

**RESTRUCTURING AND ECONOMIC REFORM
IN THE
KINGDOM OF SAUDI ARABIA**

OCTOBER 2003

The Saudi Arabian Government has implemented a number of structural reform measures to encourage Foreign Direct Investment (FDI), real GDP growth and employment of nationals. These ambitious efforts include privatizing twenty (20) major state enterprises, setting up fourteen (14) regulatory authorities to implement the reform, improving foreign investment laws, revising a broad range of commercial laws, implementing intellectual property rights, and seeking membership in the World Trade Organization (WTO).

This report covers:

Development Plans	Page 2
Economic Indicators	Page 2
Saudi Arabia and Economic Reform	Page 4
Saudi Arabia and Privatization	Page 6
Saudi Arabia and Foreign Investment	Page 8
Saudi Arabia and Oil	Page 9
Saudi Arabia and Economic Diversification	Page 10
Saudi Arabia and Employment	Page 11
Saudi Arabia and New Legislation	Page 13

DEVELOPMENT PLANS

The Kingdom of Saudi Arabia follows economic development plans in order to achieve diversification and growth. This planning process has proven to be successful in the Kingdom's rapid and ongoing economic development.

The first Five-Year Development Plan (1970-1974) was introduced in 1970. The first phase of this process involved establishing an infrastructure that could support a modern economic base. The next step was to develop the human resources necessary to implement the economic transformation. Finally, the focus shifted to economic diversification, including the expansion of the industrial and agricultural sectors. This stage is now well advanced.

The Fourth (1985-89), Fifth (1990-94), Sixth (1995-99) and Seventh (2000-04) Development Plans have all emphasized strengthening the growing private sector and increasing the efficiency of the industrial sector. With the upcoming completion of the Seventh Development Plan, the Ministry of Planning and Economy is preparing for the Eighth Five-Year Plan (2005-09). Its focus is on higher growth rates, increased investment, foreign as well as domestic, and continuing to develop human resources. Its emphasis is on the commitment to a long-term development strategy linked to time frames and quantitative objectives.

ECONOMIC INDICATORS

The best indicator of Saudi Arabia's economic growth is the increase in the gross domestic product (GDP). On July 22, 2003, Minister of Petroleum and Mineral Resources Ali Al-Naimi stated: The Kingdom's GDP has grown from U.S. \$20 billion in 1970 to \$190 billion today, a remarkable nine-fold increase. Saudi Arabia's current economy is now the largest in the Middle East, with a potential for even more substantial growth.

Another indicator is that Saudi Arabia has received an A credit rating by Standard and Poor's with regard to both long-term and short-term local and foreign currencies based on the Kingdom's macro-economic stability and substantial external liquidity.

Today, Saudi Arabia stands as the world's 25th largest importer/exporter with a foreign investment trade balance of \$78 billion. In 2002, trade between Saudi Arabia and the United States, the Kingdom's largest trading partner, totaled some \$17.9 billion.

On July 31, 2003, Saudi Arabia and the United States signed an agreement on the development of commercial and investment relations between their two countries. The U.S.-Saudi Council for Trade and Investment was established to meet at least once a year and representatives of both countries will review the signing of additional agreements on trade, protection of intellectual property rights, investment, vocational training, and environmental issues. With about 280 Saudi-U.S. joint ventures, American companies are the largest group of foreign investors in the Kingdom.

Saudi Arabia is the world's largest producer and exporter of oil and has the world's largest spare production capacity. The Kingdom has utilized oil revenues to expand and diversify the Saudi economy in order to reduce its dependence on oil. Efforts to promote growth in the non-oil sector have resulted in impressive gains. In 2002, non-oil exports grew by 5.7 percent to reach \$8.65 billion, while the number of operating factories rose from 199 in 1970 to 3,381 by 2001.

In response to the positive progress in economic reform, the Saudi bourse, the most capitalized stock exchange in the Arab world, recently surged to an all-time high of more than 3,600 points on June 16, 2003. This peak was partly the result of endorsement by the Council of Ministers of the Capital Market Law establishing a formal stock exchange in the Kingdom.

“The underlying goal of these reforms is to realize the country's vast economic potential while creating new opportunities both inside and outside Saudi Arabia, and to expand and diversify the Kingdom's economy while creating job opportunities for a rapidly growing population.”

**Ali Al-Naimi, Minister of Petroleum and
Mineral Resources, July 22, 2003**

SAUDI ARABIA AND ECONOMIC REFORM

The following is a list of agencies established to help implement economic reform in Saudi Arabia.

Supreme Economic Council (SEC)

In August 1999, Saudi Arabia announced the formation of the Supreme Economic Council (SEC). The SEC evaluates economic, industrial, agricultural and labor policies to assess effectiveness. Privatization efforts have gained momentum since the creation of the SEC, which oversees economic restructuring aimed at opening Saudi markets and attracting investments.

Saudi Arabian General Investment Authority (SAGIA)

In April 2000, the Saudi Arabian General Investment Authority (SAGIA) was set up to further promote foreign investment and serve the business community as a one-stop shop. The 2000 Foreign Investment Law included property ownership rights for foreign investors as well as reducing tax rates. SAGIA works with the Supreme Economic Council and the Supreme Commission of Tourism and serves as a mediator between investors and the government.

Supreme Council for Petroleum and Minerals (SCPM)

Saudi Arabia established the Supreme Council for Petroleum and Minerals (SCPM) in January 2000 as a body responsible for policymaking on the exploitation of petroleum, gas and other hydrocarbon materials. The SCPM passed the Gas Initiative to further develop national gas fields and related petrochemical projects.

Supreme Commission of Tourism (SCT)

The Supreme Commission of Tourism (SCT) was established in April 2000 to help the tourism sector grow and coordinate with the private sector for further investment. Each year, two million Muslims from all over the world visit Saudi Arabia to perform the Hajj, and many more come to perform the minor pilgrimage of Umrah. But the Kingdom also hosts non-religious tourism. Saudi Arabia is rich in history and culture and has a variety of tourist attractions to offer, including archeological sites, varied landscapes and shorelines rich in marine life. A \$1.5 billion expansion of King Abdulaziz International Airport in Jeddah will be implemented in 2003 to accommodate an additional 13 to 21 million passengers a year.

Food and Drugs Authority (FDA)

In March 2003, a Food and Drugs Authority (FDA) was established to secure consumer protection regarding the safe utilization of all foodstuffs, pharmaceuticals, medical devices and electronic products.

In addition, the following initiatives have been taken:

Enacting the GCC Customs Union

The Customs Union was established on January 1, 2003 by the Gulf Cooperation Council (GCC) to standardize customs duties in the six member countries. In accordance with the Customs Union, the Government of Saudi Arabia approved the reduction to 5 percent of customs for goods formerly charged 12 percent and 7 percent. The GCC further agreed to the principle of single port of entry. Most related laws and regulations will be standardized by the end of December 2005.

Applying for accession to the World Trade Organization (WTO)

Saudi Arabia is currently one of the largest economies outside the World Trade Organization (WTO). Recent steps towards privatization and market liberalization have called for fresh negotiations regarding Saudi Arabia's bid to join the WTO. The Council of Ministers approved a new Copyright Law on June 9, 2003 consistent with the WTO agreement on trade-related aspects of intellectual property rights. In addition, the Kingdom of Saudi Arabia and the European Union signed a bilateral agreement on August 31, 2003, guaranteeing free access to goods and services. In the accession process, the Kingdom is negotiating bilateral agreements with current WTO members while adopting the organization's trade rules. Saudi Arabia has already signed 14 bilateral trade agreements with other members of the WTO, including Japan, Canada, Brazil, Argentina and Australia. Membership will bring a wide range of benefits to Saudi Arabia, including economic expansion.

Proposing the Charter to Reform the Arab Stand

In January 2003, the Kingdom of Saudi Arabia presented a new initiative entitled 'Charter to Reform the Arab Stand'. The initiative encourages economic and political reforms as well as greater economic integration in the region and broader participation by Arab citizens in the political process. As part of an economic reform agenda, the initiative calls on Arab states to implement a Greater Arab Free Trade Area (GAFTA) that will result in unified tariffs and duties by the end of 2005, a move that will serve as the basis for the establishment of a Common Arab Market (CAM). The initiative also encourages members of the Arab League to modernize local economies, privatize government-owned industries and open economic development to outside investment and participation.

SAUDI ARABIA AND PRIVATIZATION

In November 2002, the Kingdom of Saudi Arabia announced plans to privatize many of its vital economic sectors. The Supreme Economic Council has taken overall charge of the program, specifying the activities to be privatized and setting out a strategic plan and timetable for the privatization program. Sectors open to privatization include: telecommunications, civil aviation, desalination, highway management, railways, sports clubs, health services, government hotels, municipal services, education services, operation and management of social service centers, Saudi employment services, agricultural services, construction and management of abattoirs, public parks and recreation centers, and cleaning and garbage disposal services.

Concrete examples of privatization efforts include:

Telecommunications

In December 2002, the Saudi Telecom Company (STC) began the process of offering shares for sale in the largest privatization in the Kingdom since 1984, selling 30 percent of its shares valued at approximately \$4 billion. In January 2003, the Saudi Telecom Company IPO was declared a huge success, and in April, it was announced that STC's first quarter net profit had more than doubled, increasing to \$603 million.

Postal Services

In 2002, the Saudi government approved the transfer of the responsibilities of the state-run postal services from the Ministry of Posts, Telegraphs and Telephones (PTT) to the private sector. In January 2003, Director General of Posts at the PTT, Dr. Khaled Al-Otaibi, reported that privatization of the postal services has been operating successfully, with about 100 agencies set up by the private sector. In April 2003, the Ministry was renamed Ministry of Communications and Information Technology.

Saudi Railway Organization (SRO)

The government has started the initial stages of research and planning to expand the existing railway network and is encouraging the private sector to participate and invest in this project. The initial phase of the proposed expansion would be a 590-mile line from Riyadh to Jeddah, a 354-mile line from Jeddah to Madinah via Makkah, and a 71-mile line linking Dammam with Jubail. The possibility of having a northern line from Riyadh to the Jordanian border is also under consideration.

Saudi Arabian Airlines (SAA)

Saudi Arabian Airlines is the largest airline in the Middle East, with a fleet of 117 aircraft carrying over 12 million passengers per year to 50 cities on four continents. Research has begun for its partial privatization. The privatization effort promises to be a successful endeavor resulting in increased revenues and enhanced performance. In addition, the SEC approved, in June 2003, the opening up of the Saudi aviation sector to private enterprise, giving national companies the opportunity to provide domestic airline services and ending SAA's longstanding role as the sole domestic carrier.

Ports Authority

The Ports Authority already assigns many projects to the private sector to expedite the handling of goods and maritime services. For instance, King Fahd Vessel Repair Yards and sections for processing re-exports at Jeddah Islamic Port and King Abdulaziz Port in Dammam are handled by the private sector.

Health Care Sector

In April 2003, the Ministry of Health announced that it had employed a private company to promote its pre- and post-natal healthcare education program. The program has been introduced in more than 85 percent of the Kingdom's hospitals.

Urban Transportation System

Transportation Minister Dr. Jubarah Al-Suraiseri announced in August 2003 that plans are under way to privatize and reorganize the transportation system of the cities in Saudi Arabia. The development of urban transport will be carried out by the private sector as the government wants to increase private sector participation, he said.

"First of all, I wish to make clear that the government of Saudi Arabia has since the very beginning been extremely supportive of the private economic sector."

**Crown Prince Abdullah, Asharq Alawsat,
(Arabic daily), May 13, 2003**

SAUDI ARABIA AND FOREIGN INVESTMENT

Foreign Investment Law

The Foreign Investment Law, enacted by the Saudi Arabian General Investment Authority (SAGIA), was set up to allow foreign investors to own property, transfer capital and profits, claim full ownership of their projects and enjoy a reduction in tax rates. The law protects foreign investors from confiscation of property without a court order or expropriation of property except for public interest against an equitable compensation. In August 2002, SAGIA passed an amendment to the Executive Rules of the Foreign Investment Act strengthening the legal framework and, for instance, allowing foreigners to own land and avoid double taxation.

Telecommunications

The Saudi Communication Commission (SCC) was established on December 29, 2001, to open up the market and enable foreign companies to invest in telecommunications.

Insurance

The new Insurance Law was passed on July 14, 2003 and will establish legal structures governing insurance and reinsurance transactions in the Kingdom. Foreign companies are encouraged to invest in the insurance sector.

Saudi Railway Organization

In January 2003, the Kingdom of Saudi Arabia short-listed eight foreign companies to consult on a 1,000-mile railway project. The winner will work closely with European and North American companies to expedite the project.

Energy Sector

As a result of the Government's push to increase foreign investment and expand the country's economic base, an agreement was reached on July 16, 2003 with a consortium comprised of the international oil companies Royal Dutch/Shell and TotalFinaElf with regard to upstream gas operations in the southern part of the Empty Quarter [Rub' al-Khali]. Saudi Aramco will take a 30 percent share in the project, one in a series of upstream gas projects that were envisioned by the Crown Prince and which will be executed by international oil companies.

Mining

In April 2003, the Minister of Petroleum and Mineral Resources announced that a new mining strategy was being finalized to bolster private investment in the mining sector. The new mining law would allow local and foreign investors to explore the country's mineral resources and create new jobs. The minerals include phosphate, iron ore, bauxite, zinc and copper.

Health Care Sector

In August 2003, the Ministry of Health announced its support for new laws to facilitate the transfer of some state-run hospitals to the private sector. In addition, the new laws allow foreign investors to own hospitals according to government regulations. The foreign investor does not need to have a medical background and does not require a Saudi sponsor.

Water and Electricity Sector

In August 2003, the Ministry of Water and Electricity invited Saudi and international companies to bid on water desalination and electricity projects worth more than \$8 billion. The offers will be opened in March 2004 and the Ministry plans to invite national and international bidders for three additional projects.

SAUDI ARABIA AND OIL

In 2002, Saudi Arabia's total oil revenue was estimated at around \$65 billion. Oil prices averaged \$23.72 per barrel and production averaged over 7 million barrels per day. In the fall of 2002, in order to maintain market stability, Saudi Arabia boosted oil production to compensate for the fall in Venezuelan production, and in the spring of 2003 it boosted output to compensate for the loss of Iraqi production.

The Kingdom has long held the view that unstable energy markets and unrealistically low or high oil prices harm both producers and consumers. After the horrific attacks on September 11, the Kingdom assured the world it would keep prices stable and supplies flowing. It dispatched 9 million barrels of oil to the United States to ensure price stability and availability. As a consequence, prices dropped from \$28 to \$22 per barrel.

On July 26, 2003, Crown Prince Abdullah presided over a meeting of the Supreme Council for Petroleum and Minerals (SCPM) that confirmed the continuation of the Kingdom's moderate policy that aims at achieving oil market stability in a way that guarantees the interests of both producing and consuming countries, the continuation of world economic growth, and stability of oil supplies and prices at reasonable levels.

At the World Economic Forum annual meeting on January 25, 2003, Al-Naimi stated:
"We have always said that regardless of the cause of the shortage, OPEC and Saudi Arabia will do their utmost to make up for the shortage."

SAUDI ARABIA AND ECONOMIC DIVERSIFICATION

According to a study conducted by the Saudi British Bank (SABB), Saudi Arabia's non-oil sector is expected to maintain growth in 2003 at a rate of 3.5 percent. Furthermore, from a low of near 40 percent of fixed investment, the non-oil private sector has risen to around 75 percent. In addition, the Middle East Economic Digest (MEED), in its latest quarterly edition of the Saudi Arabia Market Report, states that the Kingdom will witness its best year since 1981 in terms of growth, exports, balance of payments, and budget.

In 1975, Saudi Arabia had about 470 industrial plants with overall investments estimated at \$2.7 billion. By 2001, the total number of factories in the Kingdom had reached 3,381 with a total investment of over \$90 billion.

Production of gas—The Kingdom has the fourth largest non-associated gas reserves in the world. This sector is targeted for expansion.

Petrochemicals—The Saudi Basic Industries Corporation (SABIC), established to promote industrialization within the Kingdom, is one of the largest petrochemical producers in the world.

Mining—Saudi Arabia has the largest mineral resources in the region, including precious and base as well as industrial minerals. The government is encouraging enterprises for extracting and processing the minerals to make Saudi Arabia a leading exporter. U.S. companies play a major role in this area. In addition, the new mining law, anticipated to pass by the end of this year, will facilitate private investment by local and international investors.

Construction Materials—The Kingdom of Saudi Arabia is the largest producer of construction materials in the Middle East. Its products, which include cement, tiles, marble, glass, granite, cable, air-conditioning equipment, fabricated iron and fabricated steel are exported throughout the region. In 2002, the cement sector grew 17.2 percent.

Pharmaceuticals—Saudi Arabia has a large and growing pharmaceutical sector that manufactures products for the domestic market and exports to other countries in the region.

Banks—In the past decade, Saudi Arabia's 10 licensed commercial banks have seen a substantial growth in domestic banking. In 2001, combined capital and reserves of the banks increased to \$11.7 billion, with total assets of \$123.5 billion.

Stock Exchange—The Stock market has developed substantially over the past decade, and is by far the largest in the Arab world, with a capitalization of over \$80 billion at the end of 2002.

SAUDI ARABIA AND EMPLOYMENT

The following information is based on a report released in September 2002 by the Central Department of Statistics (CDS) of the Kingdom's Ministry of Planning on the labor force and employment for the year 1999.

Employment Figures

The total population in Saudi Arabia increased from 12 million in 1980 to more than 21 million in 2000. The Saudi labor force is defined as all Saudis, 15 years of age and older, who are either employed or seeking a job, and amounts to 2.82 million (consisting of 2.41 million males and 413,000 females) with an unemployment rate of 8.1 percent, 6.8 percent of the males and 15.8 percent of the females being unemployed. The labor force is estimated to grow 5 percent a year and could grow to 4.8 million jobseekers in the year 2010.

The labor participation in Saudi Arabia is low due to its largest demographic, which consists of its young population, and because it has a lower participation of women compared to other countries. As a consequence, Saudi Arabia has a high dependency ratio, averaging 6 dependents for one worker.

The Creation of Job Opportunities

The Saudi government seeks to create jobs for women as well as men through the various reforms addressed in this booklet including diversification, privatization, opening up the market and other initiatives such as the following:

The National Program for Training and Employment

The National Program for Training and Employment helps Saudi men and women find jobs in both the public and private sectors. The Program is responsible for the creation of job opportunities, job training and Saudization.

Saudization

Saudization is a measure that applies limitations on the number of foreign workers employed in order to slowly increase dependency on Saudi workers. In 1999, the non-Saudi population totaled 5.02 million, and its labor force was 3.02 million. In April 2003, the Ministry of Labor and Social Affairs reported that 501,102 Saudis are currently working in the private sector. The Government continues to urge businessmen in the private sector to get involved in job training as well as opening up more employment opportunities for Saudi nationals.

Employment of Women

Over the past two decades, the percentage of Saudi women in the workforce has grown from just 1 percent to 7 percent. This number is expected to increase at an accelerated rate. Saudi women are owners or part owners of over 22,000 businesses, and thousands of women invest in stocks. Computer, accounting and banking training centers have been established to train women for jobs that will not violate Islamic and social traditions. Recently, Saudi Arabia announced that women are encouraged to pursue careers in technological, automotive and other industrial sectors.

SAUDI ARABIA AND NEW LEGISLATION

The Capital Market Law

In July 2003, the Council of Ministers passed the new Capital Market Law, which allows financial opportunities for both Saudi and non-Saudi institutions. The new law will (1) establish the Saudi Arabian Securities and Exchange Commission to protect investors; (2) license brokerage services; and (3) establish a new and privately owned Saudi Arabian Stock Exchange (SASE).

Stock Exchange

The new Capital Market Law establishes a new stock market, the Saudi Arabian Stock Exchange (SASE), that will be privately owned. The board will include government officials and shareholders of the Stock Exchange. It will be the only Stock Exchange in the Kingdom and will ensure fairness and transparency of the markets and maintain high standards of corporate governance.

Mining Code

In April 2003, Minister of Petroleum and Mineral Resources Ali Al-Naimi announced the drafting of a new mining law to come into effect at the end of this year. The new mining law will facilitate private investment by local and foreign investors in non-hydrocarbon minerals.

Other issues to be addressed in 2003/2004 are new laws governing companies, agencies, commercial competition, and anti-trust measures.



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