

# BTI 2008 | Saudi Arabia Country Report

<b>Status Index</b>	1-10	<b>4.36</b>	# 96 of 125	
Democracy	1-10	2.72	# 119 of 125	➔
Market Economy	1-10	6.00	# 54 of 125	↗
<b>Management Index</b>	1-10	<b>3.81</b>	# 101 of 125	

scale: 1 (lowest) to 10 (highest)    score    rank    trend

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## Key Indicators

Population	mn.	23.1	HDI	0.78	GDP p.c.	\$	13,978
Pop. growth <sup>1</sup>	% p.a.	2.6	HDI rank of 177	76	Gini Index		-
Life expectancy	years	73	UN Education Index	0.72	Poverty <sup>3</sup>	%	-
Urban population	%	81.0	Gender equality <sup>2</sup>	0.24	Aid per capita	\$	1.1

Sources: UNDP, Human Development Report 2006 | The World Bank, World Development Indicators 2007 | OECD Development Assistance Committee 2006. Footnotes: (1) Average annual growth rate 1990-2005. (2) Gender Empowerment Measure (GEM). (3) Percentage of population living on less than \$2 a day.

## Executive Summary

During the period under review, Saudi Arabia was marked by two themes: political stagnation combined with an economic boom. The boom, together with the end of the domestic terror campaign of 2003 and 2004, has eased pressure on the Saudi regime. Abdullah, king since August 2005, has introduced several liberalizing reforms since his accession, but has not initiated any political liberalization of great substance. To the contrary, the pace of political change has decreased somewhat since the last report period, particularly insofar as leeway for frank political debate among dissidents has been curtailed. At the same time, Abdullah seems to remain genuinely popular, despite a stock market crash in 2006 that affected numerous low- and middle-income households. There are no strong or organized grassroots demands for fundamental political change. To the extent that oppositional structures exist, these are to be found among Islamists. But even here, dissidents tend to be marginalized or co-opted, and Abdullah has signaled his limited tolerance of criticism by temporarily imprisoning prominent Islamic dissident Mohsen Al-Awaji in March 2006. Key political reforms initiated by the government during the observation period included municipal elections in early 2005, further “National Dialogue” sessions in which issues of social and cultural change are debated, the licensing of several (albeit tightly controlled) “civil society” institutions, and steps toward women’s inclusion in the labor market and parts of public life. These initiatives have served partially to boost Abdullah’s credentials as a reformer both domestically and internationally. Much of these steps have bypassed the bulk of Saudi society, however. The most substantial political change has been a reform within the royal family itself; namely, the 2006 allegiance law, which formally gives sons of Saudi Arabia’s founder, King Abdul Aziz Al Saud (Ibn Saud), a vote in future succession processes. Although not a measure of political liberalization in a strict sense, this is an important step toward stabilizing future power transfers within the royal family. On the economic front, progress has once again been relatively

consistent, although here too, implementation is often sporadic. Abdullah has enjoyed more unfettered leadership, which has allowed him to push through liberalization measures related to WTO accession, privatizations and gradual stock market reform. Despite such progress, reform in other areas – such as within the court system and regarding competition policy – have moved ahead more slowly or not at all.

## History and Characteristics of Transformation

The Kingdom of Saudi Arabia was declared by Ibn Saud 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 Ibn Saud, who died in 1953. The first council of ministers was created in 1953, at 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 in the kingdom.

At the same time, remnants of national and local consultative councils – mostly carryovers from the western Hijaz region, which was historically more politically developed than other regions on the peninsula – withered away and eventually disappeared, leaving the massive state bureaucracy as the main formal instrument of rule. Informally, the system was buffeted by networks of personal patronage, distribution and favoritism, which the sprawling Al-Saud family controlled. The clergy, which had acted as a strategic ally to of the Al-Saud family in the state's emergence, grew even more loyal to and materially dependent upon the royal family, but nevertheless remained an essential legitimating force behind Al-Saud rule.

Saudi Arabia's large-scale oil-fueled 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 1960s during the heyday of Arab nationalism. However, the palace managed to both suppress strikes in the country's oil-rich eastern province and to avert a number of military coup attempts. Official announcement of timid reforms – appointment of a consultative council, drafting of a basic law – usually came to nothing. One of the royal family's persistent advantages, which has aided them greatly in their political survival, was their deep embeddedness in significant parts of the administration, 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 of about \$18,000 in 1981, the year of the highest real oil prices thus far. Given the rapid economic expansion at that time,

however, this figure should be considered with care, as it does not reflect the actual standard of living. Since then, the overall economy has not been able to keep pace with demographic growth, which for a number of years expanded at an annual rate of approximately 4%. The regulatory framework for business has been improved in recent years, but in practice, it is applied inconsistently. Nonetheless, the Saudi private sector has matured considerably in recent decades and has more sophisticated managerial structures than most of its peers in the Middle East and North Africa region.

After the seizure of the Grand Mosque in Mecca by Islamist dissidents in 1979, the regime emphasized the enforcement of conservative social mores, yielding more power to religious conservatives in education, domestic and international cultural policies and enforcement of public order. Nonetheless, after the 1990/1991 Gulf War, both Islamists and liberals were disappointed by the ruling family, with its apparent inability to protect the region without U.S. aid and its 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 a number of symbolic concessions. These included:

Establishing the Basic Law that laid out basic features of the political system and ensured basic rights, albeit without properly articulated mechanisms for recourse.

The creation of a Majlis ash-Shura (consultative council), which functioned as an appointed consultative body chartered with reviewing draft legislation. The Majlis has been enlarged three times since 1992, and has now grown to 150 members, up from its original 60. Although the Majlis is not representative and has a certain technocratic bias, it has acquired increasing importance in more technical fields of legislation.

A law of regions, setting out basic structures of governance in the kingdom's 13 regions. The political situation calmed down subsequent to these reforms, not least due to the fundamental splits among oppositional groups. Whereas liberals had been socially isolated all along, popular Islamist dissidents were either co-opted or oppressed by the regime. Two prominent opposition preachers were detained from 1995 to 1999, and at least one of them is today close to the government. Crown Prince Abdullah became the effective head of government when a stroke incapacitated King Fahd in 1995. Abdullah gained more political power after 1998 and initiated a number of economic reforms from 1999 onwards, with mixed results. He became king in August 2005, after Fahd's death. Abdullah is popular and generally seen as a driver of both socioeconomic and political reforms, although he has moved more slowly on the latter. The recent economic boom has relieved some of the pressure for political reform. Moreover, 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 prospects of reform.

## Transformation Status

### I. Democracy

#### 1 | Stateness

Saudi Arabia has not witnessed significant violent conflict within its borders since the 1930s. Today, all regions and tribes recognize the sovereignty of the Saudi state, and there is a rather broad consensus on the role of the royal family as a lynchpin of the polity. The domestic terror problem between 2003 and 2005 has been largely overcome.

Monopoly on the use of force

Saudi citizens are Muslim by definition; no indigenous non-Muslim groups live in today's kingdom. The Shi'ite minority – Twelver Shi'ites in the east and Ismailis in the south – is denied important cultural rights. They also suffer from political marginalization and socioeconomic deprivation, although King Abdullah has pledged more government attention for underdeveloped regions. There is an implicit ethnic hierarchy in Saudi Arabia, with Najids from the Central Province on top, Hijazis and Eastern Province Sunnis second, and the rest below. Najd is associated with the Hanbali Islamic school of law and its Wahhabi interpretation. While non-Hanbali religious practices are relatively more tolerated under King Abdullah than they had been under previous rulers, Shi'ites are still clearly situated at the bottom of the hierarchy and suffer from government abuse. The freedom of Shi'ite political activists is particularly constrained. Some Shi'ite opposition leaders in exile have doubts about the Saudi state as it is organized today, but open secessionism is not currently advocated. Some members of the jihadi political fringe do not accept the Saudi state as a legitimate entity, but they do not have a clear alternative vision.

State identity

The Saudi state is officially defined as Islamic, with the Quran as its constitution. The 'ulama (Muslim clergy) are part of the state apparatus and wield considerable influence in issues of public morality, personal status law, education and culture. Shari'ah courts are the centerpiece of the judicial system. There is no freedom of worship for non-Muslims, although tolerance of actual practice varies by the nationality of the practitioners. Secularism is beyond the pale of Saudi discourse, both official and, to a large degree, public discourse. In late 2005, a Saudi teacher

No interference of religious dogmas

was sentenced to 750 lashes as a punishment for discussing non-Muslim religions in the classroom. Officially, all legislation is to be based on Shari'ah. In practice, however, significant sections of the administration are run according to secular principles, including the regulation of Saudi banks. Inopportune fatwas (judicial opinions) have been repeatedly ignored by the regime, or alternatively, the clergy were forced to issue verdicts more convenient for the regime. On economic matters, Shari'ah courts are often circumvented through administrative tribunals.

The Saudi state is large and the administration reaches out to even remote villages, as do, increasingly, its basic services. However, the bureaucracy is excessively bloated, with an estimated number of one million state employees. The state's "infrastructural strength" is not very powerful, as it finds it hard to enforce economic rules, apply regulations consistently, and gather information about its constituents. The fact that residency registration and the introduction of residential addresses was only begun in recent years illustrates this infrastructural weakness. As a rentier state, Saudi Arabia has no comprehensive tax system. As such, the government's information about economic activities can be deficient.

Basic  
administration

## 2 | Political Participation

There are no democratic elections at the national level. Municipal elections were held in spring 2005 on a nation-wide scale for the first time. However, women were excluded and only half of the members of the rather weak municipal councils were chosen by popular vote. National elections have been mooted, but are not likely any time soon, not least while the economic boom continues to ease political pressure on the leadership.

Free and fair  
elections

As there are no political officials elected on the national level, there is no influence which could be wielded through this channel. Currently, the only elected persons with some influence in society are the heads of chambers of commerce, but they tend to represent big business families.

Effective power  
to govern

Parties and unions are not allowed and formal associations require royal fiat to obtain a license. The regime has allowed some "civil society" activities in recent years. In the voluntary sector, there have been bottom-up initiatives. Although some of these address controversial social topics, none have ventured into open political advocacy. Some political interest groups – professional associations and a human rights group – have been licensed in recent years, but they are state-controlled. In its attempts at political modernization, Saudi Arabia seems to be evolving toward a rather anemic state corporatism.

Association /  
assembly rights

Saudi citizens today have much more space for discussing cultural and social issues as compared with only a few years ago. This is significant, as these issues

Freedom of  
expression

are to some extent tied up with the political identity of the state. Little public debate occurs about substantial political issues that go to the core of the ruling family's monopoly on state power, however. As such, whereas the outcome and relevance of municipal elections can be criticized, no journalist has dared to openly demand national elections. Similarly, criticizing princes in the media is a line no one dares to cross. Newspapers are controlled through the Ministry of Information, over which the Ministry of Interior has considerable control. Editors-in-chief must be approved by the state. The press has little statutory guarantees against encroachments when they occur (Article 39 of the 1992 Basic Law justifies censorship relatively openly). A minimal degree of pluralism of opinions is guaranteed by the fact that different newspapers are controlled by different factions of the royal family, which tend to have different ideological orientations.

### 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 liking of non-royal Saudi elites. Large parts of the functional bureaucracy are staffed by commoners, and commoners dominate technical posts. Day-to-day intervention of the royal family is limited as long as there are no immediate political or economic interests at stake.

Separation of powers

To the extent that a judiciary run by the clergy can be considered as independent, it has considerable day-to-day autonomy, insofar as the regular administration has very little leeway to control (or predict) judicial proceedings. Judicial professionalism, especially when it comes to more technical areas as commercial law, is often limited. 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 generally yields to royal pressure. Administrative tribunals function reasonably well.

Independent judiciary

Mechanisms to hold accountable and investigate political elites exist in principle, but are not activated very often. Princes very rarely lose their office – it usually takes a major, publicly visible offense for that to happen. Commoners are fired (and sometimes tried) more frequently, but corrupt officials with good royal patronage can cling to their office for decades without having to fear retribution. Public naming of corrupt officials does not happen often, but when someone does get fired, the word tends to spread. While occasional clean-ups by a new minister do occur, their range is usually limited.

Prosecution of office abuse

The Saudi state does not usually resort to mass violations of existing civil rights as other Arab authoritarian states are wont to. Unlawful arrests are rather rare. At the same time, however, existing rights are very limited: there is no right of assembly, freedom of opinion, organization, religion etc. A few rights are enshrined in the 1992 basic law, such as privacy of residence and mail correspondence, and the concept of “nulla poena sine lege.” They do not include basic political rights, however. Discrimination, both de facto and de jure, remains rampant in the kingdom. Women are systematically disadvantaged in public life and in the judicial system, as are Shi’ites, although their position has been improving somewhat under the new king. Foreign workers have no political rights and often must live in terrible conditions. In spite of attempts by the regime to redress their situation, they still enjoy scant protection against widespread abuse by their employers. Effective access to judicial redress for all the groups mentioned above is limited.

Civil rights

#### 4 | Stability of Democratic Institutions

There exist no democratic institutions on the national level in the Western sense, although there are mechanisms of informal accountability, in that princes are keen to react to public sentiment and be perceived as benevolent patriarchs. Different groups in society have different degrees of access to these mechanisms, however. The municipal councils are the country’s only elected public bodies, and have to date done little and found limited resonance in society.

Performance of democratic institutions

#### 5 | Political and Social Integration

There is no party system in Saudi Arabia. Past attempts to set up parties have been suppressed. Not even party-like entities, such as an independent human rights association initiated in 2004, are tolerated. That being said, there is no historical tradition of party politics in the country and societal demand for it seems correspondingly limited. The only (highly imperfect) substitutes for parties are the patron-client relationships which revolve around various centers of power.

Party system

Associational life is controlled by the state. There is a lively voluntary sector attending to various social problems, although its socioeconomic base is mostly in the upper class. Many charities have a strong Islamist character. The functional-corporatist interest groups (professional associations, women’s and youth associations etc.) are state-controlled and do not reach out sufficiently to the groups they are supposed to represent. That being said, many interests are represented within the state – through various functional agencies – or through informal clienteles of princes, partially taking up the functions of associations (although political restraints are different, of course).

Interest groups

There is no survey data on Saudi support for democracy. Impressionistically, the interest in formal democratic mechanisms is limited in large parts of society. Turnout for the municipal elections in 2005 was very low; in some locations less than 15% of the eligible population. Assent to the rule of the Al-Saud dynasty appears more established than interest in substantive democratization.

Consent to democratic norms

While formal associational life remains state-controlled, informal aid networks can be extensive. Being usually based on friendship or kinship, they remain functionally undifferentiated. Trust between strangers is rather low in the kingdom, and society remains fragmented into regional and (intra-Islamic) denominational sub-groups. There is little tradition of formal association, and social bonds, even if powerful, are often vertical. Society has been demobilized not in the least by an omnipresent provider state.

Associational activities

## II. Market Economy

### 6 | Level of Socioeconomic Development

A Gini coefficient for Saudi Arabia is not available, but anecdotal evidence indicates that inequality widened somewhat after the 1980s oil boom, due both to population growth and the state's limited employment provision. Abdullah's regime has recently taken steps to alleviate poverty, however, that have been based on a national poverty strategy announced in rather general terms in mid-2005 and ratified in October 2006. These steps include an augmented rural development focus in the 2005, 2006 and 2007 budgets, increased social security expenditure and a national housing program. The effects of these programs have yet to become visible on a large scale. In contrast to other Middle Eastern states outside of the Gulf, most free or subsidized public services (utilities, education, health, housing credit) have not been dismantled. Job market opportunities have improved somewhat, but employment generation remains insufficient to decrease the very high dependency ratio in Saudi Arabia – an estimated 6 persons per wage earner. The 2005 UNDP human development report ranked Saudi Arabia 32nd of 103 developing countries on the Human Poverty Index. Income distribution data is not available. The Gender Development Index ranks Saudi women 72nd in the world (at 0.744) based on 2004 data. This reflects good access to education and health, but also an exclusion from large parts of the job market and public life. Poorer groups in peripheral regions of the kingdom such as the south still tend to be excluded from development. Similarly, the vast majority of expatriate workers

Socioeconomic barriers

earn subsistence wages at best. Average salaries of expatriates are less than half of Saudi salaries.

Economic indicators		2002	2003	2004	2005
GDP	\$ mn.	188,551	214,573	250,339	<b>309,778</b>
Growth of GDP	%	0.1	7.7	5.3	<b>6.6</b>
Inflation (CPI)	%	0.2	0.6	0.3	<b>0.7</b>
Unemployment	%	5.2	-	-	-
Foreign direct investment	% of GDP	-	-	-	-
Export growth	%	-7.2	20	-	-
Import growth	%	0.8	11.5	-	-
Current account balance	\$ mn.	11873.1	28047.9	51926.0	<b>87131.5</b>
Public debt	\$ mn.	-	-	-	-
External debt	\$ mn.	-	-	-	-
External debt service	% of GNI	-	-	-	-
Cash surplus or deficit	% of GDP	-	-	-	-
Tax Revenue	% of GDP	-	-	-	-
Government consumption	% of GDP	26.1	24.6	23.6	<b>23.1</b>
Public expnd. on edu.	% of GDP	7.7	7.2	6.8	-
Public expnd. on health	% of GDP	-	-	2.5	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	9.8	8.7	8.3	<b>8.2</b>

Sources: The World Bank, World Development Indicators 2007 | UNESCO Institute for Statistics | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security

## 7 | Organization of the Market and Competition

Prices are largely free in Saudi Arabia, and the Saudi riyal has been internationally convertible for many decades. Saudi Arabia's economy is less statist than that of most other countries in the Middle East and North Africa.

Market-based  
competition

Nonetheless, despite all reform attempts of recent years, Saudi bureaucracy can still be stifling, and setting up a business can be relatively cumbersome: the good of Saudi Arabia's privileged position in the World Bank's 2006 "Doing Business" survey at rank 38 has more to do with changes in the Bank's methodology than with actual substantive improvements in administrative procedures. In terms of enforcing contracts, protecting investors and starting a business, Saudi Arabia ranks worse than the global average. In the Heritage Foundation's Index of Economic Freedom, Saudi Arabia has maintained a moderate score of about 60 during the past decade, without significant trends up- or downwards. Numerous smaller initiatives have been taken by state agencies and chambers of commerce to further the development of small and medium enterprises. It remains difficult for smaller entrepreneurs to operate, as personal connections are still an important facilitator in dealing with the state (and other businesses). In such an environment, larger and more powerful players have a natural advantage. This also explains why few new large companies have come into being in recent decades, despite the fact that mobility has improved with the new boom. The informal sector is not very large in Saudi Arabia as there are no taxes beyond religious zakat, which itself is not very thoroughly collected. Many formal companies circumvent formal regulations though, being registered under a business type different from their actual operation, not sharing data with authorities etc. Regulatory power of the bureaucracy remains limited.

Regulation of competition differs from sector to sector. Telecommunication, electricity, banking and financial services all have their own regulatory agencies, which are active, but sometimes seen as not as strong as they could be. New banks have been licensed, and a third mobile phone license will be auctioned off soon. A national competition authority was established in 2004, but little has been heard of its activity. De facto oligopolies remain in commerce through the commercial agency system, which channels distribution and retail of international goods through local agents. This system can be circumvented under new WTO-related rules, but in fact remains strong.

Anti-monopoly  
policy

Saudi foreign trade has traditionally been rather free, although it could on occasion encounter costly non-tariff obstacles. Further steps toward liberalization have been taken in the course of WTO accession in November 2005 and the (yet incomplete) GCC tariff integration. Tariffs, already set at a low weighted average of 7.3% in 2004, will be reduced further over the coming years; remaining exceptions (on products such as dates) are rather minor. Cumbersome shelf-life rules, inspection and documentation requirements and product standards have been streamlined formally, although the full trickle-down of liberalization to the government agencies involved might still take a while.

Liberalization of  
foreign trade

The Saudi financial system is well-developed and generally very well-capitalized. Foreign banks own minority shares in some of the big players, and fully foreign-

Banking system

owned banks have been licensed over the last five years, although their operations have remained on a relatively small scale, not involving retail activities. SAMA, the central bank, is a qualified and well-respected regulator that cooperates rather well with the banks. There are still some large bad loans given to influential players in the system, but not to the extent that it would put any bank in danger. The new Capital Markets Authority (CMA), created in July 2004, has been put to a test with the 2006 share crash. Although well-intentioned and qualified, it has struggled to develop control over the market's more powerful actors. In some cases, market manipulators have been named and prosecuted, but many have gone unpunished. The CMA has recently started to take some junk stocks out of operation, but there is still considerable speculative trading, and disclosure rarely exceeds the legally required minimum. That being said, Saudi Arabia has an array of very solid blue chips, and the licensing of new investment firms will improve the quality of information.

## 8 | Currency and Price Stability

Among Gulf countries, Saudi Arabia has been most successful in containing the inflation problems created by the recent oil boom; the official inflation rates in 2005 and 2006 were 0.7% and 1.8% respectively. Actual inflation is likely to have been higher, possibly twice as high. The exchange rate has been stable, as the riyal remains pegged to the dollar. Despite much speculation in the press, this peg is unlikely to change any time soon. The peg severely limits the scope of independent monetary policy, but has generally served Saudi interests well. The central bank, SAMA, is operationally independent and well-respected, although politically dependent on the Ministry of Finance. SAMA foreign assets have increased dramatically, to more than \$200 billion in 2006.

Anti-inflation /  
forex policy

Saudi fiscal policy has by and large been balanced in recent years: like other Gulf states, the new boom has not been used as an opportunity for reckless spending, but rather for judicious increases which helped to catch up with the damage done by forced austerity budgets in the 1990s. Public wages were adjusted upwards by 15% in the summer of 2005, and spending on human development and the partially dilapidated infrastructure has strongly increased. Government debt has decreased significantly, from more than 100% of GDP in 1999 to 28% of GDP in 2006. Informally, the rule is to accumulate reserves in fat years, while deficits are incurred in years of low oil prices. Should the price of oil ever collapse again, however, Saudi Arabia will be faced with spending that has been "locked in" on a considerably higher level than ever before, with spending for 2007 planned at 380 billion Saudi riyals, roughly twice the volume of the late 1990s. The state budget remains highly dependent on oil, so that long-term fiscal problems cannot be ruled out. There is no formal budget stabilization mechanism.

Macrostability

## 9 | Private Property

Property rights are generally respected, but claiming them through the court system can be a time-consuming and frustrating exercise. In some important areas, such as real estate, regulation of property rights is deficient, as there is no public registry and powerful players can muscle their way into obtaining land deeds. Similarly, hundreds of thousands of small enterprises are de facto owned by foreigners, while the official Saudi owner collects a monthly fee from them. Ownership rights to these “cover-up businesses” are accordingly precarious. There can also be marginal infringements on property rights by bureaucrats or princes through commission-taking or demanding a silent share in a successful operation.

Property rights

Private companies dominate most sectors in Saudi Arabia. There are, however, two sectors of significant economic and strategic value in the country that are totally and significantly state controlled, respectively: oil and petrochemicals. In banking, the state has shares in several large important banks, including a majority share in the important National Commercial Bank, which has yet to be privatized. Most other sectors (retail and wholesale, most industries, services etc.) are largely privately controlled. Privatization in general – such as the further sell-off of “Saudi Arabian Basic Industries,” water and electricity services, Saudi Arabian Airlines, Saudi Railway Organization etc. – is progressing only slowly. Some successes are notable, however, such as the sell-off of 30% of the national telecommunication company in 2003 and 70% of the national insurance company in early 2005, as well as the initiation of a number of large independent water and power projects with foreign participation.

Private  
enterprise

## 10 | Welfare Regime

In what is clearly an overstatement, Saudi Arabia is often described as a state with “cradle to grave” welfare provision. More precisely, it offers many public services for free or at great discount, but does not offer social security guarantees of the quality comparable to that found in advanced European states. Water and electricity are strongly subsidized for lower income brackets, while public education and health care are free, although they are sometimes of questionable quality. There is a system of social security payments, but it is patchy and administered on a case-to-case basis, not alleviating the kingdom’s considerable poverty problem. State pension payments are financially secured for many decades to come, but may not be sufficient. There is no unemployment insurance, and the informal public sector job guarantee was abrogated in the mid-1980s. As family networks remain tight, many individuals are prevented from sliding into poverty thanks to assistance from wealthier relatives, but these networks are

Social safety nets

becoming increasingly stretched. The recent oil boom has not yet trickled down to the majority of the population. Millions of expatriate workers continue to live in poverty.

In principle, the state makes public services available on a relatively broad basis, including women, and regional and sectarian minorities in its network. Personal relations to the government institutions can play an important role in the administration of public services, however, which can make for de facto inequality in access. Being from a peripheral region or of Shi'ite creed can be a disadvantage. King Abdullah has made a special effort to cater to peripheral regions and to women's needs, but much remains to be done. Saudi women are often faced with the problem of needing a male intermediary to deal with the state, which can make them more vulnerable to fraud and make interaction with the rather opaque bureaucracy especially cumbersome. Although they have good access to (segregated) higher education, their job chances are largely restricted to sectors such as health and education, and the government's pledges of betterment have not yet led to significant employment in other sectors. Saudi Arabia ranks 74th out of 75 countries in the gender empowerment index, with a value of 0.242.

Equal opportunity

## 11 | Economic Performance

The Saudi economy experienced powerful growth in 2005 and 2006, expanding by 6.5% and 4.2% in real terms respectively. This has been a function not only of the oil boom, but also of private investment: during the same years private sector growth was 6.6% and 6.3% respectively. Inflation remains under control, and state debt has been heavily reduced. The trade balance is overwhelmingly positive, largely due to oil. Foreign investment has picked up from modest levels, reaching \$4.6 billion in 2005 according to UNCTAD, which represents 0.5% of the world total. Although the economic boom has been well-managed, some potential threats remain on the horizon. The economy remains precarious in the long-run, as an oil crunch would severely undermine business confidence and the state's fiscal leeway. Saudi Arabia still lacks a viable system of taxation. Private employment generation for Saudis still is insufficient to accommodate the estimated 200,000 new entrants to the labor market per year, as levels of wage inequality are between "cheap" expatriates and more expensive Saudis are high in most sectors.

Output strength

## 12 | Sustainability

Environmental concerns have received more media coverage in recent years than previously, and the Meteorology and Environmental Protection Agency has received an institutional upgrade. State oil giant Aramco has woken up to global environmental challenges and has organized conferences on issues of climate

Environmental policy

change mitigation. Environmental awareness is not deeply anchored in the public and bureaucratic consciousness, however, and the formal obligation of environmental impact assessments for new projects is usually treated in a cavalier manner. Powerful follow-up mechanisms are lacking. All major cities suffer from sewage problems, industrial spills are not uncommon, and the average Saudi household produces large amounts of garbage.

Education expenditure has risen sharply in the course of the recent oil boom, reaching 26% of the national budget and about 6.4% of GDP in 2006. The quality of public education has not necessarily increased at the same rate, however. Teaching still is oriented toward rote learning, and Arabic and Islamic studies have a dominant position in curricula. Teaching reform has been discussed for several years now, but results on the ground are still limited, as teachers' qualification remains an issue. The number of private schools has grown, and recently more than a dozen private universities have been licensed. Access to quality education for the less affluent remains a problem, however. As in other Arab countries, R&D spending in Saudi Arabia is still very low, with Aramco and state heavy industry giant SABIC the only entities engaging in significant research. With the exception of the small University of Petroleum and Minerals, public universities are of low quality. Awareness of all these issues has risen significantly, however.

Education policy  
/ R&D

# Transformation Management

## I. Level of Difficulty

Structural constraints on governance in Saudi Arabia are moderate, as the state has considerable resources, has not seen major epidemics or wars for many decades and is in an advantageous geo-economic position. Saudi Arabia remains thinly populated relative to its size, however, which increases infrastructure costs and makes it difficult to develop peripheral regions and avoid the over-centralization of population and economic activity in its three main city clusters. Moreover, the Saudi state suffers from capacity deficiencies due to its recent emergence, the rentier mentality of many of its employees and its limited regulatory penetration of society. This can make consistent policy implementation difficult.

Structural  
constraints

There were regional traditions of civil society in Saudi Arabia before the onset of large-scale oil income in the 1950s. Since then, the state has taken over many welfare functions and has generally prevented independent social organization. Although there are numerous welfare societies with considerable resources, these still exist in the shadow of the state and are tightly controlled by it. In the aftermath of the terror problem in 2003/2004, religious organizations have also come under increasing control by the state. There are no powerful independent unions, syndicates, or issue groups in the kingdom, leaving Saudi society deeply fragmented. The only social structures most Saudis can rely on are small-scale informal networks of kinship and friendship. Recent government attempts to set up formal interest groups in a top-down fashion have largely failed to gain public participation.

Civil society  
traditions

Regional, tribal – and in some regions, sectarian – identities in Saudi Arabia remain strong, although at the same time a strengthened sense of nationhood has emerged in the aftermath of 9/11. The Iraq war and Saudi-Iranian tensions have heightened the sense among Saudi Sunnis that Shi'ites could act as a fifth column of outside interests, decreasing national cohesion across sects (which had always been very brittle). The overall level of sociocultural integration remains rather low. Nonetheless, the Saudi state and its patronage networks remain strong enough to prevent sub-state identities to challenge it or other communities in an organized fashion. Although there informal discrimination exists, however, violent incidents are very rare.

Conflict intensity

## II. Management Performance

### 14 | Steering Capability

Insofar as political leadership under King Abdullah has expressed a commitment to gradual economic and sociocultural reform, Abdullah's accession to the throne is a clear improvement over the situation under King Fahd. Relative fiscal restraint under the new boom reflects Abdullah's desire to pursue long-term, sustainable economic policy, and his opening of debate about cultural issues reflects a clear commitment to reforming some of the rigidities of patriarchal Saudi society. At the same time, Abdullah's understanding of technical issues remains limited, and he is dependent on his senior advisors, some of whom pursue their own interests. Consistent follow-up on long-term reforms is deficient and policy initiatives sometimes have a knee-jerk quality. Moreover, at age 83, Abdullah could exit the stage any moment, making for a possible rupture in policy-making. His successor Sultan is almost as old as him, and claimants to the throne after Sultan are scarcely younger, which could make for a phase of extended political paralysis and short-term policy-making. Abdullah's 2006 succession law will help to stabilize the family when a new king gets elected, but hardly solves the problem of an over-aged, oligarchic leadership. More fundamentally, no one in the Saudi elite seems committed to substantial political change. Serious popular participation through national elections, public fiscal accountability of the government or freedom of organization remain off-limits.

Prioritization

Saudi Arabia does not have a serious political reform program, and the few steps that have been taken – such as municipal elections or the licensing of specific interest groups – have been inconsistently implemented. The oil boom has further reduced pressure toward political reform. On the economic reform front, Abdullah has rather gained power to push changes through thanks to his status as king. WTO accession in late 2005 has been used to modernize a large number of regulations and start the reform of important parts of the bureaucracy. Change however is easier to effect on the formal-legal level than on the level of bureaucratic implementation, where the atmosphere has changed little since Abdullah's accession. Although some reforms are implemented effectively – such as the creation of a capital markets authority and specific privatizations – others get stuck among bureaucratic infighting and sluggishness.

Implementation

Abdullah is clearly a more consultative ruler than his predecessors, and is more willing to recognize new challenges and discuss change. At the same time, his age, limited education and reliance on advisors prevents him from envisaging any radical change in the political sphere. In other realms, there has been increased political flexibility: The current handling of the oil riches indicates significant learning over the last oil boom, when resources were squandered rapidly. Similarly, willingness to engage in limited cultural opening indicates that the leadership has recognized the political problems arising from Wahhabi religio-cultural rigidities. The large and immobile state apparatus and the complex structure of political clienteles attached to both the state itself and the Al-Saud family limits the pace of any large-scale change however.

Policy learning

## 15 | Resource Efficiency

Resource efficiency in Saudi Arabia has by and large increased since the last oil boom, as administrative capacity and experience in fiscal management have grown. The fiscal balance has tremendously improved during the last two years, although this is as much due to higher oil prices as to good fiscal management. The balance of current and capital spending is also much-improved since 2004. National budgets are regularly overspent by about 15%, which as an informal rule actually tends to guarantee reasonably predictable macro-policies. However, when it comes to specific allocations, budgets remain non-transparent and closing accounts are not published. The Majlis ash-Shura (consultative council) lacks budgetary powers. Moreover, many inefficiencies are deeply embedded in the state apparatus: Abdullah has reined in princely corruption to some degree, but large institutions like the Ministries of Interior and Defense are still unaccountable, as the public comptroller has no effective leverage over them. Many agencies remain overstaffed, and dismissal of surplus personnel is practically impossible. There are more Saudis employed by the state than by the private sector. New appointments are based on reasonably competitive examinations in a considerable share of government institutions, but due to wage stagnation and low career mobility, the public sector has ceased to be a competitive employer for the most talented Saudis. Principles of good governance have not pervaded the bureaucracy. It remains opaque, over-centralized and unaccountable. Inter-ministerial administrative reform committees have not produced any significant policy proposals during the last 20 years. Still, compared to many other oil states, the efficiency of the Saudi state is decent.

Efficient use of assets

Policy coordination at the top of the system has improved since Abdullah's accession. The strong centralization of authority in the system contributes to this. By the same token, however, at the ministerial level and below, redundancies

Policy coordination

and overlapping responsibilities in implementation still exist. Inter-ministerial coordination is strongly deficient, as communication is vertical rather than horizontal. Policies and procedures which involve more than one institution often suffer from inconsistencies. Examples include the incorporation of new joint stock companies, which is handled by both the Ministry of Commerce and the Capital Markets Authority in often inconsistent ways; or the treatment of foreign investors, which often get lost between different bureaucratic “fiefdoms”. Policy areas such as education and health remain fragmented, as large institutions such as the Ministries of Defense and Interior have their own educational and health establishments. In some cases (e.g., labor and water issues), responsibilities have been consolidated, but in others this has not been technically or politically feasible.

Corruption in Saudi Arabia has always been worst at the most senior levels of the government, but long-term observers generally agree that there has been a gradual trickle-down effect during the last 20 years due to slowly rising costs of living and stagnating wages. This being said, administrative corruption is still less widespread than in poorer Arab countries such as Egypt or Syria. Certain government institutions have traditionally been rather free of corruption, such as state oil company Aramco, the Central Bank SAMA or the Royal Commission for Industrial Cities. In Transparency International’s Corruption Perception Index, Saudi Arabia received a middling rank of 70 for 2006, virtually unchanged from 2004 and 2005. There is no real public accountability for bureaucrats, as there are no disclosure rules. The Majlis ash-Shura is reluctant to deal with specific cases of misconduct, while the press is, with some notable exceptions, generally tame. There are intra-bureaucratic integrity mechanisms in Saudi Arabia such as an administrative supervision agency and a disciplinary board for bureaucrats, but these generally lack weight. What is more important is the personality of different ministers, which can have a significant impact on the level of corruption in different institutions – although even a reportedly hard-hitting reformer such as labor minister Ghazi Al-Gosaibi has not been able to clean up the large-scale influence peddling in the labor ministry. Abdullah has curbed princely corruption and has thrown out several corrupt administrators such as the head of the Jeddah airport. He is, however, unable to supervise effectively what his older brothers are doing in their respective ministries. The pending aircraft procurement by the Ministry of Defense will be a test case.

Anti-corruption  
policy

## 16 | Consensus-Building

The most fundamental political consensus in Saudi Arabia pertains to the Al-Saud’s status as ruling family. This is currently questioned only by marginal dissidents who lack an organizational base. Correspondingly, there is no

Consensus on goals

consensus on democratization, which remains alien to many Saudis and a generally ill-understood concept. Similarly, there is no general agreement on steps of political liberalization among the elite. Abdullah has been willing to concede some tokens of political opening, while other senior princes are more skeptical. The kingdom's course could change accordingly with Abdullah's death. While the consensus on market economy and on gradual economic reform is more broad-based among senior princes, technocrats and merchant families, the details remain disputed and vested interests in both bureaucracy and business are strong.

Insofar as there are powerful players that can cast a definite veto against specific reforms, these are found at the senior levels of the royal family. Vetoes can also be cast by 'ulama, merchants or government agencies on specific policies, but in these cases, opposition can be overruled if senior princes deem necessary – although they often shirk back from this due to their cautious policy-making style. The consensual nature of the Saudi decision-making process means that specific reforms can get stalled for long periods.

Anti-democratic veto actors

Abdullah is generally perceived as a reconciler, and previously marginal groups – be it due to geography, religion or gender – generally perceive him as the best hope they have among the senior princes. He has received Shi'ite and women's delegations and in his own paternal way is genuinely concerned about making the Saudi system inclusive. This does not mean that deep social cleavages have disappeared overnight, however. The Al-Saud monarchy is still historically and ideologically tied to a brand of Islam that is exclusivist, patriarchal and has been identified with the supremacy of elites from the Central Najd Province. Senior advisors of the royals still predominantly stem from that region, and inclusion of other groups does not automatically imply equality.

Cleavage / conflict management

There is little "formal" civil society with which the regime can engage in the policy deliberation process, with the notable exception of private sector representatives, which are relatively well-organized through chambers of commerce and industry. Other recently created formal interest groups are still largely excluded from policy deliberation within the bureaucracy. Social interests can however be informally represented through community leaders who engage with princes or, indirectly, through the information-gathering services that the various hangers-on of princes provide. The capacities of these channels to represent the interests of an increasingly complex society are limited, however. Abdullah is open to consultation but organized partners to consult with are not always available in society. The disjointed process of policy-making in the Saudi bureaucracy can also mean that social interests might be taken on board at a certain point of deliberation, while they are ignored later on by different institutional actors.

Civil society participation

Saudi Arabia has not seen major atrocities or acts of violent suppression in its modern history. Due to the hegemony of Wahhabi ideology emerging from the Central Province, it has nevertheless been a socially and culturally very exclusive system. Abdullah has taken significant symbolic steps to bring previously excluded groups (women, Shi'ites, non-Hanbali Sunnis, tribes of poor regions etc.) back into the fold. Higher oil income allows the government to attend to neglected communities, and the general period of soul-searching after the terror phase of 2003/2004 has created space for previously marginalized voices and for criticism of Wahhabi ideology. This does not amount to an official apology, but still means significant decompression of the Saudi public space.

Reconciliation

## 17 | International Cooperation

The Saudi government has always been relatively good at adopting technocratic consultancy input from international organizations, both private and public. This has once again been demonstrated in the course of WTO accession in late 2005, as well as through the management of independent water and power projects and the privatization process of telecommunications. That being said, as the kingdom pays for most consultancy, international actors have limited leverage over implementation of policies and it is in this phase that special interests in the bureaucracy can often stall or alter the course of reform. On political issues, the rather prickly Saudi elite almost uniformly rejects international involvement. This does not mean that pressure behind the scenes never works – it did to some extent when the United States pressured the kingdom on educational and certain social reforms. In general, however, there is a strong sense of Saudi exceptionalism, and attempts to publicly counsel Saudis on political change tend to backfire.

Effective use of support

Throughout its history, Saudi Arabia has pursued a very conservative foreign policy and is considered a reliable partner in international diplomacy and economic cooperation, albeit not in democratic reform. Even in economic change, Saudi Arabia is very conscious of its sovereignty and has been criticized for not fully implementing international obligations, most recently under the WTO, and is very reluctant to subject itself to non-Saudi judicial mechanisms. There is little cooperation with political INGOs, but better cooperation with development bodies such as World Bank, UNDP or IMF. Although it is not always an easy environment to operate in for foreign investors, Saudi institutions are generally perceived as stable, and detrimental changes in basic economic rules do not occur.

Credibility

Saudi Arabia has a vested interest in a calm regional environment, as this allows it to flex its economic muscle. It has hence taken a leadership role in the Arab League and the GCC to work toward economic cooperation and a nuclear weapon free zone in the Gulf. Its relationship with Iran has significantly improved after 1997, and while it does not recognize Israeli statehood, the government is ready to strike informal, pragmatic deals if they benefit the Palestinian cause. That being said, some Saudi institutions also have a track record of supporting extremist ideologies and movements in the Islamic worlds, and the historically anti-Shi'ite bias of important parts of the Saudi establishment make its role as neutral arbiter suspect in cases such as Lebanon or Iraq. Aggressive Iranian foreign policy since 2005 has led to a partial reversal of the bilateral détente, although the relationship has not yet deteriorated to the full-scale enmity witnessed in the 1980s.

Regional cooperation

## Strategic Outlook

Possibilities for substantive political reform remain very limited in the short run, and might become even more so after Abdullah's death. The kingdom does not currently have the social infrastructure for sustaining a peaceful democratic transition and an open contestation of political interests, and the interest in such a development in the elite is very muted. The most serious advocates of political participation are to be found among Islamists, who in the medium-term could emerge as the main partner in a transition toward meaningful participation.

The kingdom is a complex society in which paternal, top-down governance is becoming increasingly difficult. In preparing moves toward a more inclusive political process, meaningful civil society institutions will have to be built first. This means allowing public space for the independent organizations of social interests on the basis of regional, professional and religious affinities. While such groups are likely at first be dominated by Islamists, this does not per se prevent pluralism, as the Islamist spectrum is very wide in Saudi Arabia and covers very different points of view. What is needed is a national infrastructure to aggregate interests that is not based on kinship or patron-client relations.

The more open debate in recent years is a first, but modest step toward making Saudis accept political differences. Electoral politics can be rehearsed through civil society groups, and their gradual inclusion into policy-making processes should make for a more participatory style of politics. To overcome its cleavages, Saudi society needs to get used to the public interplay of different opinions and interests, as well as to political negotiation and compromise as a way of organizing national public life. The organization of political parties will have to be allowed at some stage.

Much of the Saudi political opening will have to be negotiated domestically, and it has to be made clear to the royal family that relinquishing some of their control over day-to-day policy matters does not imply an end to their role as ruling family. Quite to the contrary, disengagement from daily politics can help them to focus on their role as arbiter in crisis situations and as reconciler in case of fundamental disputes. Disengaging from micro-issues will allow them to keep their distance from mundane problems of administrative corruption and mismanagement, which could, in turn, improve their legitimacy. Reducing the role of numerous princes in government will require some tough bargaining within the royal family. Defining clear stages and aims of reform can help to lock in commitments.

External actors can be helpful by publicly accepting that Saudi Arabia has to find its own way toward participative politics, while remaining firm on the basic vision of introducing elements of democracy. States, IGOS and INGOs can help assist with the development of Saudi civil society, but should do so carefully and in reaction to local demands, not on the basis of external ideas of what Saudi society should look like. It needs to be remembered that Saudi Arabia is fiscally autonomous from external players that have little leverage over its domestic political course.

Whereas criticism by other states can backfire and pressure should rather be exerted silently, INGOs can play a more explicitly critical supervisory role regarding human rights and other political issues. Criticism levied by groups like Amnesty International (AI) and Human Rights Watch (HRW) has been discussed in the kingdom and has triggered policy reactions. Even if these discussions are cosmetic, they seem likely to make future problems harder to brush under the carpet. 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 substantive change on the ground.

It will also be important to look at less salient, more structural political and human rights issues. The Western view of legally sanctioned limb amputation as an atrocity is not, for example, something that Saudis themselves are greatly concerned with. Criticism will be most effective if it makes sense within the cultural frame of reference of Saudi society, focusing on large-scale issues – such as political transparency, accountability, and behavior of state representatives – which resonate in Saudi society itself.

International institutions and media should highlight the importance of reformist voices in the kingdom and give them international fora. While there is great interest among the often highly educated and internationally-oriented Saudi intellectuals to communicate with international peers and civil society institutions, but there are as yet too few connections.

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.

The scope for cooperation on the economic level is much wider, as Saudi Arabia has a long track record of cooperation with bilateral committees, international agencies and consultancies. International players can draw on a broad stratum of sophisticated technocrats with Western education, and they

should play on the strong Saudi interest in international benchmarking and “best practices” to support further economic reform. The kingdom should be assisted in particular in building up monitoring and follow-up mechanisms for its economic reforms. Recent moves toward sociocultural reform have also opened more opportunities in cultural and educational cooperation, for which there is great interest in Saudi society.