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Saudi Arabia Enters The 21st Century:

VIII. Saudi Arabia at the Start of the 21st Century: Key Conclusions

Final Review

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Saudi Arabia faces a wide range of challenges as it enters the 21st Century. These problems include foreign policy and security, internal political stability, Islamic extremism, demographics and over dependence on foreign labor, restructuring and diversifying the economy, and developing the oil and gas sectors in ways that meet the is the domestic challenges that are most likely to challenge Kingdom’s long term needs. All of these challenges are important, but Saudi Arabia is scarcely a fragile state or one without allies.

It is not foreign threats, but internal challenges which pose the most serious threat to the Kingdom’s future. The Saudi Arabia of the 21st Century must evolve into a very different state from the Saudi Arabia of today. It must move from oil wealth to a more diversified economy or it eventually sink into oil poverty. It may not need Western style democracy, but it does need political reform, modernization of its government, and more advanced forms of consultation. Saudi Arabia can only deal with Islamic extremism if it reshapes its Islamic practices to make them more tolerant and more flexible, and evolves a clearer picture of what Saudi society should become.

Saudi Arabia must deal with major population problems, sharply reduce its dependence on foreign workers, and shift its youth from dependence on the state to a competitive role in the global economy. Saudi Arabia must also shift its energy sector from one dependent on state investment to one with enough private investment to reduce the strains on the Saudi budget while steadily expanding production to meet world demand.

Political Change

While Saudi Arabia must remain sensitive to its Islamic character, it must ensure that Islamic extremism cannot challenge the legitimacy of the government or block social and economic change. Saudi religious practices now make far too many concessions to hard-liners and extremists, and live in the past, rather than seek to adapt to the future. They oppose, rather than propose.

Saudi Arabia's political system must evolve if it is to preserve its internal stability. The Kingdom must continue to expand the role of the Majlis, and find ways of allowing peaceful debate of social and economic issues. It must preserve the almost universal Islamic character of the Saudi state and society while resolving the differences between modernism and traditionalism. It must allow popular debate and increasing popular control of its national resources. It must come to grips with the issue of defining a rule of law that applies to all its citizens, and to the royal family as well as ordinary citizens. It must create better legal protection of human rights and provide for a uniform commercial code and fully competitive privatization, while resolving the inevitable tensions and conflicts between religious and civil law.

The leadership of the royal family needs to set clear limits to the future benefits members of the royal family receive from the state and to phase out special privileges and commissions. It needs to transfer all revenues from oil and gas to the state budget, rather than allow some to be treated differently by members of the royal family and to ensure that princes obey the rule of law and are not seen as "corrupt" or abusing the powers of the state. The royal family already has the wealth to do this, and it does not take much vision to see that the Saudi monarchy cannot give 15,000 princes the same rights and privileges it once gave several hundred. The vast majority of the royal family will have to be cast loose from state support and forced to earn its own living.

The Majlis as Shura needs to be steadily expanded in power, and in regional and sectarian representation, to provide an evolution towards a more representative form of government. The Majlis has made a good beginning, but it needs younger members, members that are moderate critics of the royal family, and some Shi'ites that are permitted to speak for this ethnic group. It needs to play a more direct role in reviewing the Saudi budget, and its debates need to be more open and reported in the media. It may be some years before Saudi Arabia is ready for an elected Majlis or National Assembly, but the Saudi government needs to be more open and some body other than the royal family needs to be seen as playing a major role in decision-making. The present closed, over-centralized process of government breeds extremist opposition.

Saudi Arabia must be given a "rule of law" which gives guarantees to its peaceful opposition to openly criticize the government, and which protects human rights. A lack of repression is certainly more important in the near-term than a formal movement towards stronger representative government. While Saudi Arabia has never been particularly repressive, it must do better and it must also place firm limits on its legal abuses by its Islamists and religious police.

A modern commercial rule of law is equally important. The Saudi private sector and foreign investment need to be able to operate in a secure environment that makes Saudi commercial practices competitive on a global basis. The occasional legal abuses of princes, ministers, and the privileged and the tolerance of excessive corruption, are dated remnants of the past.

Population, Youth, and a Vision of the Future

Saudi Arabia needs to face the fact that its most serious threat is its own population growth. The failure of the Arab and Islamic world to face demographic realities has been an act of continuing intellectual cowardice and one of the great disgraces of the 20th century. This cowardice cannot be allowed to continue long into the 21st century.

The Saudi royal family, Saudi government, and the people of Saudi Arabia must come to grips with the fact that Saudi oil wealth is limited, that economic reform and diversification can only evolve slowly and face serious structural limits, and that Saudi Arabia faces a potential demographic crisis. Strong leadership is needed to persuade the Wahhabi ulema that voluntary population control is needed and Saudi families that they should limit their number of children. There needs to be a firm understanding that even the best economic development plan cannot maintain the present standard of real per capita wealth in Saudi Arabia without a sharper decline in the birth rate and that population growth is a major factor affecting political stability.

At the same time, these same demographic pressures illustrate why the government cannot succeed in dealing with Islamic extremism by a combination of accommodating the most fundamental and regressive Wahhabi practices while forcibly repressing Islamic extremists that actively criticize the government. These policies are dragging Saudi Arabia back into a past that cannot be viable in the future and which makes the problems young Saudis face in finding rewarding careers and a valid place in society even more difficult. The Saudi royal family and government need to face the problem of social alienation and religion much more directly, and push for slow but steady reform. They need to face the fact that the present cost of such efforts at change is likely to be much lower than waiting and relying on the present policy.

Social reform requires religious reform and evolution. Islam is more than flexible enough to deal with any pace of social and technological change, but Saudi Arabia must encourage such change. The Saudi royal family and government, as well as all educated Saudis, do, however, need to start asking existential questions about the future of Saudi social customs and religious practices, and about the role of young Saudis in an evolving society. Even today, most educated Saudi women face a dead end at the end of their education and most Saudi young men graduate into purposeless jobs that offer little real future or productive value to the economy.

The impact of Saudi religious practices and demographics on Saudi society and the Saudi job market has been partially disguised by the fact that half of the population is still under 18 and living with an extended family. With the next half decade, however, something like 20% of the present native population want real jobs and careers. Unless Saudi Arabia succeeds in reform, it will have no where to go. Only radical efforts to stimulate the private sector and remove foreign labor can begin to deal with this problem.

This need for steady evolutionary reform does not mean Saudi Arabia should be an imitation of the West. Saudi Arabia must find its own path within these constraints. It is unrealistic and impractical for Saudi Arabia to attempt to adopt Western standards of human rights. The West needs to be careful not to be trapped into supporting the efforts of Islamic extremists who claim to advocate human rights and democracy as a way of attacking the Saudi regime. At the same time, Saudi Arabia does need to give Saudi Shi'ites a special religious status and proper economic rights, emphasize the protections of the individual already granted under Saudi law, and sharply rein in the growing abuses of the religious police. The government must reestablish public faith in the Saudi legal process and the rule of law.

The Need for a New Social Contract

Saudi Arabia's present and structural economic problems must be kept in careful perspective. None of its near to mid-term financial problems are critical. The Saudi government may be acting slowly, but it has recognized virtually all of the nation's economic problems except the need to reduce the rate of population growth. Many of the solutions the government has identified are workable, and Saudi Arabia has ample time in which to take decisive action.

Oil Wealth or Oil Poverty?

As the previous analysis has shown, Saudi Arabia's budget deficit has already been reduced by a combination of higher oil prices and austerity measures. Saudi Arabia has been able to repay its foreign debt and has already financed much of the infrastructure needed to modernize the country. It is unlikely that Saudi Arabia will have to pay for another Gulf War, and many Saudi arms purchases have been "front loaded" so that arms imports in the late 1990s and early 2000s will cost substantially less than in the aftermath of the Gulf War.

There are many positive trends in the Saudi economy as well as negative ones. Some of the increase in the governments domestic civil debt has gone into investment, rather than paying for services, the deficit, and foreign loans. These expenditures will eventually be repaid in the form of added future revenues. Foreign debt has been reduced to low levels, although at the cost of rising central government domestic debt.[1]

Nevertheless, Saudi Arabia faces serious economic problems that greatly compound the impact of constant social change, high birth rates, internal political divisions, and a "youth explosion." No one outside Saudi Arabia -- and probably no one within it -- can be certain of just how serious the impact of the resulting tensions within Saudi society really are. None currently seem to threaten the government, and there are few signs that a cohesive opposition is beginning to emerge. Nevertheless, the Saudi government can scarcely ignore the importance of such tensions, and it faces the added problem of dealing with a highly conservative Islamic revival at a time when it must move towards internal reform, in modernizing Saudi society, and dealing with the West.

Creating the Need for a New Social Contract

Saudi Arabia cannot live in the past or stay in the present. Saudi society, the economy, and government must evolve relatively rapidly if Saudi Arabia is to preserve its internal stability. The government must continue to expand the role of the Majlis, and find ways of modernizing the Saudi economy and society that can at least win the tolerance of most of its traditionalists.. It must allow popular debate and increasing popular control of its national resources. It must come to grips with the issue of defining a rule of law that applies to all its citizens, including the royal family. It must replace "statism" with a dominant private sector. This means it must provide for a uniform commercial code and fully competitive privatization, while resolving the inevitable tensions and conflicts between religious and civil law.

Saudi Arabia cannot ignore the political realities created by its welfare and entitlements programs. It must continue to ensure that oil wealth is shared throughout its society. At the same time, it must move beyond a petroleum and service-based economy, and a subsidized welfare state. This is not simply a matter of dealing with declining oil revenues per capita. It is a matter of creating a work ethic and economy that employs young Saudis, giving them a real career and share in the future of the nation, and steadily reducing Saudi Arabia's dependence on foreign labor.

Saudi Arabia must redefine its "social contract." It must look beyond oil exports to ensure its budgets are brought into better balance and that its society and economy develop. It must increase revenues by directly taxing wealthier citizens. It must reduce state spending and create a more balance economy by eliminating most subsidies and converting to market prices. It must make a full commitment to privatization and adopt much more stringent restrictions on foreign labor that put far more native citizens to work. In an effort to tighten restrictions on foreign labor, the Kingdom is considering a proposal to double the cost of work permits for foreign laborers, increasing the fee from 1,000 Riyals to 2,000 Riyals ($533). The London-based Saudi paper Al-Hayat reported that the Kingdom expects to make 80 million Riyals ($21.3 million) from the work permit fees.[2]

The State Budget, Subsidies, and Welfare

The government needs to reform the structure of the national budget, and find new sources of revenue by reforming the tax system, and by taxing earnings and sales with progressive taxes that reduce or eliminate budget deficits. At the same time, it needs to make the budget open and transparent and allow an effective debate over both the preparation of the budget and future five-year plans within Saudi Arabia's consultative bodies.

It should ensure that all income from enterprises with state financing is reflected in the national budget and is integrated into the national economic development and planning program, and ensure that all of the nation's revenues and foreign reserves are integrated into the national budget and into the planning process. It should reduce the amount of money going directly to royal accounts, and clearly separate royal and national income and investment holdings. It should place limits on the transfer of state funds to princes and members of the royal family outside the actual ruling family, and transfers of unearned income to members of other leading families.

It should place national security spending on the same basis as other state spending and integrate it fully into the national budget, including investment and equipment purchases. It should also replace the present emphasis on judging purchases on the basis of initial procurement costs and technical features with a full assessment of life cycle costs**,** including training, maintenance, and facilities and implement specific procedures for evaluating the value of standardization and interoperability with existing national equipment and facilities, those of other Gulf states, and those of the US and other power projection forces.

Privatization and Encouraging the Private Sector

The private sector is the only force that can create real jobs and career opportunities for native Saudi Arabians, and open opportunities to a wider range of investors. Saudi Arabia needs to carry out much more rapid and extensive privatization to increase the efficiency of Saudi Arabian investments in both downstream and upstream operations. At the same time, privatization must be managed in ways that ensure all Saudi Arabians have an opportunity to share in the privatization process and that it is not conducted in a manner that benefits a small, elite group of investors and discourages popular confidence and willingness to invest in Saudi Arabia.

Where Saudi Arabia does continue to rely on a major public sector, but it should establish market criteria for all major state and state-supported investments. There may still be a case for a major state role in some aspects of oil and gas production, and utilities, but the government should require detailed and independent risk assessment and projections of comparative return on these investments, with a substantial penalty for state versus privately funded projects and ventures. It should downsize the scale of programs to reduce investment and cash flow costs and the risk of cost-escalation. It should remove distortions in economy and underpricing of water, oil, and gas. It needs to enforce a firm rule of law for all property, contract, permitting, and business activity and reduce state bureaucratic and permitting barriers to private investment.

Saudi Arabia needs to come fully to grips with the fact that no nation can isolate itself from the global economy and the growing role of multi-national corporations. The government needs to encourage foreign investment and allow such investment on more competitive terms. Saudi Arabia currently allows only limited foreign investment in certain sectors of the economy, in minority partnerships, and on terms compatible with continued Saudi Arabian control of all basic economic activities.

Reform is measured solely in macroeconomic success, never in intentions, plans, decrees, or rhetoric. Some sectors of the economy--including oil and gas, banking, insurance and real estate--have been virtually closed to foreign investment. Foreigners (with the exception of nationals from some GCC states) are not permitted to trade in Saudi Arabia, except through the medium of Saudi firms. Protection should not extend to the point where it prevents investment in upstream or downstream operations, eliminates efficiency and competitiveness, and restricts economic expansion. Saudi Arabia needs to act decisively on proposals such as allowing foreign equity participation in the banking sector and in the upstream oil sector.

The government should consider creating new incentives to invest in local industries and business and disincentives for the expatriation of capital. At the same time, it must put an end to the present kind of "offset requirements" that often simply create disguised unemployment or non-competitive ventures that act as a further state-sponsored distortion of the economy. Some Saudi Arabian firms and businesses are now subsidized in ways which prevent economic growth and development, and which deprive the government of revenue.

Saudis need to learn to be truly competitive. Policies that strongly favor Saudi Arabian citizens and Saudi Arabian-owned companies in ways that block constructive foreign investment should be amended. Income taxes are only levied on foreign corporations and foreign interests in Saudi Arabian corporations, at rates that may range as high as 55 percent of net income. Individuals are not subject to income taxes, eliminating a key source of revenue, as well as a means of ensuring the more equitable distribution of income. Saudi Arabia needs to tax its citizens and companies and ensure that wealthier Saudi Arabian's make a proper contribution to social services and defense.

Population and Foreign Workers

The government must make good on its attempts to force radical reductions in the number of foreign workers, with priority for reductions in servants and in trades that allow the most rapid conversion to native labor. It must eliminate economic disincentives for employers hiring native labor, and create disincentives for hiring foreign labor. Saudi Arabia's young and well-educated population needs to replace its foreign workers as quickly as possible, and it will only develop a work ethic and suitable skills once it is thrust into the labor market.

State efforts to encourage Saudi to work and develop a work ethic are useful, but the keys are creating a climate where Saudis must work for a living on market terms and restructuring the educational system to focus on job training and competitiveness. The government needs to create strong new incentives for faculty and students to focus on job-related education. Sharply downsize other forms of educational funding and activity, and eliminate high overhead educational activities without economic benefits.

The West and the Pace of Saudi Modernization

it is always far easier to call for reform that it is to implement it, and Saudi society does not make reform easy. The West needs to understand that the Saudi royal family and most Gulf royal families can only make such changes as fast as their societies can accept them. In Saudi Arabia, for example, there is already a major fundamentalist reaction to the existing rate of change. Over-accelerating the pace of change would lead to conservative reaction, rather than actual progress:

The West can only help Saudi Arabia if it accepts these facts and if it pays more attention to Saudi Arabia's real needs for economic and social reform, and makes fewer vacuous calls for instant democracy. Quiet progress is also more important than noisy gestures. The Saudi government often prefers to use private and informal methods in modernizing, in supporting the Arab-Israeli peace process, and in limiting the influence of Arab and Islamic radicals; the West and Israel prefer formal and visible arrangements. Israel has often made the mistake of treating Saudi Arabia and other moderate and conservative Arab states as enemies, and insisting on formal arrangements as signs of progress.

Saudi Arabia cannot survive letting Islamic conservatives and hard-liners dictate the future structure of Saudi society. At the same time, it is important for both the West and Israel to understand that Saudi Arabia must preserve its Islamic character, avoid provoking Arab radicals, and minimize the risk of confrontation with Iran, Iraq, and Syria. Informal success is always preferable to formal failure, but this is a lesson that the US and Israel have found very difficult to learn.

Partnership is also based on respect and a clear understanding that any partner must give priority to its own national interests. Crown Prince Abdullah made this point quite clearly in an interview in the Lebanese newspaper, As-Safir, in June 1997,[3]

> "We are friends with the Americans, this is known. But we are the ones who know our interests. We can't give precedence to their interests over our interests. We are Arabs and our interests are those of Arabs and Muslims everywhere. On many occasions we have to tell the Americans...you have your policy and we have our policy...you have your interest and we have our interests? Do you want weak friends who are of no benefit and burden you, or do you want strong friends?"

The US and the West also need to understand that Saudi Arabia has the right to make different choices about foreign and security policy and its approach to key issues like the Arab Israeli conflict, Iran and Iraq. Such differences do not mean that underlying common security interests do not remain and the US needs the strongest friend in Saudi Arabia that it can create. Its grand strategic and economic interests all depend on the continuing development of Saudi Arabia as the lynchpin of any effort to create stability in the Gulf. At the same time, much depends on Saudi willingness to work with the US and show flexibility in supporting US interests as well as its own. No nation likes to admit its dependence on another, but the success of Saudi military forces ultimately depends on the effectiveness of US power projection capabilities. Saudi Arabia will remain as dependent on the West for security as the West is dependent on Saudi Arabia for oil.

Endnotes

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[1] Data are taken from working papers distributed during the Royal Institute of International Affairs conference on Saudi Arabia in October 4-5, 1993.

2 Reuters, May 6, 1999.

3 Middle East Economic Digest, September 19, 1997, p. 25.