



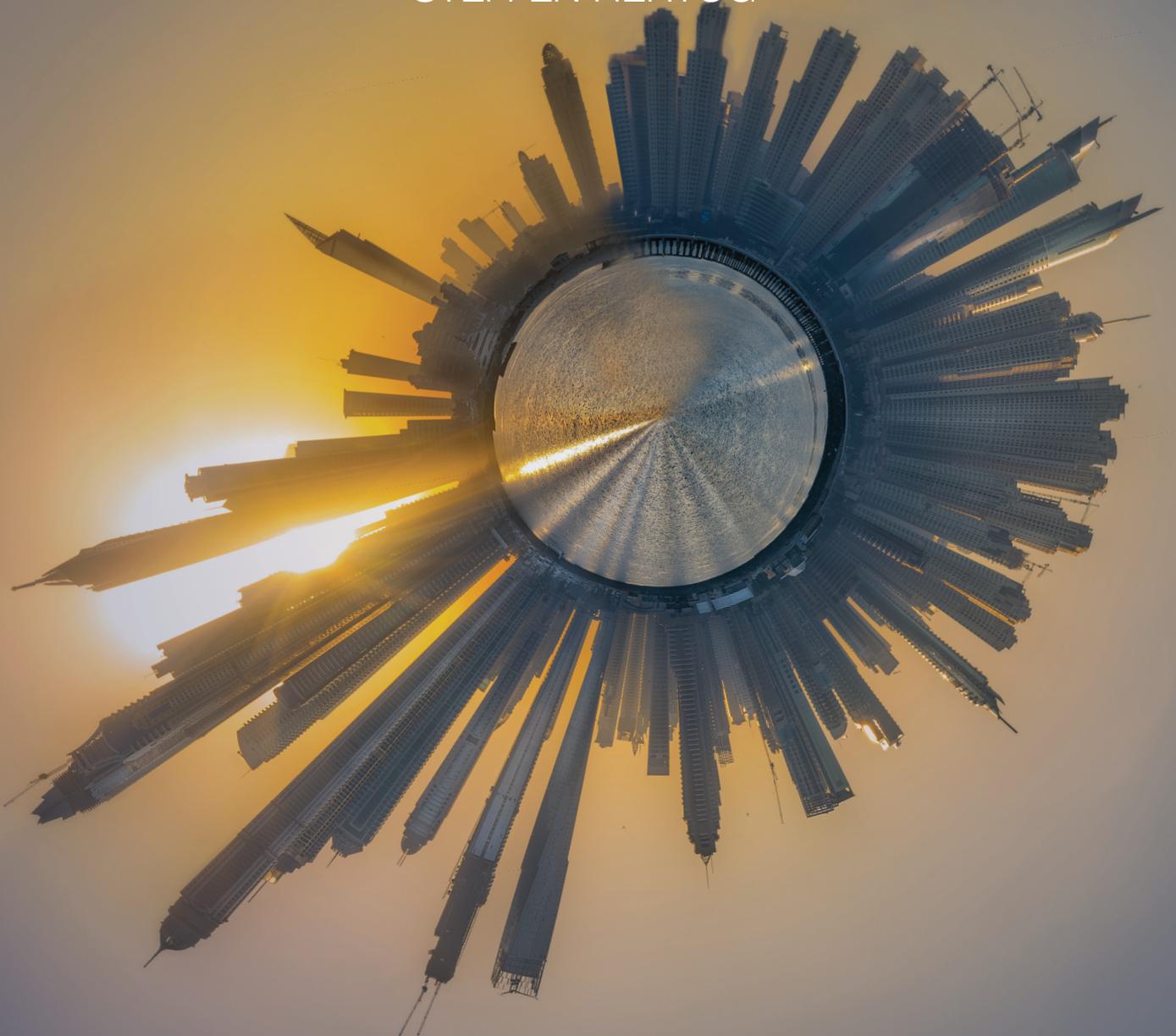
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RENT DISTRIBUTION, LABOUR MARKETS AND DEVELOPMENT IN HIGH RENT COUNTRIES

STEFFEN HERTOOG



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Abstract

This paper argues that hydrocarbons producers with high rents per capita constitute a specific category in the broader universe of rent-dependent countries, facing a specific set of development challenges that are not shared by mid-rent countries (MRCs). The paper surveys patterns of rent distribution in high-rent countries (HRCs), focusing on energy subsidies and excessive public employment, and analyses their developmental consequences. It then proposes unconditional cash grants for HRC citizens in combination with energy subsidy and public employment reform as a mitigation strategy to minimise HRC-specific negative effects of rent distribution.

Introduction

The discussion on the ‘resource curse’ has increasingly moved into the terrain of policy prescriptions. One of the most prominent proposals for avoiding some of the pathologies that natural resource wealth can engender is the direct distribution of resource rents to the population.

This paper seeks to add to the growing literature on cash grants in rentier states by focusing on their potential impact in a particular class of resource-rich states in the developing world: countries with very high per capita resource rents, which are starting to be recognised as a category of their own, with their own political and economic development challenges.¹

Such high-rent countries (HRCs) – a limited number of mostly small-population resource exporters in the developing world – face somewhat different challenges from the mid-rent countries (MRCs) on which much of the resource curse debate has traditionally focused, yet challenges that are in many ways as daunting. These have never been systematically analysed, and are surveyed in the first half of this paper. The second half of the paper then makes a case that direct cash grants are a potent remedy for most of them. As we will see, the case for such a ‘citizens’ income’ is even stronger for HRCs than for MRCs: while retaining most of the redeeming features that cash grants are argued to have in the rentier state universe at large, citizens’ incomes would be easier to finance and justify, involve less acute trade-offs and, most importantly, help overcome HRC-specific development challenges.

To anticipate the paper’s main arguments, economies of HRCs typically distribute oil rents among their populations through two channels that create large inequities and distortions:

- very low domestic energy prices, which privilege wealthy consumers and lead to over-consumption, distorted investment decisions, declining energy efficiency and reduced long-term resource export capacity; and
- over-employment in the public sector, a similarly costly and unfair way of sharing the wealth, which distorts labour markets by drawing nationals out of private employment. This effect is typically magnified by migration regimes that allow or tolerate large-scale imports of cheap foreign labour for private employment, resulting in low labour productivity.

While the first mechanism of distribution is widespread among rentier countries in general, the latter is more specific to HRCs in its scale and scope. It undermines citizens’ interest in privately driven economic development and creates a potential zero-sum distributional conflict with local capitalists.

Most, though not all, HRCs have achieved reasonable levels of human development. This has happened, however, almost exclusively on the back of state spending. In the absence of privately driven economic diversification, HRCs’ long-term development challenges

¹ Justin Gengler, *Group Conflict and Political Mobilization in Bahrain and the Arab Gulf: Rethinking the Rentier State* (Bloomington: Indiana University Press, 2015). Michael Herb, ‘A Nation of Bureaucrats: Political Participation and Economic Diversification in Kuwait and the United Arab Emirates’, *International Journal of Middle East Studies* 41/3 (2009), pp. 375–95. Terry Lynn Karl, *The Paradox of Plenty: Oil Booms and Petro-States* (Berkeley, CA, 1997), p. 11.

are even more acute than those of MRCs: their dependency on cheap domestic energy, rent-financed public employment, transfers and services is even greater, and has deepened rather than lessened over time.

A citizens' income could help move HRCs onto a more sustainable path in several ways. It would be a more incentive-neutral, transparent, fair and efficient way of sharing the nation's wealth, and act as potent political justification for increasing domestic energy prices and reducing public sector recruitment. It would allow nationals to 'top up' modest private sector earnings so as to reach an acceptable overall income without creating some of the disincentives to work that means-tested social security provisions create. Basic income security would allow citizens to compete with migrant labour and enable the former to upgrade their skills and take risks as entrepreneurs. The larger number of citizens that would hence be active in the private economy would create a political constituency for private-driven growth.

A citizens' income could be financed through subsidy reductions, reduced public sector hiring and, in the long run, a permanent dividend on HRCs' overseas investments. It would create none of the fiscal trade-offs, economic disincentives and moral problems that bedevil the basic income concept in tax-based economies, where the discussion about unconditional cash grants originated.

This paper contributes to several literatures: the resource curse and rentier state debates, the debate about subsidy reform in the developing world, and, finally, the broader literature on the 'basic income' concept that extends beyond politics, development and economics into political philosophy and whose useful insights – and caveats – are often ignored in the rentier cash grants discussion.

Selection of Cases

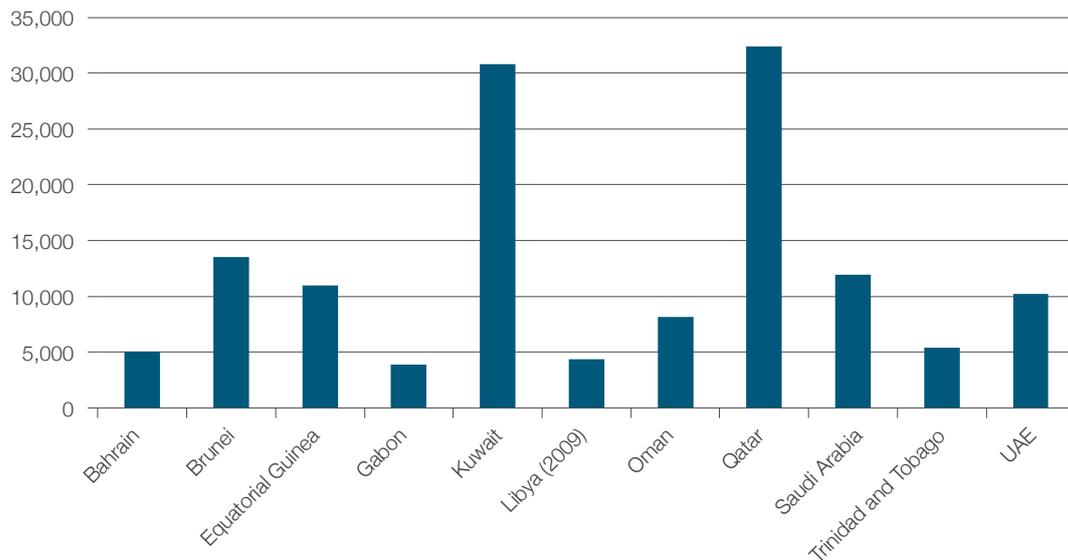
Any cut-off point to define high-rent status is arbitrary: 'HRC' is not a discrete empirical category but rather an ideal type which countries tend to approach as their per capita rents increase. To select cases for the empirical illustrations in this paper, a threshold of USD 3,000 per year has been chosen, resulting in the 11 countries shown in Figure 1. This does not mean that this paper's arguments do not apply in weaker form to countries below this threshold.

Every effort has been made to collect comprehensive labour market, subsidy and macro-economic data on all 11 cases, but for Gabon and Equatorial Guinea in particular, information is patchy and contradictory.

To situate HRCs in the wider rentier universe, we occasionally include MRCs with rents between USD 500 and 3,000 in this paper. In 2011, 13 non-OECD cases fell into this category: Algeria, Angola, Azerbaijan, Congo-Brazzaville, Ecuador, Iran, Iraq, Kazakhstan, Malaysia, Russia, Syria, Turkmenistan and Venezuela.

Figure 1. Developing Countries with Per Capita Oil and Gas Rents above USD 3,000, 2010.

Source: Based on 2013 World Development Indicators data.



Current Outcomes in Rentier States

With the potential exception of Equatorial Guinea, all HRC regimes appear to feel a political need to share their resource wealth with the wider population. The way this is done, however – with cheap energy and public sector over-employment playing a leading role² – is uniquely inefficient.

While these forms of distribution might have been justifiable at times of lower international energy prices and low domestic consumption, and when populations were smaller and state apparatuses just being built, they have now become extremely costly. Cheap energy and excessive public employment are inefficient, regressive and often exclusive tools of distribution, with deleterious consequences for non-oil diversification, fiscal sustainability and, in the long run, the potential of local societies to find a growth-oriented compromise between national workers and business.

² There are of course many other forms of rent distribution, including free or subsidised public services, non-salary transfers (including pensions), preferential contracts for local business etc. Their scale is relatively small, however, and they are often less distortionary, have fewer negative externalities and are harder to compare across countries.

Energy Subsidies

Energy subsidies in the developing world have been widely discussed in recent years.³ Cheap energy is typically provided through transport fuel, gas and electricity that are sold at far below international market prices.⁴ The available literature demonstrates convincingly that distribution of rents through cheap energy is regressive: according to International Monetary Fund (IMF) estimates, the richest quintile of households in developing countries capture six times more in fuel subsidies (43 percent) than the poorest quintile.⁵ Unlike subsidised public services such as health and education, energy consumption also entails negative environmental externalities.

The size of implicit subsidies can be tricky to estimate: not all types of energy are easily exportable, and it is not clear whether all of the potentially 'liberated' energy production could be exported without pushing international prices downwards.⁶ But even under restrictive assumptions, subsidies are very substantial for most of the countries being studied, and their regressive distributional impact and negative externalities obtain independence from their direct fiscal opportunity cost. For the purposes of this paper, we will use the IMF's 2011 energy subsidy estimates, which are comparable across countries (see Figure 2). They show that, with the exception of Gabon and Equatorial Guinea,⁷ our cases lie far above the global average of 0.7 percent of GDP. MRCs also have substantial, but for the most part lower, energy subsidies.⁸

³ Taimur Baig, Amine Mati, David Coady and Joseph Ntamatungiro, 'Domestic Petroleum Product Prices and Subsidies: Recent Developments and Reform Strategies', *IMF Country Report 07/71* (2007). Available at <https://www.imf.org/external/pubs/ft/wp/2007/wp0771.pdf> (accessed 13 October 2015). Joseph Charap, Arthur Ribeiro da Silva and Pedro Rodriguez, 'Energy Subsidies and Energy Consumption: A Cross-Country Analysis', *IMF Working Paper 13/112* (2013). Available at <https://www.imf.org/external/pubs/ft/wp/2013/wp13112.pdf> (accessed 13 October 2015). Benedict Clements et al., 'Case Studies on Energy Subsidy Reform: Lessons and Implications', *International Monetary Fund*, 28 January 2013. Available at <http://www.imf.org/external/np/pp/eng/2013/012813a.pdf> (accessed 13 October 2015). Glada Lahn and Paul Stevens, 'Burning Oil to Keep Cool: The Hidden Energy Crisis in Saudi Arabia', *Chatham House Programme Report*, December 2011. Available at <http://www.chatham-house.org/publications/papers/view/180825> (accessed 13 October 2015).

⁴ Average diesel and gasoline prices in HRCs, e.g., were less than half of the US benchmark price in 2010; if Gabon is left out, average prices were about a third. See Gesellschaft für Internationale Zusammenarbeit, *International Fuel Prices 2010/2011* (2012). Electricity and natural gas prices in some cases are even lower. See Jim Krane, *Stability versus Sustainability: Energy Policy in the Gulf Monarchies*, PhD dissertation, (Judge Business School, Cambridge University, 2013).

⁵ *Energy Subsidy Reform: Lessons and Implications*, International Monetary Fund (2013), p. 19.

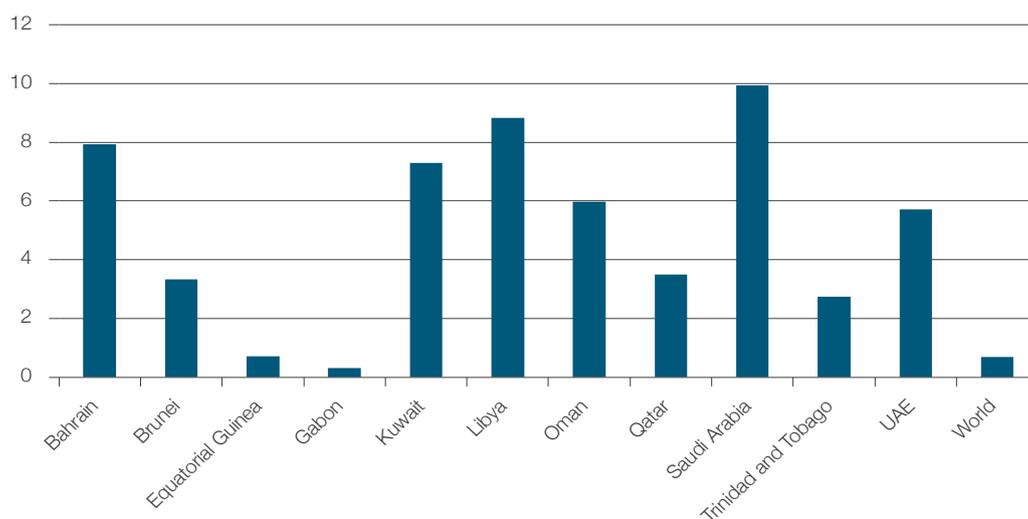
⁶ Giacomo Luciani, 'Domestic Pricing of Energy and Industrial Competitiveness', in Giacomo Luciani (ed), *Resources Blessed: Diversification and the Gulf Development Model* (2012).

⁷ As recently as 2006, Gabon's fuel subsidies alone were estimated at 2 percent of GDP; see Moataz El-Said and Daniel Leigh, 'Fuel Price Subsidies in Gabon: Fiscal Cost and Distributional Impact', *IMF Working Paper 06/243* (2006). Available at <https://www.imf.org/external/pubs/cat/longres.aspx?sk=19906.0> (accessed 13 October 2015). The more recent estimates seem to reflect subsequent pricing reforms.

⁸ The median subsidy estimate is 5.7 percent of GDP for HRCs and 3.8 percent for MRCs. Absolute per capita values, however, are seven times lower in low-rent countries (LRCs), which are considerably poorer.

Figure 2. Pre-Tax Subsidies for Petroleum Products, Electricity, Gas and Coal, 2011 (percentage of GDP).

Source: Based on IMF, *Energy Subsidy Reform*.



We do not have a reliable breakdown for energy consumption in the hydrocarbons and non-hydrocarbons sectors. Typically, however, the former uses only a small fraction of total energy, although it constitutes half or more of GDPs in our cases. This means that the energy subsidies in the non-hydrocarbons economy are even higher. They are even higher relative to a counterfactual in which environmental externalities and foregone tax revenue are considered.⁹ Whatever measure for subsidies is used, their share in government revenue is typically more than twice as high as that in (total) GDP, reflecting enormous foregone revenue.

Over the last three decades, domestic energy consumption has increased above population growth and, in most cases, above GDP growth (see Table 1, and Figures 5 and 6 below). In 2010, average per capita energy consumption in our cases was 1.5 times the average of the world's high-income countries.¹⁰ Anecdotally, much consumption is frivolous, caused by bad insulation, inefficient equipment and gas-guzzling vehicles that are incentivised by low prices, hence adding little to citizens' welfare.

⁹ IMF, *Energy Subsidy Reform*.

¹⁰ Based on World Development Indicators; no data were available for Equatorial Guinea.

Table 1. Compound Annual Growth Rates of Domestic Energy Consumption and Real GDP, 1980–2010.

Source: Based on EIA, IMF and World Bank data.

Country	Energy (%)	GDP (%)
Bahrain	4.8	4.3
Brunei	2.0	0.6
Equatorial Guinea	15.8	16.5
Gabon	1.6	1.9
Kuwait	3.3	2.0
Libya	2.5	0
Oman	9.0	6.1
Qatar	5.6	5.8
Saudi Arabia	5.3	1.8
Trinidad and Tobago	5.8	2.1
UAE	9.0	3.2

In some cases, most notably Saudi Arabia, growing domestic consumption has started to threaten countries' hydrocarbons export capacity, further reducing potential government revenue.¹¹

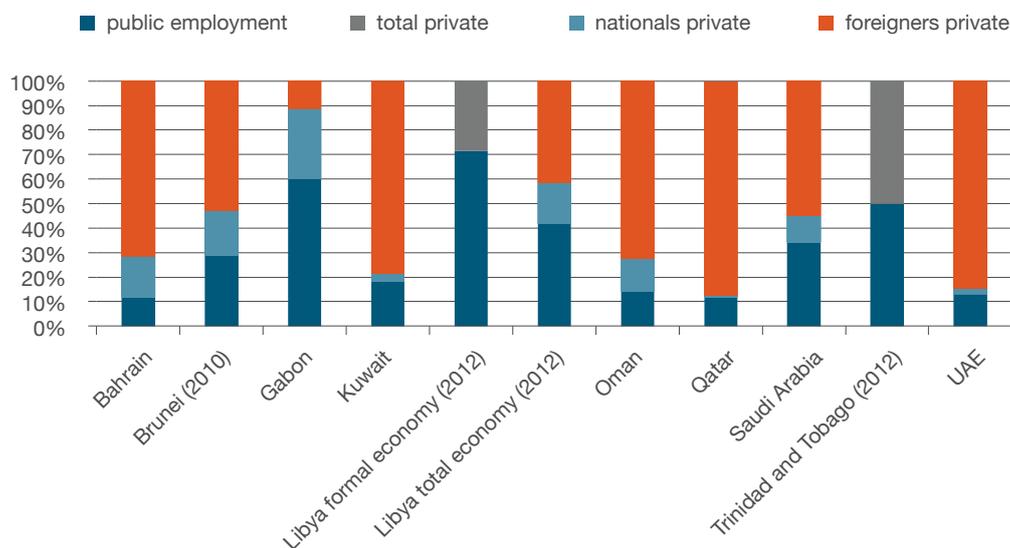
Labour Market Outcomes

Over-employment of citizens in the public sector under generous conditions is the second main channel of mass rent circulation that all our HRCs bar Equatorial Guinea have engaged in, and it is the distribution tool that truly sets them apart from other rentiers. Combined with large-scale labour migration (see Figure 3), government job guarantees typically result in a large public sector dominated by nationals, and a private sector with a strong or dominant presence of foreign workers (see Figure 4). Only Trinidad and Tobago forms an exception to the migrant dependence pattern, possibly as a result of its domestic tradition of low-wage plantation labour.

¹¹ Krane, *Stability*. Lahn and Stevens, *Burning Oil*.

Figure 4. Labour Market Structures, 2009 Unless Marked Otherwise.

Sources: Based on national authorities, World Bank and IMF data.¹⁴



There is much anecdotal evidence of over-employment and bloated bureaucracies in HRCs, as job creation is typically driven by the need to provide jobs for new labour market entrants rather than by administrative needs. Administrations often perform poorly due to overstaffing and weak incentive systems.¹⁵

A survey of the available primary and secondary sources shows that HRC public sectors also typically pay much higher salaries, offer more perks, provide higher job security and extract less performance than private employers do. The pattern is strikingly uniform across cases.¹⁶

¹⁴ No labour market data were available for Equatorial Guinea; unlike those of other HRCs, its public sector appears to be rather small as most rents are siphoned off by corrupt political elites. See G. Wood, 'Business and Politics in a Criminal State: The Case of Equatorial Guinea', *African Affairs* 103/413 (2004), pp. 547–67.

¹⁵ Abdul Rahman Al Ageli, 'Youth Employment in Libya', *Libya Herald*, 16 December 2013. Available at <http://www.libyaherald.com/2012/12/16/youth-employment-in-libya-a-structural-solution-is-needed-part-23> (accessed 13 October 2015). Christopher Colclough and Martin Godfrey, 'The Economics of Labour Shortage: Three Case Studies from Northern Borneo', *IDS Bulletin* 17/4 (1986), pp. 1–9. Ugo Fasano and Rishi Goyal, 'Emerging Strains in GCC Labour Markets', *IMF Working Paper* 04/71. Available at <https://www.imf.org/external/pubs/cat/longres.aspx?sk=17286.0> (accessed 13 October 2015). Ingo Forstenlechner and Emilie Rutledge, 'Unemployment in the Gulf: Time to Update the "Social Contract"', *Middle East Policy* 17/2 (2010), pp. 38–51. Steffen Hertog, 'A Comparative Assessment of Labour Market Nationalization Policies in the GCC', in Steffen Hertog (ed), *Labour Market, Unemployment, and Migration in the GCC* (Geneva, 2011). Richard Shediak and Hatem Samman, *Meeting the Employment Challenge in the GCC* (Dubai, 2010).

¹⁶ Martin Baldwin-Edwards, 'Labour Immigration and Labour Markets in the GCC Countries: National Patterns and Trends', *LSE Kuwait Programme Paper Series* 15 (London, 2011). Forstenlechner and Rutledge, 'Unemployment'. Hertog, 'Comparative Assessment'. Lim Hong-Huat, 'Economic

Unlike those of developed economies, public sectors in HRCs typically act as wage-setters for nationals,¹⁷ shaping their general expectations regarding salaries and work conditions. Private sector wages in all but the highest-skilled categories, however, are typically low and work conditions comparatively harsh due to the preponderance of migrant workers there. The low-skilled foreigners who satisfy most of the private labour demand enjoy limited formal rights, including lower job security than nationals and low or no labour market mobility, allowing for significant rent extraction by employers, who often employ them informally.¹⁸

As a result, most citizens evince a pronounced preference for public sector employment and many are happy to queue for positions in the overstuffed bureaucracy, preferring unemployment to private sector jobs.¹⁹ Conversely, private employers prefer foreigners.

The ironic result of government attempts to create public jobs for everyone is low labour market participation among nationals in most HRCs as well as high citizen unemployment in all but the highest-rent countries. Nationals' labour market participation in the four highest-rent Gulf monarchies ranges from 36 to 51 percent;²⁰ (total) participation ratios reach 61 percent in Trinidad and Tobago,²¹ 60 percent in Gabon and 53 percent in Libya.²² This compares with a world average of 69 percent.²³

Crisis, Unemployment and Training in Brunei Darussalam', presented at the APEC Forum on Human Resources Development, Chiba, Japan, 18–20 November 2009. 'Gabon: 2012 IMF Article IV Consultation', *IMF Country Report* 13/55 (March 2013), p. 15. Ralph Chami et al., *Libya beyond the Revolution: Challenges and Opportunities*, International Monetary Fund Middle East and Central Asia Department (Washington, DC, 2012), p. 11. Reshma Mahabir, Vishana Jagessar, Crystal Neptune and Delvin Cox, 'Understanding Wages in a Small Open Economy: The Case of Trinidad and Tobago', *Central Bank of Trinidad and Tobago Working Paper* 11/2013 (February 2013), pp. 8–9.

¹⁷ Colclough and Godfrey, 'Economics'. Andrew Downes, 'An Economic Analysis of Unemployment in Trinidad and Tobago', *SSRN Scholarly Paper* 1817180 (Rochester, NY, 1998), p. 16. Available at <http://papers.ssrn.com/abstract=1817180> (accessed 13 October 2015). 'Brunei Darussalam: Recent Economic Developments', *IMF Country Report* 99/19 (April 1999), p. 33.

¹⁸ Ingo Forstenlechner and Emilie Jane Rutledge, 'The GCC's 'Demographic Imbalance': Perceptions, Realities and Policy Options', *Middle East Policy* 18/4 (2011), pp. 25–43. Geoffrey Gunn, 'Rentier Capitalism in Negara Brunei Darussalam', in Kelvin Hewison, Richard Robison and Garry Rodan (eds), *Southeast Asia in the 1990s: Authoritarianism, Democracy and Capitalism* (St Leonards, 1993). Raimundo Soto and Rosalía Vasquez-Alvarez, 'The Efficiency Cost of the Kafala in Dubai: A Stochastic Frontier Analysis', *Instituto de Economía, Pontificia Universidad Católica de Chile, Documentos de Trabajo* 399. Available at <http://ideas.repec.org/p/ioe/doctra/399.html> (accessed 13 October 2015). John Willoughby, 'Ambivalent Anxieties of the South Asian–Gulf Arab Labour Exchange', *Revista de Economía Mundial* 14 (2006), pp. 31–56. Wood, 'Business'.

¹⁹ Forstenlechner and Rutledge, 'Unemployment'. Gunn, 'Rentier Capitalism', p. 115. Hong-Huat, 'Economic Crisis'. Monitor Group and Cambridge Energy Research Associates, *National Economic Strategy: An Assessment of the Competitiveness of the Libyan Arab Jamahiriya* (Tripoli, 2006), p. 135. Douglas Yates, 'Neo-'Petro-Monialism' and the Rentier State in Gabon', in Matthias Basedau and Andreas Mehler (eds), *Resource Politics in Sub-Saharan Africa* (Hamburg, 2005), p. 187.

²⁰ Baldwin-Edwards, *Labour Immigration*, p. 13.

²¹ Mahabir et al., *Understanding Wages*, p. 5.

²² World Development Indicators.

²³ For research linking low female labour market participation in particular to oil income, see Michael L. Ross, 'Oil, Islam, and Women', *American Political Science Review* 102/1 (2008), pp. 107–23.

Citizen unemployment statistics are unreliable and contested, but available estimates for most HRCs are high: 12 percent in Saudi Arabia in 2013, 24 percent in Oman in 2010, 27 percent in Gabon in 2012, and 26 percent in Libya in 2010.²⁴ Only in Brunei, Kuwait, Qatar and the UAE is citizen unemployment in single digits, as there are sufficient surplus government jobs at least for male citizens, while in Trinidad and Tobago sufficient numbers of nationals work in low-wage sectors like tourism and agriculture to have reduced unemployment to around 5 percent in 2011 (down from 20 percent in the late 1980s).²⁵

Most HRC nationals shun productive economic activities in their own countries. In many HRCs, there are quota-based attempts to increase nationals' private employment levels, which most employers, whose incentives are stacked against employing demanding locals, evade with relative ease.²⁶

There are huge direct and indirect costs to surplus public employment. A large, usually dominant share of potentially productive national manpower is 'parked' in jobs whose economic contribution is questionable. Public sector employment policies give questionable education incentives, leading to an undersupply of national skills relevant in the private market.²⁷ Public sector over-employment also creates large, unnecessary overhead costs and negative environmental and infrastructure externalities.²⁸ It is also an inequitable way of sharing the wealth: quite apart from micro-level issues of favouritism and unequal pay scales, even in the richest HRCs a significant – usually young and/or female – segment of the population remains structurally excluded from this form of rent distribution, as public employment policies favour older, male job seekers.

Migrant dependence and labour-intensive growth have also led to very high population growth rates, requiring additional infrastructure investment: from 1990 to 2010, HRC populations grew an average of 110 percent, compared to 30 percent worldwide population growth and 60 percent growth in low-income countries.²⁹

²⁴ Saudi Arabia: Central Department of Statistics, *Manpower Research Bulletin* 2013-1 (Riyadh, 2013). Saleh Al-Shaibany, 'Choosy Omanis Add to Government's Unemployment Headache', *Reuters*, 14 September 2012, citing the IMF. Available at <http://www.reuters.com/article/2012/09/14/us-oman-jobs-idUSBRE88D15820120914> (accessed 13 October 2015). Dominique Puthod, Mouhamadou Sy and Bakary Dosso, 'Gabon 2015', *African Economic Outlook*, 2015. Available at <http://www.african-economicoutlook.org/en/countries/central-africa/gabon> (accessed 13 October 2015). Ralph Chami et al., *Libya beyond the Revolution*.

²⁵ Mahabir et al., *Understanding Wages*, p. 3.

²⁶ African Development Bank, 'Equatorial Guinea', *African Development Bank, African Economic Outlook* (Tunis, 2008), p. 296. Laura El-Katiri, Bassam Fattouh and Paul Segal, 'Anatomy of an Oil-Based Welfare State: Rent Distribution in Kuwait', *LSE Kuwait Programme Paper Series* 13 (London, 2011). Forstenlechner and Rutledge, 'Unemployment'. 'Gabon Oil Workers Strike over Foreign Workers', *BBC News*, 15 April 2010. Available at <http://news.bbc.co.uk/1/hi/world/africa/8622688.stm> (accessed 13 October 2015). Hertog, 'Comparative Assessment'.

²⁷ Hertog, 'Comparative Assessment'.

²⁸ Karl Widerquist and Michael A. Lewis, *The Basic Income Guarantee and the Goals of Equality, Efficiency, and Environmentalism* (New York, 2009). Available at <http://works.bepress.com/widerquist/17> (accessed 13 October 2015).

²⁹ World Development Indicators.

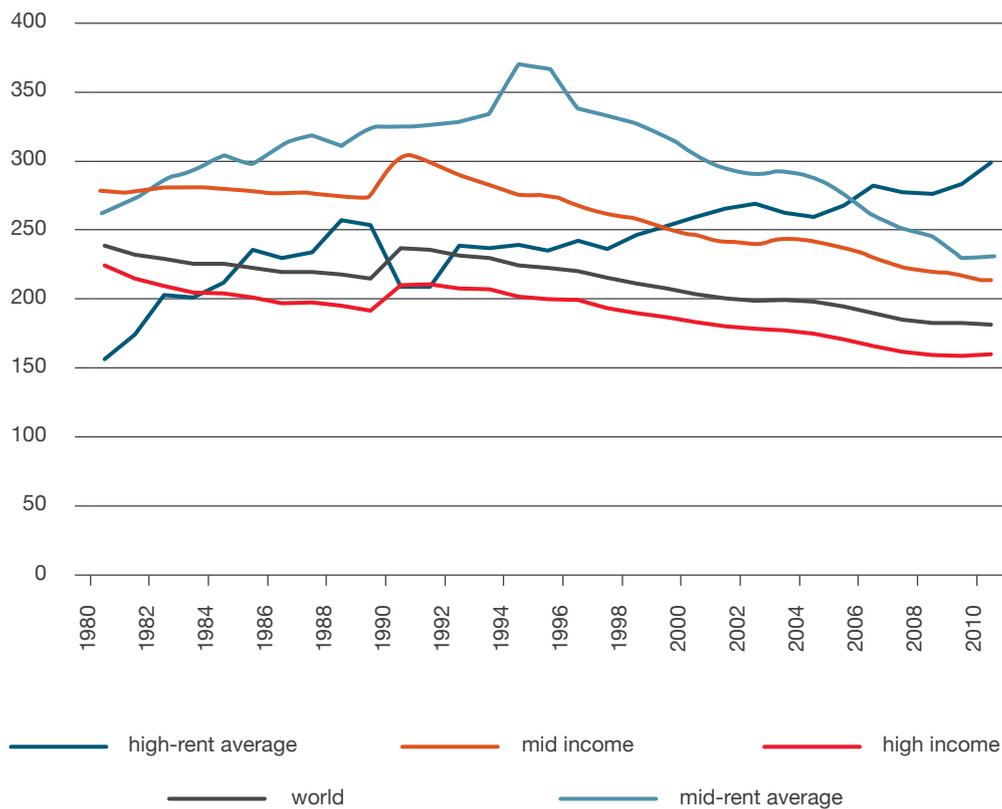
Economic Development Outcomes

The skewed energy and labour market structures described above seem to have led to large macro-economic distortions: descriptive statistics and simple econometrics show that energy efficiency and labour productivity have strongly declined over the last few decades for most HRC cases – a result that does not obtain for MRCs, where, at least per capita, subsidies are much lower.³⁰

Figure 5 demonstrates that while economies across the world have become more energy efficient over the last three decades, energy intensity of production has strongly increased in HRCs, a result that must at least in part be explained by low domestic energy prices.³¹

Figure 5. Energy Use (Kg of Oil Equivalent) Per USD 1,000 GDP (constant 2005 PPP).

Source: Based on World Bank Development Indicators data.³²



³⁰ Based on World Development Indicators; no data were available for Equatorial Guinea.

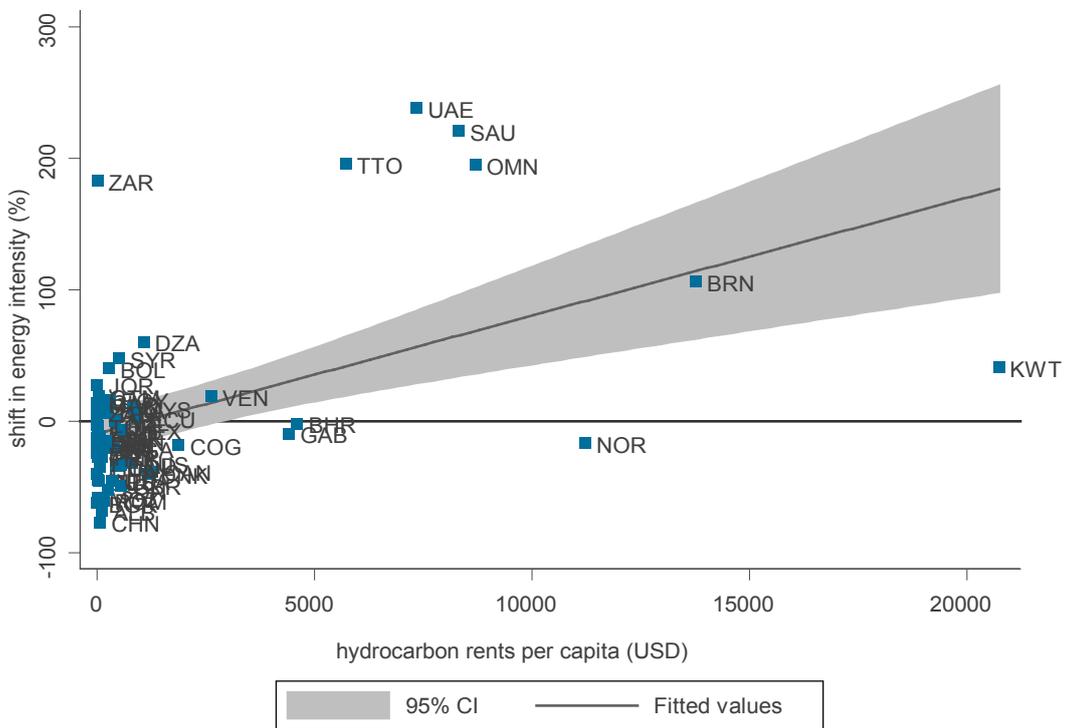
³¹ The improvement in energy efficiency in MRCs from the mid-1990s is partially, but not wholly, driven by former Soviet republics.

³² Equatorial Guinea, Qatar and Libya are not included in the calculation, as no data are available for most years.

Relative to the rest of the world, HRC energy intensity has increased by 150 percent since 1980. Saudi Arabia is now using as much energy as the UK, a country with more than twice the Saudi population and 3.6 times its GDP. As Figure 6 shows, this result is not driven by individual HRCs.

Figure 6. Rents Per Capita and Shifts in Energy Intensity, 1980–2010.

Source: Based on World Development Indicators data.



The relationship disappears if HRCs are excluded from the comparison (Figure 7). Conversely, it continues to hold even if the sample is limited to non-OECD countries and/or only rentier countries above USD 500 per capita rents.

Figure 7. Rents Per Capita and Shifts in Energy Intensity without HRCs, since 1980.

Source: Based on World Development Indicators data.

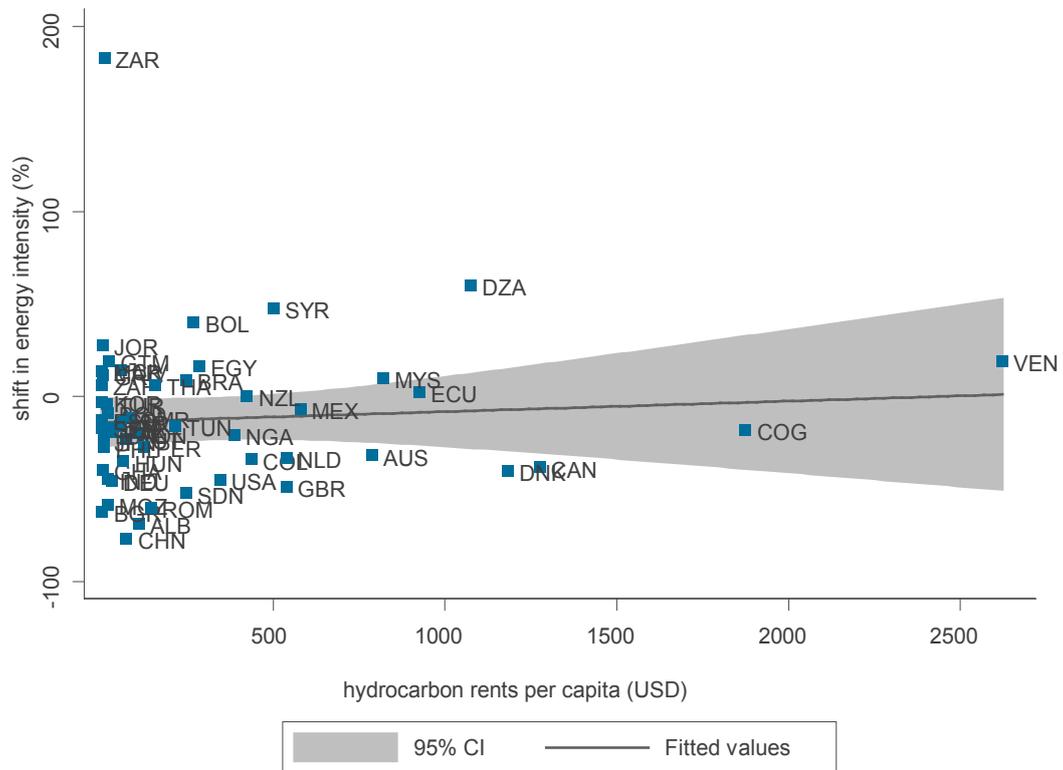
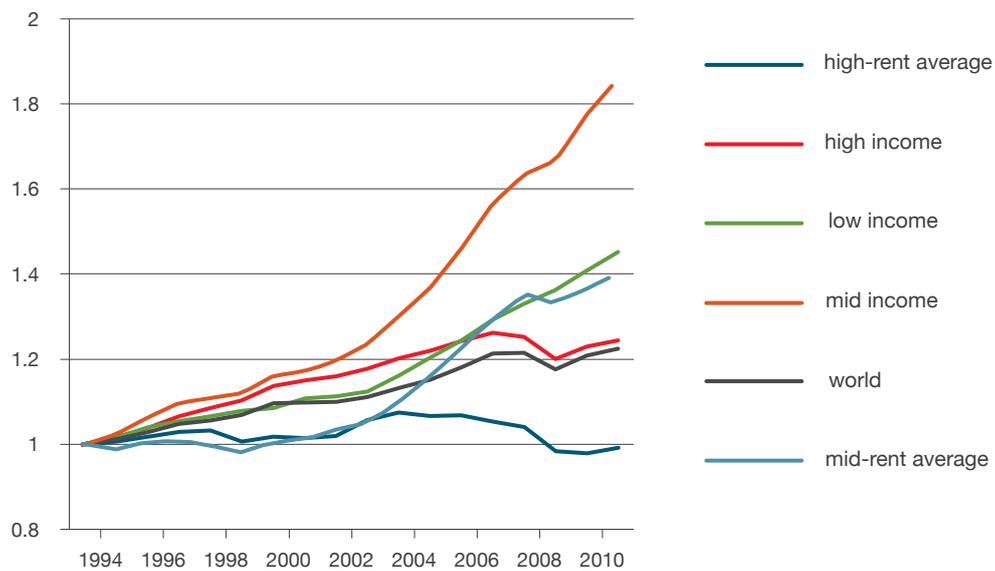


Figure 8 shows a similar trend over time with regard to labour productivity, where incentives in HRCs are similarly skewed due to the availability of low-cost foreign workers and the limited availability of skilled national labour for productive employment.³³

Figure 8. Output Per Member of the Labour Force (constant 2005 USD; 1994 = 1).

Source: Based on World Development Indicators data.



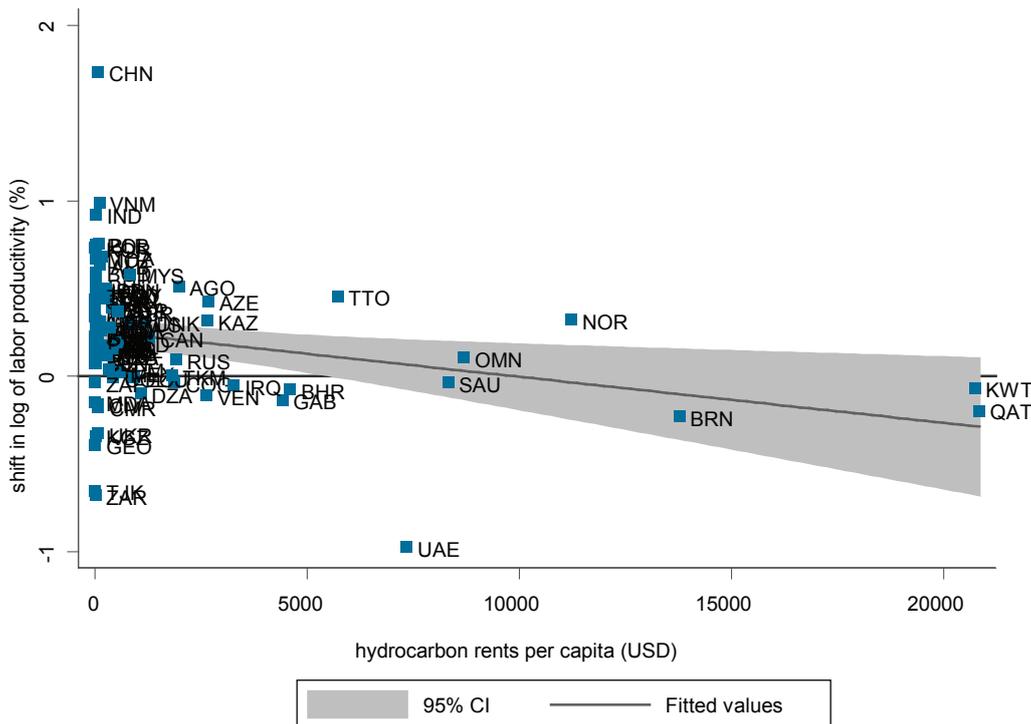
Note: Mid-income countries are standardised at 1 in 1993 due to lack of earlier data. Note that the graph does not measure labour productivity strictly speaking, as the unemployed are not taken out of the labour force due to a lack of reliable time series data on unemployment in HRCs. It is unlikely, however, that unemployment levels shifted so strongly, and differentially over time in different country groups as to affect relative orders of magnitude.

³³ Growth results are not discussed here, as in HRCs even the growth patterns of non-oil sectors are too strongly influenced by oil price developments and hence very dependent on the time window chosen for longitudinal comparisons.

As Figure 9 shows, there is a statistically significant relationship between rents per capita and the shift in labour productivity from 1990 to 2010.³⁴

Figure 9. Shifts in Labour Productivity and Rents per Capita, 1990–2010.

Source: Based on World Development Indicators data.³⁵



In line with our expectations, the one non-migrant economy among our HRCs, Trinidad and Tobago, was the only one to witness any substantial improvements in productivity,³⁶ while also maintaining relatively high citizen labour market participation and low unemployment.

³⁴ The earliest year for which time series data are available for most countries is 1990. All countries whose productivity time series started before 2001 were also included (with productivity data from the earliest available year used in the denominator). This, if anything, flattened trends over time; the omission of such cases did not materially change results. Equatorial Guinea was left out of the estimates as data indicated a 15-fold increase in productivity, which, given the country's widely reported development failures, appears highly implausible.

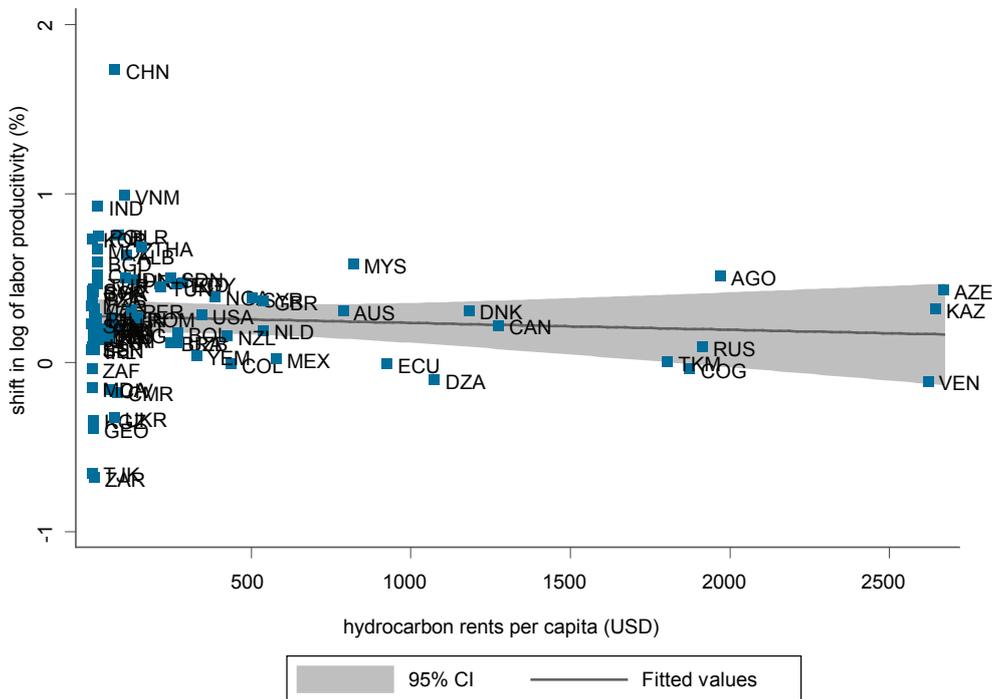
³⁵ The change in labour productivity is measured in log terms to make sure that increases and decreases are measured on the same scale. Statistical tests (see Table 2) yield essentially the same results if change is measured in percentage terms.

³⁶ See also 'Trinidad and Tobago: 2006 Article IV Consultation – Staff Report', *IMF Country Report* 07/10 (Washington, DC, 2007), p. 20.

Again, as Figure 10 shows, the correlation disappears when HRCs are taken out of the sample.³⁷ And conversely, the relationship once more persists even if only countries with rents above USD 500 per capita are included and/or OECD states are excluded.

Figure 10. Shifts in Labour Productivity and Rents per Capita without HRCs, 1990–2010.

Source: Based on World Development Indicators data.



Some simple cross-sectional OLS (ordinary least squares) regressions give us further confidence in the robustness of the relationship and provide additional hints as to the causal processes at work (data are insufficient for a full panel specification that could allow more conclusive tests).

Table 2 shows that hydrocarbon rents per capita are a significant and substantial predictor of a decline in productivity from 1990 to 2010. In the simplest model, an additional USD 1,000 of rents implies a productivity loss of about 2.6 percent (column 1). For a country with per capita rents of USD 10,000 (which Oman, Saudi Arabia and Equatorial Guinea are close to), the predicted loss amounts to 22 percent; for a country with rents of USD 20,000 (less than Qatar and Kuwait had in 2010), it reaches 40 percent (as the dependent variable is logged, the percentage effect is not scale-invariant).

Just like growth, labour productivity in standard macro-economic models is influenced by a

³⁷ Gengler, *Group Conflict*, points to a similar phenomenon regarding the widespread regressions of democracy scores over levels of rent.

number of structural variables, most importantly an economy's capital stock and the quality of its human resources.³⁸ Rents per capita could be correlated with either, and hence both need to be controlled for. The inclusion of gross fixed capital formation as a control variable does indeed much improve the fit of the model, but hardly changes the effect of rents (column 2). The rent effect also survives the addition of the average secondary enrolment ratio from 1990–2010 as a control variable, which can be taken as a rough measure of the citizen population's skill level (column 3).

Rents only become insignificant when the share of migrants in the population is added to the model, tentative evidence that an important causal mechanism linking rents and productivity losses might indeed be the dominance of low-skilled foreigners in the private labour market (column 4).³⁹ As we would expect, the share of migrants itself has a (weakly) significant negative effect on productivity in model 4, which just about slips into insignificance if secondary enrolment is included as a control variable, resulting in the loss of 16 observations (column 5).⁴⁰ None of the significant effects of rents in Table 2 obtain if HRCs are left out of the model.

³⁸ For a classical theoretical and empirical statement on determinants of growth, see N. Gregory Mankiw, David Romer and David N. Weil, 'A Contribution to the Empirics of Economic Growth', *Quarterly Journal of Economics* 107/2 (1992), pp. 407–37.

³⁹ Including the share of individuals with secondary education in the labour force as a control variable has a similar effect to the inclusion of migrants, which is likely to be the case because in HRCs the composition of the labour force (as opposed to school-age enrolment ratios) is strongly impacted by the presence of migrants. This argument is also made by Gassan Al-Kibsi, Claus Benkert and Jörg Schubert, 'Getting Labour Policy to Work in the GCC', *McKinsey Quarterly*, special edition (2007), pp. 19–22; also by 'Labour Market Reforms to Boost Employment and Productivity in the GCC', *International Monetary Fund*. Available at <http://www.imf.org/external/np/pp/eng/2013/100513.pdf> (accessed 13 October 2015).

⁴⁰ The results in models 1 and 2 survive a number of robustness tests such as the inclusion of an OECD dummy, that of an Arab world dummy, the omission of OECD cases and that of the UAE as an influential case; rents in model 3 become insignificant in some of the robustness tests, but the direction and size of the estimated effect remain similar. Rents also remain significant in models 1 and 2 if they are estimated only for the 27 rentier states having per capita rents of at least USD 500, while capital formation ceases to be significant, indicating that returns to capital in rentier countries might be uniquely low. The latter effect is confirmed by a model that controls for the interaction of rents per capita with capital formation, which turns out to have a negative impact at $p < .1$ (while results for the individual rent, capital formation and migrants variables remain similar to those in column 5). A similar model with an interaction term for rents and migration, by contrast, is not significant.

Table 2. OLS Regressions with Change in Logged Labour Productivity 1990–2010 as a Dependent Variable.⁴¹

Model	1	2	3	4	5
Hydrocarbon rents per capita (USD '000 in 2010)	-.026*** (0.001)	-.025*** (0.009)	-.021** (0.009)	-.007 (0.013)	-.005 (0.013)
Gross fixed capital formation (percent of GDP, 1990–2010 average)		.038*** (.007)	.035*** (.009)	.037*** (.007)	.035*** (.009)
Secondary enrolment ratio (percent, 1990–2010 average)			-.0006 (.001)		.000 (.001)
Migrants (percent of population in 2010)				-.007* (.004)	-0.006 (.004)
Constant	.259*** (.041)	-.566*** (.168)	-.474** (.201)	-.523*** (.167)	-.487** (.199)
Adjusted r-squared	0.063	0.2707	0.1974	0.289	0.2154
N	89	87	71	87	71

The above is suggestive rather than conclusive and does not provide clear-cut causal identification. Even if the core link holds true, there could be other causal channels linking high rent levels to productivity declines (although there is no good evidence that the quality of institutions, one of the most prominent variables in the resource curse debate, is one of them).⁴²

In descriptive terms, it is clear, however, that growth in HRCs has been factor-intensive, relying on rapidly growing inputs of energy and cheap labour, while witnessing declining productivity. While the national labour force is parked in the public sector, most of the work in the private sector is done by cheap, low-skilled and low-productivity migrant workers.⁴³ The available studies about total factor productivity – which is, roughly speaking, the efficiency at which inputs like capital and labour are utilised – also show it as stagnating or

⁴¹ Standard errors are reported in parentheses. *, ** and *** indicate significance at the 90 percent, 95 percent and 99 percent level, respectively.

⁴² Adding the World Bank's 'Country Policy and Institutional Assessment' variable to models 1 or 2 reduces the number of cases to 25; its coefficient is insignificant (as is that for rents, which, however, switches to positive in both cases). Perhaps more conclusively, the HRCs' average score on the World Bank's 'Government Effectiveness' indicator is 0, equivalent to the global average. The average score of the MRCs – which evince better productivity trends than the HRCs – is -0.7, two thirds of a standard deviation below the global average. Similar patterns apply for other measures of institutional quality. This indicates a potentially curvilinear relationship between rents and institutional quality which cannot explain the observed productivity trends.

⁴³ For a general case that public sector over-employment can hamper economic growth, independent of the role of migrant labour, see Alan Gelb, John B. Knight and Richard H. Sabot, 'Public Sector Employment, Rent Seeking and Economic Growth', *Economic Journal* 101 (1991), pp. 1186–99.

falling in HRCs,⁴⁴ including in the non-oil sector.⁴⁵ While this might indicate optimal use of available, very cheap labour, it prevents the technology development, diversification and private employment of nationals that all HRCs aspire to in their development plans.

Large-scale employment of foreigners also results in a high share of labour remittances in non-hydrocarbons GDP (at an average of 12 percent),⁴⁶ thereby reducing private demand generation in the domestic economy. The ratio of public to private consumption is on average twice as high in HRCs as in both MRCs and non-rentiers.⁴⁷

Political Economy Outcomes

There is one more consequence of nationals' weak presence in private employment: a weak interest on their part in privately driven economic development and a lack of shared interests with the capitalist class. While this cannot be proven with hard data, Michael Herb has illustrated this pattern convincingly in a paired comparison of economic policy in the UAE and Kuwait. Because few citizens in these countries are privately employed and business contributes almost no taxes that could finance public services, nationals have no rational interest in a thriving private sector – which has led the Kuwaiti parliament to pursue populist public employment and subsidy policies consistently and undermine government attempts to support privately driven diversification. Pro-business policies in the UAE could only be pursued by an authoritarian leadership.⁴⁸

In HRCs – especially the very richest ones – citizens and capitalists face an unusually harsh zero-sum game in which both vie for a larger share of the distributional pie while having little of the shared interest in capitalist development that underpins compromise between classes in advanced economies.⁴⁹ To the extent that citizens' populist demands are fulfilled in the shape of excessive government employment, their incentives to acquire relevant skills and seek private employment are further undermined, in turn weakening their interest in private sector development. Business for its part demands and becomes more dependent on migrant workers, the consequences of which have been discussed above. The political economy of HRCs can create a self-reinforcing anti-development equilibrium.

The lack of shared class interests can undermine developmental policies particularly if regimes are sensitive to popular sentiment. In HRC cases where the private sector is weak

⁴⁴ 'Gabon: Selected Issues and Statistical Appendix', *IMF Country Report* 05/147 (Washington, DC, 2005), p. 29. 'Qatar: 2010 IMF Article IV Consultation – Staff Report', *IMF Country Report* 11/64 (Washington, DC, 2011), pp. 47f. 'World Bank, Socialist People's Libyan Arab Jamahiriya: Country Economic Report', *World Bank Social and Economic Development Group, Middle East and North Africa Region* 30295-LY (July 2006), p. 29. Available at <http://siteresources.worldbank.org/INTLIBYA/Resources/libyacountryeconomicreport.pdf> (accessed 13 October 2015).

⁴⁵ 'Labour Market Reforms', *IMF*.

⁴⁶ Based on World Bank remittance data.

⁴⁷ UNSTATS data.

⁴⁸ Herb, 'Nation of Bureaucrats'. Further evidence of populist anti-business sentiments among the citizens of Gulf monarchies is adduced by Steffen Hertog, 'The Private Sector and Reform in the Gulf Cooperation Council', *LSE Kuwait Programme Paper Series* 30 (London, 2013).

⁴⁹ On 'class compromise' in mature capitalist countries see Adam Przeworski, *Capitalism and Social Democracy* (Cambridge, 1986).

but public employment extensive – Libya, Brunei and to a lesser extent Gabon – there is less of a class conflict, but arguably little citizen interest in developing the private sector in the first place.

Summary

The above empirical sections have demonstrated that HRCs form a distinct class of resource-rich state. HRCs evince a fairly uniform pattern of costly and often inequitable domestic rent distribution in the shape of cheap energy (as some other developing and rentier countries also do) and excessive public sector employment (on a scale unique to HRCs). Arguably as a result, HRC economies are characterised by strongly declining energy efficiency and – in combination with open labour migration regimes – declining labour productivity.

The inequity and negative externalities of the status quo should be a concern under all circumstances. Inefficient use of resources and lack of non-oil private-driven growth and development might not be an issue if HRC resources were infinite. They are not, however. There is no space for a discussion of fiscal breakeven prices of oil and gas here, but we know that they have increased rapidly for most HRCs in recent years – a pattern that is typically hard to reverse, especially when it involves entitlement spending – and HRCs might soon be eating into their reserves.⁵⁰ Energy consumption and public employment costs typically have been rising considerably above population growth, a trend that could only be sustained if energy prices continued increasing forever – an unlikely scenario.

As HRCs approach the limits of their fiscal capacities, inefficiency and rapid growth of resource consumption are becoming problematic. Insufficient investment into productive skills and assets as well as low levels of private demand generation mean that HRCs are ill-prepared for the time when state spending will have to plateau and shrink.

⁵⁰ ‘Regional Economic Outlook: Middle East and Central Asia’, *IMF* (Washington, DC, 2012), p. 93. ‘Middle East and North Africa: Defining the Road Ahead’, *IMF Regional Economic Outlook Update: Middle East and Central Asia Department*, May 2013. Available at <http://www.imf.org/external/pubs/ft/reo/2013/mcd/eng/pdf/mcdreo0513.pdf> (accessed 13 October 2015). Paul Stevens and Matthew Hulbert, ‘Oil Prices: Energy Investment, Political Stability in the Exporting Countries and OPEC’s Dilemma’, *EEDP Programme Paper* 2012/03 (October 2012). Available at http://www.chathamhouse.org/sites/default/files/public/Research/Energy,%20Environment%20and%20Development/1012pp_opec.pdf (accessed 13 October 2015).

The Challenge of Distribution and the Citizens' Income Concept

Rent distribution in HRCs is a political fact; even the most authoritarian ruler would find it difficult to rescind his material obligations towards his subjects.⁵¹ Quite apart from political exigency, the moral case for sharing national wealth with the population is cogent, as citizens are its rightful owners.⁵² The relevant policy question hence becomes how to reform distribution.

How should distribution be reorganised in an ideal world? Four basic criteria appear to be relevant. Rent recycling should:

- provide the largest and most widespread economic welfare for citizens;
- minimise distortive incentives regarding energy consumption, technology choice and productivity;
- help to integrate the citizenry into the national economy; and
- not undermine the long-term fiscal basis of the state.

This paper proposes a general and unconditional cash grant to all adult HRC citizens, combined with and financed through energy pricing and public employment reform, as the most appropriate means to achieve the above objectives. Although it will not by itself be able to fulfil all the above aims conclusively, it can achieve important improvements on all of them.

General Arguments for Cash Grants in Rentier States

There is a great deal of literature arguing for a tax-financed, unconditional basic income for citizens of advanced economies.⁵³ The discussion here will initially focus on literature specific to rentier states; we will later draw on the general basic income literature when discussing cash grants' specific implications for HRCs as well as potential objections to them.

There are real-world precedents for regular cash grants in a number of rentier economies, including Iran, Bolivia and Alaska.⁵⁴ These experiences have been accompanied by a growing

⁵¹ Only the regime in Equatorial Guinea seems to share remarkably little of its wealth with the wider population.

⁵² Paul Segal, 'Resource Rents, Redistribution, and Halving Global Poverty: The Resource Dividend', *World Development* 39/4 (2011), pp. 475–89. Leif Wenar, 'Property Rights and the Resource Curse', *Philosophy & Public Affairs* 36/1 (2008), pp. 2–32. An unconditional basic income scheme has been supported as compensation for the infringement of common ownership rights more generally; see Philippe Van Parijs, 'Competing Justifications of Basic Income', in Philippe Van Parijs (ed.), *Arguing for Basic Income* (London, 1992). This argument is all the more pertinent in the rentier state context. For a global variant of resource-based cash grants, see Thomas W. Pogge, 'An Egalitarian Law of Peoples', *Philosophy & Public Affairs* 23/3 (1994), pp. 195–224.

⁵³ For a concise statement see Philippe Van Parijs, 'Basic Income: A Simple and Powerful Idea for the 21st Century', presented at the Basic Income European Network VIIIth International Congress, Berlin, 6–7 October 2000.

⁵⁴ Paul Segal, 'How to Spend It: Resource Wealth and the Distribution of Resource Rents', *LSE Kuwait Programme Paper Series* 18 (London, 2011). Hamid Tabatabai, 'The "Basic Income" Road to

discussion about subsidy reform and cash grants for resource-rich economies in general, notably in the pages of *World Development*.⁵⁵ The Center for Global Development is undertaking a full research initiative on rent-financed cash grants in resource-rich states.⁵⁶

There are numerous general arguments for rentier cash grants: compared to existing subsidy systems that privilege insiders and rich households they are more equitable,⁵⁷ less distortive of consumption decisions and more transparent.⁵⁸ Compared to means-tested support systems, they are easier to administer, generate smaller overheads, and are less prone to stigmatisation and errors of exclusion.⁵⁹

Cash grants could keep at least part of the state's resource revenues out of the hands of self-interested politicians, thereby reducing corruption.⁶⁰ They could impart a sense of ownership to citizens, increasing their 'buy in' to the political system,⁶¹ and create both a constituency for sound natural resource management and a more level playing field between state and citizens.⁶² Pressures for fiscal transparency and accountability could increase, especially if cash grants are combined with the introduction of a broad-based tax system.⁶³

By providing a secure revenue stream to citizens, cash grants could boost private investment, entrepreneurship and the development of local markets, including financial ones.⁶⁴ Authors in the cash grants literature – including the broader discussion on conditional cash grants in developing countries in general – have adduced considerable evidence that private agents are adept at investing their money well and at smoothing their consumption over time in case of windfalls.⁶⁵

Reforming Iran's Subsidy System', presented at the 13th International Congress of the Basic Income Earth Network (BIEN), Universidade de São Paulo, São Paulo, Brazil, 30 June–2 July 2010.

⁵⁵ Martin E. Sandbu, 'Natural Wealth Accounts: A Proposal for Alleviating the Natural Resource Curse', *World Development* 34/7 (2006), pp. 1153–70. Segal, 'Resource Rents'.

⁵⁶ Todd J. Moss, 'Oil to Cash: Fighting the Resource Curse through Cash Transfers', *SSRN Scholarly Paper* 1824605 (Rochester, NY, 2010). Available at <http://papers.ssrn.com/abstract=1824605> (accessed 13 October 2015).

⁵⁷ Sandbu, 'Natural Wealth Accounts'.

⁵⁸ Todd J. Moss, 'Oil to Cash'.

⁵⁹ Segal, 'Resource Rents'.

⁶⁰ César Baena, Benoît Sévi and Allan Warrack, 'Funds from Non-Renewable Energy Resources: Policy Lessons from Alaska and Alberta', *Energy Policy* 51 (2012), pp. 569–77. Nancy Birdsall and Arvind Subramanian, 'Saving Iraq from its Oil', *Foreign Affairs* (July/August 2004). Available at <http://www.foreignaffairs.com/articles/59923/nancy-birdsall-and-arvind-subramanian/saving-iraq-from-its-oil> (accessed 13 October 2015).

⁶¹ Thomas Palley, *Combating the Natural Resource Curse with Citizen Revenue Distribution Funds: Oil and the Case of Iraq* (Washington, DC, 2003).

⁶² Alan Gelb and Sina Grasmann, 'How Should Oil Exporters Spend Their Rents?', *SSRN Scholarly Paper* 1660570 (Rochester, NY, 2010). Available at <http://papers.ssrn.com/abstract=1660570> (accessed 13 October 2015). Alexandra Gillies, 'Giving Money Away? The Politics of Direct Distribution in Resource Rich States', *SSRN Scholarly Paper* 1824444 (Rochester, NY, 2010). Available at <http://papers.ssrn.com/abstract=1824444> (accessed 13 October 2015).

⁶³ Sandbu, 'Natural Wealth Accounts'. Segal, 'Resource Rents'.

⁶⁴ Gelb and Grasmann, *How Should Oil Exporters Spend Their Rents?*. Palley, *Combating the Natural Resource Curse*. Sandbu, 'Natural Wealth Accounts'.

⁶⁵ Birdsall and Subramanian, 'Saving Iraq'. Alan Gelb and Stephanie Majerowicz, *Oil for Uganda – or Ugandans? Can Cash Transfers Prevent the Resource Curse?* (Washington, DC, 2012). Sandbu, 'Natural

The above arguments generally also apply in the HRC context, although with some nuances: with the exception of Gabon and Equatorial Guinea, corruption is a less acute problem in HRCs than in MRCs;⁶⁶ conversely, as we have seen above, the need to develop private markets (and employment) is arguably even larger. The main ambition of this paper, however, is not to scrutinise the validity of existing rentier cash grant arguments in detail, but to analyse such grants' specific and additional implications for HRCs, which the following sections do.

Energy Consumption

The rationale and implications of providing a citizens' income in lieu of energy subsidies are quite straightforward and to some extent already covered in the literature. We have seen that energy subsidies favour the rich and have particularly distortive economic effects in HRCs. The need to reform energy subsidies is widely accepted by now across the developing world, and substituting less distortive welfare measures, including cash grants, for cheap energy has become a standard policy recommendation.⁶⁷ In fact, Iran introduced unconditional cash grants as compensation for higher energy prices from 2010 on. Although the programme has met some elite-level political resistance, popular resistance has been limited, not least because, unlike means-tested welfare schemes, it included all citizens.⁶⁸

Higher energy prices would help reduce energy consumption both through immediate price effects and by providing longer-term incentives to choose more energy-efficient technology and lifestyles. Drawing on panel data of 66 countries, Charap et al. estimate a long-term price elasticity of energy consumption of 0.3 to 0.5.⁶⁹ This indicates considerable energy savings potential in HRCs: on the modest assumption that HRC energy prices could be doubled, consumption would decrease by between 19 and 29 percent given Charap et al.'s elasticity estimates.

Less consumption would both reduce negative environmental externalities and help HRCs to preserve hydrocarbons export capacity (or at least reduce their need to maintain expensive extra production capacity), thereby helping finance the cash grants. Given the highly skewed distribution of energy consumption and the typically larger utility of cash than of subsidies in kind, it should be possible to improve the material situation of the vast majority of citizens on a fiscally neutral basis. The large elasticity estimates also show that technology choices react strongly to price signals; HRCs would hence be likely to leave the path of declining energy efficiency and move away from subsidy-dependent production.

Wealth Accounts'. Chang-Tai Hsieh, 'Do Consumers React to Anticipated Income Changes? Evidence from the Alaska Permanent Fund', *American Economic Review* 93/1 (2003), pp. 397–405.

⁶⁶ The average HRC score for the World Bank's 'Control of Corruption' indicator is close to the global average of 0, while the average for MRCs is -0.9 , almost a standard deviation below the average.

⁶⁷ Benedict Clements et al., 'Case Studies'. As recent riots in Nigeria have shown, increasing energy prices without compensatory measures can be politically risky; see Adam Nossiter, 'Under Pressure, Nigerian President Relents on Gas Price', *New York Times*, 16 January 2012. Available at <http://www.nytimes.com/2012/01/17/world/africa/nigerian-president-rolls-back-price-of-gasoline.html> (accessed 13 October 2015).

⁶⁸ Benedict Clements et al., 'Case Studies', pp. 30f. Tabatabai, 'Basic Income' Road'. The Iranian programme is somewhat different from the citizens' income proposed here as the former's grants are paid to heads of household rather than individuals, giving it a patriarchal bias.

⁶⁹ Charap et al., *Energy Subsidies*.

Labour Markets

The rationale and impact of providing an HRC citizens' income in return for reduced public sector employment are somewhat more complex, but of potentially even larger developmental import. As explained above, public sector over-employment is a costly and inequitable tool of wealth distribution, undermines government effectiveness and has resulted in the exclusion of HRC citizens from the private labour market, which is typically dominated by cheap migrant labour and characterised by declining labour productivity.

Creating a citizens' income in return for more selective public sector employment could help mitigate all of these issues. As we will see, arguments from the general basic income literature are more relevant than those of the rentier cash grants debate, and are particularly applicable in the HRC context.

How would public sector employment be reduced? In practice, it could prove difficult to dismiss significant numbers of the existing stock of public employees (even if they received a cash grant guarantee in return), but the grants could be used to justify much more selective and needs-based future recruitment. It should be easier to persuade future labour market entrants to exchange the more or less vague hope of future public employment for a concrete and lifelong – if more modest – entitlement. For incumbent public sector employees, the citizens' income should be incorporated into their existing salaries – which *de facto* already include a strong rent-sharing component – rather than paid on top of them, to avoid making (scarcer) government employment even more attractive.

The delinking of public employment and rent distribution would make wealth sharing broader, less exclusive, less discretionary and much less distortionary in terms of labour market incentives. Incentives provided by a citizens' income would be very likely to increase citizens' private employment. Due to the reduction in public jobs and the cash grant's income effect, its net effect on citizens' total labour market participation is ambiguous; if higher participation is taken as a policy objective, further complementary policies would be necessary, particularly among HRCs with very high rents.

Under unconditional cash grants, citizens would not have to take on idle, often unrewarding government jobs to share in the country's wealth but would be free to pursue their own preferences, including on the private labour market. Although the size of the private employment effect is hard to estimate and would depend on grant level as well as prevailing wage levels, it appears clear that with prospects of an easy public job more remote, at least some citizens would seek other sources of work income.

In this context, the citizens' income would function somewhat analogously to an unconditional wage subsidy.⁷⁰ Nationals could achieve acceptable total income levels even if holding less well-paid jobs than currently, as their citizens' income would top up their private sector wages without penalty. It would allow them to compete in lower-wage labour market segments currently dominated by migrant workers. Incentives to perform would be stronger, as the public sector's low effort benchmark would be more remote.

Private jobs would also become more attractive compared to government employment as the

⁷⁰ Not strictly analogously, as wage subsidies are only paid when an individual is in paid employment.

wage gap between the two would be narrowed by the amount of the citizens' income. The greater attractiveness of private employment would also incentivise nationals to seek education and skills that are relevant in the private economy and which HRC citizens often lack.

Due to its secure nature, a citizens' income would also give job seekers a better bargaining position vis-à-vis employers than conditional benefits schemes, leading to better job market matching and potentially higher wages. A citizens' income would provide 'the administrative security which will enable many people to take the risk of accepting a job or creating their own',⁷¹ raising the level of citizen entrepreneurship, which typically is very low in HRCs.

It would also function as a quasi 'study grant' allowing nationals to drop out of the labour market occasionally or reduce work engagements to acquire new skills, leading to 'significantly more stepping-stone, training-intensive, often part-time jobs',⁷² thereby improving human capital accumulation, a particularly grave concern in HRCs. Conversely, secure cash grants could make hiring and firing nationals less socially and politically problematic, thereby bringing citizen employment closer to the flexibility that employers currently enjoy with migrant workers.⁷³

Economist James Meade has made the argument that a citizens' income in Western economies would allow full employment without exposing low earners to unacceptably low total incomes.⁷⁴ It is noteworthy that he argued for such a policy in a context in which implementation would be fiscally vastly more complex – and in which the need for income supplements for private employees is much less urgent, as most private sector wages in the West are much higher than in HRCs, despite similar levels of overall wealth.⁷⁵

Compared to a hypothetical (and unrealistic) scenario of no wealth sharing at all, the citizens' income would reduce citizens' private labour supply through a pure income effect.⁷⁶

⁷¹ Philippe Van Parijs, 'Basic Income and the Two Dilemmas of the Welfare State', *Political Quarterly* 67/1 (1996), pp. 63–6.

⁷² Philippe Van Parijs and Claudio Salinas, 'Basic Income and its Cognates: Puzzling Equivalence and Unheeded Differences between Alternative Ways of Addressing the 'New Social Question' (Louvain, 1998). Van Parijs, 'Basic Income and the Two Dilemmas', p. 65.

⁷³ Hertog, 'Comparative Assessment'.

⁷⁴ James Edward Meade, *Full Employment Regained?* (Cambridge, 1996).

⁷⁵ The above arguments apply less clearly to Equatorial Guinea, where civil service employment is limited and hence unlikely to serve as a benchmark for citizens' labour market behaviour. The positive labour market effects of a citizens' income would accordingly be smaller, and the scheme might lead citizens to drop out of the market altogether. Given Equatorial Guinea's small formal economy and severe poverty, cash grants would, however, be likely to have a stronger positive impact on improving basic livelihood as well as micro-entrepreneurship, as they have had in other under-developed countries.

⁷⁶ Some experimental studies in the West have shown that income maintenance schemes have a modest negative effect on the working hours of beneficiaries. Some of this modest effect appears to be due to rising marginal taxes (i.e. a substitution effect), which would not apply in HRCs. See Alice H. Munnell, 'Lessons from the Income Maintenance Experiments: Proceedings of a Conference Held at Melvin Village', *Federal Reserve Bank of Boston Conference Series* 30 (September 1986). Available at http://econpapers.repec.org/article/fipfedbcp/y_3a1987_3ai_3asep_3an_3a30.htm (accessed 13 October 2015). See also Karl Widerquist, 'The Bottom Line in a Basic Income Experiment', *Basic*

It does potentially give recipients the option not to work at all, especially if it is set at a high level compared to available private salaries – a scenario that is more likely (or feasible) among very rich HRCs like Brunei, Kuwait, Qatar and the UAE. Even then, work disincentives are less strong than with conventional means-tested support mechanisms, as unconditional grants would avoid the substitution (or ‘tax’) effects of unemployment assistance or insurance and other forms of conditional income support, where benefits are lost as work is found and/or wages increase.⁷⁷

A case can be made that choosing not to work because one is born wealthy can be a perfectly rational and optimal decision resulting from a widened choice set, superior to forcing citizens into meaningless jobs as a condition of rent sharing. If we take citizens’ higher labour market participation in productive jobs as a social objective, however, complementary reforms aimed at improving private wages would be likely to be necessary. These can only be briefly adumbrated here. They should, however, include improvement in migrants’ rights, notably through allowing them mobility between employers, which would improve migrants’ bargaining position, thereby increasing prevailing wages.⁷⁸ Targeted wage subsidies could also be considered.

Migration reform would be politically and economically easier to undertake if more skilled national labour were available to start with – which citizens’ income and public employment reform would contribute to. They would be likely to result in better albeit fewer jobs for migrants from poor countries – a trade-off that would result from any serious migrant rights reform, on which there seems to be widespread international consensus.

Macro-Economic Implications

We have already alluded to some of the macro-economic effects that a cash grant scheme combined with public sector reform could have: more nationals, with typically higher skills than migrants, would join the private labour market and the market for entrepreneurship; national human resources would be better formed and utilised, which would be likely to lead to higher levels of production and productivity. Businesses themselves would have incentives for productivity enhancements to make better use of a higher-skilled labour force. Complementary migration reform could reduce incentives to rely on (and exploit)

Income Studies 1/2 (2006), pp. 1–5. More recent pilot projects in developing countries – in admittedly quite different socio-economic contexts – have shown no effect on or increases in economic activity among recipients of a basic income. See ‘Basic Income Grant Coalition, Towards a Basic Income Grant for All!’ *Basic Income Grant Pilot Project Assessment Report*, September 2008. Available at www.bignam.org/Publications/BIG_Assessment_report_08a.pdf (accessed 13 October 2015). See also Gelb and Majerowicz, *Oil for Uganda*; Segal, ‘Resource Rents’. In any case, the income effect for more productive workers with higher earnings will be smaller, as the grants will constitute a smaller part of their overall income, further tempering its aggregate impact. See Segal, ‘Resource Rents’.

⁷⁷ Widerquist and Lewis, *Basic Income Guarantee*. Targeted subsidies for low-wage workers (like the Earned Income Tax Credit in the US) would have similar, if weaker, disincentive effects relative to the citizens’ income, reducing work effort and incentives to upgrade one’s skills.

⁷⁸ Suresh Naidu, Yaw Nyarko and Shing-Yi Wang, ‘Worker Mobility in a Global Labor Market: Evidence from the United Arab Emirates’, *NBER Working Paper* 20388 (August 2014). Available at <http://www.nber.org/papers/w20388> (accessed 23 October 2015).

low-skilled foreign workers, further motivating businesses to invest in technology and processes that can use better-skilled workers.

Stronger private labour market participation of nationals would also increase privately generated domestic demand, as a larger share of private earnings would remain in the local economy, thereby reducing the economy's reliance on state spending. The more even income distribution achieved through cash grants would probably also lead to demand growth, as poorer households, which would disproportionately benefit, have a higher propensity to consume.

Political Economy Consequences

In line with the predictions of the rentier cash grant literature, a citizens' income could put state–society relations on a more equal footing, giving more autonomy and imparting a sense of equality to HRC citizens. The effect could be even stronger than in MRCs because in HRCs the client status of citizens tends to be particularly pronounced, as state dependence and reliance on discretionary patronage, including through public employment, are so widespread. Stronger participation in the private labour market under decent income conditions and more widespread entrepreneurship could accelerate the formation of the modern middle class that HRCs by and large lack.

This middle class would develop a vested interest in private-driven growth, paving the way for a potential class compromise with local capital and for stronger demand for industrial, regulatory and educational policies that could undergird the private-driven diversification that HRCs urgently need. Such class compromise would mitigate the vertical divisions and zero-sum conflicts that currently characterise HRC political economies, in which business and citizenry tend to be separate and rival clients in a hub-and-spoke system organised around the distributional state.

Addressing Counter-Arguments

There are many potential counter-arguments to cash grant schemes, both from the general basic income literature and from the literature on rentier cash grants in particular. The following section will address both in turn, showing that neither set of arguments applies to HRCs.

Counter-Arguments from the Basic Income Literature

The most prominent arguments against 'basic income' schemes relate to tax rates, labour market incentives and redistribution.⁷⁹ A basic income in the West, as well as in lower-rent countries under at least some proposals,⁸⁰ would require significantly higher tax rates on middle to high earners, which could lead to battles over redistribution and reduced polit-

⁷⁹ See Van Parjjs, 'Basic Income: A Simple and Powerful Idea', for an overview.

⁸⁰ Sandbu, 'Natural Wealth Accounts'. Segal, 'Resource Rents'.

ical feasibility – one main drawback of basic income schemes compared to other policies.⁸¹ In rentier countries, by contrast, the basic challenge is not how to raise revenue and from whom, but rather how to distribute the existing rent that accrues from outside of the local economy.⁸² HRC fiscal policy is by definition a voluntarist regime that is forced to make decisions on allocation; there is no (immediate) need to build up and justify the extraction of resources from the richer strata of society.

Globalisation is also seen as a challenge to basic income schemes, as high taxes could drive capital and highly qualified labour out of the country; another issue that does not apply to HRCs.⁸³ To avoid the politics of taxation, Van Parijs and Salinas in fact consider the creation of a basic income from some common asset among advanced economies, but concede that this would be likely not to yield enough revenue.⁸⁴ In HRCs, by contrast, it certainly would.

A citizens' income in tax-based systems would potentially decrease work incentives for mid and high earners.⁸⁵ A basic income implies a 'principled though partial disconnection between labour and income'.⁸⁶ This again is not the case for HRCs, at least as far as productive work is concerned: as we have argued above, a well-designed citizens' income would in fact substantially increase private sector work incentives for HRC nationals compared to the status quo.

Closely related, the moral argument that a citizens' income creates a system of free riders clinging to the coat-tail of taxpayers does not apply in the HRC scenario.⁸⁷ Critics of basic income schemes in the West paint a gloomy picture of an army of idle or near-idle citizens living off state-provided payments. In most HRCs, however, the idle armies already exist – including significant parts of the public sector – and are supported in very inequitable ways. There would be fewer of them under a citizens' income.

We have mentioned above that a citizens' income would have an income effect, which could potentially reduce citizens' desired work hours compared to a hypothetical scenario of radical austerity (and, in the status quo scenario, for the small number of nationals already privately employed). It is, however, not clear whether maximising individuals' hours of work is really a socially desirable goal.⁸⁸ This is especially the case in HRCs: as we have seen above, there is currently a shortage of reasonably paid private sector work for HRC nationals; spreading the available jobs across a broader population with shorter working

⁸¹ Van Parijs and Salinas, *Basic Income and its Cognates*.

⁸² Paul Segal, 'How to Spend It: Resource Wealth and the Distribution of Resource Rents', *Energy Policy* 51 (2012), pp. 340–8.

⁸³ Philippe Van Parijs and Yannick Vanderborght, 'Basic Income in a Globalized Economy', in Brigid Reynolds and Seán Healy (eds), *Does the European Social Model Have a Future?* (Dublin, 2012).

⁸⁴ Van Parijs and Salinas, *Basic Income and its Cognates*.

⁸⁵ Van Parijs, 'Basic Income: A Simple and Powerful Idea', p. 15. Widerquist and Lewis, *Basic Income Guarantee*. Note that a higher marginal tax on earnings does not necessarily mean less net income, as every citizen receives an untaxed basic income in addition to her private income. Low-to-mid earners might hence be better off materially although potentially working less due a combination of income effect and tax rate effect.

⁸⁶ Van Parijs, 'Basic Income and the Two Dilemmas', p. 64.

⁸⁷ Philippe Van Parijs, 'Free Riding versus Rent Sharing', in F. Farina, F. Hahn and S. Vanucci (eds), *Ethics, Rationality and Economic Behaviour* (London, 1996).

⁸⁸ Segal, *How to Spend It*, pp. 484f.

hours might be a good idea. While in tax-based production states, more work effort tends to beget a growing economy and more work opportunities, this link is less strong in HRCs, where much growth and demand will remain driven by exogenous rents for a long time. Basic income proponents have made the argument for cash grants as a 'soft strategy for job sharing',⁸⁹ a particularly relevant point for small HRC labour markets.

Counter-Arguments from the Rentier Cash Grant Literature

The literature on cash grants in conventional rentier states also (both implicitly and explicitly) points to a number of potential weaknesses of such schemes. Many authors, for example, assume that individuals will use cash more smartly than governments. A citizens' income in HRCs does not necessarily require this assumption, as its objective of incentivising citizens to join the private labour market would obtain independently of how citizens spent their grants. As important, HRC cash grants could be financed through subsidy reforms and reduced public sector recruitment, thereby attacking particularly inefficient ways of using public resources. Closely related, the argument that cash grants could 'deny a cash strapped government the opportunity of improving the delivery of its services to its citizens'⁹⁰ or deny such a government the opportunity to build critical infrastructure⁹¹ is not relevant to HRCs, whose delivery of public services and infrastructure spending could remain untouched as surplus public sector employment is reduced.

Similarly, at least some variants of the rentier cash grant proposal assume that distributing rents through cash grants will require governments to raise taxes to pay for hitherto rent-financed activities.⁹² While creating a broad-based tax system is a worthwhile long-term objective for HRCs too, it is not a necessary requirement for the creation of a citizens' income. This drastically increases the latter's political and administrative feasibility.

Many of the supporting arguments for rentier cash grants – such as the developmental utility of building taxation capacity, and the creation of a sense of citizen ownership that leads to enforcement of transparency and governance⁹³ – are not required for the citizens' income to make sense in HRCs, where it also stands on other merits.

A final critique of rentier cash grants in the literature is that they might not be administratively feasible in weak states.⁹⁴ There are general counter-arguments to this: many low-capacity administrations have rolled out wide-ranging systems of cash transfers using new technologies such as biometric identification, smartcards and payments into mobile bank

⁸⁹ Van Parijs, 'Basic Income and the Two Dilemmas', p. 64.

⁹⁰ Giorgio Brosio, 'Bypassing Government: Oil Related Conditional Cash Transfers', prepared for presentation at the 24th Annual Meeting of the Società di Economia Pubblica, Pavia, 24 and 25 September 2012, p. 9.

⁹¹ Gelb and Majerowicz, *Oil for Uganda*, p. 9.

⁹² Birdsall and Subramanian, 'Saving Iraq'. Gillies, *Giving Money Away?*. Sandbu, 'Natural Wealth Accounts'. Segal, 'Resource Rents'.

⁹³ These are critiqued in Brosio, 'Bypassing Government'.

⁹⁴ Michael Ross, 'How Mineral-Rich States Can Reduce Inequality', in Macartan Humphreys, Jeffrey D. Sachs and Joseph E. Stiglitz (eds), *Escaping the Resource Curse* (New York, 2007).

accounts.⁹⁵ In any case, with the exception of Equatorial Guinea and to some extent Gabon, HRCs generally have stronger administrative capacity than low- to mid-rent countries.⁹⁶

Two more counter-arguments not present in the literature are worth considering. First, one potential danger of creating a citizens' income is that it might in the future again be complemented by other, less efficient methods of rent circulation. This is why the simultaneous implementation of cash grants and of subsidy and public employment reforms is crucial, and why public awareness of this quid pro quo probably needs to be built before any reforms. It might be difficult to prevent inefficient patronage from seeping back into the system later on, but expanding patronage would be even more likely under a continuation of the status quo scenario. A citizens' income would almost certainly allow a clearer and more effective stance warding off demands for future mass patronage than is possible under the current distributional setup.

Secondly, HRC rulers might just be so self-interested and politically autonomous as to avoid almost any meaningful distribution to the population, thereby making them uninterested in equity and efficiency of distribution. This seems to be the case in Equatorial Guinea.⁹⁷ This problem, however, is not specific to the citizens' income idea: in such cases, no policy prescription about how resources should best be used is of immediate practical relevance, and one might have to wait for a ruler's survival or intended legacy to become contingent on the welfare of his population.

If an HRC regime has any interest in better resource allocation, a citizens' income should in principle be politically feasible, as it would create many more winners than losers. Gillies, moreover, has argued that 'the costs of allocating revenues to citizens will be lower if the leader enjoys some autonomy from inter-factional political competition and if the resource rent is sustainably large'.⁹⁸ The former is the case in all HRCs, the latter arguably in most of them, as they are typically small, authoritarian and centralised, and face low levels of political mobilisation in society.

Policy Design and Feasibility

A detailed discussion of a citizens' income's practical policy design is a subject for future work, but we will nevertheless venture some preliminary observations on grant level, transition arrangements and financing, which are critical for labour market impact and for political and fiscal feasibility.

The level of the citizens' income should ideally be fixed quasi-permanently or at least for a considerable period, the latter possibly by tying it to a long-term moving average of resource income (or subsidy savings). Only in this way will consistent labour market planning be possible for both government and individuals; for the scheme to have its full incentive effects, HRC citizens need a constant, predictable income stream.⁹⁹ At the same

⁹⁵ Gelb and Majerowicz, *Oil for Uganda*. Moss, *Oil to Cash*. Segal, 'Resource Rents'.

⁹⁶ See n. 38.

⁹⁷ Antony Goldman, *Poverty and Poor Governance in the Land of Plenty: Assessing an Oil Dividend in Equatorial Guinea, Oil-to-Cash Initiative Background Paper* (Washington, DC, 2011).

⁹⁸ Gillies, *Giving Money Away?*, p. 16.

⁹⁹ Against this background, a recent proposal of one-off grants for citizens once they reach maturity

time, the scheme might have to be phased in gradually, at least if it is to be financed by subsidy reductions which in turn need to be undertaken in an orderly fashion to allow households and businesses to adjust to new prices. Energy subsidy reforms should also be gradual, to allow the wages of migrants to catch up with the resulting cost-of-living increases – which in turn would be facilitated too by an improvement in migrant workers' labour rights.¹⁰⁰

The financing options for a citizens' income could vary from case to case. Detailed country-by-country estimates are beyond the scope of this paper. To give a sense of the possible magnitudes involved, however, Table 3 shows the estimated size of a monthly cash grant, for all adults aged 20 and older who are not employed in government, that could be financed through the complete removal of energy subsidies as estimated by the IMF for 2011.¹⁰¹ Figures are particularly high in countries with large foreign populations.

Table 3. Monthly Citizens' Incomes Financed by Removal of Pre-Tax Energy Subsidies, 2011 (USD).

Source: Based on IMF and World Bank data, various national reports.

Country	Income
Bahrain	1141
Brunei	411
Equatorial Guinea	26
Gabon	8
Kuwait	4642
Libya	290
Oman	394
Qatar	10072
Saudi Arabia	924
Trinidad and Tobago	77
UAE	5811

appears only a second-best solution. See Giacomo Corneo, 'Stakeholding as a New Development Strategy for Saudi Arabia', *Review of Middle East Economics and Finance* 7/1 (2011), pp. 1–19.

¹⁰⁰ Governments could also consider providing subsidised energy for small households, i.e. up to a certain (low) monthly level of consumption. The inclusion of migrants in this arrangement might, however, be politically hard to justify.

¹⁰¹ The assumption is that any energy not used domestically as a result of higher prices could be exported internationally. At least in the short run, this will not be the case for large exporters like Saudi Arabia; the figures are hence upper-boundary estimates.

In some cases, the grant level would be more than enough to bridge the gaps between citizen wages in the public sector, citizen wages in the private sector and migrant wages in the private sector. In Saudi Arabia, for example, average citizen wages in 2010 were USD 1,900 in government and 1,000 in the private sector, while (typically less-educated) migrant workers earned an average of USD 300 in the private market. The estimated cash grant of more than USD 900 would easily bridge both gaps – if anything, it would be too generous, making at least low-skilled Saudi citizens prefer inactivity to private employment unless complementary labour reforms, as outlined above, served to increase the general wage level on the private market.

In other cases, complementary sources of finance would be needed for a citizens' income to have meaningful welfare and incentive effects. Savings on reduced public sector hiring would only kick in over a longer period, meaning that a substantial citizens' income would initially imply additional spending – which current hydrocarbons prices, government reserves and returns on overseas assets would easily allow.¹⁰²

In the very long run, the citizens' income could potentially be financed entirely out of returns on HRCs' sovereign wealth, and thereby be turned into a permanent revenue stream. Such a scheme has again been proposed for financing basic income provisions in advanced economies,¹⁰³ but would be much more substantial and more easily justified in HRCs.

Conclusion and Outlook

The ambition of this paper has been twofold: first, to document patterns of resource distribution in HRCs and their distinct developmental consequences, which put HRCs into a class of their own within the rentier state universe; and second, to propose cash grants in combination with energy subsidy and public employment reform as a mitigation strategy to minimise the negative impact of rent distribution in HRCs. These policies would improve resource efficiency and productivity, enable entrepreneurship, help to integrate nationals into the private labour market without exposing them to socially unacceptable income levels, facilitate political compromise between social classes, and help put HRCs onto a fiscally sustainable path.

Much further work is required on country-level policy design and quantitative estimates of the impact of different policy packages. The implications of and justifications for a citizens' income will differ somewhat from case to case, but arguments in favour are always strong: this paper's new, HRC-specific arguments are most applicable to HRCs with both large subsidies and public employment (Brunei, Libya and the Gulf monarchies). For the other cases, a different mix of rationales applies, including the existing arguments from the broader cash grants literature, many of the counter-arguments to which are less pertinent

¹⁰² In Gabon and Equatorial Guinea in particular – countries with low energy subsidies, relatively small government sectors and comparatively limited overseas assets – a citizens' income might have to be part-financed through an earmarked portion of regular resource revenue.

¹⁰³ Karl Widerquist, 'An Introduction to Citizens Capital Accounts', in Miriam Kennet (ed.), *Proceedings of the Green Economics Conference: Social Aspects of Green Economics*, Green Economics Institute, (Oxford, 2008). Available at <http://works.bepress.com/widerquist/15> (accessed 13 October 2015).

in the case of HRCs. In the case of Equatorial Guinea and Gabon in particular, cash grants can be justified with weak governance and limited capacity to make good public use of resources, and the fact that relative abundance lessens concerns over having to cut government programmes or to create a broad-based taxation system immediately.

Quite apart from future research on HRCs themselves, their conceptualisation as a distinct category raises important questions for the broader resource curse literature: due to their large resource income, these cases are likely to have an outsize importance for many of the statistical studies in that literature. This paper has shown that the characteristics and maladies of mid-rent and high-rent countries might be quite distinct; conflating the two could hence easily lead to invalid conclusions. Investigating the extent to which existing results might be driven by distinct subsets of resource-rich countries is hence another important avenue of future research.

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