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The Saudi Sheikh Up

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Saudi Arabia's history has been dominated by oil, Islam and the al-Saud family. The ruling family formed the government, controlled the armed forces and allocated oil revenues. This system, reinforced by the alliance between the al-Saud family and the religious authorities in the kingdom, has been the source of both Saudi strength and weakness. The dramatic events of November 2017 were a demonstration of the power of the monarchy: King Salman and his son, Crown Prince Mohammad, ordered the arrest of eleven senior princes, several serving or former ministers, the owners of three major television stations, the head of the most important military branch, one of the wealthiest men in the world, and many others. The most powerful to be arrested was Prince Miteb bin Abdullah, the head of the National Guard and a son of the late King Abdullah. More than forty years older than the current Crown Prince, he had once been considered a potential future king and led the most powerful military force in the country, whose duties include protecting the royal family. These developments follow the removal from office in June 2017 of the then Crown Prince and minister of the interior, Muhammad bin Nayef.

Since the death of the founder of modern Saudi Arabia, King Abdulaziz Al Saud in 1953, succession has been decided by consensus among the major royal clans. The clans were willing to accept their place in the succession as long as they could be in charge of one of the main military forces: the Border Guards, the National Guard, and the army, air force and navy that are controlled by the Ministry of Defense. The National Guard is a key example. It is separate from the army and from the Border

Guard. It was created in the 1950s and 1960s, and was originally designed to be a counter-coup force to defend the royal family from potential threats from the regular army. In 2011, it was used in Bahrain to secure the survival of the Sunni minority ruling family against protesters from the Shi'i majority and is still there.

This system maintained stability at senior levels of leadership for many years. However, a new, younger generation in Saudi Arabia is taking over the levers of power, represented by Crown Prince Mohammed bin Salman who is 32 years old, and has the support both of his father the king and of Saudi youth. Those under the age of 30 account for 70 percent of the population. Given the lack of meaningful jobs for this generation, as well as the rapidly declining financial reserves of the kingdom, the old system dominated by a few privileged persons who were, in effect, above the law, became ever more dysfunctional and unacceptable. As such, it became a threat to stability. The main economic trends are illustrated in Table 1.

	Population (millions)	Oil export revenues (\$ billions)	Oil export revenues/capita (\$)
1980	9.3	101	10,860
1985	11.9	25	2,101
1990	15.2	40	2,632
1995	18.1	44	2,431
2000	20.5	71	3,463
2005	23.3	162	6,952
2010	27.6	214	7,754
2016	32.2	134	5,776

Source: Calculated from OPEC, Annual Statistical Bulletin 2017

In recent months, the leaders of the three main clans - the Nayef, Abdullah, and Sultan have been removed from command positions and from the funding that these institutions received. Other royal clans have benefitted from business deals using capital from real estate deals or agent fees on military and other contracts. These clans have been savaged, especially the Fahds, with the arrests of global investor Prince Alwaleed bin Talal, Abdulaziz bin Fahd, and Waleed Al Ibrahim. The moves against corruption have met with broad public support in Saudi Arabia, and those arrested in the recent purge have apparently been offered their freedom in exchange for handing over funds that they acquired through corruption. These have been estimated by the

Saudi attorney general to be worth at least \$100 billion, or about 15 percent of GDP. Other estimates suggest that the amount may be much higher.

The purge is not only a dramatic event with legal and financial consequences; it also represents a political and cultural revolution. The Crown Prince with the backing of his father, King Salman, has centralized power in his hands. This can be seen as a return to the days of the founding King Abdulaziz, when a single, undisputed leader controlled the country. During years of Abdulaziz's rule, from the 1930s to the 1950s, the economy developed due to income from oil production, but there were no established merchant and bureaucratic structures. Since then Saudi Arabia has developed and the population has grown massively. A huge bureaucracy has been created and the armed forces have expanded. Saudi Arabia has become a much more complex country to govern, hence the compromises between the clans and the blind-eye to corruption. In recent years population pressure has been manifest in rising unemployment among Saudi youth and oil revenues have fallen. Power has been centralized by a prince who, ironically, has called for a more decentralized system.

The purge is not the first dramatic policy put forward by Crown Prince Mohammed. In April 2016, as Deputy Crown Prince and Chairman of the Council for Economic and Development Affairs, he announced plans to reduce the country's reliance on oil and diversify the economy. A stake in the state-owned oil company would be floated in an IPO by 2018. The funds from that and other asset sales — estimated at up to \$2 trillion or more — would be invested in a new sovereign wealth fund to provide the country with a regular investment income from non-oil sources. Saudi Arabia was to be opened up to tourism and foreigners would be allowed to own property in the Kingdom. New small and medium-sized enterprises would be encouraged to the point where they would account for 35 percent of economic activity. Subsidies for oil, water, and electricity would be progressively eliminated. A range of new industrial sectors were to be developed, including petrochemicals, manufacturing, and finance based on foreign investment. Reforms would lead to the diversification of the economy. Increased labor market productivity would be achieved through increasing domestic participation in it (especially of women and youth), improving education and training, in order to add to the flexibility and mobility of the labor market, while reducing the growth of public-sector employment, and increasing the cost of hiring foreign labor. A stronger private sector would develop through the improvement of

the business environment, removing limitations to competition, investment in infrastructure, professionalizing management practices, and attracting foreign and local investment. Fiscal management would be transformed by controlling government deficits, decreasing the role of government in investment, increasing non-oil revenues, reforming energy market prices, and improving the returns from state-owned assets.¹

In October 2017, Prince Mohammed announced plans to build a new city on the Red Sea coast, to be called “NEOM.” NEOM is an acronym combining “neo,” or new, and a derivation from the Arabic word “mustaqbal,” or future. It will be partly located in an area known as Ras Sheikh al-Hameed, a peninsula of land jutting about 31 miles (50 kilometers) into the Red Sea opposite the Egyptian resort of Sharm el-Sheikh and the Straits of Tiran. Some 10,000 square miles (26,000 square kilometers) have been allocated for the development of the urban area that will stretch into Jordan and Egypt. The area was chosen because of its strategic location, near Egypt and proximity to international shipping routes. Egypt has signed a treaty to give Saudi Arabia two islands that link the project to the Sinai.

NEOM will operate independently from the existing governmental framework and private sector investors will be consulted at each stage during development. The project will be backed by more than \$500 billion from the government, through its sovereign wealth fund and local and international investors. It may be thought of as a new Dubai, with a bridge planned to Egypt, and it may be of great interest to China.

The attempt to isolate NEOM from existing governmental structures and conservative cultural norms is reminiscent of the King Abdullah University of Science and Technology (KAUST), founded by the late King Abdullah in 2009. KAUST is the first mixed-gender university campus in Saudi Arabia. When it was founded, the authorities hoped that the mixed-gender center would help modernize the Kingdom's deeply conservative society. The religious police do not operate on-site and women are allowed to mix freely with men and to drive on campus, and they are not required to wear veils in classes that are coeducational. NEOM is similar but on a much larger scale.

As well as these internal developments, Saudi Arabia faces major regional challenges. It views Iran as a serious threat, and the ending of sanctions against Iran, following the nuclear agreement, has strengthened this feeling. Saudi Arabia is now fighting wars, or proxy wars, against Iran in Yemen and it was involved in Syria. In Syria, Russian intervention in favor of the Assad regime coincides with Iranian interests and threatens those of Saudi Arabia. These interventions in Yemen and Syria, along with financial support for Egypt, are another huge burden on the budget.² The tensions between Iran and Saudi Arabia have also manifested themselves in Saudi relations with Lebanon, resulting in the November 4th resignation of the Prime Minister, Sa'ad al-Hariri, who is a Saudi citizen and originally made his announcement from Riyadh.

Saudi Arabia also has to cope with the prospect of lower oil prices in the foreseeable future. The rise of US shale production has changed the world oil supply map. Plans to phase out petrol-powered vehicles in parts of Europe, increasing environmental concerns in China, India and elsewhere, are all expected to moderate demand for oil. This means that revenues from Saudi oil exports are likely to stagnate, and may even decline, if domestic consumption is not contained. These pressures, both internal and external, have forced the Saudi leadership to gamble on radical change.

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¹ Andrea Helfant and Paul Rivlin, "Saudi Arabia's Plans for Change: Are they feasible?" *Iqtisadi*, 31 May 2016. Available at <http://dayan.org/content/saudi-arabias-plans-change-are-they-feasible>

² Paul Rivlin, "Saudi Arabia's Multiple Crises," *Iqtisadi*, 24 February 2016. Available at <http://dayan.org/content/iqtisadi-saudi-arabias-multiple-crises>.