

# Saudi Arabia

<b>Status Index</b> (Democracy: 2.57 / Market economy: 5.43) <b>4.00</b>		<b>Management Index</b> <b>3.65</b>	
<b>HDI</b>	0.772	<b>Population</b>	23.3 mn
<b>GDP per capita (\$, PPP)</b>	13,226	<b>Population growth<sup>1</sup></b>	4.2 %
<b>Unemployment rate</b>	9 %/*	<b>Women in Parliament</b>	0 %
<b>UN Education Index</b>	0.72	<b>Poverty<sup>2</sup></b>	-
		<b>Gini Index</b>	-
Source: UNDP: Human Development Report 2005. Figures for 2003 unless otherwise indicated. <sup>1</sup> Annual growth between 1975 and 2003. <sup>2</sup> Population living below \$1 a day (1990- 2003). * Officially – inofficial estimates 20-30 %.			

## A. Executive summary

Like in many other places, reform has been the catchword in Saudi Arabia for the last five years. The actual record has been uneven, with somewhat more substance in the economic than in the political realm.

Independent of actual institutional outcomes, the character of the public debate in the kingdom has changed substantially – one might even say that in many ways, an officially permitted domestic political debate as such has started for the first time. Issues in the debate have included the cultural foundation of the Saudi state, possible forms of societal renewal and possibilities for political participation. For the first time in modern Saudi history, religious pluralism within Islam has been officially recognized.

The regime, under the leadership of Crown Prince Abdullah, has experimented with a number of symbolic initiatives, including a “National Dialogue”, which has so far been held four times, with select representatives of various societal groups participating (so far mostly intellectuals, clergy, women, youth). The regime has also attempted to create state-controlled political “interest groups,” including a human rights organization and lawyers’ and journalists’ associations. The Saudi princes have yielded somewhat more decision-making power to the Majlis Ash-Shura, an appointed quasi-parliament. In early 2005, partial elections for municipal councils were held in all regions of the kingdom.

Most initiatives were attempts to counter social disintegration and disaffection with the regime in the wake of the jihadist terror wave that has swept over the kingdom since May 2003. The terror has not endangered Al Saud rule. Nonetheless, the Al Saud are slowly recognizing that Saudi society has become considerably more complex than it was when the state first was created, and they have tried to increase their citizens’ identification and mobilization within the system.

None of this has changed the fundamental distribution of power in the system, in which the Al Saud rule supreme. Initiatives have been “granted” by the leadership, and Saudi Arabia is still the formally least participatory political system in the Middle East and Northern Africa (MENA) region. However, it does indicate a new recognition that the Saudi polity has to modernize, in whatever fashion.

In economic terms, the kingdom has had two excellent years thanks to strong oil-induced growth. It has also seen through a number of substantive reform measures, including further opening up for FDI, adaptation of the national laws to WTO requirements, the creation of a Capital Market Authority, the privatization of Saudi Telecom and the entry of Ettihad Etisalat as a second mobile provider.

Many further initiatives remain stuck however, including most other privatizations, competition and company laws and the introduction of commercial courts. Even in areas where the broad legal framework has been changed, mid-level administrative and judicial structures frequently remain unchanged, and little has been gained in terms of transparency. Barriers to entry in the Saudi markets can still be very high.

Thanks to the oil windfall, more money has been available for the creaking Saudi welfare state. The provision of health, education and other services, however, still suffers from inefficiency and a lack of administrative accountability. The Saudi state apparatus still awaits fundamental reform.

## **B. History and characteristics of transformation**

The Kingdom of Saudi Arabia was declared by King Abdalaziz of the Central Arabian Al Saud clan in 1932, after a three-decade campaign of conquest covering most of the Arabian Peninsula. Formally, the state is an absolute monarchy ruled by the sons of Abdalaziz, who died in 1953. The first Council of Ministers was created in 1958, a time when oil income had started to play an increasing role in the Saudi process of state formation. Subsequently, the national administration expanded rapidly, state services and the standard of living of the country's population were augmented substantially and the state increasingly played a strong, direct role in people's lives.

At the same time, remnants of national and local consultative councils – mostly carryovers from the politically more developed Western Hijaz region – withered away and eventually disappeared, leaving a massive bureaucracy as the main formal instrument of rule. Informally, the system was buffeted by networks of personal patronage, distribution and favoritism, which were centered on the sprawling Al Saud family. The clergy, traditionally the main coalition partner of

the Al Saud, descended even further into fealty and material dependence than it had already been in previous centuries, but remained an essential legitimating prop of Al Saud rule.

The large-scale oil-fuelled rentier economy led to the creation of a new business class of merchant and contractor families close to the royals. The kingdom experienced some political unrest in the 1950s and 60s, the heyday of Arab nationalism. However, the Al Saud managed both to suppress strikes in the (oil-rich) Eastern Province and to avert a number of military coup attempts. Official announcements of timid reforms – such as the appointment of a consultative council and drafting of a basic law – repeatedly came to nothing. One of the Al Saud's persistent advantages for political survival has been their deep embeddedness in significant parts of the administration and especially in the security services, where hundreds of princes hold offices. Their presence in business is also considerable, even if many of them act only as facilitators and commission-takers.

The kingdom reached its highest GDP per capita in the early 1980s, with a figure of about \$18,000 in 1981, the year of the highest real oil prices thus far (due to rapid economic expansion, however, the number does not quite reflect the actual standard of living). Since then, the overall economy has largely not been able to keep pace with demographic growth, which was at 4% annually well into the 1990s. The regulatory framework for business is still deficient in practice. Nonetheless, the Saudi private sector has matured considerably in recent decades and has more sophisticated managerial structures than most of its peers in the MENA region.

After the seizure of the Grand Mosque in Makkah in 1979, the regime put special emphasis on the enforcement of conservative social mores, yielding more space for religious conservatives in education, domestic and international cultural policies and enforcement of public order. Nonetheless, after the 1990/91 Gulf War, both Islamists and liberals were disenchanted with the Al Saud, their apparent inability to protect the realm without U.S. aid and their generally authoritarian and non-transparent governance. A number of liberal and Islamist political petitions were sent to the royals, and in 1992, King Fahd was forced to make a number of symbolic concessions. These included:

- Eventually, a “Basic Law.” This set out basic features of the political system and enshrined some basic rights, although without properly articulated recourse mechanisms.
- The creation of a Majlis Ash-Shura. This is an appointed consultative body for review of draft legislation and has been enlarged three times since its creation (from 60 to 150 members). Although the Majlis is not representative and has a certain technocratic bias, it has acquired increasing importance in the more technical aspects of legislation.

- A law of regions, setting out basic structures of governance in the kingdom's 13 regions.

The political situation calmed down subsequently, not least due to the fundamental divides between oppositionist groups. Whereas liberals had been socially isolated all along, popular Islamist dissidents were either co-opted or oppressed by the regime.

Crown Prince Abdullah has been the effective head of government since a stroke incapacitated King Fahd in 1995. Abdallah gained a greater political profile after 1998 and initiated a number of economic reforms in 1999, with mixed results. He is relatively popular and generally seen as a driver of both socioeconomic and political reforms. The latter have been put on the agenda again through the internal security crisis and international scrutiny following 9/11.

Altogether, however, the leadership is of a collective nature and grossly over-aged and several of Abdallah's half-brothers are even more cautious about reforms than he is. The succession problem of transition into the next generation – all kings so far have been sons of Abdalaziz – has not yet been solved.

Wide strata of Saudi society are very conservative in social and political terms, and despite increasing social differentiation, the level of political mobilization is rather low. This augurs relatively well for mid-term political stability, but not for the prospect of reform.

## **C. Assessment**

### **1. Democracy**

#### **1.1. Stateness**

Saudi Arabia has not witnessed violent conflict within its borders since the 1930s. All regions and tribes nowadays recognize the sovereignty of the Al Saud state.

Saudi citizens are Muslim by definition. The Shi'ite minority, unofficially estimated at about 10%, is denied certain cultural rights and it suffers from socioeconomic deprivations. Arguably, however, the largest issues of socioeconomic and legal status are not among indigenous groups, but between Saudis and the millions of low-paid foreign workers. The issue is less that labor migrants do not easily qualify for citizenship, but rather that they are held in conditions sometimes akin to bondage.

The 1992 "Basic Law" is not officially seen as a constitution, as the Quran is supposed to be the real constitutive text of the Saudi polity. Officially, all

legislation is to be based on Shariah. In practice, however, significant parts of the administration are run according to secular principles, including the regulation of the powerful Saudi banks. Incompatible fatwas have been repeatedly ignored by the regime, and often the clergy were forced to issue new verdicts acquiescing to new facts (such as the 1990-1991 presence of U.S. forces in the kingdom). Among the ruling princes, pragmatism often rules supreme.

The Saudi state is large, and the administration reaches out to even remote villages. However, the bureaucracy is very bloated, with an estimated 1 million state employees. The “infrastructural power” of the state is not very high, as it finds it hard to enforce economic rules, apply regulations consistently and gather information about its constituents. State services in peripheral areas are often very deficient.

## **1.2. Political participation**

There are no democratic elections at the national level. Municipal elections were held in the spring of 2005 on a nation-wide scale for the first time. However, women were excluded, and only half of the members of the rather toothless municipal councils were chosen by popular vote. One reason for this was probably to preempt control by religious extremists.

The national administration continues to be wholly selected by the Al Saud. Municipal councilors still have to prove their mettle.

Parties and unions are not allowed, and formal associations require royal fiat for obtaining a license. Since 2003, there have been certain top-down attempts to corporatize and formalize political life and interest formations. A bar association and a Saudi Journalists' Association were formed in 2003 and 2004 respectively. Further formal interest groups have been announced or are about to be licensed (teachers, doctors, publishers, workers on enterprise level etc.). All this is regime-driven, however, and autonomous attempts to organize interests are suppressed if they are deemed too political (for instance, an independent human rights organization in early 2004). There is no freedom of political assembly.

A limited public debate on national political issues has been conducted in the press in recent years, specifically since 2003. The 13 Saudi papers are largely owned by princes, and the Ministry of Information has full power of censorship and can control editorial appointments. Nonetheless, public debate has become much livelier, despite occasional crackdowns, as in the summer 2003. Open criticism of the royal family is still off-limits, but the religious foundations of society, censorship, corruption and the desirability and form of elections are debated openly. This partial liberalization notwithstanding, the press has little statutory guarantees against encroachments when they occur (Article 39 of the “Basic Law” makes an open case for censorship).

### **1.3. Rule of law**

The king is the highest judicial, executive and legislative authority, and senior princes can avoid the judiciary more or less at will. At the same time, the clergy – although appointed by the king – has been given some limited autonomy to run the judicial system, not always to the delight of non-royal Saudi elites. Large parts of the functional bureaucracy are staffed by commoners, and commoners dominate technical posts. Day-to-day intervention by the royal family is limited as long as there are no immediate political or economic interests at stake. Smaller princes can often leverage their names in the administration, however.

To the extent that a judiciary run by the clergy can be considered independent, it has considerable day-to-day independence in the sense that the regular administration has very little leeway to control (or predict) judicial goings-on. Judicial professionalism, especially when it comes to more technical areas, such as commercial law, is often dubious, especially in Shariah courts. Judicial corruption occurs, but is less rampant than in many other MENA countries. When it comes to more political questions or decisions in which royal family interests are involved, the judiciary often yields to royal pressure.

Corruption scandals in the bureaucracy occur, and convictions are occasionally reported. There are formal civil service supervision and trial procedures, but they are underutilized, and the prosecution efforts are dwarfed by bureaucratic corruption. Royal family members are largely immune to prosecution, and commoners can be so too if they enjoy protection by a significant royal.

Civil rights are not violated on a large scale, and apart from recent terrorism problems, the political setting in Saudi Arabia still is rather quiet. Traditionally, the kingdom is not a highly coercive regime, and the leadership usually tries to avoid harsh collective punishments such as those common in countries like Syria or Egypt. At the same time, civil rights are by official definition severely limited. There is, for example, no freedom of religion whatsoever. There are a few rights enshrined in the basic law, such as privacy of residence and mail correspondence, and the “*nulla poena sine lege*” concept. They do not include basic political rights, however. A number of prominent dissidents received a public trial in 2004 and 2005, but this was based on an ad hoc decision. When under pressure, the regime can react with targeted, severe repression. The largest human rights problem by far is the treatment of foreign workers.

### **1.4. Stability of democratic institutions**

There are no democratic institutions as such in the kingdom whose stability could be evaluated. The jury is still out on the only semi-democratic element of the polity, the municipal councils. Their successes, if any, are likely to be on a very small scale.

## **1.5. Political and social integration**

Parties are prohibited in the kingdom, and the only (highly imperfect) substitute is the clientele attached to various centers of power.

Representation of societal interests, as indicated, has become a bit more formalized, but is still anemic, lopsided and tightly controlled by the regime. Informal politics and access to the regime usually matter more. Many professional, cultural and socioeconomic interests are not formally represented at all.

There are no reliable survey data on attitudes to democracy in the kingdom. Anecdotal evidence indicates that interest is modest among large parts of the population, and the concept remains rather poorly understood. The actual turnout at the municipal elections in February 2005 in Riyadh was below 30%. Assent to the rule of the Al Saud appears more established than interest in substantive democratization.

Self-organization in civil society encounters numerous barriers. All formal groups are licensed and monitored by the state, and most of them are restricted to functional elites. All over Saudi society, informal networks of friendship, patronage, family and clan are very strong and mutual bonds of assistance very powerful. Little of that has been translated into formal “bottom-up” organization, however, and trust and civility between strangers tends to be quite low. There is little tradition of association, and social bonds, even if powerful, tend to be vertical. Large parts of society have been demobilized by an omnipresent provider state.

## **2. Market economy**

### **2.1. Level of socioeconomic development**

In certain regards, Saudi society is a strongly exclusive society, but it has its egalitarian features too. On the one hand, women’s freedom of action is severely curtailed (2004 Gender Development Index 0.739, rank 72), Shi’ites have been marginalized and millions of foreigners are excluded. On the other hand, women can have considerable informal social power and are often highly educated. Although general economic inequality is probably worsening, Saudi Arabia is – as far as its citizens go – still a relatively equal society materially speaking, and tight social networks can prevent abject poverty (Gini coefficient not published, but no persons with less than \$1 per day). It ranked 30 in the 2004 Human Poverty Index, of developing countries (15.8%). Poverty does exist and there are regional biases, with the south being particularly deprived. The regime has become aware of the problem and has been trying to develop a poverty strategy.

## **2.2. Organization of the market and competition**

Market competition is freer than in many other MENA states, but still suffers from weak regulation and informal inequalities. Prices are mostly free, trade restrictions are limited, currency is convertible and profits can be repatriated. Formally, foreign investment has been allowed up to 100% ownership in the majority of sectors. However, informal monopolies and oligopolies are ingrained, and the administrative connections of established players can result in an uneven playing field. All businesses are officially registered, as the tax burden is low and taxes and other regulations can frequently be avoided.

There is no general law or institution dealing with cartel issues. There are, however, a number of regional regulatory agencies (information technology and telecoms, electricity, capital market), which have a reasonable reputation. An attempt to introduce a general competition law tied to the abolition of national commercial agency privileges was brought down by business lobbies.

The general external tariff level is 5%, in line with the GCC customs union. There are still a number of protective tariffs of 20% on specific goods. Agency regulations prevent the direct entrance of foreign goods into the Saudi market and require international exporters to distribute goods via a local dealer. Customs procedures and the application of Saudi norms and standards can be arbitrary and cumbersome and sometimes involve corruption.

There are ten banks in Saudi Arabia, which are mostly privately owned, generally well-managed, stable and rather closely supervised by the Saudi Arabian Monetary Agency (SAMA), which is one of the more efficient state agencies. They have greatly profited from the high oil prices of recent years. A number of foreign banks have been approved for licensing since 2003. A Capital Markets Authority was created in 2004 and it operates according to rather strict standards of listing and supervision. Independent brokerage firms are to be licensed soon. The United States is pressing for further financial market liberalization in its ongoing WTO negotiations with the kingdom.

## **2.3. Stability of currency and prices**

The Saudi Riyal has long been pegged to the dollar. Although the kingdom's balance of payments is inevitably strongly influenced by oil price fluctuations, SAMA has managed to keep inflation at a very low level over many years, with the cost of living actually slightly declining between 1999 and the first quarter of 2004, according to SAMA. The kingdom was able to stock foreign assets in the surplus year 2004, increasing by 46% to \$87.6 billion.

Although monetary and exchange rate policies are well managed, the same cannot be said about fiscal policies. Saudi Arabian public budgets still strongly fluctuate

with the oil price, although to a lesser degree than they used to (in 2004, for example, a surplus of about \$30 billion could be retained, but spending had nonetheless increased by almost \$20 billion). There is no formal budget stabilization mechanism, and the reduction of the government's large debt will depend on favorable oil price developments. Debt is about 70% of GDP, although domestically owed and to a significant degree to state agencies. About three-quarters of public income come from oil revenues.

#### **2.4. Private property**

Although most Saudi business actors do not have to be afraid of wholesale abuse of their property rights and basic commercial laws are reasonably clear, there are cases of marginal to moderate infringement, such as commission taking by officials and princes and the non-fulfillment of contracts. Debts and other liabilities in general are not very easily enforced, and outcomes of judicial arbitration can be unpredictable. In special areas of property, such as the real estate market and mining, powerful actors can bend the rules to their advantage and at the expense of smaller actors. Property informally owned by foreigners is regularly infringed upon. Judicial safeguards generally are deficient.

There are two strategic sectors in Saudi Arabia that are totally and significantly state controlled, namely oil and petrochemicals. Most other sectors (banking, retail and wholesale sales, many industries, services etc.) are largely privately owned. Big players sometimes corner the market, such as in the important cement sector and in contracting. Privatization of state assets – the further sell-off of “Saudi Arabian Basic Industries”, water and electricity services, Saudi Arabian Airlines, Saudi Railway Organization etc. – is moving ahead, but only slowly.

#### **2.5. Welfare regime**

Social networks are well developed, but they do not cover all risks for all strata of the population. Family structures are still powerful but becoming increasingly stretched as more and more people rely on one income. Poorer families are at risk of being excluded from networks of distribution altogether. State employees receive pensions, but these are not always sufficient for them and their dependants. Health services are free for Saudi nationals but not always satisfactory. Despite the rather extensive operations of the Ministry of Social Affairs and numerous private charities, there are no clearly defined minimum benefits or entitlements, and there is no unemployment insurance. Welfare for low-income foreigners is practically nonexistent.

Although general education is in principle available to everyone, nepotism can considerably influence the admissions processes of higher educational institutions, public and private job markets. Women have good access to (segregated)

education and constitute the majority of higher education students now. They have very limited access to many public and private vocations, however. Official unemployment estimates are around 9%, while unofficial numbers range between 20 and 30%. More importantly, the participation rate of the overall Saudi population of working age in the labor force is very low at about 37%. Social mobility has slowed down considerably since the expansion of the state and the end of many of its programs in the mid-1980s.

## **2.6. Economic performance**

The kingdom witnessed considerable growth in 2003 and 2004 under conditions of macroeconomic stability (see below). Most of this was oil-induced, however, and growth has not translated into employment generation on the scale needed to accommodate an estimated 200,000 new entrants to the labor market per year. Unemployment and underemployment constitute the single biggest socioeconomic challenge for the coming years. For a number of reasons, including sluggish bureaucracy and terrorism issues, foreign investment has decreased rather than increased since the foreign investment reforms of 2000. Although the economy is somewhat more robust and less immediately oil-dependent than in the 1980s, lower oil prices – however unlikely in the short term – still have the potential to create an economic crisis.

## **2.7. Sustainability**

The Meteorology and Environmental Protection Agency (MEPA) theoretically acts as environmental watchdog and regulator, and awareness of environmental issues is slowly increasing through symposia and other educational initiatives. Nonetheless, environmental regulation is still very weak and tends to get lost between different segments of the administration. Although an environmental impact assessment is prescribed for any bigger project, in reality, the state's supervisory capacity is strongly limited. In some cases, neglect has led to dramatic situations. Jeddah, the second biggest city in the kingdom, suffers from massive sewage problems due to industrial waste, and these problems are only being tackled slowly. The disposal of the enormous amounts of private and industrial waste in the kingdom is still haphazard.

Roughly, one-quarter of the official budget has been spent on education in recent years. However, the quick, large-scale expansion of the system based on imported labor has led to quality deficits. The output of the educational system is generally not geared toward the needs of the labor market, a much-discussed problem for which solutions – like private schools and universities and revisions of curricula and admissions policies among public institutions – are slow to emerge. Curricula have been reevaluated since the escalation of the terrorism problem and under U.S. pressure. Despite important changes to individual aspects, however, the strong focus on Islamic and Arabic teaching is unlikely to disappear any time

soon. As in other Arab countries, the scientific research output of the university system is miniscule.

### 3. Management

#### 3.1. Level of difficulty

Structural constraints on governance are moderate. The kingdom has an impressive physical infrastructure, considerable fiscal resources and a largely healthy and reasonably educated population. However, the Saudi administration suffers from a number of capacity defects that cannot be overcome quickly. They are often results of past distributional decisions, but also of rapid, oil-based state growth in general. They include:

- the low monitoring and information-gathering capacity of the state, despite the large size of state apparatus,
- a low level of integration of various state agencies,
- a low level of performance of state employees who often view their posts as entitlements, and
- informal patronage networks that prevent equitable and predictable administrative behavior.

Policies often lose momentum when they are transmitted to lower levels of the administration, over which the leadership only has very indirect control. This is especially true of economic reforms.

Due to a long history of oppression of autonomous organization, the state has few formal partners in society with whom to work in implementing reform strategies. Trust in institutions is rather low. Societal “dialogue” is only now being established and occurs either in the supervised press or in state-sponsored forums like the “National Dialogue.” This forum has held four sessions since 2003 in which selected intellectuals, women and youth participate and debate specific, pre-defined topics.

There have been some attempts to allow or even engineer “grassroots” institutions on community or school levels in recent years, but not much has come of it so far, not least due to the top-down nature of these ventures. Recently, the state also tried to organize more politically sensitive groups (lawyers, journalists, human rights advocates, etc.), so far with little resonance.

#### Profile of the Political System

Regime type:	<i>Autocracy</i>	Constraints to executive authority:	<i>1</i>
System of government:	<i>Monarchy</i>		
1. Head of State:	<i>King Fahd Ibn 'Abd al'Aziz Al Faysal Al Sa'ud</i>		
Source: BTI team, based upon information by country analysts, situation in July 2005. Constraints to executive authority (1-6 max.) measures the institutional constraints posed by a federal or decentralized state, a second parliamentary chamber, referenda, constitutional and judicial review and the rigidity of the constitution.			

As the generally low level of political mobilization might suggest, most social and cultural cleavages within the kingdom have not yet found much open political expression. Considerable cleavages exist along two main lines:

- Regional: the Central Province (Najd) is often perceived by other regions as being politically, economically and culturally dominant, with the western region being particularly keen on its own identity and the south being particularly disadvantaged.
- Sectarian: the clearest cleavage is between the Sunni-Wahabi establishment and the Shi'ite minority (Twelver Shi'ites in the Eastern Province and some Ismailis in the south). Recently, adherents of Wahabi Puritanism, often associated with Central Province dominance, have been pitted against most other socio-cultural strands in Saudi society. The "National Dialogue" under the Crown Prince's patronage has allowed open debate of Islamic pluralism in the kingdom for the first time, with various trends – Salafi, Sufi, liberal etc. – being represented.

There is also a certain generational cleavage, with younger Saudis lacking a role and having little to say in a stagnating patriarchal society. The overall level of internal socio-cultural integration is low. Due to the dominant role of the Saudi state and the Al Saud as political arbiters in the system, even larger groups in society have not yet found their political voices. Organizational means and a tradition of mobilization are both lacking. Popular dissident preachers are the only figures who can drum up a popular following, but many of them have been co-opted or locked up (most recently, the state began a trial against three jihadist preachers who had previously recanted their views on TV in late 2003).

### **3.2. Steering capability**

The political leadership claims to think of future generations' needs in terms of education, economic development and political stability. At the same time, a rhetorical premium is always put on national unity and gradualism. In reality, shortsighted budgetary planning and other automatic policies show that effective long-term planning is often lacking. Although economic reforms are being tackled, these often happens in a haphazard fashion and with insufficient follow-up (cf. the incoherent "Saudization" of labor markets, the half-hearted foreign investment reform since 2000, the sluggish and uneven privatization process, the ever-stalled introduction of commercial courts and company laws etc.).

Although the right ideas are often mooted, the octogenarian leadership often has very little patience and tends to resort to declamatory measures once a problem becomes salient, with little subsequent attention to policy details or feasibility. Regime survival and the maintenance of maximum power reigns supreme, and policies are executed so that crucial coalition partners are not hurt. Full democratization is explicitly not for a goal. Although some leaders, among them the Crown Prince, harbor sincere if patriarchal concern for the well being of the

populace, in practice they often end up muddling through with the preservation of Al Saud rule as the top priority.

Correspondingly, political reforms (see above) have so far been superficial. Economic reforms have been more serious, but they have also been only partial and have suffered from the capacity deficits of the bureaucracy outlined above, compounded by age, limited attention span and restricted technical understanding on the part of the leadership.

The technical ministers in the cabinet who might have reform know-how cannot see through a coherent economic reform strategy by themselves, as they are often factionalized, represent different institutional interests and are oriented toward the patronage of senior princes above them rather than collegial decision-making. Moreover, they often have limited power over their own sprawling institutions. This set-up inter alia leads to parallel and inconsistent labor force policies, the obstruction of privatization by the agencies whose assets are concerned and the obstruction of foreign investment liberalization through lower-level red tape.

The Crown Prince is known to be amenable to discussion and is fond of consultation processes. Despite his limited understanding of technical issues, he appears to be reasonably flexible in reviewing policies, although the basics of Al Saud rule are off limits to any discussion and his role is patriarchal in nature, with discussion being “granted”.

As first of the senior princes, he indicated in the late 1990s that Saudi Arabia’s economic model would have to be adjusted, as the fat years were undoubtedly over. In November 2002, he visited poor quarters of Riyadh and announced the need for a national poverty strategy, again breaching new territory. Similarly, he has recognized the need for national dialogue in a society that is increasingly culturally and ideologically fragmented.

Few of these landmark reorientations have led to a fundamental restructuring of politics, however – mostly due to the structural policy-making problems outlined above, and in particular to the fact that other senior leaders are more sluggish in their recognition of challenges than Abdallah.

### **3.3. Resource efficiency**

Against this background of limited policy control and adaptability, it comes as no surprise that the government is not always able to use available resources efficiently. Since the late 1980s, a disproportionate share of public spending (consistently above 80%) has gone to current expenditure, a large share of this being the cost of employing a bloated public labor force. Capital expenditure has usually been below replacement requirements, which means that public infrastructure has been deteriorating. With a few large and significant exceptions,

tender procedures tend to be non-transparent, and public procurement is a field of major waste.

Although in principle, meritocratic procedures exist in public services, hiring is often determined either by favoritism or through random pickings from lists of university graduates. Administrative efficiency is accordingly low.

As indicated, although there was a \$30 billion budget surplus in 2004, spending overshoot original planning by \$20 billion (about 20%), indicating slightly improved but still very wobbly fiscal discipline. The budgeting process has remained opaque. Although estimates for different areas of expenditure are given at the beginning of a fiscal year, closing accounts have not been revealed since 1989. A considerable share of oil revenues is siphoned off before it reaches the official budget; estimates are up to 20%. Public sector auditing and expenditure control remains embryonic, and the budget is set up according to an archaic line-item process.

Although Defense Minister Prince Sultan has announced possible elections to regional councils and the introduction of regional budgets in 2003, the administration is still highly centralized, to the extent that bureaucrats in provincial offices or on lower levels in the capital have practically nothing to decide.

On the other hand, the level of technical expertise in the cabinet is relatively high, certain institutions like SAMA are relatively efficient and the overall output of state services in education and health care is more than acceptable by regional standards. Bureaucratic procedures, although cumbersome, tend to be relatively more predictable than in many other developing countries.

The fragmented structure of the administration means that policies of a crosscutting nature are seldom implemented in a coherent fashion. The situation is exacerbated by the fact that different institutions often attempt to regulate the same policy area. A prominent example is “Saudization”, where different agencies have set different quotas and rules (agriculture, SAMA, health, education ministries), and where the Ministry of Interior was for a long time freely issuing work visas to its clients while the Ministry of Labor had the hopeless task of controlling the overall labor force (the Ministry of Labor was partially empowered to control overall visa issuance in early 2004).

Similarly, when it came to implementing the April 2000 foreign investment act, the Ministry of Interior and the Ministry of Commerce, among others, counteracted the drive of the new General Investment Authority to open up the economy, protecting vested interests in business and bureaucracy. The WTO accession process is another example of haphazard implementation, with agencies beyond the Ministry of Commerce taking little note of the need for new rules. The crosscutting nature of formal and informal structures of authority complicates

such problems. Agencies led by a senior prince, like the Ministry of Interior, tend to be impervious to pressure from other institutions. Inter-agency councils, sometimes on the cabinet level, tend to reproduce the broader cleavages.

Defense and security is another fragmented area, with various Ministry of Interior forces under Prince Naif's control, the National Guard under Crown Prince Abdallah's control and the Ministry of Defense forces under Prince Sultan's control. This fragmentation has led to incompatible procurement and to a lack of interoperability. Institutions often have their own residential, health care and educational facilities, which inhibits standardization and economies of scale and increases local vested interest and a certain "fiefdom" character. Senior leaders can negotiate and coordinate on larger policy questions, but smaller issues – often tied to implementation – frequently remain stuck between various agencies and spheres of power.

Saudi Arabia ranks 71 in Transparency International's Corruption Perceptions Index, which places it at the lower end of the rich Gulf countries. There are formal supervision mechanisms within the bureaucracy (such as through the Ministry of Civil Service), but they do not operate on a regular basis. The Majlis Ash-Shura has issued recommendations on corruption but has not investigated any particular instances. Civil society supervision is lacking; the press occasionally does some muckraking on lesser political corruption but is rather toothless and reluctant to name names. Different government agencies suffer from various degrees of corruption; the "cut-taking" within the Ministry of Defense is legendary. The obtainment of "Saudization certificates" from the Ministry of Labor was at least until recently mired in corruption, and the Ministry of Commerce and Ministry of Interior have reputations of non-transparency and venality. Princes can get involved as "middlemen" in administrative dealings and tenders, even without occupying an administrative post.

Certain processes have been insulated from blatant corruption through the Crown Prince's personal involvement, often connected with the hiring of international advisors. Examples include the corporatization and 30% initial public offering (IPO) in early 2003 of Saudi Telecom and the tender of the 2<sup>nd</sup> GSM license, which was won by a consortium led by United Arab Emirate's Etisalat in the summer of 2004 (other, apparently more powerful consortia, some of them with substantial royal family interests, lost out).

Accountability rules are generally embryonic, and the opacity of accounts and administrative procedures and the haphazard nature of prosecution mean that corruption remains a systemic problem, leading to significant deadweight losses – although not to the extent that doing business in Saudi Arabia becomes impossible. In relation to overall GDP, the share of bribes is significantly lower than in places like Egypt or Syria, and probably not higher than in most southern European countries.

### **3.4. Consensus-building**

There is very little interest in substantive democratization among powerful groups such as royals, clergy or big business. Democratization, it is thought, would lead to loss of influence and status and possibly to instability. Calls for substantial democratization usually come from intellectuals and religious extremists, for example, through a number of petitions since 2003. These actors may have access to specific princes, but do not have much of an independent power base, especially if secularly inclined. The Saudi elites' interest in economic opening is more substantial, but the royals, the cabinet and business are frequently split on the details, and vested interests are often defended successfully.

To the extent that there is interest among the leadership in social and economic reform, implementation is often stalled. Powerful veto players are seldom overcome due to a largely consensual style of policy-making among senior players. Prince Naif, although generally seen as an anti-reform figure, seems to have increased his power influence over the last five years (despite the initial failures of his Ministry of Interior in hunting down terror suspects).

The Crown Prince, more than anyone else in the leadership, has tried to address some of the social cleavages indicated above through his "National Dialogue" and more generally through a controlled opening of the public space. So far, the top-down initiatives do not appear to have led to a substantial reconciliation of various groups (salafis, the religious establishment, liberals, representatives of different regions and age groups and Saudi men and women in general). Only some segments of the Saudi Shi'ites may have moved closer to the regime due to the partial lifting of restrictions on their communities. Generally, Saudi society appears to have become more complex and fragmented. Nonetheless, the vast majority of Saudis seem to acknowledge the Al Saud as the rulers of the realm and credit them with the foundation of the state and the capacity to hold the Saudi system together and there is tangible fear of disintegration without the Al Saud.

Since May 2003, the terrorism problem has engendered fears of social disintegration, which were a major reason for the regime's top-down efforts to create more formalized social and political institutions. In addition to the initiatives outlined above, youth and community centers, student unions with elected leaders and a national group representing workers' interests may be in the offing. There has been an increasing rhetorical emphasis on "civil society" and "citizenship" in the last two years, especially from Abdallah. This has not yielded any impressive results yet and it is unlikely to do so unless more freedom is granted for truly autonomous initiatives. Otherwise, the indifference of most Saudis toward such initiatives will probably persist.

Among societal interests, only business currently has a relatively powerful organizational basis, and as a result, it has been extensively consulted on tax issues, foreign investment regulation and labor law among other issues in recent

years. Other professional associations are not part of the policy-making process in a regularized way. Many potential interest groups – consumers, workers, independent human rights groups, local and regional interests etc. – simply are not (yet) organized. Intellectuals are heard (especially by Abdallah, but also by other princes, such as the “modern” members of the Al Feisal clan) but on an ad hoc basis. They have little formal organizational resources. The Majlis Ash-Shura is comprised of handpicked representatives of different functional strata and it has come to play a significant role in many policy areas, but in the absence of powerful intermediary institutions, their representational claim is doubtful.

The national myths of Saudi Arabia are still being taught in Saudi schools, and those who suffered in the process of state formation (Shi’ites, non-Wahabi Muslims in general, parts of the population in the western and southern regions) are voiceless. As the Al Saud are so intimately connected to the political history of the state, even the relatively open atmosphere of the recent years has not allowed for debate of past injustices.

### **3.5. International cooperation**

The kingdom has a peculiar attitude to international technical assistance. Technical cooperation is extensive. This is not in the form of development aid, but rather consultancy, which the Saudis buy on their own terms. Although the resources spent are often immense, international expertise can be used to good advantage, as the Saudi Telecom privatization shows. The kingdom also “bought” international aid for preparing its municipal elections, and the IMF and World Bank are the originators of many original drafts of economic legislation (e.g. the 2003 income tax draft). Often, however, consultants are kept at arm’s length as state agencies are afraid of losing control or divulging sensitive data, and resources spent on consultants are lost.

International political criticism from international organizations and non-governmental organizations (NGOs) is not completely ignored by the regime anymore. Instead, the leadership takes care to refute it or at least qualify it strongly (for example, religious freedoms, human rights and rights of foreign workers, after the Amnesty International or AI and Human Rights Watch or HRW campaigns in 2000 and 2004 respectively). Generally, the regime is very sensitive about political interventions.

Saudi Arabia has a reasonable record of accomplishment on international economic cooperation, and it has been trying to establish a general leadership position in the Arab and Islamic worlds with some success, such as a number of multilateral statements on terrorism and Palestine in recent years. There is very little cooperation with NGOs, although some human rights workers have been allowed to visit the kingdom since 2000. The degree of cooperation with international institutions varies. Saudi Arabia is an important contributor to the

IMF and World Bank, but it is very sensitive about its sovereignty. Article 4 consultations are still not published, and Saudi data is kept secret even within the Bretton Woods institutions. The kingdom is still not a WTO member despite the U.S.'s demands that it join.

Western political distrust has increased since 9/11, but economic cooperation is still substantial, and the kingdom is seen as a rather reliable partner, as a constant trickle of visiting heads of state and of bilateral trade and investment agreements shows. Saudi Arabia's Standard & Poor's June 2004 sovereign ratings were A/A-1 for foreign currency and A+/A-1 for local currency, which indicates a good level of creditworthiness and a solid stability outlook. Although international criticism after 9/11 was harsh, the kingdom has become - by the United States's own admission - more cooperative on terrorism issues, especially since 2003. The 9/11 report and the Financial Action Task force have generally given the kingdom good marks. Islamic charities are closely supervised and the government conducted a big international terrorism conference in February 2005.

By Middle Eastern standards, Saudi Arabia is a state that puts a premium on cooperation, if only because it is situated in the rather exposed, rich and underpopulated Gulf region. The Saudi-led Gulf Cooperation Council (GCC) is the only relatively successful sub-regional body in the Arab world. Despite repeated spats and technical hitches, a customs union was initiated in 2003, and a monetary union is planned for 2010. A US-Bahraini free trade agreement has created tensions within the GCC since the autumn of 2004, but an open rift between Saudi Arabia and its smaller neighbors has not occurred.

Some of Saudi Arabia's relations with the wider neighborhood are strained, not least due to the uneven distribution of populations and resources. Relations with Iran have improved markedly since 1997, however, and cooperation with Yemen has improved, with a 2000 border agreement being slowly implemented. Interestingly, a recent poll in Iraq showed that Saudi Arabia appears to be the most desired partner in rebuilding the country. Iraqis apparently harbor much smaller fears of undue Saudi intervention like in the case of Iran. Finally, Saudi Arabia is an implicit rival of Egypt's for leadership in Arab world, but when push comes to shove both are moderate countries with common stability interests.

#### **4. Trend of development**

##### **4.1. Democratic development**

Stateness, political participation and the rule of law have at most improved slightly in the 2003 to 2005 period. Although some analysts see auspicious signs in the National Dialogue, increased public debate, partial municipal elections and talk about workers' rights, this does not amount to any systemic political, legal or social change in itself. The Al Saud are still not held accountable, the court system

is still creaky and non-transparent and judicial reform still stuck. The administration is opaque and redress mechanisms are lacking. If substantial change is to take place, it will certainly take more time. There have been public trial balloons regarding regional elections and elections to the Majlis Ash-Shura, most prominently in a 2003 interview with Prince Sultan, but these were usually followed by denials. Freedom House has consistently given Saudi Arabia the score of 7/7 (practically no political rights or civil liberties).

For the time being, there is no political participation on the national level, although increasing discussion of democratization issues has been allowed. It remains to be seen whether municipal elections will trigger a broader process of participation. The extralegal status of large parts of the royal family is a formidable obstacle to meaningful political opening and accountability, however, especially as hundreds of princes hold public office. Moreover, other MENA precedents of partial political openings are not auspicious.

#### **4.2. Market economy development**

According to the United Nations Development Program's human development index, the standard of living in Saudi Arabia has improved slightly in the past five years. The HDI increased from 0.747 in 2000 to 0.768 in 2004 (however, it had been at 0.778 in 1998, indicating a possible inconsistency of Saudi statistical sources). Educational spending in particular has benefited from the oil windfall of recent years, and infrastructural bottlenecks, especially in poorer regions, are likely to be mitigated. Generally, however, the slow reform of state services is still competing with demographic momentum, as the population continues to grow at more than 2% per year. Although the leadership is aware of poverty and exclusion issues, the administration is slow to adapt to new challenges, and resources may soon be stretched again if oil incomes falls. The efficiency gains required in public services to provide full, high-quality health care and education to the population are still to be made.

Repeated announcements of public-private partnerships in education have not yet resulted in the infusion of substantive expertise into the public education system, and private providers are slow to get off the ground. Among the promising exceptions are Kingdom Schools, the new Prince Sultan University in Riyadh, Prince Sultan College for Tourism in Abha and the Queen Effat and Dar Al-Hikma Colleges in Jeddah – all notably under the patronage of various factions of the Al Saud.

Health care provision has also benefited from the increased budgets of recent years but it also suffers from efficiency problems. It is currently part public and part private. In the fragmented public health sector, procurement and management tend to be non-transparent, and common Saudis have complained about the insufficient services of the Ministry of Health's institutions (which are accessible

to the public, as opposed to institutions tied to other ministries). The national poverty strategy yet has to come up with tangible numbers and policies.

Although the institutional framework for business has not much improved globally, the kingdom has made a few specific and significant advances. The Capital Markets Authority became operational in 2004 and is likely to make future privatizations, and IPOs are in general more transparent, improve overall liquidity, provide more investment vehicles for Saudi nationals and offer capital for new, large-scale business ventures. It still has to demonstrate how efficiently it can combat insider trading and improve general disclosure. Regulators have been created for electricity and telecoms, but these still have to prove their mettle too. New foreign investment rules have formally opened a number of important sectors for 100% foreign ownership, including electricity, water and telecommunications, and provide a number of investors' rights, like access to cheap public credit and appeals procedures.

Administrative and judicial practice, however, has in fact remained largely the same, and new rules often go unimplemented. According to the World Bank's "Doing Business in 2005" report, "entrepreneurs can expect to go through 12 steps to launch a business over 64 days on average, at a cost equal to 69.7% of gross national income (GNI) per capita." This means even more red tape than the MENA average. Contract enforcement can be problematic, and market and client information is often lacking.

Openness to competition has in many areas not yet changed substantially, despite various adjustments to WTO demands, such as lower tariffs and increased formal intellectual property protection. Barriers to entry are effectively high both for Saudi and international newcomers, as established players usually can defend their turf successfully. Many legal reform projects are still stuck, and e-government initiatives yet have to make a difference in the administration's daily dealings.

In quantitative terms, economic development since 2001 has been impressive. While growth stagnated in 2002, real GDP increased by about 7% in 2003, and growth for 2004 has been estimated above 5%. Much of this was oil-induced, however, and is not primarily a result of better regulation or higher competitiveness. Much private investment currently goes into the real estate and retail sectors, whose value added is limited and which might soon be subject to cyclical fluctuations. The private sector has been slowly expanding into productive industrial areas like petrochemicals and plastics (most recently through the 2004 Sahara Petrochemicals IPO), but not on the scale required for sustainable non-oil growth and job growth. The licensing of telecoms consortium Ettihad Etisalat in 2004 augurs well for efficient provision of high value-added mobile communications services, but again, employment effects are limited.

**Table: Development of macroeconomic fundamentals (2000-2004)**

	2000	2001	2002	2003	2004
Growth of (real) GDP in %	4.9	0.5	0.1	7.2	5.3
Oil Export growth in %	57.9	-15.6	6.7	28.9	23.3
Non-oil Export growth in %	13.9	23.7	5.7	26.9	23.8
Import growth in %	7.9	3.3	3.6	14.3	n.a.
Inflation in % (CPI)	-1.1	-1.1	0.2	0.6	0.2
Investment in % of GDP (gross fixed capital formation)	17.5	18.4	18.1	17.6	n.a.
Tax Revenue in % of GDP (non-oil state revenue)	6.2	6.4	6.6	7.7	n.a.
Unemployment in %*					
Budget deficit in % of GDP	+3.2	-3.9	-2.9	+4.5	+10.5
Current account balance in billion \$	14.3	9.4	11.9	28.0	51.5

Sources: SAMA (years 2000-2003); Saudi American Bank, Arab News (2004, preliminary data).

\* Various unemployment estimates have been given from various agencies. For some time, figures between 8 and 9.6% were offered by the Central Department of Statistics, but after a registration campaign in late 2004, the Ministry of Labor has claimed that there are only 180.000 job-seekers, implying a figure of about 6%. Unofficial estimates are between 20 and 30%.

#### D. Strategic perspective

Political change, if it occurs at all, is likely to be gradual. For better or for worse, the Al Saud are seen by most relevant parties as the indispensable center of the political system. Similarly, socioeconomic problems and issues of administrative development are likely to be tackled in a gradualist fashion. International actors have various degrees of advantage in different areas.

When it comes to issues of security, sovereignty and the structure of rule, international actors can exert only limited influence. Pressure will often have to be exerted behind closed doors, as public demands and condemnations tend to result in backlashes from the regime, but often also from the Saudi populace. Whereas the heightened public tensions between the United States and Saudi Arabia have often led to retrenchment and defiant statements by figures like Prince Naif, the United States has been rather successful in exerting non-public pressure regarding educational curricula and the control of financial flows since 9/11.

In some cases, however, public criticism appears morally necessary, such as in the case of migrant workers' rights. It should then be primarily channeled through multilateral institutions, which enjoy much more international and regional credibility. The inchoate opening of Saudi politics should be encouraged, but also explicitly addressed as part of a deeper, more meaningful process that has only just started.

NGOs can play the most explicitly critical supervisory role regarding human rights and other issues. Criticism of AI and HRW has been discussed in the kingdom and it has triggered policy reactions. Even if these developments are only cosmetic, problems will be harder to brush under the carpet in the future. Installing international follow-up mechanisms will be important, as the occasional sensationalism of Western media can usually be dealt with through a few declamatory statements without any substantive change on the ground. It will also be important to look at less salient, more structural political and human rights issues. The (very occasional) amputation of limbs in the judicial system is an atrocity in Western eyes, but not something with which Saudis themselves are greatly concerned. Criticism will be most effective if it makes sense within Saudi society's cultural frame of reference. It will be successful if it focuses on issues that have a certain scale and that resonate with Saudi society itself, such as political transparency, accountability and the behavior of state representatives.

International institutions and media should highlight the importance of reformist voices in the kingdom and give them international forums. There is great interest among highly educated and internationally oriented Saudi intellectuals in communicating with international peers and civil society institutions, but there are too few connections at this point.

The Saudi setting, although ossified, is relatively pluralist and has many access points for discussion, research and exchange. Foundations run by liberal princes can be used to increase international communication. Fledgling interest groups, even if controlled by the state, can be given technical assistance and be integrated into international structures.

There are many avenues of technical cooperation for international actors, especially in "less political" areas like education, public sector reform, technical and administrative aspects of security, as well as certain legal and political reforms. The latter can include assisting in the holding of elections and the building certain types of civil society groups. Saudi Arabia is in desperate need of public and societal supervisory mechanisms that create accountability for state actions, even if this only begins on lower levels. The regime is likely to approach international cooperation cautiously, but many members of the elite recognize various reform deficits.

Especially when it comes to public sector reform, there is great eagerness among technocrats to learn from other systems. It is even more important, however, to build high-level interest in reform among senior actors. Again, follow-up mechanisms and clear benchmarks are needed. They can help the leadership understand the deleterious nature of the fragmentation and opacity of the Saudi administration.

The fact that the kingdom can pay for the delivery of assistance has both advantages and drawbacks; international actors should seek a minimum of autonomy for their action within the kingdom.

Socioeconomic change will have to be engineered domestically, as it is mostly an issue of using the available resources more transparently and equitably. International players can offer technical assistance and advice. Further inclusion in the UN reporting systems will be helpful (the first Saudi human development report was issued in 2003). International benchmarking will help the country profit from lessons learned elsewhere. The technocratic interest in best practices in public-private partnerships, indicative planning, administrative networking etc., is considerable.