THE PURSUIT OF STABILITY: FINANCIAL LIBERALISATION AND REGIME STABILITY IN SAUDI ARABIA AND IRAN

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Abstract

The stability of the two most dominant regional forces in a region prone to instability is an indication of broader regional stability. Moreover, in the age of financial warfare and free capital movement, understanding the influence of money and finance on political regimes stability is of utmost importance. This research investigates political (in)stability in Saudi Arabia and Iran by exploring the impact of financial liberalisation policies on their political regimes' (in)stability. Using the Most Similar Systems Design, it shows, on the one hand, that Saudi Arabia is politically more stable than Iran, for it enjoys greater levels of financial liberalisation and openness with significant linkages to the international financial system, which boosts growth, incomes, foreign policy, and regime legitimacy. On the other hand, Iran, facing financial sanctions and warfare, limited successful financial liberalisation, and risky foreign policy making is more prone to instability as it fails to achieve growth and higher incomes and sustains inflation and currency crises. The research speculates that future regional stability, among other things, will be influenced by how states in the region conduct their financial liberalisation policy in a way that does not hinder their economic prospect, political stability, and societal cohesion.

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List of abbreviations

EFL	Economic and Financial Liberalisation
EL	Economic Liberalisation
FDI	Foreign Direct Investment
FL	Financial Liberalisation
GDP	Gross Domestic Product
IMF	International Monetary Fund
IRGC	Islamic Revolutionary Guard Corps
MENA	Middle East and North Africa
SA	Saudi Arabia
SAMA	Saudi Arabian Monetary Authority
SOE	State-Owned Enterprises
WWII	World War II

Chapter 1: Introduction

1.1 Overview

The global trend of economic integration has been growing ever since the end of WWII. One Belt One Road and the European Union are few examples of regional integration projects. The common motive between the different integration projects has been the desire to allow efficient allocation of resources, levelling the playing field among competitors, which ensures prices' optimisation for consumers. In pursuit of that and since 1970s, EFL took place guided by neoliberal policies and Washington Consensus and leading to our current global economy where the integration of business cycles, value chains, and national economies is the norm. Among other things, this has resulted in the growing importance of financial industry for political regimes. Furthermore, while it created abundant economic opportunities, it also posed political challenges. For some countries, the yields from adopting liberal policies were high and thus the political support for it. Moreover, it made other countries vulnerable to external shocks and speculative attacks and thus led to political crises and societal discontent.

In recent decades, the MENA has become an integral part of the global economy and EFL increased. Growth of available capital meant that rising regional powers were interested in expanding their business activities in the region's neighbouring countries. This move towards liberalisation was accompanied by great levels of political instability that is still ongoing today. Furthermore, the competition between different political regimes has been translated into conflicts. Wars, forced migration, economic slowdown are few symptoms of the resulting conflicts. In light of this, political regime stability is an important area of research. By exploring how EFL has influenced political regimes' stability in the region, the research draws up conclusions about its future prospects, which is important for the global economy growth.

1.2 Research problem

With around 3.3 trillion dollars GDP in 2017, the MENA region makes about 4.5 % of the world's GDP (ISTIZADA, 2018). Therefore, its stability is important for the global political order, as it constitutes an important resource of natural gas and oil, marine routes, and security. The region's stability is compromised without the stability of its constituting regimes. Since the 1970s, EFL have moved the region towards economic integration, but not political integration. However, mass protests have become a recurring theme in the region, usually demanding a change of economic policies such as better pay, increasing subsidies, and demands for social and health services. In the meantime, a political and economic competition is taking place between two regional rivals who claim to have answers to people economic and political ills. However, both regimes' own political stability is questionable. By investigating regime stability in SA and Iran, the research investigates how EFL decreases/increases regime stability socially, economically, and politically and if so, to what extent and in which ways. Furthermore, reflections on regional stability are presented with some agenda for future research.

1.3 Aims

- Exploring the literature on the impact of EFL on regime (in)stability in SA and Iran.
- Undertaking in-depth cross-case analysis to illustrate the ways by which FL influences regime (in)stability in SA and Iran.
- Drawing up some reflections on FL influence on the future of regional (in)stability in MENA region.

1.4 Research questions

1. Does FL induce regime (in)stability in SA and/or Iran?
2. How can FL induce regime (in)stability in SA and/or Iran?

3. Does FL (de)stabilise the Middle East?

1.5 Research significance

The research is a ground-breaking study on the link between FL and regime stability in the MENA region. Using SA and Iran as case studies, the research lays the foundation for a better understanding of the MENA region and its future stability.

Chapter 2: Literature Review

2.1 Introduction

This chapter explores the settings of the research by discussing EL concept, rationale, process, implications and political entanglements. Furthermore, it addresses the discussion about FL concept, rationale, process, implications and political entanglements. Additionally, the chapter reviews the most recent research on the relationship between EFL and political (in)stability and regime change.

2.2 EL

2.2.1 Overview and definition

EL is defined as the reduction of impediments to the efficient functioning of domestic and international markets (Tower, 1984). Particularly, EL reforms can be defined as the set of policies adopted by the state in order to achieve efficiency in delivering many societal objectives such as political stability, economic growth, poverty reduction, and foreign policy objectives (Chaudhry, 1993, 1994). Generally, the adopted policies include the devaluation of the exchange rate to achieve external balance, restricting the domestic supply of money to reduce inflation and achieve internal balance of budget, and reducing budget deficits by conducting fiscal reforms (Edwards, 1987). The question of how to measure the degree of EL in a country and in the world remains a contested one. This because EL is composed of policies that are sometimes impossible to measure directly and thus inaccurate proxies are used as alternatives. For the purpose of this research, measurement issues are not of concern and a broad qualitative definition is sufficient to understanding the phenomenon.

2.2.2 Distortions EL solves

(a) High inflation or overpriced currency; (b) large fiscal deficit (c) controlled interest rates and weak domestic financial market; (d) impediments to trade in the form of tariffs; (e) capital controls; (f) price distortion due to government intervention (g) corruption, malfunctioning government apparatus, and rent-seeking (Edwards, 1989, 1990).

2.2.3 Reform policies associated with EL

There are various reforms associated with EL. They are usually referred to as the Washington Consensus and were set by the IMF and the World Bank (Williamson, 2004).They include: (1) fiscal reforms to improve the balance of payments such as cutting subsidies; (2) tax reforms such as reducing income tax; (3) trade liberalisation to remove tariffs and other impediments to trade; (4) privatisation of state-owned enterprises, (5) deregulation to increase the competitiveness of industries; (6) labour markets reform such as relaxing rules on part-time work; and (7) bureaucratic reforms such as capacity building. Other reforms are related to FL and will be discussed later.

2.2.4 Successful EL considerations

- First, the sequence of economic reforms. Usually, trade reforms should precede financial reforms (Edwards, 1987, 1989). Political reforms are trickier but, generally, they should follow trade and financial reforms because they will help accommodate the change to societal political culture (Edwards, 1990).
- Second, the pace of reforms. Some scholars argue that gradualism is better while others see that shock therapy is more efficient and expedient (Rodrik, 2004).

- Third, the combination of EL with unorthodox policies. Such combination can help accommodate policies necessary to the particular context such as in China (Rodrik, 2004).
- Fourth, a committed government with domestic and international support (e.g. via aid) (Morrissey, 1999). Long-term government commitment is crucial for market relations and regulations to be enforced (Hays, Ehrlich, & Peinhardt, 2005).

2.2.5 Main implications of EL

2.2.5.1 Growth

As stated earlier, states usually embark on the quest for EL in order to achieve growth. However, the evidence of the link between EL and growth is one of the most contested subjects in economics. Generally, the developed world has benefited from EL and it increased its growth (Dowrick, 2004). However, in the developing world the issue was trickier (Santos-Paulino, 2005). Nonetheless, many scholars agree that GDP and per capita incomes growth were some of the consequences of EL (Greenaway, Morgan, & Wright, 1997, 2002). It is usually argued that growth takes place through two main channels, productivity and capital increases (Rodrik, 2004). Furthermore, technology, factor mobility, and knowledge transfers are usually seen as qualitative growth areas (Rodrik, 1999).

2.2.5.2 Poverty and income

It is undisputable that EL has helped alleviate poverty (Winters, 2002). However, it has also created greater income inequality (Sapri, 2004). Unskilled labour received less income and thus their poverty increased. Skilled labour experienced wage increases, but the wages of the poor dampened. Since women constituted the largest number of unskilled labour, they were the hardest hit by income inequality, which increased gender inequality in developing countries. Furthermore, inflation resulting from floating the domestic currency hurt workers purchasing power while export industries gained a competitive advantage on their expense. Growth, therefore, was not sufficient to tackle poverty or inequality. Consequences of poverty and income inequality have been increased societal unrest and/or revolutions.

2.2.6 The rationale for EL

In the post-colonisation era, the emerging countries strived to assert independence and self-reliance politically and economically. In that process, nationalist, communist, populist, and authoritarian regimes tried to improve the state apparatus and rejuvenate the economy. They followed protectionist economic policies in that pursuit while providing welfare for their citizens as part of their revolutionary promises. However, decreased oil prices, higher interest rates, a slump in real commodity prices, lower inward FDI, international recession, and reduced access to foreign markets contributed to serious balance of payment problems and other forms of macroeconomic instability in many developing countries (McGillivray & Morrissey, 1999). Such reality drove home the realisation that decisive policy interventions were necessary (Chang, 2012). Countries, in response, either went to the IMF and the World Bank for advice and direction, or went on their own and liberalised their economies in order to fix economic distortions.

On the one hand, in the developed world, the logic was clear: as liberal societies prosper, they could benefit from collective actions such as EFL, which would increase individual and societal benefit by maximising resource allocation and profit-making to member of societies (Henderson, Lawson, & Friedman, 2001). However, on the other hand, the rationale in the developing world was different. There was a fundamental rift in ideology and neoliberalism rose converting fiscal crises to political ones. The outcomes of reforms varied across countries. The divergence has been studied thoroughly and attributed to several factors such as the quality of government and technocratic competency, domestic resistance, outside intervention, the initial level of development, and regime type (McGillivray & Morrissey, 1999). Introducing market competition as a driving political force to fix societal distortions in the economic sphere led to reshaping society substantially. For example, while privatising, the new owners gained new political power and rent seeking became harder (Glade, 1989). Subsequently, the growing transnational interest affected and challenged national politics. Those changes were because functioning markets provided opportunities for mobility that undercut lineage and traditional privileges (Chaudhry, 1993). Overall, market reforms threatened the position of the elites in developing societies and destabilise the historical balance of power within society.

2.2.7 The process of EL and its considerations

EL process is governed by many sub-processes, undertaken by various actors, via different policies, and within a broad variety of societal contexts, history, and politics. While crisis and economic hardship were some of the main drivers for reforms, domestic political desires were crucial to ensure its success. Established regimes may have initiated EL insofar it would have improved its own survival. Vested interests, such as protected industries or labour unions, may have resisted EL if they saw it as a threat to their power position. It was only when they were willing to change their own interest whether under pressure or intellectual change; they went along with the government in its pursuit (Dornbusch, 1992). For example, EL saw the rise of new financial relations and elites that emerged to service trade liberalisation, which created strong ties between the banks and business elites and superseded government. If incumbent elites preferred state funding and cronyism, they would have attempted to curtail the government reform efforts. Another strong motive for elites to support EL was their countries being under external military threats, such as South Korea and East European countries (Acemoglu & Robinson, 2006). New technology and political partnerships were seen as necessary for survival in that case. Governments' inability to compensate the losers from reforms gave rise to the politics of resentment and in cases the spread of domestic terrorism (Vannetzel, 2017). The beneficiaries of EL, mostly manufacturing and exporting sectors, were high and rising, but to the detriment of the poorest of the population. Therefore, economic reforms were liable to become entangled in deep-seated regional and ethnic conflicts and created risks such as secession (Chaudhry, 1993).

In a seeming paradox with the competitive market idea, the state and the government were crucial for the potential success of EL (Ehteshami & Miyagi, 2015). Governments needed to introduce regulations and market relations into the economic system and to encourage societal changes (Tanzi, 2011). To create competitive markets, it was not enough to undercut the state bureaucracy that owns, controls, and regulates goods and services. Rather, the instruments of the state needed to be redeployed to perform the tasks of regulating and administrating competitive markets (Tanzi, 2011). Subsequently, the role of governments was as guardians for an ongoing process (Huffman, 2013). Consequently, the government needed to ensure that the domestic market became competitive so that it became competitive in international markets. The choice between gradualism versus radicalism in introducing reforms was not uniform among the reforming countries. On the one hand, proponents of radical reforms argued that radicalism reduced the net cost of reforms in terms of time and resources. On the other hand, its opponents argued that speed would harm the ability of business and labour to absorb the shock in a productive way and cause different kinds of distortions that some countries were not able to deal with. China, for instance, has followed the gradualism path and, among other things, this helped it reap the benefits of reforms with fewer disruptions to the political systems (Ramo, 2004). In Eastern Europe, shock therapy and radical reforms were pursued and caused significant societal and political disruptions (Stevens & Kennan, 1992).

There were many factors that affected the EL process in developing countries. First, the level of economic development was important to the prospects of EL success (Edwards, 2001). Where there was more evolved nascent industries, benefiting from EL was more likely. In countries with greater human capital stock, many received the reforms as opportunities, which made them able to increase income and thus overall economic growth. Second, in countries where income inequality was high, EL may have increased distortions in incomes and deemed the reforms failed or caused societal disruptions or even failure of reforms. Third, a challenging task for the government throughout the process was to convince the public that the reforms were needed and that they should support them (Kaltenthaler, Gelleny, & Ceccoli, 2004). This was proved to be challenging since the public neither was aware of the economic reality of the state nor had a clear agenda on how to run the economy.

Despite the advancement of EL, it still faces some challenges such as behind-the-border barriers (such as different technical standards, safety and environmental regulations, antitrust policies, tax systems, and restrictive national procurement practices) within trade blocs and common markets, which continues to thwart further liberalisation and economic integration (Sadikov, 2007; Hernandez & Taningco, 2010). Lately, the fear of backsliding to protectionism and narrow national interest and the domination of security and power considerations over economic logic is growing. The recent episodes of Brexit and American tariffs against China are few worrying signs. Nonetheless, the emergence of regional rivalry of economic blocks should not be seen as backsliding to economic protectionism. Because liberalisation is still up and running and will, more likely, continue to do so despite setbacks. However, it is foreseeable that phenomena such as authoritarian neoliberalism and far-right populism would continue to persist and potentially expand which will intoxicate the political life of both democratic and non-democratic countries.

2.2.8 Concluding remarks

In conclusion, while EL was pursued in response to crises: political, economic, and financial, it had indeed caused new political, economic, and financial crises. The promise of sustainable growth was not always delivered. Income inequality has significantly increased. However, poverty reduction did indeed take place. Society has responded with greater resentment to EL and its reforms.

2.3 FL

2.3.1 Overview

FL was instigated hand in hand with EL. This is because of the inevitable link between money and the real economy. For EL to work, money needed to be given the freedom to move across countries. Trade surpluses could only be moveable if capital account liberalisation took place. As for prices, liberalising the exchange rate and following a floating system was necessary to avoid price distortions. In this section, the research delves into FL definition, rationale, context, brief history, political economy, and implications. The aim is to see how FL affects society on political, economic, and social levels.

2.3.2 Definition and policy overview

FL took place in developing countries in the 1980s as a part of market reforms (Andrews, 1994). It was a reaction to several factors specific to finance. The first factor, the costs, corruption, and inefficiencies that were associated with using finance as an instrument of state-led development (Zagha, 2005). The second factor, a desire for more financial resources by society (Chipeta, 2012). The third factor, the pressures exerted on repressed financial systems by the globalisation of politics and economics (Andrews, 1994). The fourth factor, the spread of neoliberal ideology and the Washington Consensus policies (Chwieroth, 2007). Therefore, FL can be defined as the elimination of impediments in the financial sector that caused inefficient resources allocation (McKinnon, 1973; Shaw, 1973). That included the privatisation of the banking sector, allowing foreign entry to it, increasing credit extension to the private sector, stock market liberalisation, currency exchange regime liberalisation, capital account openness, and several institutional and regulatory reforms and set ups such as central bank independence (Andrews, 1994). Many researchers and policy advocates argued that the key prerequisites for successful FL were the effective supervision of commercial banks, price stability, fiscal discipline, adequate and efficient competition by banks, appropriate sequencing, and a non-discriminatory tax system imposed on financial intermediaries (Bhattacharya, 1999; Chipeta, 2012).

Many benefits were expected from FL including lowering borrowing cost as cheaper international capital made its way to domestic companies and debtors and better resource allocation due to the elimination of price distortion (Guisinger & Brune, 2017). Furthermore, growth was achieved because more FDI increased domestic investments and savings (Chipeta, 2012). Politically, FL meant more freedoms, which was needed to build adequate capacity, transparency, and accountability in the state apparatus. Particularly, FL gave a political voice to borrowers. This was reflected in a desire for complete liberalisation of their economy to foreign bank entry in order to obtain cheaper credit. As a result, the enlarged borrowing group had diffused interests, which meant they would prefer political openness and democratisation (Andrews, 1994; Pepinsky, 2013). Furthermore, a political voice for foreign investors in the domestic policy processes was granted, reinforcing political liberalisation (Pepinsky, 2013). There were downsides to FL, however. In some cases, FL contributed to the destabilisation of the national and the international economy. For example, greater speculations in financial markets were observed and led to financial crises (Wafa, 2013). FL contributed to increases in anti-capitalist sentiment, societal discontent, and protesting (Funke, Schularick, & Trebesch, 2016). For example, the rise of populism and anti-establishment rhetoric indicates a severe backlash around the world against FL (Frieden, 2018). Lastly, FL led to sanctions on state policy autonomy as it responded to international creditors' expectations not national interest per se. Thus, it destabilised state interests as seen by domestic elites or constituency (Pepinsky, 2013).

As for political actors' support for FL, on one hand, authoritarian regimes, preferred capital controls to channel resources to their political support bases (Girma & Shortland, 2005). Financial repression was preferred as a policy instrument to control resource allocations. Through policies such as public ownership of banks and government allocated credits, authoritarian regimes controlled the national economy and domestic political elites (Girma & Shortland, 2005). Left-wing governments supported when it ensured more jobs, and righ-wing governments supported FL in case it ensured more capital mobility freedom (Li & Smith, 2002). Banking sector supported FL when it helped to get cheap foreign capital, but opposed it if it meant competition from abroad (Pepinsky, 2013). The major political hurdle against FL was that governments were being forced to give away fiscal and monetary autonomy to market forces. By losing control over these policies, governments risked backlash from vulnerable groups who provided political support for FL (Priewe, 2008).

2.3.3 The political economy of FL

Like EL, FL offered mobility to previously underprivileged classes of society especially in developing countries where incumbent regimes were often interested in financial repression so that they could maintain their patronage network and narrow elite interests (Pepinsky, 2013). Free financial markets provided resources to new entrants, who used the resources to compete in the international market by, for example building exporting industries (Haggard & Maxfield, 1996). Governments representing small military/industrial elites that would suffer economically from increased competition and consequential erosion of their political powers may have opposed FL or restricted the entry of new domestic and foreign competitors (Girma & Shortland, 2005; Pepinsky, 2013). The resulting protectionism allowed the domestic elite to arbitrage prices between international and national markets. (Bird & Rajan, 2001; Pepinsky, 2013). Therefore, arbitrage of loans prices and other financial instruments, which generated high profits, but caused a higher cost of borrowing for domestic sectors. Consequently, financially repressive political regimes (e.g. authoritarian regimes) saw weakly developed financial systems and slower development of financial markets (Pepinsky, 2013). This may have led to the failure of FL. Generally, FL could lead to democratisation and democratisation reinforced FL reforms. When competition was introduced into the financial system, political competition ensued (Haggard & Maxfield, 1996). In already democratic societies, support for FL was usually maintainable. In competitive elections, governments can be punished for mismanagement. Building on Acemoglu and Robinson (2006) political replacement effect argument, competition in democratic societies meant that elites wanted innovation and change and thus supported FL. Furthermore, in societies were external threats were imminent; elites may have pursued FL to strengthen alliances with foreign powers (e.g. South Korea and Central and Eastern Europe with the USA). The durability and success of FL were not always assured. Financial and fiscal crises may have constrained or furthered FL (Kose, Prasad, Rogoff, & Wei, 2006).

2.3.4 Implications

2.3.4.1 Growth

There are good proofs for the growth benefits of broad capital account liberalisation (Lajili & Gilles, 2018). For example, a number of papers in the finance literature reported that equity market liberalisations did significantly boost growth (Kose, Prasad, Rogoff, & Wei, 2006). Similarly, evidence based on microeconomic data showed some benefits of financial integration to growth (Kose, Prasad, Rogoff, & Wei, 2006). However, other researchers captured the distortionary effects of capital controls to growth (Henry, 2007; Wafa, 2013). Therefore, evidence on the link between FL and growth via the direct impact of capital accumulation or portfolio diversification is inconclusive. Nonetheless, many studies argued that FL enhanced macroeconomic stability in developing countries, which was good for growth in the long run (Kose, Prasad, Rogoff, & Wei, 2006). However, others were sceptical of this potential as they saw FL causing more speculation, volatility, and instability (Wafa, 2013). Overall, the indirect effects of FL on financial sector development, institutions, regulations, and governance were likely to be far more important than the direct effects in the long run (Bhattacharya, 1999; Kose, Prasad, Rogoff, & Wei, 2006; Lajili & Gilles, 2018).

2.3.4.2 Poverty and inequality

Just like for growth, the impact of FL on poverty reduction and income inequality is still inconclusive. Many papers have argued that FL and FDI inflows favour certain parts in society that are more educated and skilled, while underprivileged semi-skilled labour struggled (Kose, Prasad, Rogoff, & Wei, 2006). This is because they lost state support (e.g. free education) and started relying on private debt to fund their education, healthcare, and housing, which increased their living cost and decreased their ability to save and invest in their future. Furthermore, capital mobility (particularly the threat of capital flight) contributed to the reduction of labour rights and thus made labour more vulnerable as they became subject to speculative investments and hot money (Wafa, 2013). While FL contributed to reducing poverty around the world, it generated income inequalities as unequal growth took place in certain sections of the economy (e.g. services and export industries), but less skilful labour became more underprivileged over time (Jaumotte, Lall, & Papageorgiou, 2013).

2.3.4.3 International scrutiny

Since finance relies heavily on risk assessment, FL made the domestic government more politically averse to crises as they internalised the financial cost incurable in case international investors saw that they are advancing unreasonable or unsustainable policies (Gammoudi & Cherif, 2015). Therefore, the lost monetary sovereignty was translated into a loss of state ability to freely set domestic and foreign policies (Haggard & Maxfield, 1996).

2.3.4.4 Banking, currency, financial crises

FL has been associated with banking crises especially when liberalisation was premature (Zagha, 2005; Almarzoqi, Naceur, & Kotak, 2015). This is because banks went on an uncontrollable spree for cheap international credit without supervision from strong transparent and accountable state agencies (Amri & Willett, 2015; Guisinger & Brune, 2017). Capital account liberalisation has also been linked to currency crises as the state lost control over capital movement and became subject to sudden capital flights that undermined the health of its currency and caused crises (Haggard & Maxfield, 1996; Bird & Rajan, 2001). By becoming part of the international financial system, countries became vulnerable to outside shocks more and the effects of global financial crises influenced their economies more significantly (Amri & Willett, 2015; Luo, 2004). Overall, FL contributed to financial fragility that can only be addressed by prudential policies and macroeconomic stabilisation, which requires strong state apparatus that FL made hard to pursue (Demirgüç-Kunt & Detragiache, 1999; Amri & Willett, 2015; Kose, Prasad, Rogoff, & Wei, 2006). Nonetheless, the globalisation of the financial markets developed the financial system, improved transparency, market discipline and financial infrastructure (Haggard & Maxfield, 1996).

2.3.4.5 FDI and capital flight

At the beginning of FL, inward FDI was seen to be increasing due to high potential profits (Haggard & Maxfield, 1996). However, FDI inflows were reduced and FDI outflows increased over time (Steiner & Saadma, 2016). This dynamic depended on how successful the government ran the economy to ensure adequate returns for investors (Haggard & Maxfield, 1996). As lucrative investments opportunities cease to be, inward FDI decreased (Kose, Prasad, Rogoff, & Wei, 2006). This usually took place under the influence of increased political instability and political risks (Bird & Rajan, 2001). Thus, to maintain attractiveness for FDI, governments needed to promote law and order, democratic accountability, and societal peace (Kose, Prasad, Rogoff, & Wei, 2006; Gammoudi & Cherif, 2015).

2.3.5 Concluding remarks

In conclusion, FL came about as a response to fiscal crises caused by repressive financial systems in developing countries. Failure of financial repression pushed society and governments towards financial openness. This has resulted more political liberalisation. The effect on macroeconomic indicators was positive in the beginning, but became negative over time. Therefore, the way FL destabilises the economy remains unclear. Political and regime instabilities were a natural result of FL, but their durability was not always long.

2.4 Political and regime (in)stability

2.4.1 Overview

After discussing EFL, in this section, the research gives particular attention to the literature on the political implications of undertaking economic and financial reforms. While liberalisation took place mostly as a response to global and national crises, it had created different political implications and crises. These were political instabilities or, in extreme cases, regime changes. The extent to which either would take place is disputable; however, it is well-established in the literature on EL. For FL, the literature on its political implications remains limited. In the MENA context, to the best of the author's knowledge, there has been little to no literature on the topic. Hence, the research importance.

2.4.2 Discussion of the concept of political instability

What constitutes political instability is a highly disputed question. Different measures of political instability use different indicators to suggest different outcomes. As Kjær (2010, p. 9) puts it, "Political instability as qualitative phenomena, are difficult to measure quantitatively and not easily defined. Political instability can be measured by both events and perceptions, the latter being least celebrated. The ambiguity about the meaning of this concept has led to application of a wide range of measures and an array of definitions." Jong-A-Pin (2009) & Sanders (1981) argue that the conception of political instability is multidimensional and includes political violence, civil protest, political regime instability, and within political regime tensions. Alesina and Perotti (1996) argue that income inequality, by fuelling social discontent, increases socio-political instability, which in turn reduces investments by creating uncertainty in the politico-economic environment. In their study, they use two dimensions of political instability, regime-related instability such as coups and instability caused by civil-society such as strikes. Feng (2005) studies political instability as changes of government. He emphasises the difference between irregular and regular government change on the one hand, and major and minor government change on the other hand. Butkiewicz & Yanikkaya (2005) categorises several measures of political instability in Table 1 categories:

Government stability	Social Stability	Political violence
Coups	External conflict risk	Political protests/ Riots/ General strikes
Revolutions/ Government crisis	Civil war risk	Assassinations/ Deaths from political violence
Cabinet changes	Political terrorism	Purges
Anti-government demonstrations	Racial and nationality tensions	War / War casualties

Table 1 Categories of political instability

Barro (1991) uses the number of assassinations and the occurrence of violent revolutions and military coups as proxies for political instability. Hurwitz (1973) thinks of political (in)stability as an encompassing concept of several sub-concepts: (1) stability as absence of violence; (2) stability as governmental longevity/endurance; (3) stability as existence of legitimate constitutional order; (4) stability as absence of structural change; (5) stability as a multifaceted societal attribute; (6) stability as a pattern of behaviour. Therefore, when violence takes place, it can be said that political stability is jeopardised. However, it is not catastrophic for the political order survival. Furthermore, regime endurance does not translate to stability. A political regime can exist using repression. More generally, the legitimacy of the political order is often disputed and does not necessarily mean structural changes and destabilisation of the existing political order. Polarisation, populism, discontent, and protests are societal aspects of political instability, but do not reflect regime instability. Rather, they reflect societal instability. Therefore, Dowding & Kimber (1983) argue that to talk of the instability of a system at a particular moment, it does not follow that the level and nature of instability would not vary over time. For example, Wright & Bak (2016) argue that when destabilising events do not coincide with regime collapse, they are often manoeuvres by elites to prolong their rule and should not be interpreted as a loss of regime stability. Overall, there are various measures of political instability. Thus, political instability is not an abstract concept, but refers to the instability of particular facets of society – those that form the political order and its composing parts.

2.4.3 The international factor

A usually overlooked factor of democratic transition or authoritarian consolidation in most political economics models of regime change is the international factor. EFL can undermine autocracies stability by increasing linkage and leverage with the West, which makes autocrats subject to sanctions and international scrutiny (Levitsky & Way, 2002, 2005, 2006, 2007, 2010). This can contribute to their demise or weakening. However, EFL can offer a window for autocrats to stifle sanctions by increasing ties to authoritarian governments elsewhere such as China and Russia (Tansey, Koehler, & Schmotz, 2017). One important unexplored impact of FL on regime stability is the exposure to financial warfare (Fenaroli, 2016). By sanctions, manufactured currency crises, or forging currency, FL can enable adversaries to gain power over a nation's capital and trade by extension (Zarate, 2013). Using countering terrorism financing as a disguise, states often use financial warfare to achieve political gains and pressure adversaries into political concessions. Furthermore, FL restricts policy-makers' choices in front of international powers. If they control capital movement, they will lose the benefits of access to cheaper capital and FDI, which are important to induce growth and thus societal and regime stability. If they do not control capital flows, they need to learn how to be resilient to avoid catastrophic economic and financial crises. In either case, EFL opens the window for international actors to meddle in domestic politics and thus influence the regime outlook, nature, policy, and even existence.

2.4.4 The macroeconomics of political (in)stability

2.4.4.1 Growth, investment, inequality, and political (in)stability

As previously discussed, growth is a main reason for governments to undertake liberalisation despite other political calculations that could affect the decision. It is, therefore, interesting to investigate how growth affects political (in)stability in a country and vice versa.

Paldam (1998) investigates the relationship to conclude that economic growth generates higher incomes, which makes people approve of the government. Hence, growth generates political stability (e.g. Singapore). Nonetheless, growth generates complex changes in society, and therefore political instability. The author notes that this is likely to happen where the political system is not well-established. Gandhi & Przeworski (2006) argue that regimes become more stable and durable as per capita income increases. However, countries that experiment with democracy at lower income levels experience more political regime instability. Dutt & Mitra (2008) argue that income inequality leads to political instability and political stability increases fiscal, trade volatility, and thus lower investments. Consequently, the growth prospect is harmed (Ramey & Ramey, 1994). Cukierman, Web, & Neyapti (1992) show that political instability correlates positively with inflation, which is negative for growth. Overall, the direction of the relationship between growth and political (in)stability is inconsistent.

2.4.4.2 FDI, capital flight, and financial crises

Kjær (2011) finds that political instability generated by financial crises increase the country risk for investors. Therefore, they may delay or cancel investment decisions, which decreases growth. Furthermore, financial crises can create political instability in the form of political violence and protests. Additionally, financial crises cause higher inflation, which increases political instability. Ades & Chua (1997) found that political instability affects a country's economic growth through disruption of trade and increasing military spending. Funke, Schularick, & Trebesch, (2016) found that policy uncertainty rises after financial crises as governments' majorities shrink and polarisation rises. Haggard and Kaufman, (1995) observed that recession, inflation, and currency collapse deny governments the resources needed to maintain critical support in the population, which raises political discontent and instability. Li (2009) finds that when faced with challenges, democratic and autocratic leaders may decide to expropriate FDI, which stabilises the system on the short-term, but makes them lose in the long term as they lose the confidence of foreign investors and financial markets. However, he notes that governments learned to use subtle expropriation means to avoid that. Consequently, growth is undermined. Gibson and Tsakalotos (1993) concluded that political risk and expected depreciation were significant determinants of capital flight.

2.4.5 The road to regime change or consolidation

As established earlier, EFL cause many political (in)stabilities for a country. One extreme form of political instability is regime change. This is when, due to several factors, a regime ceases to exist and is replaced by another one. In some cases, EFL do not lead to autocratic regime collapse, but to consolidation. In this part, recent studies of regime collapse or consolidation are discussed. Gasiorowski (1995) found strong support to the claim that economic crises trigger democratic breakdowns. In autocracies, Haggard and Kaufman (1995) found that economic crises appeared to accelerate and even cause the collapse of authoritarian regimes in many countries. To exclude such a possibility, autocratic regimes use resources such as foreign aid or natural resources rents to reward members of their support coalition, co-opt potential opponents, and provide public goods to appease potential revolutionary parts of society (Mesquita & Smith, 2010; Morrison, 2009; Smith, 2008). This situation was referred to as a resource curse and was discussed by Auty (1993), Sachs & Warner (1995), and more systematically by Karl (1997) to explain why less economic growth, less democracy, weaker institutions, and worse development take place in resource rich countries. Kakanov, Blöchliger, & Demmou (2018) found that oil-dependent countries suffer from the resource curse, for growth is effected by higher oil prices. Furthermore, "countries allowing their currencies to float seem to gain from positive oil price shocks in the short run, but in the long run a fixed exchange rate regime is associated with higher GDP" (p. 3). Desai, Olofsgård, & Yousef (2009) argue that a fiscal crisis (e.g. lower oil revenues) that raises the cost to the regime in delivering welfare benefits to citizens will drive the regime to extend political rights. Such shift constitutes an opportunity for the opposition to seek regime change. Therefore, regimes lacking resources to resolve these crises find themselves faced with disloyalty, organised violence, a loss of legitimacy, and instability. In such cases, depending on demographic conditions, revenue sources, national wealth, corruption, repression, and political instability, the autocrats might opt for restricted elections to sustain power while seemingly offering concessions to opponents (McFaul, 2002). Similarly, Gandhi & Przeworski (2006) argue that dictators have two instruments to deal with societal discontent. Either to make policy concessions (e.g. more inclusive election) or to share rents (e.g. redistribution of oil revenues or tax cuts). Depending on their assessment of their needs to stay in power, dictators make more extensive policy concessions and share fewer rents if they need more cooperation. In addition, not only do they make larger concessions, but also distribute more spoils when the threat of rebellion is greater.

Boix (2003) discusses how regime survival depends on asset specificity and income inequality. Lower levels of income inequality lead to less distribution, which means elites can accept democracy and its tax rate. Higher inequality reduces the propensity of a society to democratise. Ansell & Samuels (2010) conducted another study to prove that inequality is correctly a key to democratisation. However, they concluded that income inequality is likely to promote democratisation as the bourgeoisie seek assets protection not as the poor threat revolution. Acemoglu & Robinson (2001, 2005) come to similar conclusions as Boix. They argue that high-income inequality increases the incentives for authoritarian elites to repress political demands for redistribution. When inequality is low, regime change will not occur due to the absence of demands for it. Haggard & Kaufman (2012) tests the inequality hypothesis to conclude that it is not always true. Therefore, they offer few alternative explanations, such as the roles of external actors, intra-elite conflicts, and the absence of mass pressure.

Logvinenko (2015) argues that FL does not necessarily lead to democratisation, but can help entrench autocratic rule. Using foreign capital, authoritarian rulers can claim credit for uninterrupted social services and stable employment, which gives them the support of lower classes without needing to change policies. Pond (2018) confirms Logvinenko's findings and argue that: first, autocrats use FL to bolster the economy, making revolution less attractive to the political opposition, which stabilises the autocracy; second, when stabilisation of the autocracy is too costly, autocrats may use liberalisation to make assets more mobile to decrease potential taxes in the case of democratisation and to allow them to threaten capital flight. Pond's model defies two predictions of democratisation theory. First, financial repression stabilises autocracies by channelling rents to supporters and thus autocrats would resist FL. Second, FL leads to democratisation by enabling new political freedoms and thus autocrats would prefer repression to prevent democratisation.

2.4.6 Concluding remarks

In conclusion, scholars do not agree on what insinuates regime change and (in)stability. Some argue that EFL and growth will further democratisation, as what happened in South Korea. However, a case like Singapore attests to the contrary. Furthermore, EFL may strengthen autocratic regimes or undermine them. Regime change indicators are various and result in different outcomes (Lueders & Lust, 2018). The effects of EFL on political (in)stability are large and induce inconclusive generalisable results for political and regime (in)stability. Depending on the case and the particular circumstances of the country studied, EFL can generate short-term and/or long-term effects on political and regime (in)stability. In this research, political instability is defined in a broad way and includes, protests, wearing off support to government, the threat of secession, political terrorism, racial and nationality tensions, and rebellion.

Chapter 3: Methodology and case selection

The research aims to study regime (in)stability in SA and Iran following the Most Similar Systems Design (MSSD). Both cases are similar in the nature of their political regimes and have undergone similar liberalisation processes in the past 40 years (SA started in 1974 while Iran started in 1988 and both are still pursuing EFL). Their regime structure is based on an authoritarian ruler (the monarch in SA and the supreme leader in Iran) supported by religious legitimacy stemmed from strong clergymen apparatus using Sunni and Shia sects of Islam respectively. Furthermore, both have moderate façades of democratisation. On the differences, SA political stability has always been seen as higher that of Iran's (for example, World Bank political stability indicator in Figure 1).

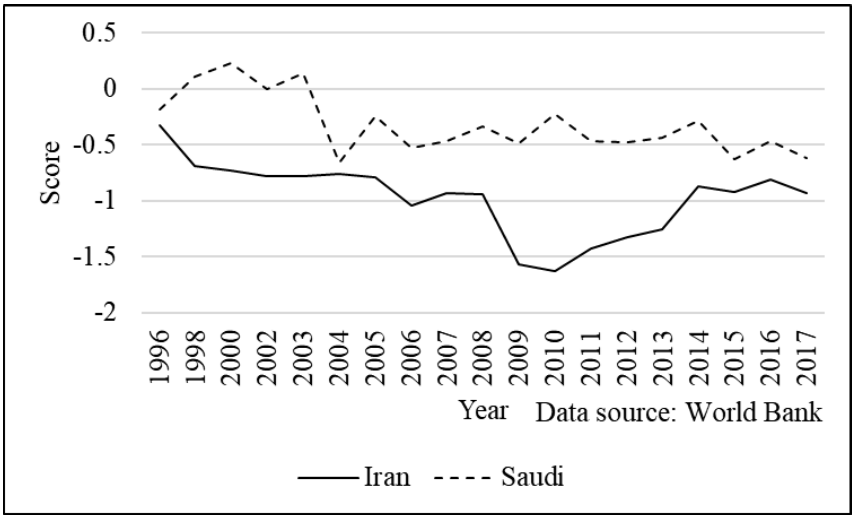

Figure 1 Political stability in SA and Iran

Note: a higher score means more stability

The research seeks to see if FL policies can be considered a key factor for such a different perception. The research ignores two variables: population size and history. While population size is influential in understanding a country, it is not clear whether population size difference is significant in this research. Both SA and Iran have undergone rapid population growth in the past 40 years, which increased pressure on the government to provide for the growing population. This fact is critical to understanding the pressure for liberalisation to achieve economic growth, but nothing more. As for history, Iran's Islamic regime builds its legitimacy on extended historical presence and reminiscence of the Persian Empire. SA state, in contrast, is a more modern phenomenon built around nationalism. Yet both countries adhere to the state-based international order. Thus, differences in history can be safely ignored for the purpose of this research. Focusing on two similar cases will allow this exploratory study to offer detailed understanding of the selected cases (Gerring, 2006). The research seeks to explore an alternative explanation to regime (in)stability in SA and Iran, thus contributing to a better understanding of EFL in SA and Iran and how that influenced the regimes (in)stability. Therefore, the research hope to transform the descriptive and exploratory objective into an explanatory one. Since this is a new area of research, such effort is sufficient to probe further investigation. In case this is not achieved, the study still offers explanations and interprets data that suits the particularity of both SA and Iranian cases.

There are notable limitations for using only two cases. First, potential researcher subjectivity and biases (Creswell & Creswell, 2009). However, this is not particular to the used methodology. "On the contrary, experience indicates that the case study contains a greater bias toward falsification of preconceived notions than toward verification" (Flyvbjerg, 2006: p. 237). Second, weak generalisability and external validity (Gillham, 2000; Woodside, 2010). This has been avoided to some extent by strategic selection of the case (Iran and SA cases are very similar and highly entangled). Such selection allows the revelation of more information, more actors, and more mechanisms, and this increases the study's internal validity. Evidence for this research relies mostly on secondary data produced by other researchers, international organisations (such as financial institutions, think tanks, and human rights organisation), and media reports from credible sources. An issue that encountered the research was the incredibility of government sources and statistics. Therefore, statistics used are taken from international sources and compared to national statistics when possible to ensure credibility. Furthermore, some quantitative data important to the research was missing, e.g. the number of protests and their goals, and thus qualitative data was used as an alternative. Third, it could have been helpful to conduct some fieldwork to collect more evidence, e.g. interviews with officials or civil society activists, but due to restriction on the movement of the researcher, it was not possible to do that (Gerring, 2006). Fourth, EFL are still ongoing processes and the counter-factual to them is not present. Therefore, their impact on political regimes is not fully captured and identifiable. Finally, reflections from the results are applied to the region to offer insights for future researchers about potential commonalities and differences in their experiences of the effects of EFL on their political regimes stability in the future. The hope of the research is to lay the grounds for more systematic study of the topic and provide empirical data for future researchers aiming to theorise for EFL impact on regime stability in the MENA.

Chapter 4: Analysis and discussion

4.1 SA

4.1.1 Pillars of regime stability

4.1.1.1 Regime structure

In SA, regime stability can be partly attributed to the nature of the SA political structure (Cowan, 2018). The royal family is the cornerstone of political contestation. Polarisation within society does not play a role in the stability of political life. Through blood succession and intra-family bargains, the SA monarch is elected (Al-Rasheed, 2018). The monarch has an absolute power to run the government. Furthermore, historically, the society's concession for the monarchy to rule was made by Ibn Saud alliance with many tribes who were influential in the war or were wealth holders (Chaudhry, 1997). Even when there were fights among the royals, it was mostly in-house and thus no societal instability took place. Loyalty to the monarch and in-family conflict resolution ensured that the political system remained stable overall (Davidson, 2016). Of course there have been some incidents where the royal family's coherence was in jeopardy, but it was often minor and insignificant to the overall rule of Al Saud. For example, the Free Princes Movement was declared in the 1960s to establish democracy and throw out the monarchy (Cowan, 2018). However, such movement never took hold and the princes returned to SA after initially fleeing to Cairo. Overall, the Al Saud tried to keep their family conflicts in-house and to resolve those using bargains, house arrests, and controlled violence. Such dynamics ensured a stable political structure and system.

4.1.1.2 Security and coercive power

Any regime needs to ensure its utmost security by building its state security apparatus around protecting the regime. In the case of SA, the closet tribal allies of Al Saud formed the military (Chaudhry, 1997). This ensured that Al Saud was in charge of the country's security.

The air forces, which is a command part of the royal army, filled its ranks by royals and very close allies who deem the regime survival as theirs. The SA National Guard was established also to ensure a balance against the army and the police in case either attempt to instigate any destabilisation of the regime (Al Wasmi, 2017). Externally, SA is one of the largest military spenders in the world. SA spends nearly 10-15% of their GDP on buying weapons from mostly Westerns allies, the US in particular (Figure 2).

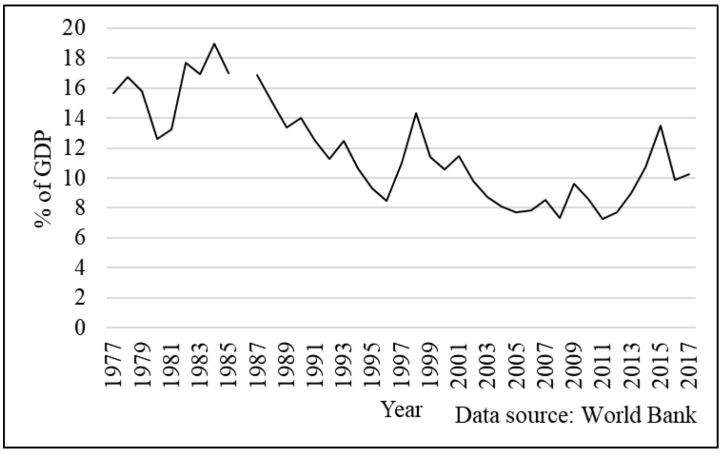

Figure 2 SA military spending as % of GDP

It is the one of the most sophisticatedly equipped and technologically advanced military in the region. Nonetheless, observers of SA military have always questioned the technological and spending edges. The arguments usually claim that the military is ill-trained to use most of the technology and the command structure is ill-conceived for actual war operations (Cordesman, 2018). Therefore, for example during the gulf war, the Saudis were afraid that their domestic forces would not be able to fend against an Iraqi attack and thus funded Western military operations in the Gulf to defeat Saddam's forces. It is true that SA military has never been challenged to a war with a peer competitor. The monarchy has as well relied on private security contractors to ensure personal security and conduct military operations abroad. Domestically, the police alone is in charge of protecting societal peace. Overall, in the near future, the security of SA monarchy is strong and durable domestically and regionally.

4.1.1.3 Religious leadership

One of the critical pillars of SA monarchy stability is its alliance with Islamic Sunni clergymen. The monarchy struck a deal with the religious clergymen (under the leadership of Mohammed Abd-Alwahab) who contributed to the establishment of the country (Blanchard, 2006). Wahhabism became the brand of SA's Islam since then. Revolutions and social tensions were frequently dismissed by the clergymen and deemed to be a threat to the country's security. This has provided additional stability to the monarchy. Regionally and internationally, SA tried to spread its own version of Islam (Blanchard, 2006). Wahhabi Islam has been spreading around the Arab world and the world and strengthening the legitimacy and the stability for the monarchy (Blanchard, 2006). For example, in Egypt Wahhabis have mostly sworn allegiance to Mubarak. When Al Sisi came to power, they casted their votes in his support. It is clear that Wahhabism was used as an integral part of SA foreign policy and to legitimise its ideology domestically. In Afghanistan, Yemen, Syria and Chechnya, Wahhabi Jihadist funded by SA played a key role in supporting SA foreign policy. The SA monarchy also draws legitimacy from being the Guardian of the two holy mosques, Mecca and Medina, and the organisers of both Hajj and Umrah. Overall, Wahhabism has been used to legitimise the regime, prevent opposition, and spread foreign policy objectives. Despite the ideology causing a terrorism problem at home and abroad, Wahhabism has solidified the SA monarch rule.

4.1.1.4 Economic development and liberalisation

Faced by the rise of Arab social nationalism in neighbouring countries, in Iraq, Syria, and Egypt in the 1970s, the SA monarchy realised that it needed to offer a more generous deal to its people if it wanted to compete with socialist regimes (Hanieh, 2016). That is why they embarked on a national development programme that later was developed into a broader EL programme to tackle the ills of the SA economy and society. These ills included reliance on oil, subsidies, large public sector, unemployment, small financial sector, limited infrastructure, poverty, and no tax base (Niblock & Malik, 2007). As of today, 10 development plans were implemented of which SA Vision 2030 is the latest most concerted effort to transform the economy from reliance on oil towards a more diversified economy that is reliant on the private sector and non-oil growth. Historically, oil revenues played a critical role in the government spending on development plans. The fist rise of oil prices in 1974 gave the government the resources to start the first five-year development plan (Figure 3). The second oil boom happened due to an oil supply shock caused by the Iran-Iraq war in the early 80s (Figure 3). The latest spike in oil prices occurred in 2003 with the onset of Iraq war and major regional instability (Figure 3). Those spikes in oil prices and revenues have given the government ample resources to fund transformative national economic development programmes with a total cost exceeding trillion SA riyals as of now. Aided with great foreign reserves (Figure 4), the government invested in physical infrastructure, human resources, social development, and economic source development (Table 2).

Development Plan	**Emphasis**
First 1970-75	Physical infrastructure
Second 1975-80	Physical infrastructure
Third 1980-85	Economic resource development and psychical infrastructure
Fourth 1985-90	Economic resource development, human resource development, social development and physical infrastructure
Fifth 1990-95	Human resource development and physical infrastructure
Sixth 1995-2000	Human resource development
Seventh 2000-2005	Human resource development
Eight 2005-10	Human resource development
Ninth 2010-15	Vision 2020
Tenth 2015-present	Vision 2030

Table 2 SA development plans and resource development emphasis

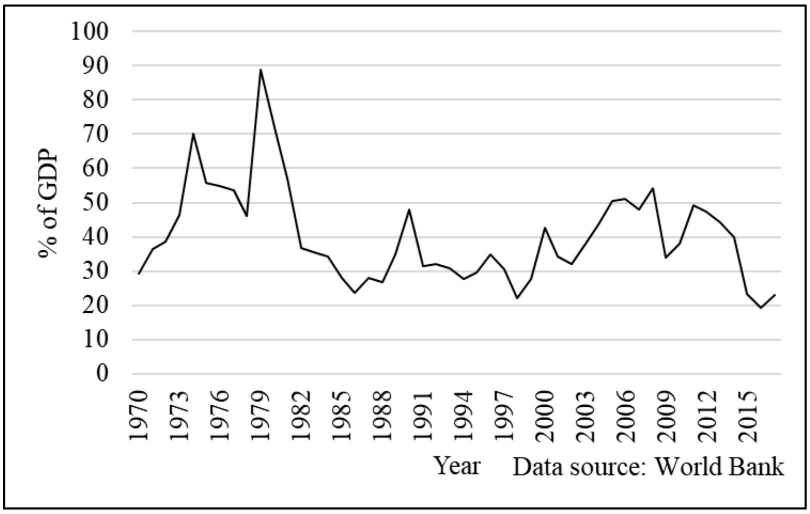

Figure 3 SA oil rents as % of GDP

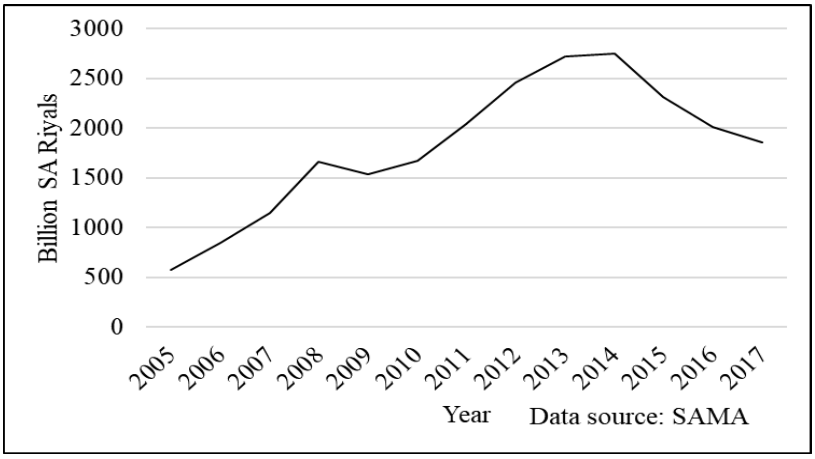

Figure 4 SA reserve assets in billion riyals

Oil has been so determinant to SA economy growth it is claimable that just by looking at oil prices vis-à-vis GDP growth, one can understand the totality of SA economy since the 1970s (Banafe & Macleod, 2017). Figure 5 shows that when oil prices were high, economic growth was high too and vice versa. Clearly, while reliance on oil was understandable in the early stages of development, the continuous reliance upon its revenues to sustain economic growth is not strategic, as oil remains a finite commodity with an expiry date of existence. Furthermore, the fluctuation in oil prices meant that the economy was held hostage to outside politics. SA was alarmed and started to think of how to detach the economy from reliance on oil (Faudot, 2019). The SA national development programmes (each of 5 years length) were aimed at improving private sector role in the economy, diversifying the economy away from oil, increasing international competitiveness, financial development and deepening, increasing employment of Saudis, encouraging sustainable development, decreasing subsidies, and deregulation (Ramady, 2010; Presley & Westaway, 1984). Many government agencies were established to fulfil these goals such as SAMA in 1952 and Central Planning Organisation in 1958. Many laws were introduced as well such as Banking Control Law 1966 and The 1968 Land Apportionment Act. More recently, specialised agencies were established such as the SA General Investment Authority in 2000 to facilitate the privatisation process. Furthermore, legal reforms continued such as the passing of the Law on FDI in 2000 that facilitated foreign investments and aimed to attract them to the country. Over the years of implementing the development plans, SA economy proved to have become more attractive for FDI. Figure 6 shows the larger share FDI has played in the SA Economy.

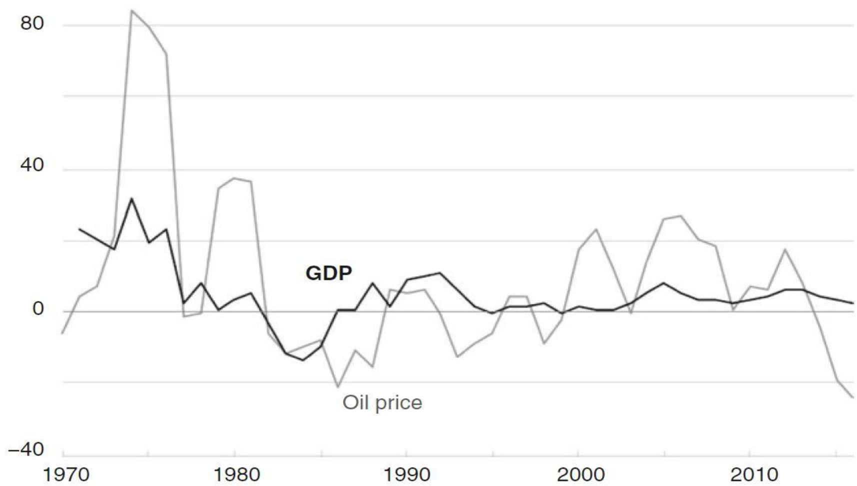

Figure 5 Change in real oil price and Saudi real GDP, 1970–2016

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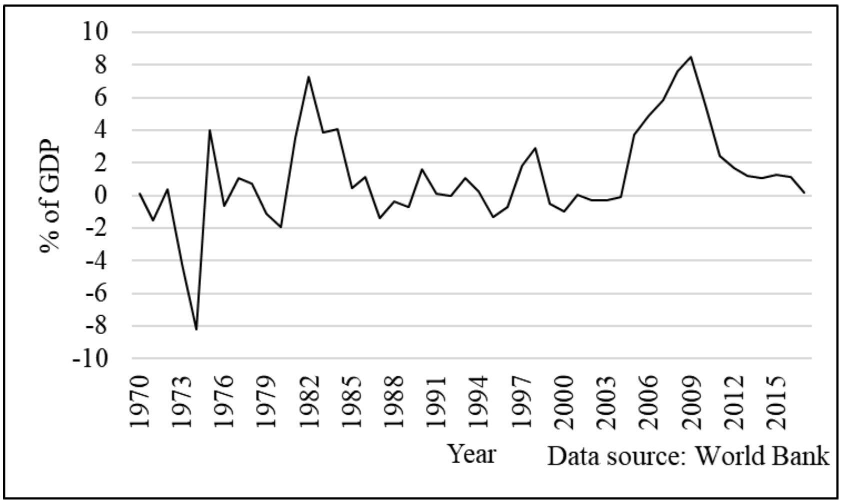

Figure 6 SA FDI net inflows as % of GDP

To attract FDI and boost domestic private spending, many SOE were privatised such as the SA Basic Industries Corporation, SA Airline, and SA Port Authority. Such privatisation has led to increased participation of the private sector in GDP. Furthermore, the diversification of GDP sources has been a continuous pattern. As of 2017, the non-oil sector contributed to 55.7% of GDP (Bhatia, 2017). By activity, this GDP covered the following sectors (Table 3):

Sector	Percentage
Producers of Government Services	24.9%
Wholesale, Retail & Hotels/Restaurants	16.1%
Non-Oil Manufacturing	14.9%
Transport & Communication	10.4%
Housing Ownership	9.0%
Construction	8.5%
Finance, Insurance & Business Services	6.3%
Agriculture, Forestry & Fishing	4.2%
Community & Social Services	3.5%
Electricity, Gas & Water	2.3%
Non-oil mining	0.7%

Table 3 SA Non-oil GDP by % of activity

Data source: SAMA annual statistics

To increase SA competitiveness internationally, industrialisation was encouraged. Particularly, petrochemical downstream industrialisation was also encouraged and promoted. Today, non-oil manufacturing contributes 15% to the non-oil GDP of SA. In order to encourage investment and increase competitiveness, many specialised credit institutions were established such as the SA Agricultural Bank (1973), the SA Industrial Development Fund (1974), the SA Credit Bank (1971) and the Real Estate Development Fund (1974). As of 2005, 37.9 billion SA riyals were loaned from the Agricultural Bank while 38.2 billion SA riyals were loaned from the Industrial Development Fund in 2006 (SAMIRAD, n.d.a, n.d.b). Over the years, the share of credit allocation decreased while the share of the private banking sector loans to the private sector increased as the economy was gradually transforming to involve the private sector more (Figure 7 & Figure 8). Consequently, the private sector influence on government policy increased. Through direct links to the royal family and indirect links (e.g. 26 Chambers of Commerce), the private sector pushed the government to privatise further and adopt a more liberal policy agenda economically and socially.

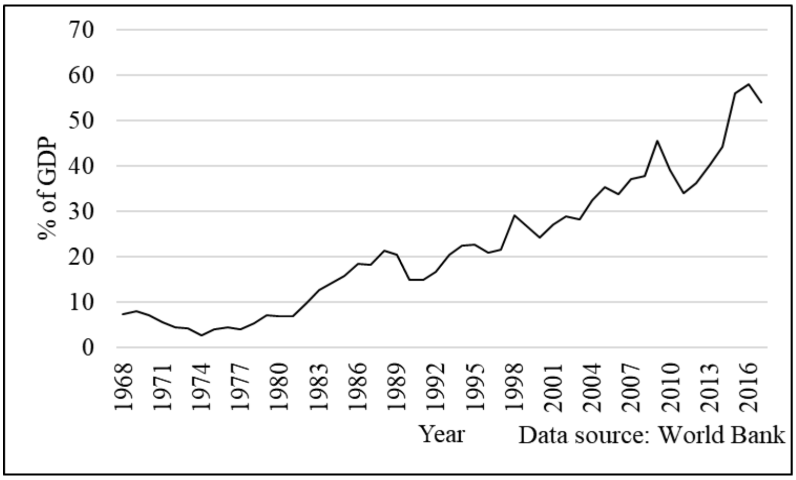

Figure 7 SA domestic credit to the private sector as % of GDP

Overall, as Figure 8 shows, domestic lending became more and more geared towards the private sector. Furthermore, the share of the private sector as a source of credit has significantly increased to reach nearly 50% of GDP (Figure 9).

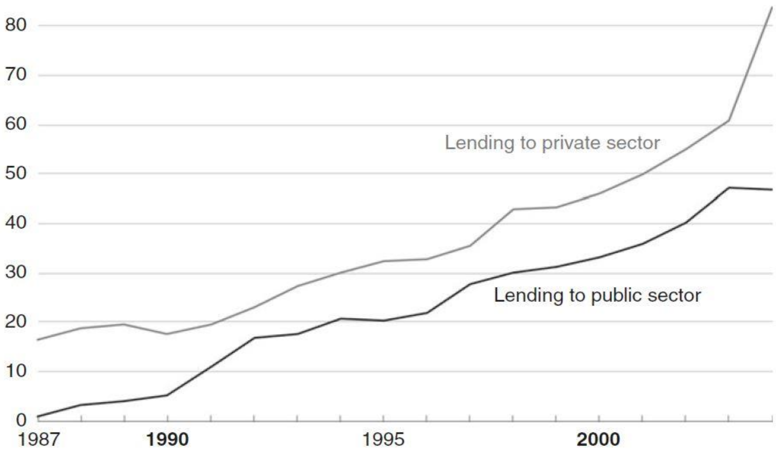

Figure 8 SA banks' domestic lending, 1987–2004 (billion USD)

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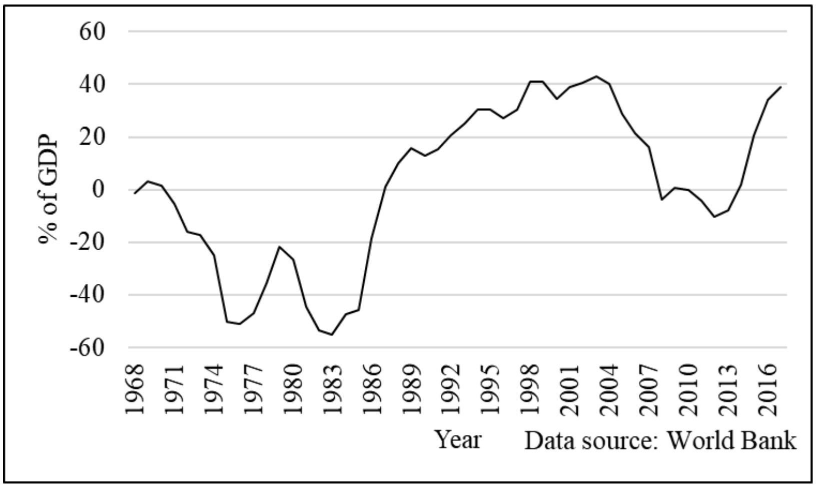

Figure 9 SA domestic credit provided by the financial sector as % of GDP

Despite the relative success in diversification and privatisation, reliance on foreign labour remained high in SA, which signaled limited success for SA investments in human development. The SA programme to nationalise many jobs. Which is called Saudisation, succeeded in increasing the number of Saudis employed in the private sector. However, the fact that many Saudis lack the necessary skills to occupy many of the jobs offered by the private sector has limited the Saudisation programme success. The Nitaqat campaign for the Saudisation of the workforce was launched in September 2011 by providing incentives that encourage firms to hire Saudis and sanctions non-compliant ones. In 2013, 2.5 million migrant workers left SA either through deportation or voluntarily. However, in mid-2017, the number of non-Saudis stood at 12,185,270 persons (37% of the total resident population) (Bel-Air, 2018). This means that SA economy remains reliant on foreign workers, which exacerbates the youth unemployment problem and regime instability.

Politically, privatisation in SA enabled the regime to sustain its survivability as the majority of the privatised companies were either owned by state-affiliated entities (such as SA Basic Industries Corporation of which 70% is owned by a company affiliated to the government) or by business elites connected to the royal family (such as many banks, e.g. Al-Rajhi Bank) (AlShehabi, 2017). Furthermore, some royal family members privately owned significant shares of many of the predominant companies in the SA economy (Al-Muftah, Al-Shihabi, & Buhazaam 2017; Al-Sulayman, 2018). Most of the business class was made of those who made their fortunes quickly in the boom period through gaining key contracts (mainly in construction or the supply of goods and services to the royal family), or as agents who negotiated arms deals with foreign suppliers of weaponry (Kinninmont, 2017). Many of these were of non-Saudi origin, but with SA citizenship. Among them were Adnan Khashoggi, Muhammad al-Fassi and Rafiq Hariri (Niblock & Malik, 2007). The second element was composed of a Najdi new middle class (Chaudhry, 1997). Family, tribal, and kinship connections with bureaucrats were utilised by aspiring Najdi businesspersons not only to get permits, register agencies and so on, but also to gather and peddle supposedly confidential information. Overall, higher links to the royal family and government bureaucrats were essential to growing your business. Higher links were offered only for businesspersons who are loyal to the monarchy. Thus, privatisation was utilisied to increase regime stability and buy loyalty. Finally, the SA economy growth (Figure 10 and Figure 11) was path-dependent on oil (Mazaheri, 2016). The substantial growth of the non-oil manufacturing sector stemmed largely from the contribution made by the petrochemicals industry, in which the government had invested so heavily since the mid-1970s. Despite that, oil remains the major contributor to the economy's revenue.

In conclusion, EL took place after a prolonged period of negotiation and postponement, and was frequently followed by inadequate implementation. Absence of taxation apparatus meant that the state had a little mechanism to influence society's behaviour. SA liberalisation led to the establishment of personalistic links between individual investors and state officials. Clientalism increased as a result. State institutions had developed as fiefdoms dominated by individuals who held their positions by virtue of deals made and compromises reached within the royal family. This pattern of the administrative organisation became locked-in through the dynamics of elite politics and bureaucratic growth. SA has a high population growth rate (Figure 12) and depends heavily on migrant labour. If Saudis could replace many of the ten million foreign workers, the economy would be better. Moreover, the growing local population is increasing its use of vast volumes of oil that could be sold abroad. Therefore, the demographic situation is probably one of the country's biggest challenge. Regime instability, overall, was not generated by economic development and liberalisation, but was enforced by it.

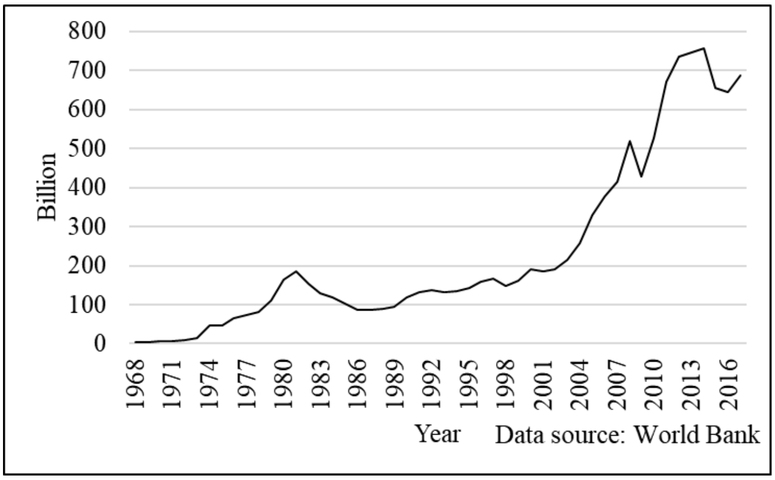

Figure 10 SA GDP in USD

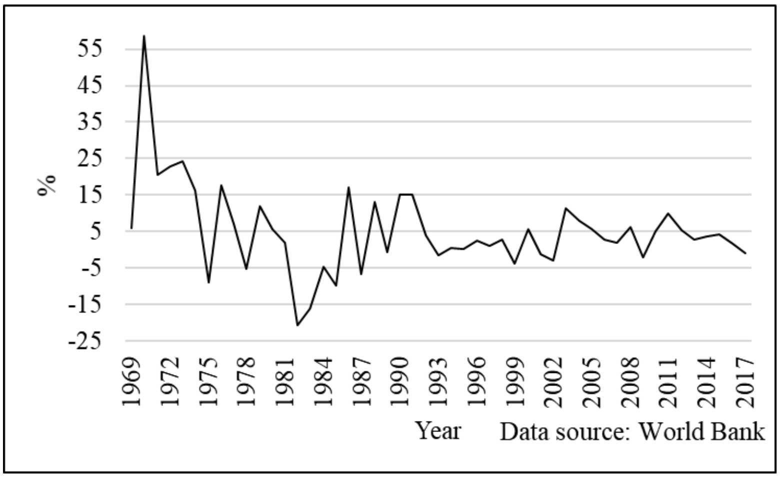

Figure 11 SA % of annual GDP growth

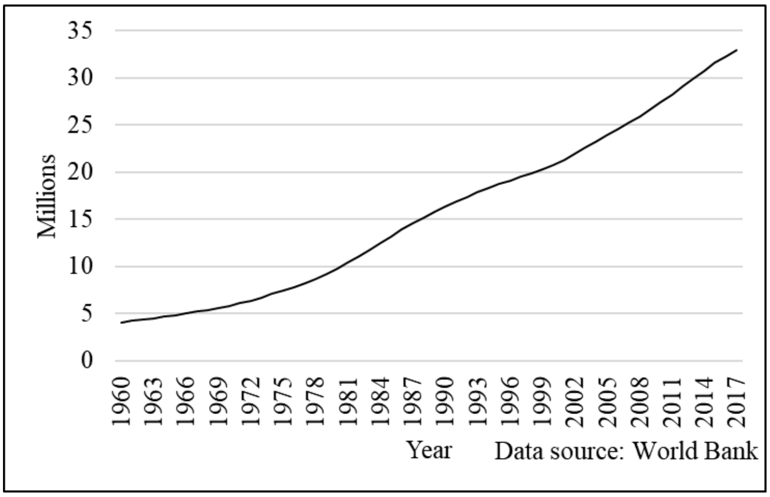

Figure 12 SA population growth in millions

4.1.2 Sources of SA regime instability

4.1.2.1 Growth, poverty, and income inequality

SA economy is known for having sustained growth throughout its history. Growth has been mainly maintained by spending oil revenues on developing the national economy by the government. The private sector in SA, which has gained momentum, is still reliant on government spending for its revenue generation and contribution to growth and employment. This has made the country vulnerable to shocks in oil prices. When these happened, growth slowed down (Figure 13). For example, the oil boom in 2003 saw a significant increase of SA GDP over the next 10 years only for it to decrease and stabilise from 2014 onward when oil prices decreased. However, despite the fluctuation in oil prices and growth, GDP per capita growth was relatively high and growing. It peaked in 2013 to reach $25,000 and then spiralled down to $20,000 as of 2017 (Figure 14). Therefore, it is no surprise that there is little to no protests due to socioeconomic issues in SA – at least, there is no data on that. What is more significant and well reported is the Shia minority's feeling of resentment coupled with religious hatred to the monarchy (Zuhur, 2012; King, 2009). While living in the richest parts of the monarchy, the Eastern Shia Saudi minority is probably the most harshly treated by the regime (Kinninmont, 2017). Therefore, poverty and inequality based on Shia-Sunni divide seem to stir substantial destabilisation to civil peace in SA (Gause, 2014). Shiites have often protested the government's neglect and demanded improvement of living conditions. The government often used force and coercion to stifle the protestors.

Estimating poverty and inequality in SA is a tricky task due to the absence of official data and the reliance on estimates from international observers. For example, according to official statistics, there is no information on the number of poor persons in the country. However, several media reports have proclaimed that 2-4 million Saudi live in poverty

(Sullivan, 2013). This is roughly 10% of the population. In spite of this number, poverty in SA does not seem to be a major issue for the regime. Income inequality, however, seems is a more serious problem. While families and merchants connected to the regime made substantial wealth from national development programmes, the majority of Saudis have not. In fact, the privatisation programmes that the government has embarked on have seen more Saudis lose subsidies and face more expensive prices for foodstuff and consumer goods. Unfortunately, there are no statistics from the government on inequality. SA has always kept such information secret. One can speculate that the reason for such secrecy is the fear that revealing such information would stir public resistance to government redistribution policies and demands for fairer share of oil revenues. Another reason could be the fact that the monarchy does not want to produce numbers that reflect the incomes of the highest earners since that would reveal the royal family dominant share of incomes. In any case, international sources have established that Gini score for SA is high at around 45 (Stoffel, 2019). Recent academic work showed that the top 1% earners have 19.7% of the total share of national income while the bottom 50% earners combined had only 7.8% (World Inequality Database, n.d.a). Wealth concentration, by extension, is a serious problem for SA in the long term.

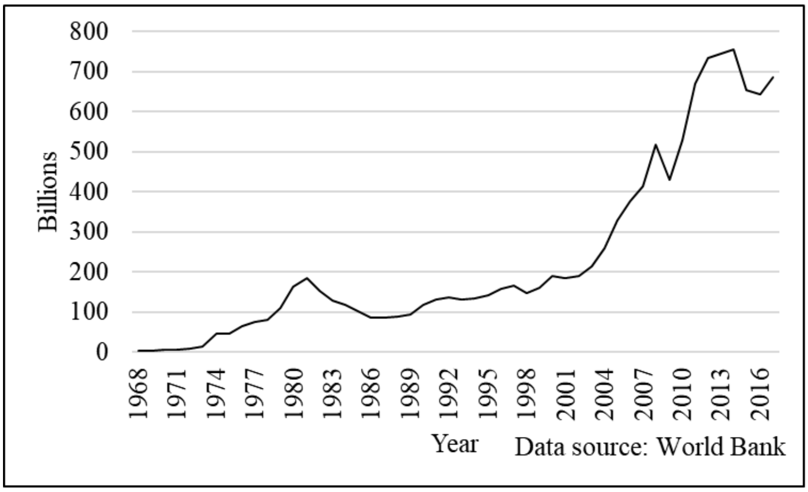

Figure 13 SA GDP in current USD

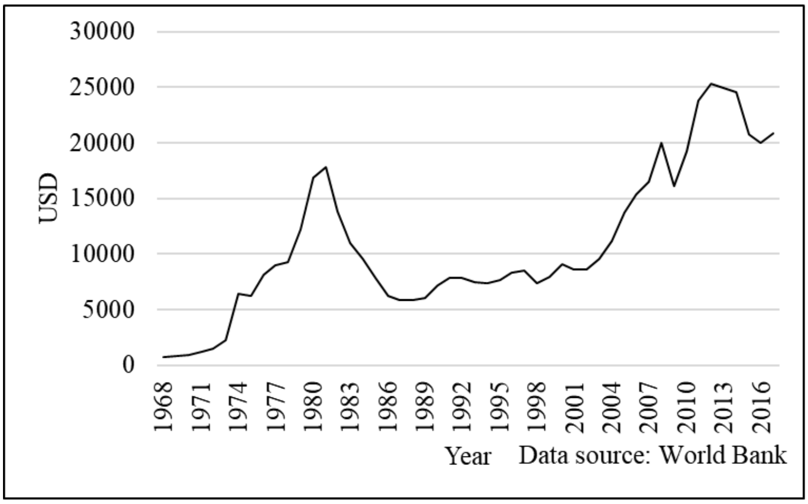

Figure 14 SA GDP per capital in current USD

4.1.2.2 Civil strife and minority secession

Indigenous minorities are small and fragmented in SA. Most of Saudis are Arabs. Since the country relies largely on foreign labour, there is a large percentage of foreigners resident in the country. However, some part of those are Arabs (World Atlas, n.d.). They enjoy no political rights and historically have had no role in the country’s politics. Other minorities are Indians and Bengalis and those are mostly doing low skilled work, had no role in political life, and constituted no political instability source. The greatest threat of secession for minorities come from ethnic Arabs who are Shia. Shiites have been harshly treated and many have demanded secession from SA. These calls were faced with harsh crackdowns by the government on activists and community leaders. Overall, discrimination among Saudis on the basis of ethnicity is not common at all. Discrimination on the basis of a religious sect, possibly geographic origin, or gender is far more common, although the general and the specific forms of any inequalities need to be understood (Etheredge, 2010). Overall, there is no serious threat of political instability in SA coming from a threat of secession or minority politics.

4.1.3 Financial stability and SA regime stability

SA has pursued FL since its first development plan, but cautiously. In the early years of the oil boom in 1974, SA has achieved great surpluses that it was unable to absorb domestically and thus had to export to other countries. The logic was that SA needs to maintain its earned dollars and not lose their value for inflation or fluctuation of USD prices (Banafe & Macleod, 2017). Furthermore, SA wanted to make sure that it could hedge its oil revenues against fluctuations of oil prices in the long run. Such moves have pushed the SA government to instruct SAMA to recruit financial managers to advise it on the best way to invest the funds (Mishrif & Al Balushi, 2018a, 2018b). Part of the excess dollars was channelled through the IMF in the form of loans given to developing countries in order to enable them to keep the demand for oil at certain rates (Ulrichsen, 2016). Ever since, SA's engagement with the international financial system has been of critical importance to global financial stability. By agreeing to sell its oil only in dollars in exchange for security guarantees from the US, SA ensured a main role in the ongoing of the international financial system (for extensive details on SA capital significance, see Hanieh, 2018). What became known as the petrodollar has since been the cornerstone of US-SA relations. It is not a surprise that when this relationship was being challenged recently by the US congress suggested a resolution to allow suing oil monopolies (including SA), SA threatened to give up the dollar as a pricing unit for its oil (Lawler, Zhdannikov, & El Gamal, 2019). Such a threat if it was acted upon will not influence the global financial system in the short run or the dollar position as the global reserve currency. However, once countries realise that they need fewer dollars to buy their energy supplies, they will be less interested in keeping more dollars and investing and reinvesting in them. Before the US know it, the dollar would influx back to the US and its price would go down due to the sudden supply shock of dollars. Therefore, it is arguable that the petrodollar was one of the cornerstones of SA regime's stability. The desire not to disturb the oil supplies of the world to maintain price levels has helped SA ensure that its political survival and stability was of the interest of the world (Krane, 2019). As a balancing supplier of oil, SA became an important country to the stability of the international order. Regime change was not conceivable or desirable.

To maintain domestic financial stability, SA maintained a more or less fixed exchange rate against the Special Drawing Rights before 1986 and the US dollar afterwards (Figure 15).The logic for such a strategic move was simple (Steinberg & Malhotra, 2014). Since SA relies mostly on oil that is sold in dollars, there were no gains foreseeable from having a floated exchange rate (Banafe & Macleod, 2017). This is because the non-oil exporting sector was/is relatively small and does not generate enough income to be seen as a beneficiary of a floated currency (Banafe & Macleod, 2017). The majority of SA imports are paid in dollars and it makes sense to peg the exchange rate so that it simplifies the national accounting system. If SA exchange rate was to be floated, it would have been a matter of time before dollarisation of the SA economy took place, an outcome that was and is not favourable to SA monarchy as it entails loss of sovereignty and ability to conduct national development policy. Of course, defending the riyal in a pegged exchange rate system meant that SA foreign exchange reserves have been always of significant importance. SA is ina constant need of dollars to defend its exchange rate regime. Since SA depends heavily on imports to suffice local consumption, having dollars, which is the currency used in international trade, is an important policy objective (Cowan, 2018). When we observe SA government spending, it is highly correlated to its foreign reserves. When reserves were high, government consumption was low and vice versa. This is because the SA economy is dependent on government spending which takes place on the backbone of dollars reserves. Even the non-oil part of GDP is dependent on oil revenues and government expenditures.

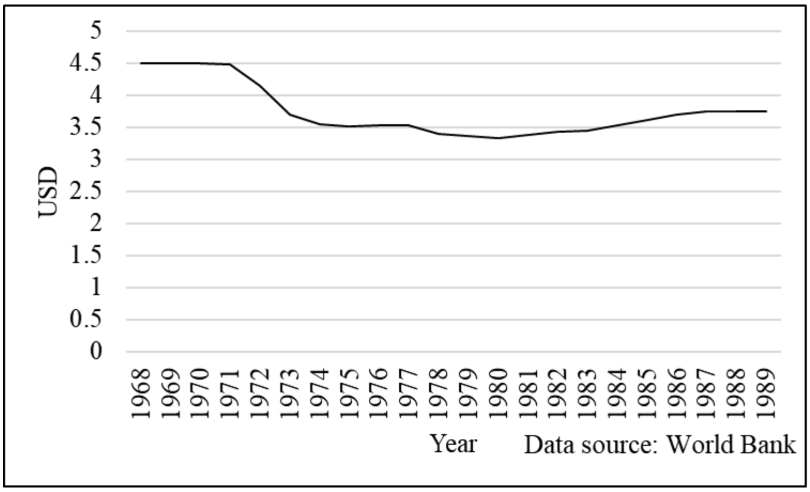

Figure 15 USD vs Saudi riyal exchange rate, 1968-1989

Capital openness has caused capital flight to be an issue for SA Economy. Fleeing low rates and a small economy that is heavily dependent on oil, rich Saudi used capital openness to move capital abroad and invest their wealth abroad (Espinoza, Fayad, & Prasad, 2013). This has affected the growth potential of the SA economy. Estimates of private SA wealth overseas in 2003 ranged from $480 to $900 billion (Banafe & Macleod, 2017). According to some estimates, over the period 1971-2015, capital flight from SA reached over 212 billion of 2010 USD, causing an annual average of 3.57% of wasted potential additional economic growth for the same period (Almounsor, 2017).

In the aftermath of threats of legal actions post 9/11, many Saudis sought to bring their wealth home and the stock market was an obvious place for the wealth that came home. The SA stock exchange known as Tadawul was established in 2007 to be the market place where privatised companies can raise capital and exchange ownership. Furthermore, it aimed at attracting diaspora investments in the home market. Initially, equity ownership rights were restricted for foreigners in order to minimise exposure to international financial risk, but that measure was later abandoned. As of now, there are 171 publicly traded companies on Tadawul. The total value of shares traded reached 870.87 billion SA riyals and 25.01 million transactions were executed during 2018 (Tadawul, 2019)

The SA banking system is considered to be one of the most stable in the world with relative high profitability. Figure 16 shows that banks return on equity in SA was relatively good over the years. Meanwhile, Figure 17 shows that the percentage of non-performing loans over the years was relatively small reaching around 1.5% of total loans, as of today. In 2011, Standard & Poor's concluded that the SA banking system was one of the safest in the world, ranking alongside Germany and France (Banafe & Macleod, 2017). The American credit agency cited SAMA's close and conservative supervision as a key factor. This is because banks operate under strict and highly prudential rules set out by SAMA that does not allow them to reach risky stages of over-lending or excessive exposure to international risk. Furthermore, the spread of Islamic banking meant that banks did not need to pay interest on deposits, which increased profitability and stability. The banking system in SA is mostly dominated by three banks of which Al-Rajhi is the largest. Recently, SAMA has awarded licences to global banks including Deutsche Bank, JP Morgan, and BNP Paribas to operate in SA (Noonan, 2017; Banafe & Macleod, 2017). Mostly, these institutions work on niche financing as most of the SA market is dominated by Islamic banking offered by domestic SA banks. National Commercial Bank, the Shariah-compliant Al-Rajhi and Saudi American Bank hold nearly half of SA assets and deposits. The trend of opening up to foreign ownership in the banking sector defied the historical stance of Saudisation of banks and signalled a greater desire for openness. Overall, banks' profits were down from pre-2008 crisis highs but were still well into double digits, with a loan-to-deposit ratio that was conservative (recently increased from 85 to 90 percent) (Ghassan, Alhajhoj, & Alaoui, 2013; Al-Hamidy, 2009)

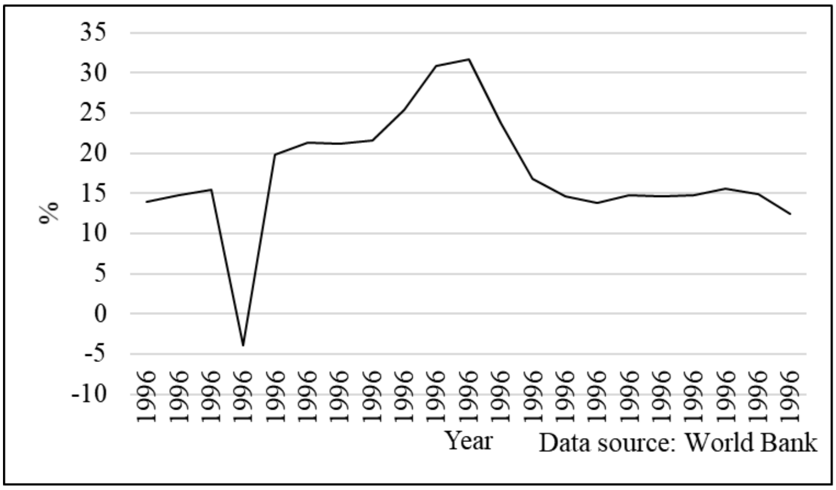

Figure 16 Banks' return on equity for SA

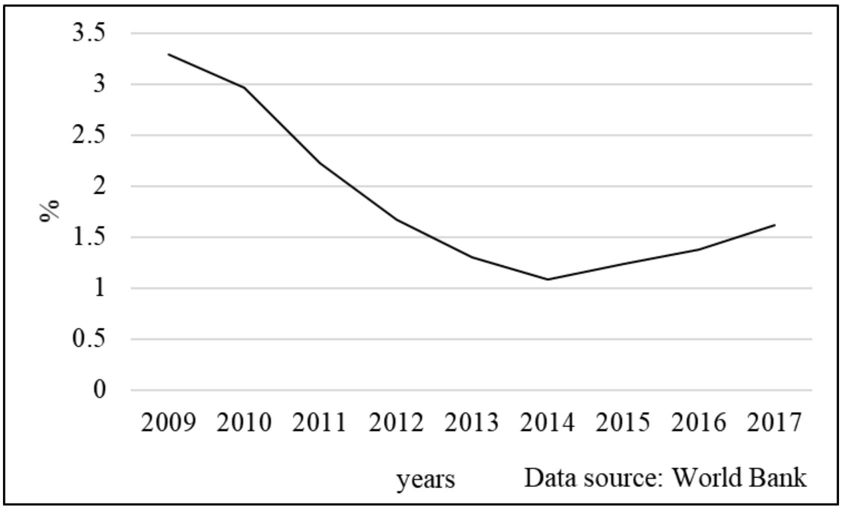

Figure 17 SA Bank nonperforming loans to total gross loans (%)

The government also started issuing government bonds for domestic and international investors. The aim was to raise capital and stockpile foreign reserves in order to maintain the fixed foreign exchange rate. Furthermore, it helped finance some of the SA government budget deficit. The billions in foreign assets held by government agencies were used to buy the issued debt. Three quasi-government funds were in the frame: the General Organization for Social Insurance, the Public Pension Agency, and the SA Fund for Development. The private sector held far more money abroad than the government. By issuing bonds, the government wanted to attract SA investors to invest at home. In the course of its lifetime, SA financial system did not face in major crisis, except in 2006. At that occasion, a frenzy in the stock market led to a financial bubble that burst to cause millions of Saudis to lose savings and investments

(Alkhaldi, 2015). Due to lack of exposure to the international financial system and minimum foreign banks presence, SA banking system was minimally disrupted during the global financial crisis in 2008 (Al-Muftah, Al-Shihabi, & Buhazaa, 2017). Overall, the SA financial system can be characterised as a stable system throughout its life span.

4.2 Iran

4.2.1 Pillars of regime stability

4.2.1.1 Regime structure

Since the Islamic revolution in 1978 against the Shah of Iran, building regime stability has been of great concern for the new revolution supreme leader and his associates. The conundrum that the new leadership met was how to sustain the revolutionary spirit domestically and expand it regionally in a way that considers global power relations (Kamrava, 2014). Since the revolution was supported by different sectors of society such as labour movement and leftist groups, the political system was designed to accommodate differences in opinions in public policy, but nonetheless maintain the supremacy of the Islamic nature of the revolution and the legitimacy of its absolute leader (Mohammidi, 2013). On the one hand, the supreme leader would ultimately possess and retain the veto power in political life. His fellow clergymen and IRGC would aid him in this. IRGC consist of thousands of volunteers and military leaders who run extensive social, economic, and political networks. IRGC operate as guardians for the revolutionary principle and work to protect the revolutionary ideal at home while attempting to expand its influence outside the borders of Iran (Heydemann & Leenders, 2013). On the other hand, the political power in Iran would be shared between an elected president and a house of parliament called The Islamic Consultative Assembly (Majlis) (Saikal, 2019).

The Majlis can legislate laws on all issues within the limits of the constitution. The members are elected in a free election after being filtered for loyalty and scrutinised for commitment to the revolution by the supreme leader. Similar procedures happen with regard to electing the president. Such power dynamics have ensured that the supreme leader is always faced with friendly faces in political life and that his legitimacy is never challenged on a fundamental level (Saikal, 2019). In the same time, it made sure that the façade of democratic elections and consultation with the public with regard to the matters of the nation remains ongoing. This has coated regime legitimacy and stability with another cover. Furthermore, it gave the supreme leader the chance to influence the political landscape by ensuring that no political alliance is formed that would constitute a political risk for the Islamic revolution survival (Guzansky, 2014). Therefore, regime survivability and sustainability were ensured. Factionalism among opposition increased as they competed in a very limited political landscape with miniscule power. Such sub-optimal political influence created a situation where the regime avoids dealing with criticism and politicians fend for themselves without actually having significant power to influence the political trajectory of the country (Saikal, 2019).

The Guardian Council has the power to block any Majlis bill that it perceives to be incompatible with either religious law or the Islamic Republic's constitution (Heydemann & Leenders, 2013). Furthermore, since 1992, the Guardian Council can vet candidates and prevent them from running for election. As such, this non-elected body has been able to influence the make-up of the country's elected institutions. The Expediency Council is tasked with arbitrating in cases of legislative disputes between the Majlis and the Guardian Council. The supreme leader chooses its members directly. Overall, the capacity for Iranian elected representatives to shape national policies is significantly limited by the existence of a host of non-elected entities, of which the supreme leader, the Guardian Council, the Expediency Council, and IRGC play a major role. Furthermore, non-democratic forces ensure political stability in Iran by ensuring politics remains limited and exclusive to insiders. Iranian policy makers came from particular social groups that are highly invested in the preservation of the broader system of the Islamic Republic; any variation between them simply stemmed from the fact that they were each embedded in different parts of it.

4.2.1.2 Security and coercive power

Since inception, the Islamic Iranian regime had to plan for three main violence involving risks; domestic unrest (including terrorism), foreign invasion or secession attempts, and regime change. To tackle domestic unrest, the state built a strong coercive capacity. The police was formed in order to deal with domestic unrest and terrorist plots. It is not clear how large it is, but estimates round the number to 200,000 persons (Golkar, 2018). The Basij is the second line of protection for the regime survival and they are formed of nearly 5 million voluntary militants (Golkar, 2018). They are involved in all sort of security activities including policing, military action, and special operations. Lastly, the IRGC defend the regime against both warfare and internal challenges such as insurgency and terrorism (Golkar, 2018). A network of intelligence apparatus including the Ministry of Intelligence, the IRGC Intelligence Organization, and the Intelligence and Public Security Police supports these agencies (Golkar, 2018).

For external security, the Iranian army includes Ground Forces, Air Force, Navy, and Air Defense Force that are tasked with protecting the nation from external risks. Due to sanctions, Iranian arm forces relied on manufacturing locally. Furthermore, they shifted their imports towards Russia and China (Golkar, 2018). Smuggling was extensively used. Lastly, Iran pursued self-reliance by indigenising some weapons manufacturing. This has given it more power against regional adversaries. The weapons produced included ballistic missiles of thousands of miles ranges and a jet fighter called Kowsar. Overall, Iran's military armament while not the most advanced, it is built to ensure the ability to fight an asymmetrical war and thus ensure regime survival from external threats. Domestically, the police, the Basij, and the

IRGC ensure the government enough coercive capacity in case it was faced with terrorism, civil unrest, and violent protests.

4.2.1.3 Religious leadership

Iran has taken a task since the 1978 Revolution to spread revolutionary Islam. It championed political Islam based on Shia sect of Islam. Iran has used such a claim to ensure acquiescence of the domestic population to the supreme leader rule. Furthermore, it has weaponised Islam to expand its revolutionary principles abroad as part of its foreign policy. For example, in Lebanon it supported Hezbollah, while in Gaza it supported Hamas and Islamic Jihad. The main goal of such policy was to give political Islam a greater role in the politics of Islamic countries, exactly as in Iran. By doing so, Iran wanted to claim a greater leadership role in the Islamic world so that it legitimated the revolutionary regime at home while building alliances with like-minded regimes abroad (Omid, 2016). The role of religious clergymen in Iranian society is extensive. They own many organisations that provides care for the wounded of Iran's wars and they offer Islamic schooling to the young and the elderly. Furthermore, they work to educate the next generation of religious leaders in neighbouring countries such as Iraq and Syria. Overall, Iran used religion to legitimise the regime domestically, and achieve its foreign policy objectives abroad, which increased the regime stability and survival.

4.2.1.4 Economic development and liberalisation

When the Islamic revolution took place in 1978, the emerging regime emphasised self-sufficiency and independence from outside intervention politically, economically, and socially. Rhetorically, the new regime emphasised its anti-global capitalism stance. Nonetheless, private property and foreign trade were respected. The reason for such a contradiction between reality and rhetoric may stem from the fact that Iranian revolutionaries were partly leftist who thought that capitalism was the source of injustices they faced. However, the entrenched bazaar merchants and the nascent industrial class did not see capitalism and private property as the problem (Pesaran, 2011). Therefore, once the war with Iraq finished in 1988, such discourse was largely abandoned and fundamental shifts took place in the economic thinking of the Iranian leadership. Under president Rafsanjani and between 1989 and 1997, calls for opening up the economy became louder and policy shifts started to take shape in Iran. EL was deemed necessary to help eliminate the ills of the Iranian economy; a severe decline in GDP in recent years due to war, over dependence on oil income to fund government expenditures, widespread unemployment particularly among youth, a considerable budget deficit, inequalities across geographical regions and economic sectors, a gross lack of investment, a rapidly growing population, and poor management skills among bureaucrats (Rezaei, 2011; Maloney, 2015). The post-Khomeini Iran became more realist and during Rafsanjani's presidency pragmatic policies of opening up to foreigners (capital and exports) were adopted.

Iranian EL can be characterised as intensely influenced by the factionalism of Iranian politics (Mohammidi, 2013). Each president since the Iraq War has adopted a different stance with regard to the country's direction in liberalisation. During Rafsanjani presidency, bazar merchants advocated for opening up to international trade. They wanted to be able to export and import goods more easily to and from abroad. In a sense, they were pro-free-markets agents supported by people like Rawqani-Zanjani at the Plan and Budget Organisation, Adeli at the Iranian Central Bank, and Nurbakhsh at the Ministry of Economic and Financial Affairs who were technocratic elites educated in the West (Pesaran, 2011). However, the merchants were still protectionist and wanted favourable trade conditions. For example, when they supported privatisation, they wanted privatisation so that they could own a larger share of the economy and they were against outside intervention and ownership (in the banking sector for example) (Harris, 2013). During Khatami's presidency (1997-2005), his statists support base advocated for using a mixture of state-capitalism and economic liberalism. They wanted the industrialisation of the Iranian economy (particularly petrochemical industries) and inviting foreign investments to gain knowledge and necessary expertise (Gheissari, 2009).

According to some estimates, around two-thirds of the Iranian enterprises were state-owned or semi-state owned entities (Harris, 2013). Privatising SOE was challenging as they controlled a large share of the Iranian economy with extended privileges. For example, the Bonyads, major para-statal organisations, enjoyed tax exemptions, subsidised loans and foreign currency, and freedom from governmental monitoring of their accounts (Harris, 2013). Legally operating as trusts, the Bonyads are involved in many sectors of the Iranian economy such as cotton fields, hotels, banks, soft drinks factories, auto-manufacturing, shipping lines, and banks (Harris, 2013). Even after liberalisation and privatisation, these organisations maintained a strong hold of key privatised assets such as banks, petrochemicals, and reconstruction firms (Figure 18). Overall, politically, the discussion over EL in Iran was governed by two major camps; statist industrialists and free-market merchants (Pesaran, 2011). Today, there is no conflict in Iran with regard to support for liberalisation (Maloney, 2015). In that direction, the Iranian Privatisation Organisation was founded in 2008, during the Ahmadinejad presidency (2005-2013), to manage the process and many enterprises have been successfully privatised. In order to convince Iranians of supporting privatisation and liberalisation, Ahmadinejad offered Iranians several benefits using increased oil revenues and the Oil Stabilization Fund resources. First, social justice shares were offered to Iranian citizens of lower income in the newly privatised enterprises as compensation (Harris, 2013). Second, the broad subsidies programme was scrapped and replaced by a targeted subsidies programme to increase lower income earners benefit (Maloney, 2015). Third, Imam Reza Love Fund was established to give young people loans to fund their marriages, which made Ahmadinejad popular among youth (Pesaran, 2011). What was particular about Ahmadinejad's policies was receiving full support from the supreme leader to further privatise SOE (Pesaran, 2011). By continuing to push for further privatisation of the Iranian economy and removing barriers to privatisation efforts, the supreme leader indicated that he believed in an open economy where Iran is more competitive. Nonetheless, privatisation was criticised by many observers as it has enabled greater and more private role for IRGC in the economy. For example, the Ghadir Investment Company, which is linked to IRGC, has bought many of the privatised assets in different sectors such as banks, construction, foodstuff and others (IFMAT, 2018). Such fact meant that IRGC could exercise more influence over the state. Many saw that as cheating since it de facto annulled the meaning of privatisation as means to reduce state control of the economy. In practice, the tendency toward EL was limited because the complexity of the process of negotiation made it unlikely that the neoliberalism approach favoured by institutions such as the World Bank and the IMF would ever be accepted without at the very least finding itself altered in translation by Iranian domestic politics.

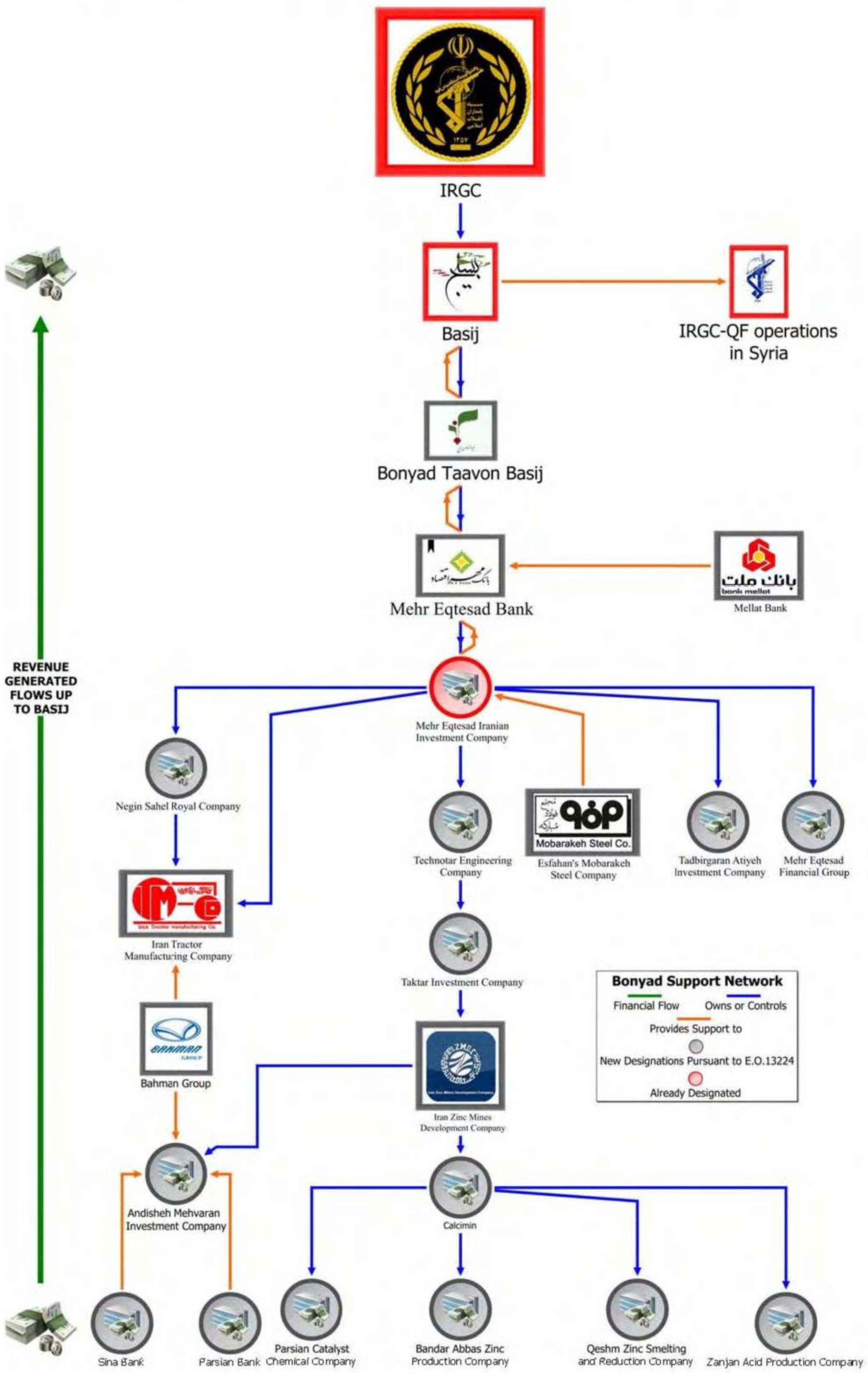

Figure 18 IRGC business and financial network.

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Alongside privatisation, diversifying the economic base was another goal for Iranian EL process. Historically, Iranian regimes relied upon oil revenues to fund government expenditures. Fluctuation in oil prices, financial sanctions, and squeezed foreign reserves kept the government hostage to whatever happens in the international oil market (Alaedini & Razavi, 2013). Therefore, diversifying the economy away from oil became a major government goal since the Islamic revolution. Oil revenue have played a cornerstone for regime's stability. By ensuring continuos flow of oil to international markets, the regime ensured the continuous flow of foreign currency (mainly dollars) to its economy. Since Iran relied heavily on imports for many of its needs such as foodstuff and electronic products, having sufficient foreign currency reserves was necessary for regime survival (Farzanegan & Alaedini, 2016). Oil has also enabled the regime to fund an extended network of patronage that supported the regime since the Islamic revolution in 1978 (Krane, 2019). Figure 19 shows that Iranian government spending relied heavily on its oil revenues. In most years, more than 50% of government spending was attributed to oil revenues.

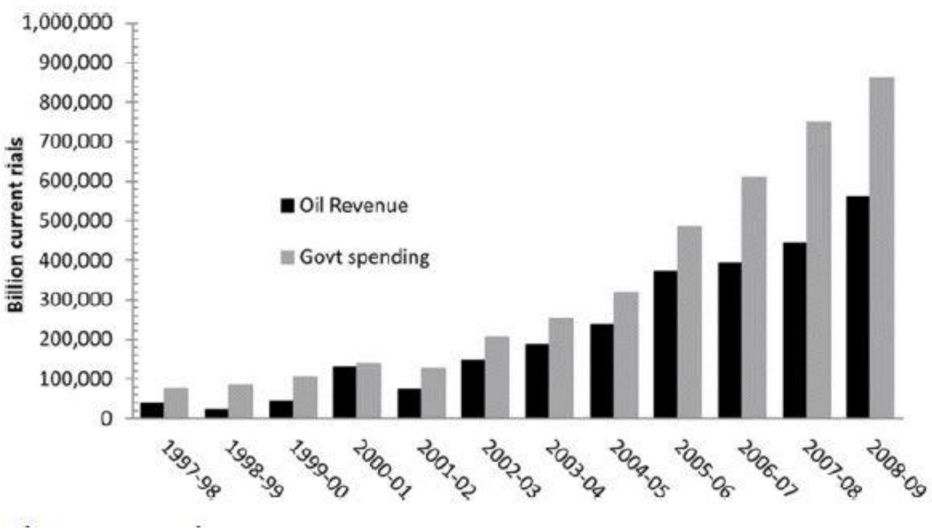

Figure 19 Iranian Government spending vs oil revenues

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Even after pursuing economic diversification since 1989, the Iranian government remains heavily dependent on oil revenues to fund its expenditures. Figure 20 and Figure 21 show that over the years, oil revenues remain higher than other revenues. Thus, thirty years of reform were still not sufficient to increase tax revenues.

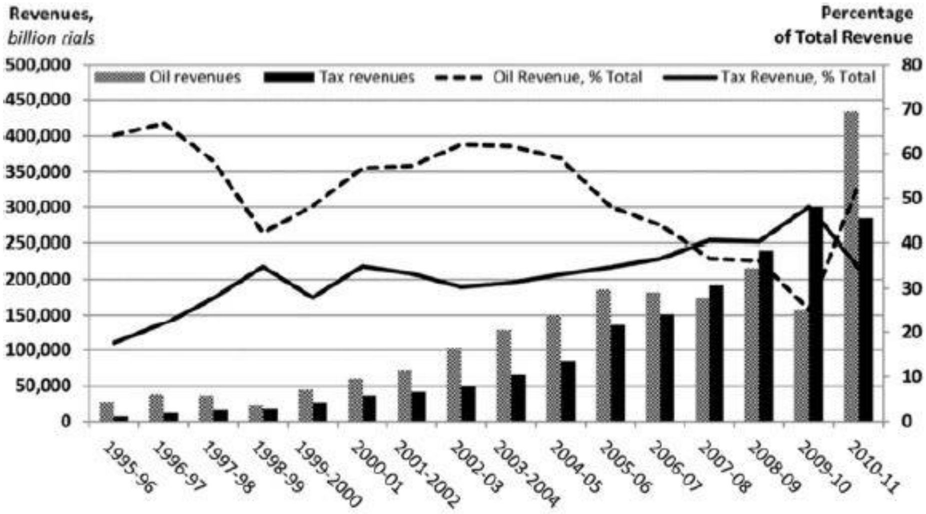

Figure 20 Iranian oil revenues vs tax revenues

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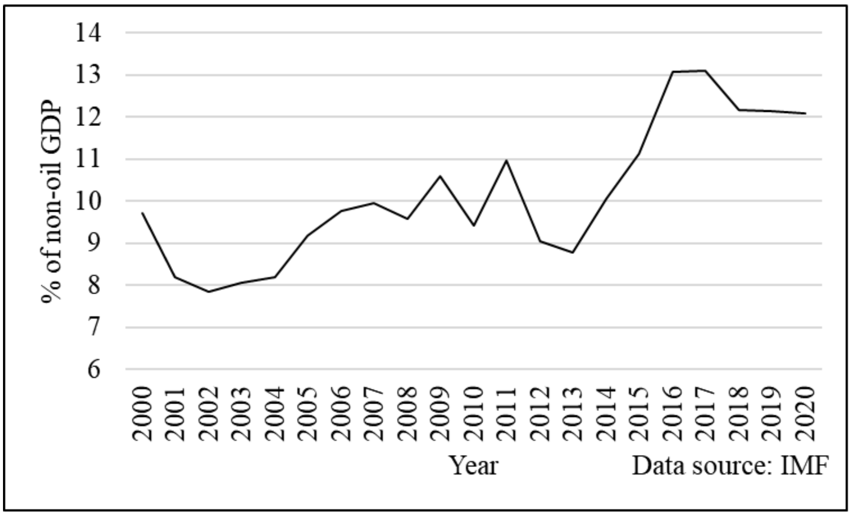

Figure 21 Iranian government non-oil revenues

Despite the continuous reliance on oil to fund government expenditures, Iran has succeeded to some extent in the diversification of the economy. The share of the oil sector in GDP accounts for only 12.3% of Iran's GDP (IMF, 2018b). However, the non-oil sector exports constituted just around 11% of GDP as of 2016 (Figure 22), reflecting the legacy of import substitution, reliance on domestic markets, and the impact of economic and financial sanctions.

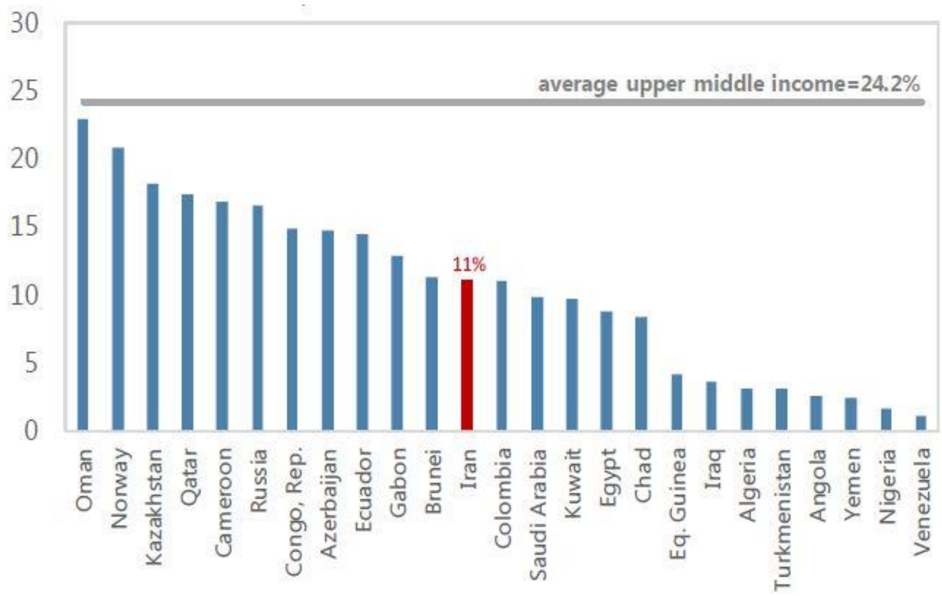

Figure 22 Iranian Non-oil exports as share of GDP

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Table 4 shows that petroleum remains the main exported commodity in Iran with polyethylene and other petrochemical and pistachios as the main non-oil exports. Figure 23 shows that between 2012 and 2018 the correlation between GDP growth and hydrocarbon sales was still positive confirming the limited success of economic diversification.

Export item	Value in USD	% of total exports
Mineral fuels including oil	48.7 billion	77.9%
Plastics	3.3 billion	5.3%
Ores, slag, ash	2.2 billion	3.5%
Organic chemicals	1.8 billion	2.9%
Iron, steel	1.4 billion	2.2%
Fruits, nuts	934.8 million	1.5%
Fertilizers	681.8 million	1.1%
Salt, sulphur, stone, cement	561.3 million	0.9%
Copper	386.2 million	0.6%
Aluminium	305.4 million	0.5%

Table 4 Iranian major exports

Data source: worldstopexports.com

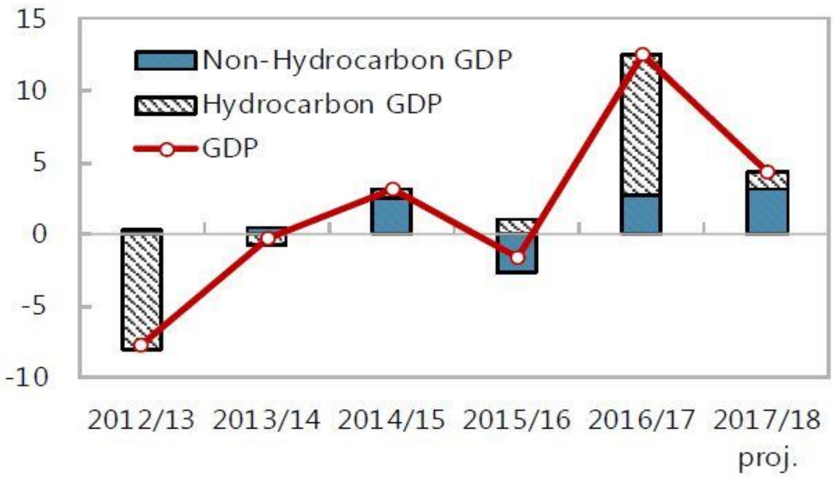

Figure 23 Iranian hydrocarbons contribution to GDP growth

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As stated earlier, privatisation and diversification aimed partially at attracting FDI to Iran. However, the share of FDI inflows to the Iranian economy were weak despite government incentives. In 2002, the Foreign Investment Promotion and Protection Act was passed to increase FDI by easing restrictions on market entry and foreign ownership. The aim was to increase competitiveness of Iranian companies, increase growth prospects, and continue diversifying economic sectors. However, FDI inflows were limited. Figure 24 shows FDI % of GDP in Iran has been limited to between 1-3% of GDP only. Comparing Iran to similar economies, Iranian FDI stock was relatively low (Figure 25). The reasons for such limited success in attracting FDI are several. First, Iran had an unfavourable investment environment with regard to regulation relatively to other countries (Karimian, Jaberi, Soltani, & Lorenz, 2016; Esfahani & Pesaran, 2009). Second, sanctions deterred many companies from investing in Iran or restricted such capacity (Azadi, 2018). Third, the attempted use of free trade-industrial zones as a backdoor to international and Iranian markets did not ease such situation because the government still controlled access to markets, which was unfavourable to foreign investors (Hakimian, 2011).

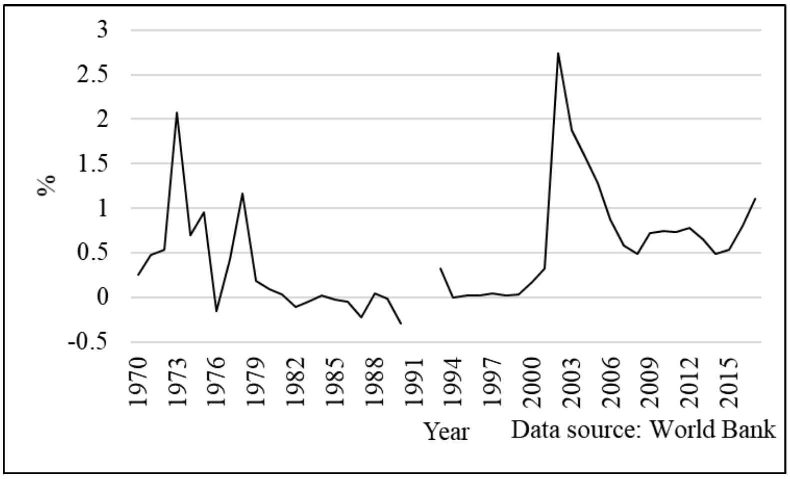

Figure 24 Iranian FDI as % of GDP

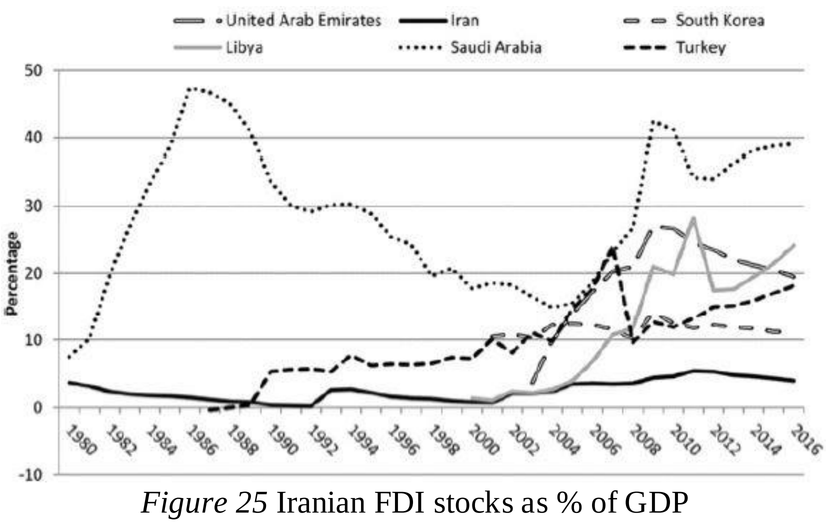

Figure 25 Iranian FDI stocks as % of GDP

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In complementarity to EL efforts, FL policies were introduced including capital account openness, a floating exchange rate, and allowing foreign ownership of domestic banks. As a result, Iran has engaged in international borrowing over the years. In the first five-year development plan between 1990 and 1995, the first permission was given to the Central Bank to accept liabilities of up to US$7.5 billion for investment in industrial and production projects (Pesaran, 2011). Consequently, the external debt of Iran increased over time. Nonetheless, it never reached a critical juncture except on one occasion in 1993 when the short-term debt could not be repaid on time due to a decrease in oil revenues (Pesaran, 2011). Thus, severe external indebtedness did not result from FL (Figure 26). This can be partly attributed to the limited capacity of Iran to take loans due to sanctions (Cordesman, Gold, & Coughlin-Schulte, 2014). This has often reduced foreign currency stock, which led to several currency crises of which the most recent took place in 2018 when sanctions were re-imposed by the US, which led to a significant drop in the Iranian currency value and the collapse of many financial institutions such as banks and non-official credit institutions (Cordesman, Gold, & Coughlin-Schulte, 2014; Leilah, 2018). A detrimental result of recurring currency crises and inadequate FL policy was chronic inflation, which increased consumer prices, reduced investments, and increased societal unrest. Figure 27 shows that inflation in the Iranian economy reached as high as 40% as of today. Overall, Iranian EFL have helped to increase regime stability in Iran by co-opting pivotal groups (merchants and industrialists) by means of patronage and by offering ordinary and poor citizens compensation for potential losses. Privatised SOE were mostly given to influential agents of the supreme leader, which ensured that liberalisation would not result a shift in power dynamics domestically. Iranians became more reliant on the state as they observed it abandoning historical legacy social programmes for more target social security programmes. Social justice shares were a populist measure that helped introduce privatisation while at the same time increased the regime's legitimacy among the poor to ensure their acquiescence. Several UN, US, and EU sanction resolutions have impeded Iranian EL and it is not clear how the process would have gone otherwise. Finally, Iranian elites remain at large loyal to the regime after going through 30 years of liberalisation. No significant shifts took place and thus the political regime stability remained sustainable.

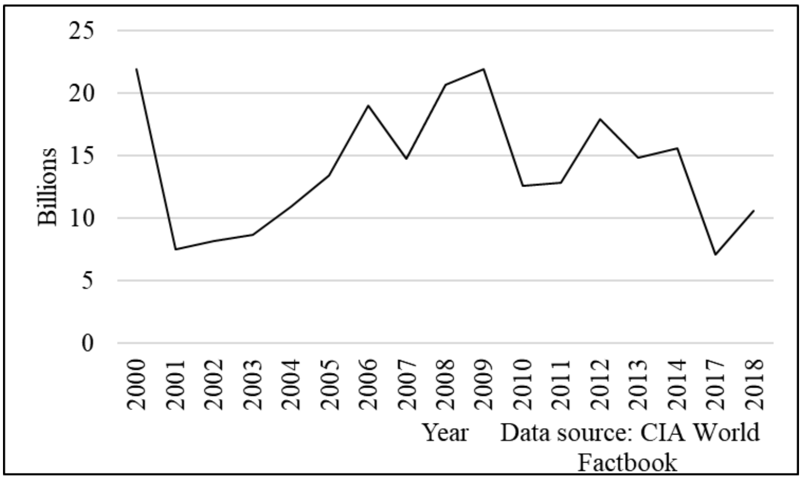

Figure 26 Iranian external debt in billion USD

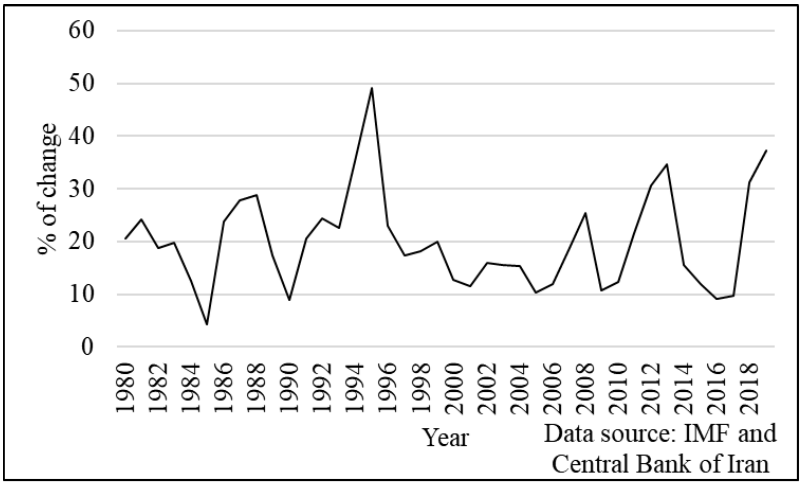

Figure 27 Annual official inflation % in Iran

4.2.2 Sources of regime instability

4.2.2.1 Growth, poverty, and income inequality

The Iranian revolution came to be partly as a representation of the lower classes disenfranchisement during the Shah’s regime and the feeling that income inequality and poverty reached intolerable levels (Vahabzadeh, 2016). Thus, the emerging Islamist regime has worked to ensure that its rural poor people support base is cared for (Farzanegan & Alaedini, 2016). This is due to a realisation, learnt by example, that if the poor dissatisfaction with the regime reached a great level, it can stir an uprising. Hence, economic growth has been a regime goal since the revolution. Figure 28 shows that since embarking on liberalisation in the 1990s, the GDP in Iran has grown. However, sanctions and drops in oil prices (particularly between 2011 and 2015) mostly interrupted that growth. The growth in GDP was associated with increases in GDP per capita that reached its peak in 2012 (Figure 29) at around $8 thousands. However, the continuous population growth and sanctions reduced GDP per capita to settle at $6 thousands by 2017. Thus, growth and growth prospects in Iran were a source of instability and protests to the regime (Cunningham & Mufson, 2018). As for poverty, the World Bank (2018) estimates that poverty has fallen from 13.1% to 8.1% between 2009 and 2013. This was attributed largely to the universal cash transfer program in late 2010, which preceded the elimination of subsidies on energy and bread. However, poverty increased in 2014, which may have been associated with a declining social assistance in real terms due to inflation. The continuation of the inflation problem has led many Iranians to protest government policy. The Iranian government responded with crackdown on protesters. As for income inequality, the Gini index of Iran decreased over the years of liberalisation (Figure 30). However, the World Inequality Database (n.d.b) reports that the income share of the top 10% earners remained 50% of total national income while the bottom 50% earners share of income remained low at 14.5%. Arguably, liberalisation did not contribute to reducing income inequality and it may have exacerbated it. Therefore, the Iranian regime may be in danger of popular uprisings motivated by a growing sense of disenfranchisement and a negative outlook of the economy.

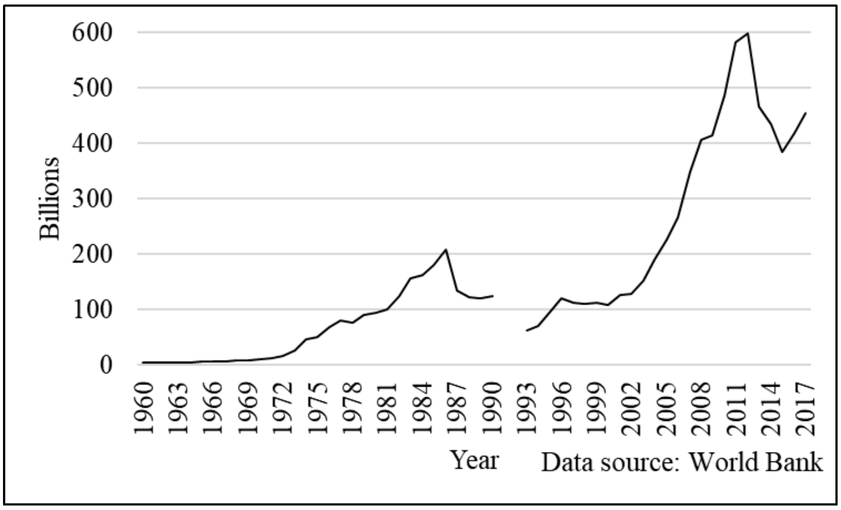

Figure 28 Iranian GDP in current USD

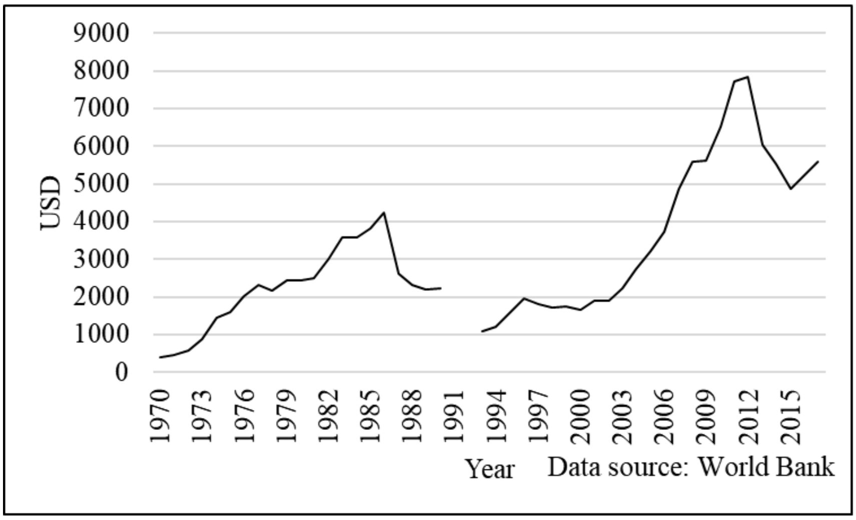

Figure 29 Iranian GDP per capita at current USD

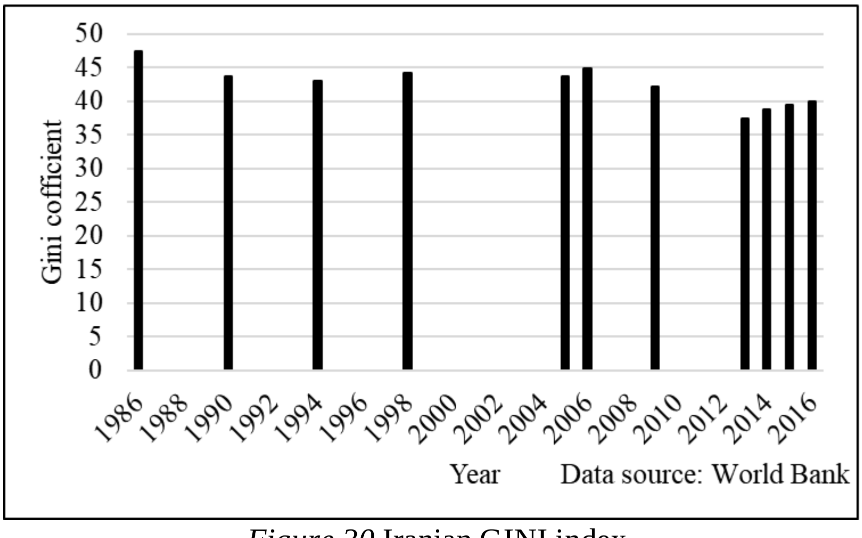

Figure 30 Iranian GINI index

4.2.2.2 Civil strife and minority succession

Civil unrest has been common in Iran. The drivers of such unrest have been demands for better living conditions, ethnic discrimination, and demands for reforms and democratisation and better working conditions by labour (Jones, 2011; Salehi-Isfahani, 2011; Parker, 2018). Many Iranians have seen their living conditions deteriorate over the years and their wages stagnate (Schwarz, 2018; Salehi-Isfahani, 2009). Furthermore, inflation and price hikes have often made life more expensive. This has regularly pushed Iranians to protest government policy and demand higher wages in some cases or the continuation or the increase of subsidies in others (Parker, 2018; Salehi-Isfahani, 2011). Minorities have particularly stood out in Iran as an instigators of civil unrest (Etheredge, 2011). Feeling discrimination and state oppression, many minorities, such as the Kurds and the Arabs, have often protested state policy and discrimination in government jobs, access to education, and linguistic rights (Beehner, 2006). For example, Arabs have protested their inability to teach their children Arabic in schools and expressed that the state's sanctions against their language rights is a form of racism and discrimination by ethnic Farsi state apparatus (Vahabzadeh, 2016). They have often complained about weak public investment in infrastructure despite the fact that their region is one of the richest in the country and where most of Iran's oil is extracted (Saikal, 2019).

The feeling of disenfranchisement has pushed some of the Arabs to seek secession and demand separation from Iran. Ahwazi Democratic Popular Front is a diaspora-based group that sought to attack Iranian forces in the Ahwaz region and claimed that it is actively pursuing secession from Iran to establish a state for its "people" (ADPF, 1990). Despite these efforts, the threat of secession never reached a serious level. The Iranian government has usually responded with crackdowns on minority group activists and sustained strong surveillance of their activities (Saleh, 2013). In 2009, the green movement has become one of the serious challenges to the Islamic regime (Saikal, 2019). Thousands of protesters took to the streets to protest what they saw as a fabrication of election results in favour of Ahmadinejad (Guzansky, 2014). The Iranian government responded harshly to the event and deemed it as an outside intervention disguised as a demand for democracy and transparency (Guzansky, 2014). Overall, Iran suffers from discrimination of minority rights, which may lead some, particularly Kurds and Arabs, to seek secession, which can stir significant instability for the regime.

4.2.3 Financial instability and the Iranian regime instability

Iranian policymakers were always suspicious of foreign capital (Pesaran, 2011). They saw it as a channel that can undermine the country's independence by increasing reliance on foreign sources of wealth and decreasing domestic wealth. When Iran endeavoured to stabilise its financial system in the 1990s by liberalising it, cautious was always exercised. Restrictions with regard to the amount of external debt, foreign ownership, or capital movement were implemented. Consequently, the Iranian currency witnessed a distressful life. To complicate the problem, financial sanctions and warfare against the country by the UN, the US, and the EU have led to loss of confidence in the currency locally, which reduced investments and deterred FDI as prices were not predictable (Habibi, 2008). Over the course of the Islamic regime, Iran has endured financial instability. First, it used financial repression to support the cronies of the regime (Namazi & Salehi, 2010). This was done by virtually granting zero interest rates to depositors to discourage saving. Furthermore, it granted cheap credit to the regime supporters (e.g., bazaar merchants for imports) in order to support industrialisation among other things. However, what in fact happened was that the regime cronies have taken advantage of the cheap credit to profit by arbitraging Iranian rial and dollars on the secondary and black market (Maloney, 2015). The result was limited import substation, continuous reliance on imports for domestic consumption, and great resources misallocation (Pesaran, 2011). This has alarmed the regime to start FL, which it did in the 1990s, but with limited success.

Second, the exchange rate regime has been of a theatre of political contestation in Iran. Before the exchange rate liberalisation, the Iranian currency was overvalued so that the government could offer advantageous credit rates to its supporting merchants and industrialists at the expense of consumers. It used a multiple exchange rate regime to do so (Steinberg, 2015). Until March 2000, the exchange rate system consisted of three approval rates: first, official floating rate \$1= rials 1758 (Taghipour, 2013). Second, official export rate \$1= rials 3000. Third, effective Tehran Stock Exchange rate, which was determined in the market. In 2000, the official export rate was abolished (Taghipour, 2013). In March 2002, the official exchange rate was lifted and the exchange rate system was unified (Taghipour, 2013). However, in late 2010, the single exchange rate regime could not be continued due to sanctions and the significant difference between the informal market exchange rate and the official rate. In October 2012, the government formed the Foreign Currency Trading Centre to deal with the crisis. Therefore, three rates were in the economy: first, Official rate (\$1=12260 rials) for basic and necessary goods, second, the exchange rate in the Centre, and third, the exchange rate in the informal market. Finally, the exchange rate was reunified in 2018 (Motevalli, 2018). However, due to shortage of dollars, black market operations continue to undermine the official market rate (Faghihi, 2018). The longer Iran's restricted access to international financial system persists, the more critical and the longer the Iranian currency crisis would be. This will severely influence the economy by undermining growth, consumption, investments, and public confidence in domestic currency. Well aware of the problem, the Central Bank of Iran has decided to introduce a new currency (Motamedi, 2019). It is yet to be seen if this will help lessen the impact of the problem on the Iranian economy and regime stability consequently.

Third, shadow banking in Iran has risen over the years. FL has encouraged depositors in Iran to give their savings to the banks to get interest. However, the IRGC have played this situation by starting their own credit agencies which offered suburban and rural population higher interest rates than the regulated banks could do to maintain profitability (as high as 50%) (Leilah, 2018). According to many sources, this problem has led to the countrywide protests that took place in 2017 and 2018 when people realised that many of these unregulated shadow credit agencies have defaulted and they lost their savings (Radio Farda, 2019). The government responded by asking these credit agencies to default, insured part of their losses, and merged many of them (Alhurra TV, 2019). However, many of these credit agencies remain unregulated today.

Fourth, economic and financial sanctions have severely curtailed the regime's ability to sustain its liberalisation programme. By restraining imports and exports and access to the international financial markets, the regime failed to offer political, economic, and financial stability to proceed with a successful liberalisation. In a country that is heavily dependent on imports for many of its consumer goods, the inability to acquire dollars or use them for trade have made the cost of importing higher to the regime (Reuters, 2019). Using its leverage in the international financial system, the US has worked hard to deploy its financial might and influenced its multinational financial institutions and their partners and allies not to accept money sourced from Iran and to freeze existing accounts (Dubowitz, Fixler, & Ziemba, 2015; Zarate, 2013). The regime was accused of funding terrorism, developing nuclear weapons, human rights violations, and destabilising the Middle East. The exact impact of such measures by taken the US and its allies is not easily measured, but there are many estimates. For example, sources say that around 150-400 billions of Iranian dollars assets are frozen abroad. The last round of sanctions, "Executive Order 13846 of August 6, 2018 Reimposing Certain Sanctions With Respect to Iran", is being enforced to cut Iran sales of oil and access to the global financial system (Exec. Order 13846, 2018). This will hurt Iranian liberalisation efforts and limit their success as the currency suffers and exports of oil and other goods are curtailed. Furthermore, the purchasing power of Iranians will suffer and inflation will increase. Recognising the problem, Rouhani has recently said, “America is trying to decrease our foreign reserves ... So we have to increase our hard currency income and cut our currency expenditures” (Reuters, 2019). Furthermore, he announced, “We should increase production and raise our (non-oil) exports and resist America’s plots against the sale of our oil” (Reuters, 2019).

Fifth, Iran has been known for having a chronic inflation problem and several currency crises. Today, the Iranian rial exchange rate stands at around 42000 rials for $1 (Figure 31). The reason for such problems varied over the course of Iranian regime life. At times, subsidy programmes offered by the government to its populist support base meant that the government had to print more Iranian rials to fund such subsidies since growth in the real economy was below the country’s needs (Guillaume, Zytek, & Farzin, 2011). Such an influx of rials meant that the government constantly had to adjust the exchange rate to reflect the change of exchange rates. Iranians bidding against the fall of their own currency has been another source of currency rate instability (Faghihi, 2018). Currency crises usually followed. Recently, the government decided to redenominate the currency in an attempt to control the problem (Motamedi, 2019). Such inflation problems destabilised the economic cycle and foreign investors’ trust in government policy and ability to protect prices.

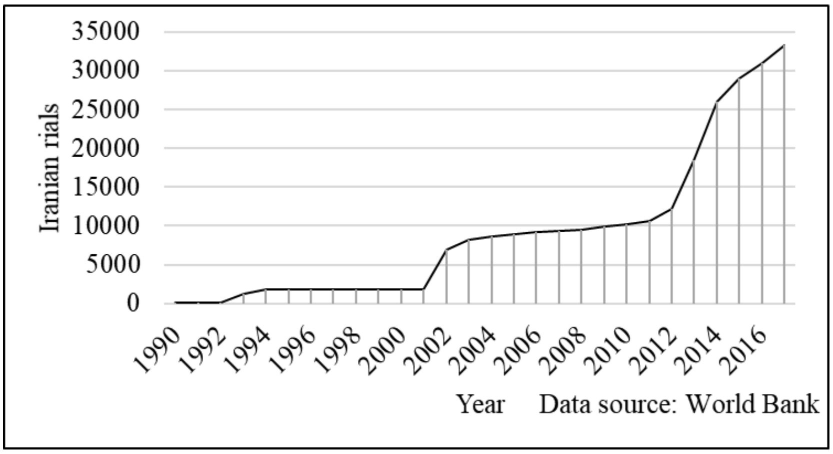

Figure 31 Iranian rials official exchange rate vs USD

Sixth, capital flight has been a problem that faced the Islamic regime since its reign to power. When the revolutionary forces took power, wealthy Iranians have started to move their capital abroad and sell off their assets at home (Maloney, 2015). As a result, a significant wealth loss happened. Furthermore, many technological skills and assets were missed, which dragged down the development of the economy. The loss of resources that took place continued after the revolution. Investors' distrust of government policy was always present due to perceived mismanagement of economic resources. Capital account liberalisation that followed FL made the process of capital flight easier and more intense. According to sources, $59 billion has left Iran just in the past two years alone (Radio Farda, 2018). This has made the economy more susceptible to government mishaps politically, particularly foreign adventures and international investors' scrutiny. The implications of capital flight were weaker economic growth, inflation, and greater income inequality. The expropriation of assets from the Shah's regime and his affiliates alarmed international investors, as the action was perceived as an attack on property rights and the capitalist economic system. This problem has continued even afterwards when several expropriation events took place. Therefore, in international rankings, Iran is ranked as a high risk for expropriation (Figure 32). This has set back international investors' confidence, as they doubt the regime commitment to protecting their ownership rights in cases of disputes. Overall, capital flight resulted a weaker economy, which undermined the regime stability.

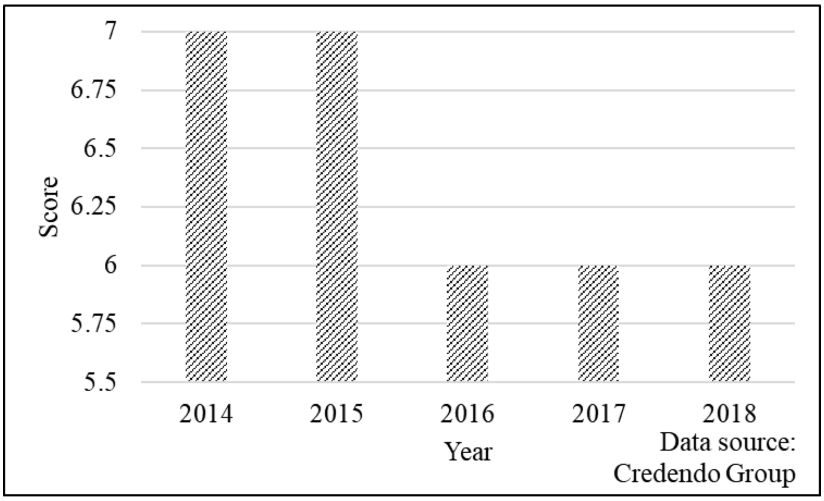

Figure 32 Iran's expropriation risk

4.3 Discussion and summary of findings

When comparing SA and Iranian regimes (in)stability, it is concludable that both have similar pillars of stability and sources of instability. However, what stands out as the defining line of their degrees of stability is the relationship between their financial stability and the regime's stability. On the one hand, EL reforms have reinforced both regimes' former support base and structure. Thus, it did not cause significant imbalances in power to cause political liberalisation and regime change. On the other hand, FL reforms have limited the regimes' power and stability. Due to finance influence on society becoming greater and outside of the hands of the regime, outside forces played a greater role in deciding the dynamics of how FL affected the regime's stability. This has been peculiar in Iran. Faced with international sanctions and warfare, Iran's regime ability to stabilise its financial system and the economy was significantly limited as it could not influence the international financial system. This has led to major disruptions to its economy such as slower growth and smaller FDI, societal discontent and protests, hyperinflation and currency crises, and general wearing out of regime domestic legitimacy and stability. Both SA and Iran enjoy a strong level of domestic security and a capable coercive apparatus as a hedge for potential instabilities. Religious legitimacy was used by both regimes to bolster their societal base and achieve foreign policy objectives. They have undergone EL with relatively similar outcomes; stronger position for regime cronies, greater involvement of the private sector, higher levels of growth, and reduced poverty. However, both seem to have sustained high levels of income inequality, which questions their commitment to societal stability in the face of potential increases in income inequalities. As the literature predicts, this may lead to political instability in the future.

Both regimes struggled in attracting FDI and preventing capital flight (SA was more successful, nonetheless) due to their own domestic policies entanglement with the regime's political survival calculations. What seems to differentiate SA from Iran is its financial links to the West and successfulness in FL. SA, due to petrodollar and historical alliance with the US, used oil revenues to ensure the regime had resources for cronies, economic development, military spending, and buying domestic acquiescence from the poor and the wealthy alike. Iran, on the contrary, struggled as its Islamic regime faced international sanctions since day one. Its inability to use the international financial system reduced its attractiveness for international investors, which reduced its ability to grow and gain knowledge through technology transfers. Furthermore, contentious foreign policy and international financial and economic sanctions made Iranians and internationals lose confidence in the currency, which have led to currency crises and hyperinflation episodes. Iranian multiple exchange rate regime was used to support the regime cronies businesses and when it was liberalising it was abused by them, which led to the collapse of the unitary exchange rate system several times and undermined the Iranian economy. The result of Iran's mismanagement of FL and subjugation to international sanctions has been greater regime instability due to loss of public confidence, isolation from the international markets, and downward economic conditions. Table 5 shows a summary of the research findings.

Factor	Iran	SA	
Regime structure	X	X	Pillars of stability
Security and coercive power	X	X	
Religious leadership	X	X	
Economic development and liberalisation	X	X	
Growth, poverty and income inequality	X	X	Sources of instability
Civil strife and minority secession	X	X	
Financial stability	0	X	
Outcome	Less stable	More stable	

Table 5 Summary of findings

Beyond SA and Iran, some generalisations can be made about FL influence on regime stability in the MENA region. First, countries that pursued FL are more susceptible to financial sanctions and warfare. Such legitimate threat means that countries are ought to be prudent so that they do not fall under such circumstances that would jeopardise political stability and cause societal unrest and economic slowdown. For example, pursuing a destabilising foreign policy may constitute grounds for international sanctions and thus it should be avoided. Second, domestically, governments that try to manipulate financial markets will encounter two main problems: capital flight and loss of public confidence in the national currency. Such problems will result in inflation and currency crises, which increases prices for consumers and reduces long-term FDI and consequently growth. Third, non-state actors pursuing regime change must be aware that the cost of regime change will be high as the national currency would struggle to gain back public confidence and the economy would struggle to regain access to international markets, which is necessary for economic growth. Thus, they are out to choose regime change tactics that reduce the damage such as non-violent protests. Lastly, FL policies can strengthen authoritarian regimes' stability without jeopardising their domestic balance of power insofar they ensure capital-friendly policies that do not turn away investors.

Chapter 5: Concluding remarks and further research

This thesis explored EFL policies theoretically and investigated how such policies can influence political regimes stability. EL was pursued by many developing countries in the 70s and the 80s in order to overcome fiscal crises caused by hikes in oil prices and increased public deficits due to social security programmes and subsidies. EL policies have helped many countries achieve growth and reduce poverty, but have also caused increases in income inequality. Politically, EL was resisted by vested interests at first as they feared it would affect their protected businesses. However, the resistance to EL faded over time. In some cases, EL caused political instability by challenging the power structure of the society and instigating class mobility. Income inequality and class played a critical role in deciding how EL affected the regime's political stability. In other cases, EL was still pursued despite the fear of societal and political instability. In these cases, EL success was limited due to the way it was implemented and political instability was limited to protests, violence, and troubled political life. Regime cronies, in these cases, were favoured and bought many of the privatised SOE along with favourable contracts with foreign investors. Ultimately, EL did not necessarily cause severe political instability.

In complementarity to EL, IMF and the World Bank, via the Washington Consensus, introduced FL policies to help fix the ills of developing countries' underdeveloped financial systems. Financial repression policies were abandoned and most governments pursued free capital movement, floating exchange rates, and allowed foreign ownership in banking sector. Politically, FL was resisted due to the fears of domestic banks that they would lose in unfair competition with foreign banks. Furthermore, the fears that FL would lead to political liberalisation by giving regime adversaries access to funds from international sources slowed down the process. The literature on the relationship between EL and political stability is rich.

Income inequality, resource endowment, linkages to the West, Western leverage, and geopolitics are but some factors that governed the relationship between EL and political stability in many developing countries. As for FL impact on regime stability, the literature on it is still limited and it is yet to be studied how FL affects political regime stability in developing countries. Early research shows that FL can help strengthen regime stability by amplifying resources available for investments, which increases employment and assets mobility and reduces the cost of government spending. Such dynamic co-opts labour and offers political and economic elites the benefits from FL with minimal disruption. An under-researched area of how FL influences regimes' stability in developing countries is how FL, in the presence of financial sanctions and warfare, can influence regime stability. The salience of FL relationship with political stability stems from its hidden and less public nature. Furthermore, FL policies tend to affect the entire societal relations indirectly. By being concerned with money that is involved in every citizen's life, FL policies tend to impact employment, wages, incomes, investments, and public spending. Each of these areas is loaded with political questions that arise once FL policies change the relationship among the different parts of society. For example, when credit is cheap due to easy access to international capital, the government can use that to legitimise policies, such as cutting public employment and inducing employment in the private sector as an alternative. As the literature discusses, such dynamics can increase or decrease regime stability. FL is more often entangled with international political conflicts. The use of sanctions and financial warfare is growing and becoming the favourable weapon for international political contestations. Whether between China and the US or Russia and the US, FL has put some countries in weaker position and others in a stronger position. In the event of financial crises, FL policies continuation distresses society and changes the political landscape. This research, therefore, hopes that it contributed to the emerging literature trying to understand how FL policies influences political stability in the age of financial crises, sanctions, and warfare.

Both SA and Iran have been dependent on oil revenues to bolster their regime survivability. However, such a view does not fairly describe the various elements of the development that took place in the SA and the Iranian economies in the past thirty years. Both countries have endeavoured to undertake EFL while keeping in mind the goal of sustaining the historical alliances that brought each regime together at inception. At this stage of liberalisation, Saudis seem to be keen to go further and increase their international business network and establish a regional alliance of business-friendly regimes in the region. Iran is also moving towards such a direction of more openness and liberalisation to its economic regime with emphasis on the role of the private sector for development. Nonetheless, Iran is strangled by its factional politics and unstable economic and financial policies. The most detrimental factor to Iran's ability to flourish is its failed FL that has undermined its EL efforts. The intervention of the supreme leader in economic and financial policymaking has undermined the ability of the government to undertake necessary policies. Faced with international financial and economic sanctions, the Iranian currency is in crisis constantly. Such a problem undermines any prospect for sustainable economic policy that can attract foreign investments and offer confidence. Capital account openness under such conditions has exacerbated the problem of capital flight and caused frequent speculations against the currency. Political instability due to the regime's domestic and foreign policies strangled the ability of the Iranian economy to be an attractive economy for foreign investors.

SA Vision 2030 promises much transformation to the economy's deadliest disease of over-reliance on oil revenues to achieve growth. However, the regime ability to reconcile the economic needs of the country with its domestic political system remains a challenge. Overall, SA outlook will remain stable in the near future. Iran, however, is less stable and more prone to crises, particularly financial ones. The regime is rapidly responding to the financial warfare that targets it of which sanctioning the IRGC was the latest episode. Currency swaps, bartering, and using cryptocurrencies and gold are few alternatives to using the dollar the Iranian regime have identified and practiced. Such moves may give the Iranian regime an extended lever to stabilise and reinforce its survival. As for future research, this research shed light on often-overlooked part of authoritarian regimes survival mechanisms. In the MENA region, governments ought to become prudent and risk averse so they do not fall under any financial traps that may affect their economic life or political survival. An interesting future research direction to be taken by MENA scholars is to study the impact of FL policies on Erdogan's regime stability. Furthermore, it would be interesting to investigate the use of financial warfare to influence regime stability in Yemen, Syria, and Lebanon and how such policy interacts with FL policies in these respective countries.

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