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## Saudi Arabia: Modern Reform, Enduring Stability

*We are a part of this world and we cannot be disconnected from it. We cannot be mere spectators while the rest of the world is progressing towards a global system.*

*King Abdullah (then Crown Prince), May 2003*

*No to change, yes to development... Whatever exists in the Kingdom is already well-established; however, there is a scope for development – development that does not clash with the principles of the nation."*

*Prince Nayif, Minister of Interior, March 2003*

### Introduction

In the past three and a half years as King of Saudi Arabia, Abdullah bin Abdul Aziz Al Saud had led unprecedented changes in the Kingdom.<sup>1</sup> At 84 years of age, he was active in advancing the country's position internationally and securing its foundation domestically. However, dramatic swings in the price of crude oil presented a major challenge to economic planning. In July of 2008, the price per barrel peaked at \$147 but dropped to \$33 by mid-December of the same year. When coupled with the global financial crisis, this volatility threatened the country's long-term initiatives for infrastructure, education and industry diversification.

King Abdullah also faced political challenges. Despite his position as monarch in an autocratic political system, the king balanced divergent constituents. The clergy, upon whom the royal family depended for social legitimacy, typically opposed social reforms. Domestically, the youth population was exploding. Pressure for expanded employment opportunities and human rights was increasing. Externally, Saudi Arabia strived to be a leader of the Muslim world. The country carefully balanced its support for Palestine, negotiations with Iran, and a strategic relationship with the United States.

The king contemplated future stability in the region, in the state, and for the royal family. Oil would not last forever and a new generation was coming into maturity. How much could he afford to push modernization: politically, socially, and economically? How much would he have to?

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Professor Richard H. K. Vietor and Research Associate Nicole Forrest prepared this case. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

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## History

Historically, the Arabian Peninsula had been an important trade area. The birth of the Prophet Muhammad, however, elevated the importance of Saudi Arabia. Muhammad, the Messenger of God (Allah), became the foundation of the Islamic religion. In A.D. 610, Muhammad began spreading the message of Islam in the town of Mecca in the Kingdom of Saudi Arabia. In 622, Mohammed moved to Medina where he lived until his death eleven years later. In the centuries since, Medina and Mecca have remained the most important holy sites for the 1.3 billion Muslims throughout the world. Each year, ten million people arrive for spiritual pilgrimages – the Hajj and the Umrah.<sup>2</sup>

For over six centuries, Saudi Arabia was ruled by various empires including the Byzantine and the Sassanids. In the sixteenth century, the Ottoman Empire assumed control of Mecca, Medina, and other parts of the Arabian Peninsula. By the eighteenth century, the area of modern-day Saudi Arabia was still largely populated by semi-feudal tribes. Two important men, however, rose in prominence and power: Mohammed bin Saud and Mohammed bin Abdul Wahhab. Ibn Saud ruled the state of Diriyah during the Ottoman's rule. His family was sedentary, lacked nobility, and had little inherent political leverage. "Any form of rule by the Saudis was unthinkable in tribal terms... It was therefore absolutely necessary for the Saudis to find a way of asserting their pre-eminence over the Arabian tribes that broke with the usual tribal syntax."<sup>3</sup> Ibn Abdul Wahhab was the leader of a conservative Islamic movement promoting a return to traditional practices and principles. He influenced a group of other conservative and puritan religious scholars and believers who adhered to a strict interpretation of the Quran, the holy book. The movement promoted monotheism and condemned other religious traditions. This movement was fervently adopted by a large population and formed the foundation for the large Salafi<sup>1</sup> community in Saudi Arabia today.

In 1744, Ibn Saud and Ibn Abdul Wahhab united to create a new state independent of the Ottoman Empire. The two men organized a strong military and a network of conservative Islamic clergy to form a new nation from the fragmented tribes and families of the Arabian Peninsula. By 1818, however, the Ottomans regained control. The Al Saud family fled in exile to Kuwait but continued their fight for an independent nation, ruled by the Al Saud family and committed to Islam. In 1824, the Saudi state was reestablished but collapsed in 1891, due to tribal conflict. The Saud family fled to Kuwait but Abdul Aziz Ibn Abdulrahman Al Saud (Ibn Saud) recaptured Riyadh in 1902. On September 23, 1932, Ibn Saud formally established the modern Kingdom of Saudi Arabia and assumed the role of king. Later, to reinforce the young kingdom's dependence on, and protection of, Islam, King Fahad adopted the official title of "Custodian of the Two Holy Mosques."

## Country Background

### *Governance Structure*

The royal Al Saud family continued to rule Saudi Arabia in 2009. While still Crown Prince, King Abdullah bin Abdulaziz governed the Kingdom for the decade following the incapacitation of the late King Fahd. Abdullah formally became king after Fahd's death on August 1, 2005. Prince Sultan bin Abdul Aziz Al Saud, the king's half brother, then became Crown Prince as well as Defense Minister. The Basic Law dictated that succession must pass to direct descendants, the sons and grandsons, of Ibn Saud. In 2007, King Abdullah introduced Bay'ah law (succession law), the first transparent process for the selection of a successor to the throne. The Bay'ah Council – composed of senior royals who are direct descendants of King Abdulaziz – would elect a successor from three

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<sup>1</sup> Salafi is part of the Sunni movement and views early ancestors as models of Islam.

candidates identified by the current king. Competence, as opposed to seniority, was deemed a primary selection criterion. Measures were also taken to ensure that an incapacitated king would not remain on the throne.

The number of princes in the royal family was estimated to be between 5,000 and 8,000.<sup>4</sup> They held varying levels of power and occasionally divergent and conflicting perspectives. Members of the Al Saud family dominated prominent positions within the public and private sector. Although the king maintained ultimate authority and veto power, a Council of Ministers advised the king and approved legislation. The Council, established in 1953, met weekly and observed term limits of four years. Another important body was the National Consultative (Shura) Council. King Fahd established the council in 1992 as a component of the Basic System of Government. The Shura Council, which has undergone substantial reform in the past decade, was based on the concept of dialogue between scholars and society. In an advisory role, it could propose and draft legislation as well as review and comment on the national budget. Its 150 members expanded from 90 members in 1997 to include broader national representation. Members of council were all appointed. In 2009, over half were recently appointed. Members under the age of forty were represented. The meetings, covered extensively by the media, convened weekly with the king addressing the council formally once a year.

The king had also developed the Forum for National Dialogue as “a strategic measure to channel social pressure and retain control over the content and pace of reforms.”<sup>5</sup> This advisory body engaged a wide variety of constituents including “pro-government spiritual leaders, liberal-Islamist reform advocates, Shi’ites and liberal intellectuals” to discuss “extremist rights and responsibilities for women, education, youth and perceptions of foreigners.”<sup>6</sup> An early achievement of the first annual National Dialogue in 2003 was the promotion of elections for half of the municipal council. Municipal councils managed each of the country’s thirteen provinces. (At the helm, a king-appointed royal governor led each province.) Although members of the Saud family openly questioned the reform, the government sponsored the first elections in 2005. Some supporters of participatory government also criticized the elections: rules included male-only eligibility, a prohibition against revealing candidate affiliation, and tight campaigning restrictions. Critics also pointed out an overall lack of information. Although municipal councils had only regional influence, the races proved to be heavily contested. Hundreds ran for less than a dozen seats in some cities and villages.

### *Islam*

Islam was the only legal religion in Saudi Arabia. “Islam, a word which means the submission of one’s will to that of God,”<sup>7</sup> rested on five pillars: 1) attesting to no god but God, and Muhammad as His Prophet, 2) praying five times daily, 3) fasting during Ramadhan, 4) paying a welfare tax (Zakat) for those in need, and 5) embarking on a pilgrimage (Hajj) to Mecca at least once in a lifetime.

The vast majority of Muslims in the country were members of the Sunni sect. Sunni Muslims believed primarily in the Qur’an and the Sunna, sayings and teachings of the Quran by the Prophet Muhammad which were recorded by his companions. Another sect, the Shiites, also believed in a spiritual successor (Imam) to Muhammad who interpreted Islamic law. Although a minority group within Saudi Arabia representing only 10% of the population, Shiites were heavily settled in nearby Iran, Iraq, Lebanon, and Yemen.

Islam penetrated economic, cultural and political life. Integration of religion and governance could be seen in everyday practices such as the closing of business five times daily for prayer. Islamic Law and Royal Decree formed the backbone of the legal system. Shari’a (“right path”) was the institutionalized Islamic law. In determining justice, the Shari’a courts issued corporal punishment for an expansive list of offences. State-sponsored religious police, the *mutawwa*, enforced

the law. Religious leaders controlled the educational system. The close alignment of religion and government limited freedoms of speech and press. Trade unions and political parties were banned.

Historically, the king interacted with and depended on the official clergy (*ulama*). However, “during the Gulf War, the state-appointed official clergy were supplemented by an empowered popular-level alternative clergy that was vocal and articulate.” As tension grew, some Saudis called for an end to the *ulama*. The push for diverse voices within Islam presented a challenge to the Al-Sauds’ national control.<sup>8</sup>

### *Geography and Demography*

The Arabian Peninsula was primarily flat with some mountainous formations. Over half of Saudi Arabia’s land was desert. The nation was the ninth largest country in the world by territory and the largest country on the peninsula with 829,996 square miles. It bordered Iraq, Kuwait, Qatar, the United Arab Emirates, Yemen, Oman, and the Red Sea. The common language was Arabic. Many spoke English as well. Saudi Arabia had a very youthful population. It was one of the fastest-growing countries with 45% of its population under the age of 14 and 73% under the age of 29. The total population stood at 24.5 million in 2008. Fewer than 75% were Saudis, 25% foreigners.

The population was largely urbanized with 81% of its people living in cities. The capital city of Riyadh, with a population of 4.5 million people, served as the political and administrative center. Jeddah, home to 2.5 million, was the commercial capital. In the Eastern Province, Dammam was the center of the oil industry. This province, with the largest Shi’a community, was heavily populated by groups originating from Iran, Bahrain, and India.

### **Gender and Culture**

Distinct social norms prevailed throughout Saudi Arabia. Men and women frequently wore uniform dress. Males usually wore a *thobe* (a white full-body garment), a *ghuterra* (a red and white head scarf), and an *aqal* (a black ring on the head). Increasingly, however, Western-style clothes had become more popular among men. Females were obliged to wear an *abaya* (a black full-body covering) and a *tarha* or *hijab* (head veil) in public. Both the *mutawwaa* and the public at-large imposed strong pressure on women to wear the *abaya* and *hijab*. Nevertheless, perspectives differed as to whether this concealment represented a form of liberation or repression, a form of religious dedication or familial respect. Saudis traced the origins of the head veil to the Quran’s mandate for women to cover their hair. By contrast, the use of the face veil was seen by many women as a cultural element meant to protect one’s privacy. For some, the veils were seen as “a sign of womanhood... it provides the social comfort of being able to see without being seen.” For others, the attire demonstrated a *traditionalism*, distinct from *tradition*. “An Islamic line of argument was here used to maintain *patriarchal* social values, whereas in fact social and religious practices were here not only distinct but contradictory.” Despite the distinction, both veils were systematically tied to Islam. Nonetheless, many women subverted the norms by discarding the garments when hidden from the religious police.<sup>9</sup>

Some scholars, such as Pascal Ménoret, traced the strains of gender relations to the founding of the Kingdom. “If there is such a thing as paternalism in Saudi Arabia, it is anchored in the strategy of taking power through women... the key to the success of the Saudis was that, in taking the helm, they knew how to break out of their natural family group and traditional region.” Abdelaziz was said to

have married dozens and possibly hundreds of wives, “choosing them from the great Bedouin<sup>2</sup> tribes, the tribal reigning families, the family of the descendants of Abd al-Wahhab, the great sedentary families of Najd or, more prosaically, families of popular stock” to create a strong web of connection and loyalty throughout the peninsula.<sup>10</sup>

Nonetheless, by the 1960s, education began to empower women. Iffat Al Thunayan, King Faisal’s wife, lobbied for girls’ universal access to schooling. By the 1970s, women had developed a louder voice, nationally and internationally. In 1977, a new law permitted women to open private businesses. During that decade,

“when Saudi women took up the pen... they were mainly concerned to challenge the categories in which both the East and the West had confined them; they therefore refused to embody inside the country either social progress or regression, or to represent, in the eyes of the world, some Islamic purity or medieval backwardness of Saudi society. They were not prepared to be the prism through which the whole society was read...”<sup>11</sup>

The opening, however, quickly faded. By the beginning of the 1990s, Saudi Arabia tightened the restrictions on women. “Significantly, it was just when the generation of state-educated women was beginning to rise up the ladder and to take an active part in the economy that the state and society, with the help of recession and political threats, hardened their line.”<sup>12</sup> In the name of Islamic values, gender segregation became the norm. Women were expected to be accompanied in public. A prohibition on women driving was rigidly enforced. The severity of the restrictions was highlighted when a group of women drove through the center of Riyadh in protest of the driving ban. Each woman was arrested, and then lost employment as punishment. Yet, formal and informal exceptions to social rules existed. Women routinely drove outside of the city and on foreign compounds. Some public spaces, such as grocery stores, were integrated. The divorce rate hovered around 30-33%.

“Islamic feminism” – women using the Qur’an to individually determine the appropriateness of gender rules – was becoming popular.<sup>13</sup> In a few select cases, women had risen to the high ranks of their professions and sought to use their position and wealth to progress women’s rights. At the same time, a conservative countercurrent deepened among some women.

Women’s education and employment opportunities continued to improve in 2009. Although most women did not work outside of the home, fifty-eight percent of [domestic] college graduates were women. [Note: More Saudi males than females receive their education abroad.<sup>14</sup>] Male professors taught female students by closed circuit television, but 88% of all working Saudi women were employed in the education sector. A few other professions, such as medicine (a field in which 9% of working Saudi women were employed), were even gender-integrated.<sup>15</sup> Women also found employment in banking and civil service in departments for female-only clients. The Islamic faith granted women property ownership rights. Saudi women held 40% of the nation’s private wealth, 70% of liquid capital, 40% of real estate assets, and 20% of investment funds and portfolios.<sup>16</sup> Although women controlled an estimated 15,000 companies, male representatives were frequently used for activities such as government relations.<sup>17</sup>

## Education, Employment, and Welfare

Saudi Arabia depended on a large foreign population for both highly-skilled and unskilled labor. Expatriates represented over 50% of the workforce.<sup>18</sup> The private sector employed 5.8 million people

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<sup>2</sup> Bedouin are tribal people who typically live in the desert.

in 2007 but only 13% were Saudi nationals.<sup>19</sup> On one end of the spectrum, expatriates dominated low-paying positions. “Saudi Arabians exhibit a low preference for relatively unskilled work, stemming from the legacy of substantial oil wealth and the ready supply of less costly South Asian labour. The developed social welfare system also acts as a disincentive to employment.”<sup>20</sup> Due to its dependence on oil and lack of taxes, Saudi Arabia had frequently been classified as a “rentier state.” Scholar Hazem Beblawi summarized the following characteristics:

“A rentier mentality... dominates social consciousness. Living off ‘unearned income’, the population orients itself toward easy gain rather than productive labour. Legal processes, requiring foreign business to find local partners, buttress such attitudes. Substantial gains accrue to the citizens through serving as the necessary *kafils* (sponsors) of foreign companies, performing no serious work but earning a share of the income.”<sup>21</sup>

In 2008, the nationwide literacy rate was 83%. The maturing youth population (ages 15 to 24) exhibited an especially high literacy rate of 95.9%. Higher education lagged when compared globally. According to the World Economic Forum, 28% of eligible Saudis attended university compared to a 67% average for the most competitive nations. Those students who did graduate from university were still poorly prepared for private sector employment needs. “For every 1000 students, Saudi Arabia produces only nine engineers, while, by comparison, Sweden and Switzerland produce 134 and 62, respectively... produces 39 science graduates per 1000 tertiary students, compared to Sweden and Switzerland, which produce 78 and 52, respectively.” Foreigners represented 80% of engineers, doctors and other scientists. “The highest-paying jobs are offered to expatriate workers.”<sup>22</sup>

To improve competitiveness, the Eighth Five-Year Development Plan (2005-2009) sought to raise university and college standards. The government had more than doubled the number of domestic universities since 2004. The national budget increased educational spending from approximately \$19 billion in 2005 to \$28 billion in 2008.<sup>23</sup> (Exhibits 9 and 10) The country’s strategy was to move directly to a knowledge economy, importing know-how and building domestic education infrastructure. The government focused on enhancing science and technical training in a system long dominated by religious study. Notably, the King Abdullah University of Science and Technology (KAUST) was planned to create an “international, graduate-level research university dedicated to inspiring a new age of scientific achievement in the Kingdom.”<sup>24</sup> The gender-integrated institution near Jeddah had an endowment of \$10 billion. “R&D is a dollar driven undertaking,” said a senior government official. “You get a long way with \$10 billion.”<sup>25</sup> In addition to being one of the best-endowed universities in the world, KAUST had a Singaporean president and attracted trustees from renowned foreign universities such as Princeton and Cornell. Other schools, like Alfaisal University, also formed strategic relationships with Western counterparts such as the Massachusetts Institute of Technology.

In 2008, the Saudi government also emphasized labor reform. Productivity levels were low. Total factor productivity was probably negative in the government sector.<sup>26</sup> According to some estimates, the oil sector employed a workforce twice the necessary size.<sup>27</sup> The labor participation rate was similarly weak. Unemployment estimates varied but appeared to be at least 11% in 2007 (Exhibit 14). A notable difference between labor participation and unemployment rates existed. “Saudi participation in the labor force seems to grow sharply as Saudis enter their thirties.”<sup>28</sup> Thus, the number of household dependents was high – 2.4 times the global average.<sup>29</sup> In direct response to low labor participation and domestic workforce productivity, Saudiization became a hallmark of proposed labor market reform. In order to increase the number of Saudis in the private sector, quotas were instituted. In some sectors, foreigners were limited to 25% of the workforce. In banking, the goal was 40%.

The Kingdom largely ignored the reality of poverty until Riyadh unrest in 2002 catalyzed the then Crown Prince, King Abdullah. Despite the fact that a large portion of the Saudi population enjoyed a lifestyle serviced by drivers and maids, standards of living varied. Income distribution data, however, were not available. A rise in crime, drugs, and vagrant behavior accompanied the idleness of unemployment and poverty. "Also troublesome is the apparent alienation or anomie that many young Saudis feel, made evident in rampages after football games, roaming street thugs after *eid* celebrations, and women being heckled at shopping malls."<sup>30</sup> One senior-level Saudi stated, "84% of the population is below 40 – I worry about the excess baggage that this group brings to the political and cultural regime; we have not prepared a strategy or vision for this 84%."<sup>31</sup>

## External Relations

### *Regional Neighbors*

Together with Bahrain, Kuwait, Oman, Qatar, and the United Arab Emirates, Saudi Arabia formed the Gulf Cooperation Council (GCC). Although the GCC countries differed in cultural norms such as traditional garb, stances on alcohol, and women's rights, travel between them was nonetheless active. They were further united by fundamental faith in Islam as well as their monarchical/sheikhdom political systems. They wielded collective power through their control of over 45 percent of the world's oil reserves and approximately a quarter of the natural gas reserves. In December 2008, they took steps to deepen their economic interdependence by approving a draft for a unified monetary union consisting of a central bank and a single currency. At implementation, citizens of each country would receive improved flexibility in migration and employment. Details regarding the new currency, such as whether it would be pegged to the dollar, had not yet been developed. Rollout was planned for 2010 but many officials doubted the transition would happen so soon. Prior to the currency conversion, the GCC would self-impose other fiscal, monetary, and employment hurdles. Oman was the only GCC country to have opted out.

From inception in 1981, the GCC had ambitions beyond economic enrichment. The organization was "formed ... against the backdrop of the Islamic revolution in Iran and the Iraq-Iran war... to guard against any threat from neighboring states and from Islamic extremism."<sup>32</sup> Saudi Arabia, the most powerful member of the GCC, felt especially vulnerable. In the 1979 Iranian Revolution, opposition overthrew the Shah with little warning. This turmoil was quickly followed by Iraq's invasion of Iran in 1980. Compounding the intensity of the conflicts was the schism between the Sunni and Shiite sects of Islam.

With a global population of 170 million, Shiites were strategically positioned within and around Saudi Arabia. Although the royal family was Sunni along with almost 90 percent of the Kingdom's population, the Shiite minority was heavily settled in the Eastern Province where they composed somewhere between 30% and 50% the population. Shiites composed 15 percent of the population in Qatar, Afghanistan, and Bangladesh; 20 percent of Pakistan; 25 percent of Kuwait; 45 percent of Lebanon; 65 percent of Iraq and Bahrain; and, 90 percent of Iran.<sup>33</sup> The Iranian Revolution ushered in new levels of visibility for the Shiites and galvanized sect loyalty.

According to critics, the United States' post-September 11<sup>th</sup> war in Iraq exacerbated the regional tensions between Sunnis and Shiites. Both groups were responsible for severe violence within Iraq. Saddam Hussein, a Sunni, was replaced by a Shiite government. The war "destroyed Iraq's army, the only force in the Middle East capable of containing Iran."<sup>34</sup> Saudi Arabia worried about the continued mobilization of Shiites and the possibility of domestic Saudi attacks fueled by the Iranian government. Iran's suspected nuclear program further contributed to the uncertainty. In December 2008, Iran attended its first GCC summit as an observer – a small sign of regional normalization.

"Palestine is the mother of all problems."<sup>35</sup> King Abdullah was committed to Middle East peace and was an ardent advocate of a Palestinian state. He attempted to broker agreements between Palestine and Israel. In 2006, Saudi Arabia earmarked \$250 million for reconstruction in Gaza and the West Bank. This contribution came in addition to \$92 million in annual aid to Palestine.<sup>36</sup> When violence erupted between Hamas and the Palestinian Authority less than a year later, the king mediated an agreement between the two groups. Discussions in Mecca led to a national unity government whereby the president of the Palestinian Authority appointed a Hamas leader as prime minister. The fragile arrangement lasted only four months.<sup>37</sup> By the end of December 2008, violence raged once again between Israel and Palestine and threatened regional stability. King Abdullah consistently sided with Palestine saying, "I support every effort that is aimed at strengthening the unity of the Muslim Ummah as well as the unity of Palestinians and their leadership... Muslims should unify their ranks and mobilize their resources for constructive activities."<sup>38</sup> The Saudi government earmarked \$1 billion for further reconstruction of Gaza.

### *The United States*

In 1933, a year after the formation of modern Saudi Arabia, King Ibn Saud granted exclusive rights for oil exploration to an American oil company – Standard Oil Company of California (Socal).<sup>39</sup> In the following years, the United States supported the Kingdom with military expertise and weaponry in exchange for a supply of oil. The Arab-Israel War of 1973, however, strained the US-Saudi relationship. Saudi Arabia aligned with the Arab states while the United States aided Israel. In response, the Kingdom imposed an oil embargo but quickly normalized relations. Both countries recognized their mutual dependence.

King Fahd's accommodation of America during the 1990 Gulf War incited anger among many Islamic fundamentalists within Saudi Arabia. When Iraq invaded Kuwait, the United States stationed 600,000 troops in Saudi Arabia, protecting the country and eventually liberating Kuwait. Following the war, American troops remained in the country.

When the official, state-appointed clergy issued a *fatwa* that justified the presence of U.S. troops in Islamic vocabulary, the popular clergy responded with *fatwas* that condemned the presence of U.S. troops, also grounded in Islamic vocabulary and reasoning... The alternative clergy decried waste and imprudence in government expenditures; it highlighted the absence of a capable military despite massive expenditures on weaponry.<sup>40</sup>

The Kingdom had fostered religious fervor and encouraged the development of "private belief systems... spiritual awakening" as a way to maintain favor during hardship. By the 1990s, a quarter of university students had enrolled in religious institutions. For some, the fervor became "an organized and explicitly political movement."<sup>41</sup> In 1990, conservative Islamists submitted a petition to the King that called for a closer relationship between Islamic law and governance. They also suggested specific social reforms such as income redistribution. In 1992, another group consisting of professors and ulema submitted the Memorandum of Exhortation. This document, instead, called for the decentralization of Islam along with a reduction in military spending and a limit to Westernization. King Fahd quickly and publicly denounced the petition. By 1996, anti-West extremists launched two fatal cars bombings targeting American soldiers.

On September 11, 2001, terrorists hijacked four airplanes in the United States and crashed into the World Trade Center and the Pentagon. The attack, coordinated by Al Qaeda, killed over 3,000 civilians. Al Qaeda leader, Osama bin Laden, as well as fifteen of the nineteen hijackers, were Saudi-born. Although the link between Saudi Arabia and the September 11<sup>th</sup> attack on the United States renewed tensions, both countries remained committed to a strategic partnership and the security it provided.



The interplay between the dynamics of the US-Saudi informal alliance, domestic and external security threats, and the country's Wahhabi religious structures and ideology, has undermined the coherence of policy in all of these areas... Saudi governments find themselves caught in an acute dilemma. Either they pursue policies which are necessary for the country's security, but which compromise their claims to religious legitimacy, or else they avoid compromising their religious claims, but thereby undermine the security of the state.<sup>42</sup>

Half of foreign suicide bombers in Iraq were Saudis. The Kingdom responded to the violence by jailing suspected terrorists. Many were killed in firefights. Saudi police reportedly visited every family with a child who had been to Afghanistan.<sup>43</sup> In some cases, extremist groups like Al Qaeda were "recruiting women, knowing that a conservative mother who has been indoctrinated with an extremist ideology can influence generations, and do it away from the eyes of authorities."<sup>44</sup> However, less than one tenth of the Saudi population supported Al Qaeda. According to a public opinion poll conducted by Terror Free Tomorrow at the end of 2007, 69 percent of Saudis surveyed favored a strong US-Saudi relationship. Forty percent held a favorable opinion of the United States, up from 11 percent in a poll taken a year earlier.<sup>45</sup>

King Abdullah carefully balanced the US-Saudi relationship while continuing to criticize the United States for its position in the Israel-Palestine conflict. Even after Hamas won parliamentary elections in 2006, for example, Saudi Arabia sent subsidies to Palestine but only through the Palestinian Authority since the West had designated Hamas a terrorist organization.<sup>46</sup>

## Oil

Socal, the oil company that solidified the US-Saudi relationship in the 1930's, became Saudi Aramco when it was nationalized by Saudi Arabia between 1973 and 1980.<sup>47</sup> As the national oil company, all shares were owned by the Saudi government. Profit flowed back to the Saudi state through three channels: taxes (an 85% tax after costs, capital expenditures, etc. are deducted), royalties at 12.5% (calculated based on well-head regardless of cost), and dividends. The effective "tax" was 92-93% of profit, leaving sufficient cushion for a retained earnings.<sup>48</sup> The state-owned behemoth was operated and managed as a private company. According to the *Financial Times*, the company was the largest in the world with a valuation of \$781 billion.<sup>49</sup>

Through Saudi Aramco's independent operations and through a series of joint ventures with foreign companies, Saudi Arabia was the largest producer of crude oil in the world. The country's production of 9.7 million barrels per day in 2008 accounted for 13% of the world's daily production and 28% of OPEC<sup>3</sup> production. Saudi Arabia was also a major exporter of crude oil. Saudi Aramco exported 26% more oil than Russia, the next largest exporter.<sup>50</sup> Rich in highly-prized, easily-refined light oil, Saudi Arabia received 90% of its \$230 billion export revenue from petroleum products. Proven oil reserves were 264 billion barrels.<sup>51</sup> At current production rates, the known reserves would last for 75 to 80 years.

The Kingdom's oil supply and capacity placed it in an influential position globally. Its oil reserves accounted for a quarter of the world's known reserves. Within OPEC, it acted as swing producer. Its production vastly outsized the next largest OPEC producer, Iran (3.8 million barrels/day).<sup>52</sup> Countries such as Japan and South Korea depended heavily on Saudi Arabia. Furthermore, the proximity of emerging Asian markets such as China and India made them high margin opportunities. Even though only 15% to 20% of Saudi Arabia's crude oil headed to the United States,

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<sup>3</sup> Organization of the Petroleum Exporting Countries is an organization of thirteen countries.

Saudi Arabia was the second largest exporter to the U.S. with an average of 1.4 to 1.5 million barrels a day in 2008. Major oil expansion and exploration efforts were underway. "The planned capacity increase would allow the Kingdom to replace *all* of Iran's or Venezuela's oil exports in the event of a future emergency."<sup>53</sup> Some of the capital projects were financed through joint venture relationships with foreign companies.

The price of crude oil had fluctuated greatly over the last decade. A wide variety of factors, including supply shocks, demand expectations, and regional instability impacted pricing. During a 1998 crisis, the price sank to \$8 per barrel. By 2001-2002, per barrel price averaged around \$25, rising to \$50 in 2005 and above \$60 in 2007 (**Exhibit 7**). Despite an annual average price of \$94 in 2008, "oil markets have had their sharpest-ever spikes and their steepest drops...all within a few months."<sup>54</sup> After the price per barrel briefly dropped to \$35 near the end of the year, it had settled at \$40 per barrel by mid-February, 2009. In 2008, Saudi Arabia enjoyed an estimated trade surplus of \$192 billion, leaving a current account surplus of \$125 billion. But world oil demand in 2009 was forecasted to decline for the first time since 1983.<sup>55</sup>

According to a Saudi Aramco official, the company planned for fluctuations by basing their budget on lower-than-market oil prices. Most oil was sold through long-term contracts which partially insulated the company and the country from short-term shifts. Further,

"there are indications that the GCC countries as a whole have been more careful this time around with their oil revenues. The spending ratio (i.e. the proportion of additional oil revenue being spent by governments) is now lower than during the boom of the 1970s. The IMF has estimated that governments have on average spent 30 per cent of their extra oil revenue from 2002 to 2005, compared with 75 per cent in the 1970s and early 1980s."<sup>56</sup>

Without an income tax, Saudi Arabia needed a price between \$49 and \$55 dollars per barrel to support the country.<sup>57</sup> The true value of oil to the Kingdom incorporates both short-term budgetary considerations and long-term opportunity costs. "Consider the real cost of oil. We have a limited supply. First of all, we need it. We need it to earn money as we go forward. If we overuse it, it is to our detriment. So, we should look a margin cost and discounted future cost."<sup>58</sup> Although Saudi Arabia had been an advocate for moderation of price spikes within OPEC, King Abdullah had said that \$75 per barrel was a "fair price." And, in the words of a Saudi national, "we could be like Iraq if something happened to the royal family."<sup>59</sup>

## Economic Reform

For much of Saudi Arabia's early history, only a skeleton of an economic system existed. In the first two decades after the establishment of the modern state, only the Ministries of Finance, Interior, and Foreign Affairs existed. The development of the oil export industry in the late 1940s, however, spurred the creation of new economic administration. Most notably, the Saudi Arabian Monetary Agency (SAMA) was founded in 1952. During the 1950s, the private sector grew as well. Although largely driven by enterprises directly servicing the oil industry, import companies fueled by oil income also proliferated. Still, political relationships drove much of the development and government spending outpaced revenue. The royal family dominated economic activity and enhanced their own personal wealth. In 1958, the royal family was forced to seek assistance from the International Monetary Fund.<sup>60</sup>

The 1960's ushered in the first wave of economic planning in the country. In 1965, the Central Planning Organization was established. By 1970, the First Development Plan was introduced. In the meantime, the Kingdom invested heavily in oil production which led to expanded capacity in the

1970's. The benefits of proactive planning were augmented by a rise in oil prices during the 1973-74 and 1979-80 periods. Saudi Arabia used the boost in revenue to embark on major economic and infrastructure projects. The country diversified its petrochemical products as well as built schools, improved health services, and paved roads. The boom of the 1970s and early 1980s also buoyed the private sector. Government spending produced new opportunities for private enterprise. Capitalizing on state prosperity and low-cost loans, independent businesses built the construction industry and expanded the importation of goods.<sup>61</sup>

Government expenditures rose with the increase in government revenue. When oil revenue dropped in 1982, Saudi Arabia resisted immediate cuts in its ambitious and expensive programs. But, by the mid-1980s, the country was in full recession. Infrastructure spending was cut and the nation's physical resources suffered greatly. Unemployment rose; poverty worsened. The balance of payments was in deficit. The 1991 Gulf War exacerbated economic and social turmoil since most of the monetary burden fell on the Kingdom. As the economic slump persisted throughout the 1990s, Saudi Arabia became more outward oriented. First, the government incurred deficits financed by tapping reserves saved abroad and loans from internal and international market. Second, the dependence on foreign labor deepened. The government began to turn to the private sector for national investment.<sup>62</sup> Despite oil revenues, the economy grew at only 1.8% per year.

At the turn of the century, Saudi Arabia began to regain control of the national economy. The evolution of the economic system seemed a matter of survival. The government renewed its 1970's-style planning and initiated a new round of large-scale development projects. This time, however, the Kingdom could not depend only on an oil windfall. It turned to the private sector and foreign direct investment. As early as 1993, Saudi Arabia had initiated the process of joining the World Trade Organization (WTO) but only became a member in 2005. "Saudi Arabia needed to carry through substantial economic reforms in order to comply with the requirements of the WTO, but the government's interest in WTO membership was also an outcome of the its [sic] acceptance that reform was necessary."<sup>63</sup>

The market liberalization measures focused on privatization, foreign direct investment, trade liberalization and diversification. As a consequence of WTO engagement and the need for private capital, opportunities for private sector involvement grew. Between 2001 and 2007, the private sector grew at an average annual growth rate of 6.2%.<sup>64</sup> Between 2004 and 2008, the number of investors in the Saudi stock market increased from 300,000 to 10 million.<sup>65</sup> (See Exhibits 3 and 4) The Ministry of Telecommunications was a prime example of the government appetite for and execution of privatization. Telecom operations at the ministry were first put into a separate corporation, fully owned by the government. After two years of "corporatization," 30% of the company was floated to the public. An independent commission was appointed to regulate the industry and introduce competition. Two additional telecom licenses were awarded. Three new fixed telephone line companies, one large fiber optic provider, and twenty internet companies appeared. The price of all telecom services declined and quality improved. The original Saudi Telecom Company was profitable and even bought interests in two foreign telecom companies.<sup>66</sup> Similarly, the insurance industry restructured as have others. Despite the growth in the private enterprise, private sector contribution to GDP declined from 40% to 28% between 2001 and 2007.<sup>67</sup>

An upswing in oil prices in 2003 converted a budget deficit of \$5.6 billion 2002 into a budget surplus of \$28 billion in 2004 and \$157 in 2008.<sup>68</sup> (See Exhibit 6: note difference in currency) In 2007, the government represented 54% of economic investment but the country's infrastructure and development needs required an infusion of foreign capital.<sup>69</sup> The promotion of foreign direct investment necessitated the development of "more explicit legal frameworks and condition."<sup>70</sup> The central bank, the Saudi Arabian Monetary Authority (SAMA), also gained increased independence

during this time.<sup>71</sup> In 1999, the Supreme Economic Council was formed to provide oversight of economic, industrial, agricultural, and employment policies and to accommodate the opening of markets to overseas investment. In 2000, the Saudi Arabia General Investment Authority (SAGIA) was created to promote FDI. That same year, a real estate law as well as a foreign direct investment law, permitting wholly, foreign-owned companies, were introduced. In 2003, a Capital Markets Law established the stock market. The following year, the Capital Markets Authority formed to regulate the stock exchange.<sup>72</sup> Legislation aimed at improving intellectual property rights had also been introduced. The domestic banking industry was largely globalized. Giant petrochemical facilities were built by joint ventures with companies through companies such as ExxonMobil, Chevron, and Shell. Significant FDI had also been made in hydrocarbons.<sup>73</sup> Total FDI was approximately 5-6% in 2007; the national goal was 9-11%.<sup>74</sup>

Saudi Arabia sought to diversify into businesses that were both value-add and energy-dependent. In addition to capital projects mining minerals in the western region and gas exploration in the "Empty Quarter,"<sup>74</sup> SAGIA spearheaded the creation of four new economic cities. Each city was to provide "diversification within boundaries of our core competencies."<sup>75</sup> The government sought \$500 billion from private sources, of which approximately \$150 billion was expected to come from abroad. The ambitious projects were projected to create over one million jobs and increase GDP by \$150 billion by the year 2020.<sup>76</sup> King Abdullah Economic City, north of Jeddah, was to accommodate a major petrochemical complex operated by Saudi Aramco. Prince Abdulaziz Bin Mousaed Economic City, near the northern city of Hail in close proximity to Iraq and Jordan, was to center around an agricultural processing center as well as a dry port and logistics center. The Jazan Economic City on the southwestern coast near Yemen was slated for a sea port and desalination operation. Finally, the Economic Knowledge City in Medina would house a science and technology cluster and an Islamic studies center. These four clusters were seen as an extension of the knowledge-society strategy that included massive educational reform.

The king, free of formal legislative constraints, enabled economic initiatives to be implemented rapidly. The National Competitiveness Center, supported by SAGIA, drove growth in innovation and market sophistication. (**Exhibit 16**) In 2008, the World Bank ranked Saudi Arabia sixteenth out of 181 economies on the "Ease of Doing Business".<sup>77</sup> Aided by the boom in oil prices, the transportation and communications sector grew by over 10% per year between 2004 and 2007; construction grew at 7.1%.<sup>78</sup> Real GDP growth in 2007 was 3.5%; nominal GDP growth was 7.1%.<sup>79</sup> In 2008, nominal GDP was expected to rise by 38.3%. This equated to an economic increase of \$145 billion when compared to the previous year. "\$145 billion is the same size as the economies of Pakistan and the Philippines."<sup>80</sup> Actual real GDP growth in 2008 was 4.2% compares to 3.4% the previous year; nominal GDP for 2008 grew 22% compared to 9.4% in 2007.<sup>81</sup> Per capita GDP regained ground towards the end of the period despite robust population growth. "Since the heyday of the oil boom, per capita income has plummeted by two-thirds, from about \$18,800 in 1981 to \$6,700 in 1995."<sup>82</sup> By 2002, it had risen to \$8,700 and to over \$18,680 by 2008.<sup>83</sup>

Despite unprecedented levels of spending, Saudi Arabia witnessed a record surplus in 2008. Although the public surplus was already projected to be \$10.7 billion, actual numbers exceeds this estimate.<sup>84</sup> The number was recorded to be 234% greater than the 2007 surplus and "double the previous record high recorded in 2006 (though the surpluses of 1973 and 1974 were larger as a percent of GDP)."<sup>85</sup> The Saudi government used the funds to 1) reduce debt (from 19% of GDP in 2007 to 13.5% of GDP in 2008), and 2) build foreign assets at SAMA.<sup>86</sup> In 2008, defense, education,

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<sup>4</sup> The Empty Quarter lies southeast of the plateau and is also known as Rub Al Khali.

and healthcare comprised the bulk of fiscal expenditures. (See Exhibit 9) Much-needed physical and social infrastructure was created and renewed.

Eighty-five percent of revenue was expected to be from oil in the 2009 budget<sup>87</sup>; “for the decade to 2004, we estimate that the oil price assumption used in the budget averaged just over \$16 per barrel, around one-third of the 2008 level.”<sup>88</sup> Oil aside, problems persisted. Saudi Arabia remained relatively uncompetitive for trade in goods unrelated to the energy sector. Inflation, particularly in food prices, was a major threat. Between 2002 and 2005, inflation rose from 0.2% to just under 1%. In anticipation of growing inflation, the Saudi government released a 17-point plan to increase public sector salaries, construct public housing, provide miscellaneous other subsidies, and encourage greater enterprise competition. Still, by the end of 2008, oil and commodity prices had driven inflation to 9.2%, double the previous year.<sup>89</sup>

## Social Pressure

“We are proud Arab Muslims.... We like to modernize but not necessarily Westernize, and we are different,” said Prince Bander Bin Sultan, former Saudi ambassador to the United States.<sup>90</sup> The September 11<sup>th</sup> attack agitated cultural and religious frictions that had been brewing for the last ten years. The international community pushed the royal family to take action. “The House of Saud has reached a watershed... when it transpired that most of the criminals of 9/11 were Saudi nationals, the Saudi family realized it was time for a showdown...”<sup>91</sup> Some Muslims believed in a so-called sixth pillar – jihad or “struggle.” Although some interpreted it to be a quest for spiritual perfection, extremists used it as a call for a fight against all non-Islamic faiths. After terrorist attacks on domestic Saudi soil, the king also had to contend with the possibility that some extremist groups such as the Taliban – a radical group of Sunni Muslims based in Afghanistan – had a political objective of overthrowing the Saudi government. According to one theory, the Taliban wanted to move from Afghanistan to Saudi Arabia in order to 1) control the spiritual heart of Islam and therefore garner religious control of the Muslim world, and 2) control a “strategic commodity the entire world depends on. It is oil... capable of controlling an important life vein in the modern world.”<sup>92</sup> Nonetheless, the Kingdom’s counter-terrorism effort was seen as widely effective.

In 2009, the king also faced the agendas of peaceful, but divergent, Islamic groups. The increasingly vocal call for conservatism had led the monarch to yield substantial power to the *mutawwa*. This had led to tightening of restrictions on women and other civil liberties. “The panicked response of the regime [to the Iranian Revolution] produced two decades of political paralysis... executing the rebels... instituting ever-tighter control over social and political life.”<sup>93</sup> Still, conservatives continued to seek even stricter enforcement of Islamic and cultural principles.

Moderate-liberal Islamic groups, by contrast, advocated political freedom as well as human rights and women rights. This constituency frequently believed in the possibility of Islamic principles coexisting with constitutional rights. In a public opinion poll, 80% of Saudi respondents questioned stated that a free press and free elections were among the most important issues for the country. Over 40% identified women’s right to drive as a top priority. Almost 90% said terrorism was a major problem.<sup>94</sup> Subtle changes, often de facto and not officially mandated, appeared. Gender integration in the workforce increased. By 2001, women were allowed to hold individual (rather than family) identity cards that included pictures of their unveiled face. In 2008, for the first time since a ban was introduced in the 1980’s, there was a public screening of a movie.<sup>95</sup> Yet, the conflicting pressures made Saudi Arabia “a land of two steps forward, one step back.”<sup>96</sup>

## Looking Forward

“An investor’s primary concern is to manage risk and return; all other factors are secondary.”<sup>97</sup> How much of a risk was the internal cultural conflict? Could attitudes towards education and innovation be changed without addressing social and religious tensions? What were the risks?

The precipitous drop in oil prices and other commodities at the end of 2008 reminded the king of what was at risk. OPEC had responded with a reduction in supply of 3.7 million barrels per day. The global financial crisis impacted Saudi Arabia beyond the decline in oil revenue. Collectively, the GCC countries held almost \$2 trillion in foreign assets.<sup>98</sup> A majority of these assets were managed by central banks and sovereign wealth funds. While these vehicles were free of mark-to-market pressures and could hold assets until maturity, their investment composition was likely weighted towards riskier instruments.<sup>99</sup> Some sources, however, claim that Saudi Arabia was distinct among Middle Eastern countries and held mostly Treasury bills. Stock market losses as a result of the global crisis were estimated to be \$254 billion in Saudi Arabia alone.<sup>100</sup> Stock-picking had become a national pastime and many lost significant wealth in the decline. In response, the SAMA aimed to buy declining stock, reduce reserve requirement to ease liquidity, and cut the repurchase rate to maintain parity to the U.S. dollar.<sup>101</sup>

A retraction of foreign direct investment was feared. There was a constricting of international credit facilities to finance megaprojects so the government stepped in and offered financing from the sovereign wealth fund and reduced central bank reserve requirements from 13% to 7% to allow banks to lend more to local companies.<sup>102</sup> Some capital projects were eliminated or postponed but the government did not plan to reduce expenditures. To the contrary, budgeted spending was expected to increase by 16% in 2009. The budget anticipated a deficit for the first time since 2002. The deficit would be a record level in absolute terms, although only 3.5% of forecasted GDP.<sup>103</sup> A sensitivity analysis showed that oil prices could dip to \$40 barrel per day at a 8 million barrel production level and still only incur a deficit equal to 10% of GDP. “This would not pose a particularly arduous challenge for the government to finance, given the strength of its underlying financial position, with public debt, for example, now reduced to below 20% of GDP, compared with over 100% at the turn of the millennium.”<sup>104</sup>

Saudi Arabia showed continued strength in the global Initial Public Offering (IPO) market. Despite the global decline in activity, Saudi Arabia represented 23% (\$3 billion) of global capital raised in the third quarter of 2008 and was second only to China in market share. Saudi Arabian Mining Company represented the largest IPO in the world for the period.<sup>105</sup>

Some scholars attributed the Kingdom’s comparative economic strength to the conservatism of Islamic law. “Speculation, one of the causes of excessive volatility in the equity market, is not permitted... credit is primarily supplied for purposes of buying goods and services which the seller owns and possesses and the buyer takes delivery... The principle of assets-backed transactions implied that each financial transaction is tied to a tangible identifiable underlying asset.”<sup>106</sup>

What would happen if oil prices experienced a collapse similar to that of 1982? Would a global commitment to sustainable energy sources drive demand down further? Would private investors, domestic and foreign, have the appetite to propel the major capital projects to completion? How could the government control inflation? “The curse of oil is real – it doesn’t create jobs.”<sup>107</sup>

Unresolved economic questions were compounded by intensifying regional violence, a restless and ill-prepared youth population, and friction among religious and social groups. Saudi Arabia’s brief, 77-year, modern history had brought significant social and economic changes but had also been marked by remarkable stability. In the words of one female activist, “do I think there are a hundred

things that need to change? Yes. But, this country has also changed massively. Just in the last ten years. Look, I am a leader in my profession.”<sup>108</sup> In 2009, King Abdullah created a Supreme Court and appointed the first women to a senior government position. Ninety-five percent of the population held a favorable opinion of him;<sup>109</sup> “it has been a long time since a king has been so loved.”<sup>110</sup> Now, he needed to use the good favor judiciously to ensure the future of Saudi Arabia.

**Exhibit 1** Saudi Arabia Map

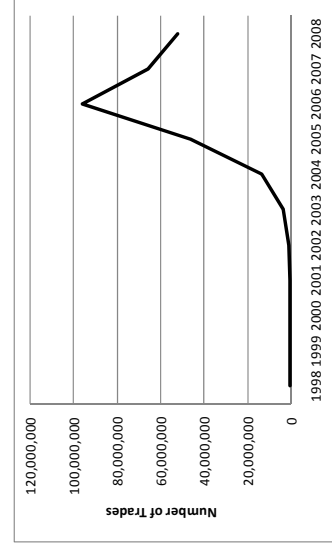


Source: Courtesy of the University of Texas Libraries, The University of Texas at Austin. [http://www.lib.utexas.edu/maps/cia08/saudi\\_arabia\\_sm\\_2008.gif](http://www.lib.utexas.edu/maps/cia08/saudi_arabia_sm_2008.gif), accessed January 2009.

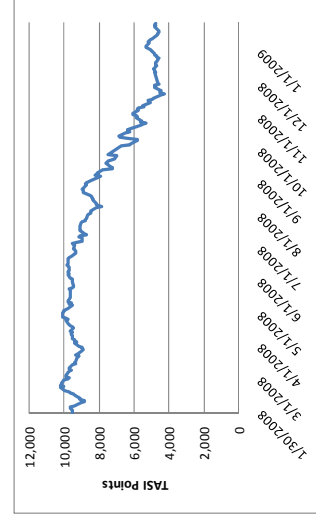
**Exhibit 2** Economic Indicators, 1998-2008

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Nominal GDP (SR billion)	546.6	603.6	706.7	686.3	707.0	804.7	938.8	1,182.5	1,335.6	1,430.6	1,544.1
Private consumption (% of GDP)	46	42	37	38	37	34	30	26	27	28	30
Government consumption (% of GDP)	28	26	26	27	26	25	24	22	23	23	23
Gross fixed investment (% of GDP)	21	20	17	18	18	18	17	17	17	20	21
Stockbuilding (% of GDP)	2	2	1	1	2	1	3	2	2	2	2
Exports of G&S (% of GDP)	30	35	44	40	41	46	53	61	63	66	71
Imports of G&S (% of GDP)	27	23	25	24	24	24	26	28	32	38	46
Domestic demand (% of GDP)	97	88	81	84	83	78	73	67	69	73	75
Real GDP (SR billion)	608.1	603.6	633	636.4	637.2	686	722.1	762.1	786.4	813	861.8
Real GDP PPP (2005 US dollars)	391.7	388.8	407.7	410	410.5	441.9	465.2	491	506.6	523.7	555.1
GDP per capita (\$ at PPP)	17,473	16,928	17,606	17,596	17,399	18,549	19,484	21,237	22,082	22,830	24,390
Real GDP growth rate	2.80	-0.75	4.87	0.55	0.13	7.66	5.27	5.54	3.17	3.40	6.00
Exchange Rate (av SR:US\$)	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Stock of M1 (SR billion)	140.41	156.82	165.71	179.70	202.57	223.22	263.94	284.57	312.94	384.11	480.14
M1 Growth Rate	-0.62	11.69	5.67	8.44	12.73	10.19	18.24	7.82	9.97	22.74	25.00
Consumer prices (% change pa; av)	-0.30	-1.28	-1.10	-1.11	0.21	0.60	0.36	0.62	2.30	4.12	9.40
3-Month Saudi riyal deposit rate	6.21	6.14	6.67	3.92	2.23	1.63	1.73	3.75	5.02	4.80	2.70
Labour productivity growth (%)			2.70	-0.90	-0.20	9.20	15.10	-6.50	-0.10	0.50	3.10
Total factor productivity growth (%)			3.50	-0.50	-0.20	8.10	10.30	-3.50	0.00	0.10	2.50

Source: Adapted from EIU, <http://secure.alacra.com.ezp-prod1.hul.harvard.edu/cgi-bin/alacraswitchISAPI.dll>, accessed January 2009. Numbers in Italics are estimates.

**Exhibit 3** Stock Market: Transaction Volume, 1998-2008

Source: Tadawul, [http://www.tadawul.com.sa/Resources/Reports/Yearly\\_en.html](http://www.tadawul.com.sa/Resources/Reports/Yearly_en.html), accessed January 2009.

**Exhibit 4** Stock Market: Tadawul All Shares Index Value, Jan 2008-Jan 2009

Source: Compiled from Tadawul, [http://www.tadawul.com.sa/wps/portal/tut/p/\\_s.7\\_0\\_A/7\\_0\\_491/.cmd/ChangeLang.uege./!/en/](http://www.tadawul.com.sa/wps/portal/tut/p/_s.7_0_A/7_0_491/.cmd/ChangeLang.uege./!/en/), accessed January 2009.



## Exhibit 5 Balance of Payments

(US\$ million)	2001	2002	2003	2004	2005	2006	2007
Balance of Payments							
<b>Current Account</b>							
Goods: Exports f.o.b.	9,353	11,873	28,048	51,926	90,060	99,066	95,080
Goods: Imports f.o.b.	67,973	72,464	93,244	125,998	180,712	211,305	234,145
Goods Balance	-28,607	-29,624	-33,868	-41,050	-54,595	-63,914	-82,597
Services: Credit	39,366	42,840	59,376	84,948	126,117	147,391	151,548
Services: Debit	5,008	5,177	5,713	5,852	6,677	7,297	7,901
Balance on Goods & Services	-7,155	-7,152	-7,936	-11,057	-14,520	-19,390	-30,798
Income: Credit	37,219	40,865	57,153	79,743	118,274	135,298	128,651
Income: Debit	4,125	3,714	2,977	4,278	4,964	10,376	15,014
Balance on Goods, Services & Inc.	-4,644	-3,925	-4,277	-3,800	-4,963	-9,734	-14,776
Current Transfers: Credit	36,700	40,654	55,853	80,221	118,275	135,940	128,889
Current Transfers: Debit	—	—	—	—	—	—	—
<b>Financial Account</b>							
Oil & other Capital Transactions*	-27,346	-28,782	-27,804	-28,293	-28,215	-36,874	-33,808
Net Portfolio Investment	-11,262	-9,137	-26,440	-47,428	-90,525	-98,172	-88,912
Other Investment Assets	20	-614	-587	-334	464	660	-8,069
Banks	-2,797	7,552	-18,738	-26,654	-67,420	-78,567	-81,727
Other Sectors	-7,197	-11,644	-6,333	-21,955	-28,717	-17,664	-11,391
Other Investment Liabilities	490	1,033	3,842	-3,124	365	-9,203	-10,411
Banks	-7,687	-12,677	-10,175	-18,831	-29,083	-8,461	-980
Other Sectors	-1,288	-4,431	783	1,516	5,149	-2,601	12,275
Net Errors and Omissions	-1,288	-4,431	-783	1,516	5,149	-2,601	12,275
Change in Reserves	1,909	-2,736	-1,608	-4,498	465	-894	-6,168

Source: Adapted from IMF, International Financial Statistics, <http://www.imfstatistics.org.ezp-prod1.hul.harvard.edu/imf/>, accessed March 3, 2009.

\*Category Heading from Saudi Arabia Monetary Agency, 44th Annual Report, p. 332, [http://www.sama.gov.sa/sites/SAMAEN/ReportsStatistics/ReportsStatisticsLib/5600\\_R\\_Annual\\_En\\_44\\_2008\\_09\\_23.pdf](http://www.sama.gov.sa/sites/SAMAEN/ReportsStatistics/ReportsStatisticsLib/5600_R_Annual_En_44_2008_09_23.pdf), accessed March 3, 2009.

## Exhibit 5a Saudi Arabia's Foreign Direct Investment, 2001-2007 - millions of US Dollars

	2001	2002	2003	2004	2005	2006	2007
<b>1990-2000 Average</b>							
Inward	245	504	778	1,942	12,097	18,293	24,318
Outward	243	612	83	78	53	1,257	13,139

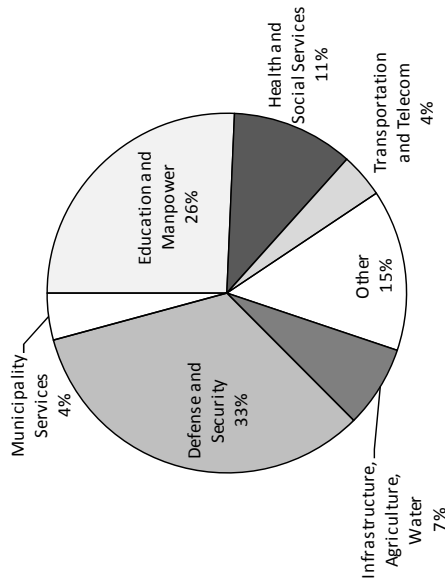
Source: Compiled using data from World Investment Report 2005, United Nations Conference on Trade and Development, [http://www.unctad.org/en/docs/wir2005\\_en.pdf](http://www.unctad.org/en/docs/wir2005_en.pdf), accessed March 5, 2009, and World Investment Report 2009, United Nations Conference on Trade and Development, [http://www.unctad.org/en/docs/wir2008\\_en.pdf](http://www.unctad.org/en/docs/wir2008_en.pdf), accessed March 5, 2009.

**Exhibit 6 Fiscal Budget**

(in SR billions)	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009 (Budget)
Revenues	142	148	258	228	213	293	392	564	674	643	1,100	410
Oil	80.0	104.4	214.4	183.9	166.1	231.0	330.0	504.5	604.5	562.2	950e	n/a
Other	61.6	43.0	43.6	44.2	46.9	62.0	62.3	59.8	34.5	80.6	150e	n/a
Expenditures	190	184	235	255	234	257	285	346	393	466	510	475
Current	171	167	217	224	204	224	248	284	322	347	n/a	250
Capital	19	17	18	32	30	34	38	62	71	119	n/a	225
Deficit/Surplus	(48)	(37)	23	(27)	(21)	36	107	218	281	177	590	(65)

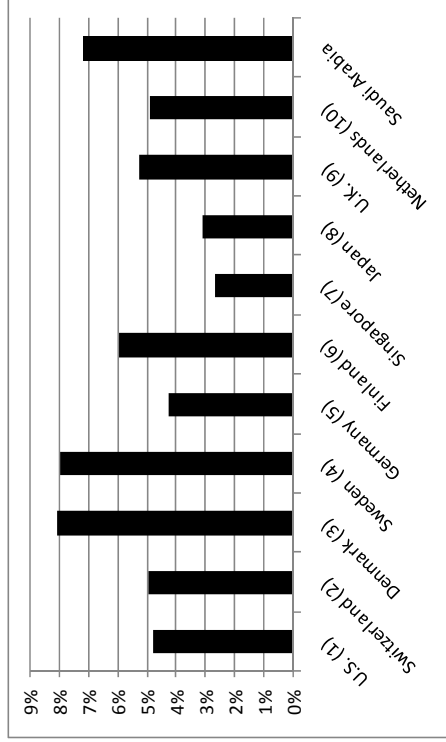
Source: Adapted from SAMA 44th Report, p. 305. References: Ministry of Finance. 2008 estimates and 2009 national budget numbers from Jadwa Investment, 23 Dec 2008. 2008 oil revenue is estimated at 85-90% of total revenue.

**Exhibit 7 Projected National Expenditures, FY 2009**



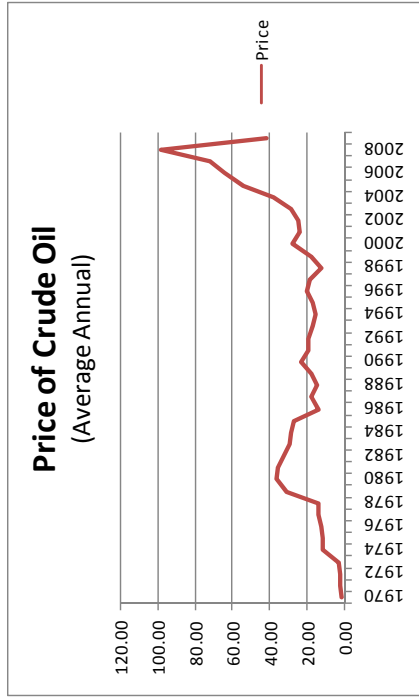
Source: Compiled from "Saudi Arabia's 2009 Budget," Jadwa Investment, 23 December 2008, pp. 2-3.

**Exhibit 8 Comparison of Education Spending as % of GNI, WEF Top 10**



Source: Adapted from "The Competitiveness Review: January 2008: The Education Sector in Saudi Arabia," The National Competitiveness Center/SAGIA, p.26. References: Global Competitiveness Report 2007-2008, World Economic Forum.

**Exhibit 9** Average Price of Crude Oil, 2007-January 2009



Source: Adapted from BP website, <http://www.bp.com/sectiongenericarticle.do?categoryId=9023773&contentId=7044469>, accessed January 2009. Number for 2009 is January only.

**Exhibit 10** Annual Energy Production, 2003-2007

	2003	2004	2005	2006	2007	2008
<b>Crude Oil (1,000 b/d)</b>	8,410	8,897	9,353	9,207	8,816	9,370
<b>Natural Gas (mn cu m)</b>	67,920	76,460	81,350	85,001	83,280	
<b>Refined Products (1,000 b/d)</b>	1,761	1,913	1,974	1,960	1,874	

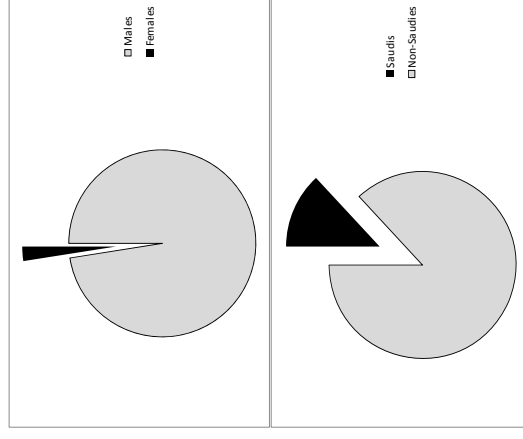
Source: "Annual Statistical Bulletin: 2007," Organization of the Petroleum Exporting Countries, pp. 58, 63, 76.

**Exhibit 11** Workforce by Age, 2007

Age	Workforce (% of Total Population)	Unemployment (% within Workforce)
15-19	1	34.3
20-24	8.7	29
25-29	18.4	10.5
30-34	21	2.8
35-39	17.8	0.4
40-44	13.5	0.7
45-49	9	0.4
50-54	5.3	0.2
55-59	2.8	0.4
60-64	1.2	0
65+	1.3	0

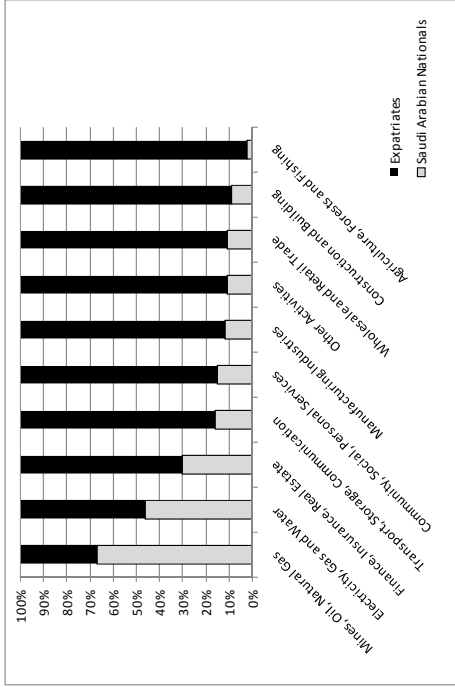
Source: Adapted from SAMA 44<sup>th</sup> Report, p.231. References: Central Department of Statistics and Information, Ministry of Economy and Planning.

**Exhibit 12** Private Sector Workforce by Sex and Nationality, 2007



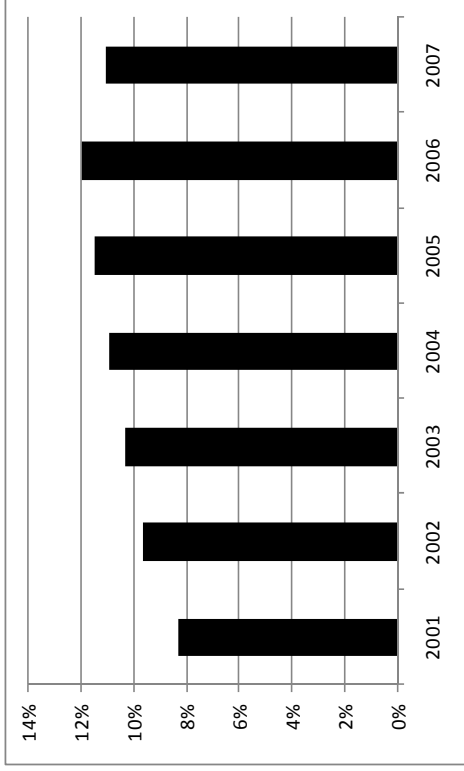
Source: Adapted from SAMA 44<sup>th</sup> Report, p.233.

**Exhibit 13** Saudi Arabian National vs. Expatriate Participation by Sector



Source: Adapted from "The Competitiveness Review: January 2008: The Education Sector in Saudi Arabia." The National Competitiveness Center/SAGIA, p. 36. References: Saudi Arabian Monetary Agency and Central Department of Statistics.

**Exhibit 14** Unemployment among Saudi Arabian Nationals



Source: Adapted from SAMA 44<sup>th</sup> Report, p.242.

Exhibit 15 "Ease of Doing Business" Ranking, 2008

Ease of Doing Business		16 <sup>a</sup>						
<b>Starting a Business</b>	28	Procedures (#)	7	<b>Protecting Investors</b>	24	Disclosure Index	8	
		Duration (days)	12				Director Liability Index	8
		Cost (% GNI per capita)	15				Shareholder Suits Index	3
		Paid in Min. Capital (% GNI per capita)	0				Investor Protection Index	6.3
<b>Dealing with Construction Permits</b>	50	Procedures (#)	18	<b>Enforcing Contracts</b>	137	Procedures (#)	44	
		Duration (days)	125				Duration (days)	635
		Cost (% of income per capita)	75				Cost (% of claim)	28
<b>Registering Property</b>	1	Procedures (#)	2	<b>Closing a Business</b>	57	Time (years)	1.5	
		Duration (days)	2				Cost (% of estate)	22
		Cost (% of property value)	0				Recovery rate (cents on the dollar)	38
<b>Paying Taxes</b>	7	Payments (#)	14	<b>Trading Across Borders</b>	16	Documents for export (#)	5	
		Time (hours)	79				Time for export (days)	17
		Profit tax (%)	2				Cost to export (US\$ per container)	681
		Labor tax and contributions (%)	12				Documents for import (#)	5
		Other taxes (%)	0				Time for import (days)	18
	Total tax rate (% profit)	15			Cost to import (US\$ per container)	678		
<b>Employing Workers</b>	45	Difficulty of Hiring Index	0	<b>Getting Credit</b>	59	Legal Rights Index	4	
		Rigidity of Hours Index	40				Credit Information Index	6
		Difficulty of Firing Index	0				Public registry coverage (% adults)	0
		Rigidity of Employment Index	13				Private bureau coverage (% adults)	14
		Firing costs (weeks of salary)	80					

Source: Compiled from "Doing Business 2009: Country profile for Saudi Arabia," The World Bank, 2008.

a Rank out of 181 countries.

Exhibit 16 Global Rankings

Ranking Agency	Focus	Countries Covered	Rank	Year
World Bank/ International Finance Corporation (IFC)	Environment for doing business	181	16	2008
World Economic Forum (WEF)	Overall competitiveness	134	27	2008
UNCTAD	Total FDI inflow	188	18	2008
	FDI performance relative to potential		51	2008
Milken Institute	Company access to capital	122	36	2007
	Corporate transparency	48	43	2008
Heritage Foundation	Degree of government economic interference	162	60	2008
Transparency International	Perceived levels of corruption	180	79	2007

Source: Adapted from: "The Competitiveness Review, January 2009: An Update on Saudi Arabia's 10x10 Program." The National Competitiveness Center/SAGIA. p.19, <http://www.saudincc.org.sa/CMSPages/GetFile.aspx?guid=fc3b89fe-b893-4a74-8749-d4b04114d398>, accessed January 29.

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