

# ECONOMIC CHALLENGES OF THE GULF ARAB COUNTRIES: THE IMPACT OF DUTCH DISEASE

## Abstract

In the 20th century, oil became a strategic raw material in the global economy, which led the Arab Gulf states to become heavily dependent on the export of energy resources and the income generated from them. An analysis of their revenues from 1995 to 2024 shows that more than 60% of total income in these states derives from energy-resource exports. An analysis of the Gulf Arab economies demonstrates that, despite substantial efforts, the overall economic structure has not undergone major transformation—with the notable exception of the United Arab Emirates.

Economic diversification has also become a key priority in the Arab Gulf states. As a result, industrial sectors linked to the energy industry were developed. The construction sector received increased attention, and national development strategies and economic visions were introduced, aiming to expand the service sector and diversify exports. These national visions placed strong emphasis on environmental protection and human social development.

However, the economies of the Arab Gulf states remain vulnerable to military crises and international shocks. Prior to the Iran–Iraq War, Iraq was the world’s second-largest oil exporter among OPEC member states, but it lost this position at the very beginning of the conflict and subsequently faced significant economic challenges.

**Key words:** Dutch disease; Gulf Arab states; economic diversification; energy-resource export; rentier economy

## Introduction

The term Dutch Disease refers to the development of one sector of the economy accompanied by the decline of other ones. The term first appeared in journal *The Economist* in 1977 and was associated with the discovery of a large gas field in the North Sea. Accordingly export of energy resources increased, and some sectors disappeared from the economy altogether (The Economist 1977).

In the 20th century, oil became a strategic raw material in the world economy. As a result, the economies of the Arab countries of the Persian Gulf became dependent on the export of energy resources and the income generated from them. Since the second half of the 1970s, the economies of these countries have grown significantly, largely due to increased energy-resource exports (Gachechiladze 2011:52). So, the issue of diversification also emerged in the 1970s. Industrial sectors related to the energy industry were created. This shift replaced a significant share of investment in extractive industries with capital-intensive and energy-

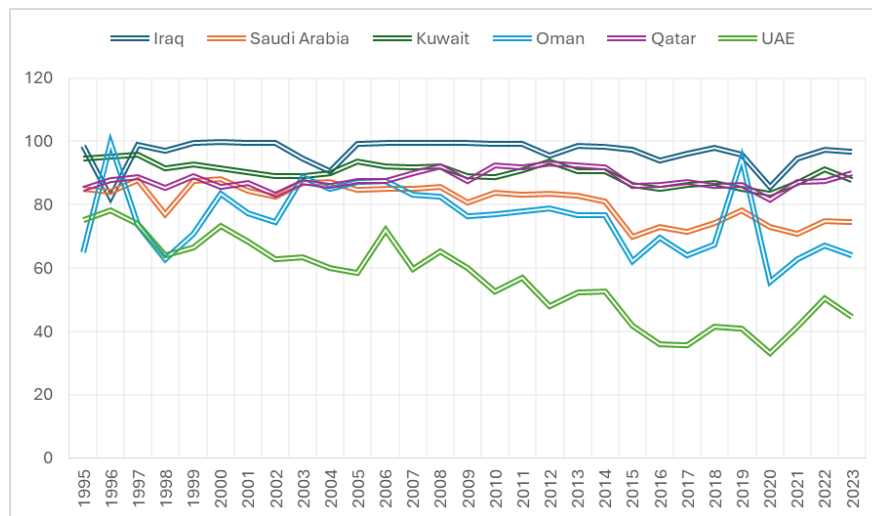
intensive sectors such as chemicals, steel, and aluminum. Attention was also directed toward the construction sector, but despite these efforts, the economic structure did not change (see Graph #1).

Various economic visions and national development strategies were developed, the main objective of which was to diversify exports and expand the service sector. These national visions focus on key issues such as human social development and environmental protection, which are the essential elements and the basis for sustainable development (Mishrif 2018:3).

The pace of economic structural change in the Arab states of the Persian Gulf remains limited. The main reason for this is their strong dependence on the energy sector. Such economies are vulnerable to military crises and international shocks. For example, before the Iran–Iraq War, Iraq ranked second among OPEC member states in terms of oil production, but it lost this position at the very beginning of the conflict. Iraq faced serious economic challenges and was no longer able to process oil (Byrne, 2013: 59).

Events in the Persian Gulf have made economic diversification a key issue on the political agenda. The economic structure of the region is unstable: each country experiences negative consequences (and occasionally positive ones, although these are reflected only in revenue levels) due to fluctuations in world oil prices. For instance, the Gulf Arab states invested in infrastructure projects using revenue generated from energy exports. However, these projects have played a marginal role in developing other sectors, as the challenges associated with Dutch disease are extremely difficult to overcome (Mishrif 2018:19).

## Findings



*The tabel was created by author based on the retrived data from The Observatory of Economic Complexity (2024), Iraq; Kuwait; Oman; Qatar; Saudi Arabia, United Arab Emirates;*

The graphs illustrate the share of energy resources in the exports of the Gulf Arab states from 1995 to 2024. In most Gulf economies, the share of energy exports exceeds 60%. The only exception is the United Arab Emirates (UAE). The UAE's performance indicates a clear trend toward economic diversification. Although it remains one of the world's ten largest oil producers, which succussed to become a major trade and financial center in the Middle East (U.S. Energy Information Administration 2018). However, this tendency of recovery and diversification, the UAE is still affected by Dutch disease. The issue remains more acute in the other Gulf Arab states.

In the Persian Gulf region, successful economic diversification depends on the political will to implement large-scale structural reforms. Diversification plays a central role in the development of the energy sector. Investments in renewable energy and the green economy are among the projects that contribute to the diversification of both the economy and the energy sector. Saudi Arabia, Qatar, and Kuwait have all announced plans for a transition to a green economy.<sup>1</sup> These initiatives create new opportunities for diversification, although given long-term trends, it is unlikely that they will be fully implemented within the projected timeframe.

## Conclusion

In the 20th century, the oil deposits discovered in the Persian Gulf reshaped the economic landscape of the region, leading to far-reaching economic transformations. The developments observed in the Arab states of the Persian Gulf are qualitatively similar to the situation that emerged in the Netherlands after the discovery of a major gas field in the North Sea. Therefore, using the term Dutch disease to describe the economies of the Gulf states is justified.

Among the Gulf countries, the United Arab Emirates stands out. Despite being one of the world's ten largest oil-producing states, it has become the region's primary trade and financial hub. Consequently, both political and economic efforts within the GCC demonstrate a clear intention to improve economic performance through diversification.

Iraq exhibits the most severe symptoms of Dutch disease, with energy and resource exports accounting for more than 95% of its economy. This is not solely the result of high energy revenues; a highly unstable political and economic environment has also hindered broader economic development. Kuwait's economy likewise faces significant risks. Despite various reforms, the country's progress toward meaningful diversification remains uncertain. Qatar's economy continues to rely heavily on the export of natural resources. Oman mainly exports refined petroleum products, while in Bahrain, the limited availability of energy resources makes it difficult to draw definitive conclusions about the extent of Dutch disease.

Saudi Arabia shows signs of gradual recovery. The share of revenue derived from the energy sector has decreased in recent years, not because income from energy exports is falling, but because revenues from other economic sectors are rising. As a result, the relative share of energy-sector exports in the economy is declining.

It is evident that dependence on energy resources has created major challenges for the countries of the region, weakening other economic sectors and leaving gaps in the market. The Gulf Arab states are attempting to revitalize their economies, yet at this stage, only the UAE shows notable success in this direction.

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