth policies and procedures that regulate domestic and foreign trade. A critical area where such policies and regulations are made evident is the Financial Market or Stock Exchange housed by each of the individual countries.

In light of the dominant similarities prevalent amongst the four Financial Markets, the notion of an integrated GCC Market further proves a feasible establishment. The fact that the region's four markets tend to rely on relatively comparative regulations, such as capital and liquidity requirements and registration procedures, among others, indicates that joining forces in one market shall not only increase trade volume, but shall also allow the region further international recognition as a dominant body. Moreover, creating a sole GCC Market would imply a boost in capital inflow into the region from increased foreign trade and would lead to more solid domestic investment grounds.

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