Introduction

Saudi Arabia is the largest member of Gulf Cooperation Council (GCC). Saudi economy is also the largest economy as compared to any other GCC countries. Prior to discovery of oil in 1938, there was no existence of integrated national economy. Economic activity outside Hejaz was confined to live stock raising, primitive agriculture and production of simple tools by craftsmen. The annual haj pilgrimage provided an opportunity for business activity in the Hejaz region. The development of Petroleum industries in Saudi Arabia was introduced with the out-break of Second World War. However, as the war ended Saudi petroleum industry grew. Saudi Arabia has vast oil resources that have shaped the kingdom’s development. The country also has large natural gas reserves, as well as deposits of Bauxite, Coal, Copper, Gold, Iron, Phosphates, Platinum, Silver, Uranium and Zinc. Non mineral resources include limestone, glassland and stone. Oil reserves in Saudi Arabia constitute more than 25 percent of the global oil reserves. Saudi Arabia as is an important member of Organization of Petroleum Exporting Countries (OPEC) as well as organization of Arab petroleum exporting countries (OAPEC). The enormous oil reserves and vast oil production capacity in Saudi Arabia provides it with a
significant influential power in the global oil market. The inflow of massive oil reserves in Saudi Arabia has resulted in unprecedented development and prosperity that Saudi Arabia presently enjoys. As far as agriculture is concerned Saudi Arabia does not have much fertile land. Most of the land areas are covered with desert and hills. So, agricultural activity required heavy investment for making her self sufficient in the food grain requirement. Saudi Arabia is a tropical region and as a result it receives temperature in summer at about 50°C and it is too cold in winter and more variation of temperature is found in hilly areas.

Saudi Basic Industries Corporation was established in 1976 as Saudi Arabia’s main non oil industrial enterprise. It includes among its holding major gas utilization projects, chief among them petrochemical development at Jubail, Jeddah and Yanbu. This Saudi company started working in collaboration with United Kingdom, Italy and European Union etc. This benefited Saudi Economy in two ways; it firstly accelerated the efficiency in the production and secondly it was to create the market. After the exploration of petroleum, Saudi Economy became substantially dependent on its export. Saudi Planner realized that petroleum reserves were limited in long run and for strengthening the economy they needed, the development of other sectors as well. So, Saudi Arabia started the five year plan for development and diversification of all sectors of the economy. So far as the economy of Saudi Arabia is concerned, it is predominantly oil based economy. Its structure and
orientation are in the process of change. It is expanding and diversifying horizontally as well as vertically, and is becoming more complex with the passage of time. Earlier Saudi economy was characterized by a highly tradition based century old value system. The chief economic activities were nomadic pastoralism, trade, agricultural activity and pilgrimage which had been one of the highest source of revenues. The emergence and consolidation of Saudi Arabia in 1930s synchronized with the discovery and exploration of petroleum oil and other natural resources. The process of unification and integration of the country socially, politically as well as economically started together and helped each other in the further development process and programs. This cultivated in the emergence of the process of transformation and modernization of the society as a whole. The Saudi government adopted the doctrine of “growth through ideology”. Accordingly they selected neither the capitalist economy based on the doctrine of laissez-faire and individual enterprises, nor the socialist system based on the philosophy of centralized planning and firm government control for its economic developments. On the contrary they adopted a mixed system (a system which the Saudis term as Islamic Economy and joint enterprises). Its main objective was to create a dynamic and modern economic system without diluting its religious, puritanical, traditional and historical legacies.

It is generally believed that Saudi economic system is constituted of single item i.e. petroleum and its by-products. It is not true at all. Some other
ingredients of its economy are gaining ground and getting consolidated over time due to the economic integration and diversification strategy launched by the Saudi government. And the second point is that the government is also trying to liberate the country from the syndrome of dominance and dependence of oil in the economy. This has been necessitated by the interplay of both domestic as well as international factors. The economy in Saudi Arabia may be divided into two parts. (1) The oil sector (2) The non-oil sector: Which are century old but now getting modernized day by day, and which comprise of agriculture, petroleum/hydrocarbon based industries, construction, non-hydrocarbon manufacturing and services etc.

First of all petroleum was struck in Saudi Arabia in 1938 and was exploited and exported in 1939, but its exploitation and exports got momentum only after world war II. The sudden increase in national assets due to export of petroleum and its by-products influenced the system as a whole. Which motivated and guaranteed forces of changes and transformation. The vast increase in national assets due to export of petroleum and its by-products helped in the process of application of modern technology in economic development. But unfortunately the religio-cultural value compatible with the modern development philosophy did not generate at the same time and at the same rate due to many weaknesses and shortcomings both fiscal as well as social which were inherent in the system.
The economies of oil exporting Saudi Arabia and other Gulf countries are entirely distinct from other developing countries in many ways and degrees. Hence their strategy of industrialization and development could not be identical. Their GNP and GDP are very high in comparison to other developing countries. They are not debt ridden countries (oil based countries). They have been also credit lender countries. But where as the degree of development of human resources are concerned, they are still behind many developing countries. Unlike other developing countries, they are entirely dependent on foreign countries for minor consumer items to the hi-tech machineries and weapons, and also for sophisticated and well trained human powers for implementation of their development strategies.

Literature Review

Saudi Arabia has vast oil resources to develop itself. So, Saudi Arabia embarked upon a long term economic development planning to reduce the exclusive dependence of the economy on a single export commodity i.e. crude oil. For this purpose Saudi Arabia started five year development plan. The development of petro chemical industries in Saudi Arabia plays a leading role in diversifying the economic structure, negates the continuum of rentier economy and making for self sustained economic growth. So Saudi Arabia plans to reduce overwhelming dependency on oil exports. It was expected that the export oriented hydrocarbon based petrochemical industries would
diversify the economic structure, and also believed that the industrialization process would involve full utilization of indigenous productive resources and it can generate forward and backward linkages.

There has been a lot of work done by different academician on the various aspects of diversification of Saudi Arabian economy. Important among them are mentioned as follows-

1. The study conducted on this issue by Rashid Masood in his book *Economic Diversification & Development in Saudi Arabia*, reveals that till 1973-74, Saudi Arabia had not recognized its importance in the international market and exported petroleum products at nominal cost which even did not recover the cost of production. But the 1973 oil boom helped confidence building in Saudi Arabia, and they realized that they were the main source of energy supply to the world. Their export earning increased. Now they were not short of capital resources for diversifying their economic structure. When Saudi Arabia realized that developed countries were heavily dependent over it for their energy resources, the country got the confidence to embark on diversification of its economy. In its first step towards diversification Saudi Arabia moved to plan for huge gas based petrochemical complexes. Since these industries were highly technology intensive, Saudi Arabia rejected the commercial criteria of investment and took into consideration the social criteria i.e. requisition of technical know how, increase in employment opportunities

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and enhancement of foreign exchange earnings. To diversify the economy, Saudi Arabia not only improved the infrastructural facilities like construction of ports but also invested in human resource development. However, the study of Rashid Masood does not explain how the petrochemical industry in the country has been providing base for agriculture and other industries, chemical and related products?

2. *Reconstructing the Saudi Economy and Privatization Development,* was the special report issued by SAMA. According to this report first step of diversification of Saudi Arabia economy was setting up of industries which use hydrocarbon (oil, gas) as raw material to convert the hydrocarbon into value added products. This has created a number of new industries in the country which is accompanied by creation of infrastructural facilities, requisitions of technical know how. The large reserves of hydrocarbon and availability of capital provide the strength to Saudi Arabia in attracting foreign companies. It paved the way for improvement in the infrastructural facilities, skills of local workers. In the wave of developing capabilities for the production of tools and machinery Saudi Arabia started assembling the imported machinery and equipment. With the development of necessary skills and fabrications capability, indigenization takes place progressively. The study reveals that the diversification of the economy reduced the flaring of the associated gas and the dependency of the economy on oil sector. The gas flared as a percentage of

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total gas production declined to 60.6 % in 1983 as compared to 71.9 in 1970. The share of oil sector has also declined in the gross domestic product of country. This sector accounted 55 percent of GDP in 1969-70 which came down to 24.3 percent in 1984-85 and became 42.42% in 2003. The Saudi Arabia monetary agency study on economic diversification has focused on the importance of petroleum products and natural gas. However, the report does not pay much attention towards the planned development and diversification of the country.

3. In his study "Saudi Arabia moves towards diversification" Neil Ford found that due to lower prices of oil during late 1990s, the per capita GDP of Saudi Arabia declined by 40 percent. This has provided the enthusiasm for the diversification of the economy and the country moved towards diversification. As a result the number of industrial complex reached to 2,557 with an investment of $43.3 billion in 1999 from 470 industrial plants with an investment of $2.7 billion in 1975. To meet the growing demand of the economy the importance of infrastructure was realized since power is an important ingredient of infrastructural facilities. It has also been expanded over time. Power sector generating capacity grew from just 1,173 mw in 1975 to 25000 mw in 2002. Accepting power generation as industrial activity, Saudi government is enabling foreign companies to invest in this sector by providing many facilities like 10 year tax holiday and concessionary finance up to 50

percent of the capital cost of the project. Agriculture sector is another area of diversification in Saudi Arabia. The study found that the area under cultivation has increased drastically to 14 million acres by 1998 while it was 3,70,000 acres in 1975. About 85 percent of the total vegetables demand is met by the domestic producers along with 60 percent of fruit supply. However, Neil Ford has highlighted the attention of government towards agriculture. He also focused on the increasing capacity of power and infrastructural development which are base for economic development. The problem with his study is that though broad development took place, but it does not sufficiently study the low development in human resources.

4. According to Al, Shaikh Said A., The Saudi Development plan aimed at achieving high economic growth. The government’s focus on employment scheme for Saudis created a situation that encouraged nationals to seek public sector employment. Consequently, this resulted in a heavy reliance on foreign labour for almost all types of work except for specific administrative and managerial jobs. But finding appropriate employment opportunities for new comers to the labour force has become difficult, with the labour market facing a growing over supply of unskilled workers and increasing more college graduates unable to find productive employment opportunities.

5. According to The Economic Bureau, **Saudi Arabia's Economic offset programme: Achievements, Emerging Tends and Recent Developments**. The performance of Saudi economy during 1998 reflected the adverse impact of the sharp decline in oil prices caused by slow down in the world economy mainly due to financial crisis in Asia & Russia. There were also some notable positive developments. The price situation continued to remarkably stable. The banking system performance continued to improve. The process of privatization made notable progress with the establishment of Saudi telecommunication followed by restricting of the electricity sector through merger of five electricity companies into single holding company. But he did not give more emphasis on development of social sector and the reduction of development of oil sector.

6. The study conducted by Robert E. Looney in his book, ***Economic Development in Saudi Arabia: Consequences of Oil Prices Decline*** states that conventional wisdom had maintained that capital scarcity is one of the most serious constraints on development. The oil price spiral of the 1970s, however, created a whole new phenomena. The sharp increase in oil income found governments, as well as development economists, unprepared to deal with the consequences of the new conditions. The response of the Saudi economy to the boom conditions of the 1970s and the bust condition of the 1980s is the subject of this important addition to the economic studies of oil based economies.

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The exact structure of Saudi economy its reliance on oil, the small size of the market and the near absence of the goods producing sectors persuaded policy makers to embark on policies that infused funds in to the economy through welfare programs, massive military spending, subsidies to the private sector, an accelerated program of infrastructural development and heavy imports of goods and labour. The two five year development programs of the 1970s concentrated on infrastructure, while the 1980-85 program ventured in to industrial development, especially hydrocarbon based industry such as petrochemicals.

Given the low absorptive capacity of the economy and the near absence of a private sector interested in non-mercantile, non speculative or non financial ventures despite the massive investment of funds in infrastructure failed to stimulate the much hoped for private sector led economic diversification. Dr. Looney points out that there were a few success stories in agriculture and manufacturing. However, we find that such success was only made possible by the heavy programs of gross subsidization. Indeed, without such government subsidies, Dr. Loony fears that about one half of the farms and nearly two third of the manufacturing industries would die. As if this were not enough, the plans failed massively the lessening the Saudi economy’s reliance on foreign labour or raising in productivity. The growth of the Saudi oil sector in 1970’s and its subsequent collapse in the 1980s forced the government to adopt austerity budgets and to attempt to lower its subsidies to
the private sector. This book was authored in the period of declining oil revenues about two decades ago. At present the situation has changed and oil sector again plays an important role in Saudi economy.

7. Hobday's study on Saudi Arabia provides the reader with an interpretation of the background and tradition of the people who make up the oil rich kingdom. It also sets out the ambitious economic goals they have set for themselves. Saudi Arabia's efforts to transform its economy is not constrained by lack of financial resources. Oil revenues and earnings from overseas holdings are ample to finance the desert kingdom's development.

The pace of Saudi Arabia's economic development is tempered, however, by a strong sense of tradition and the teaching of Islam. Saudis wish to maintain their religious and cultural values. Hobday points out that day by day, the Saudi system undergoes the slight attack of western values, either through imported technology and manpower or through the increased opportunities for Saudis to travel and study abroad.

Unfortunately, much of the economic data are out dated. New development since the book was written, such as OPEC oil price increase, and growing conservatism are additional factors that should be looked at in determining the speed and direction in which Saudi Arabia will allow herself to go.

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8. Saudi Arabia: *Rush to Development by Ragaei El Mallakh* is based on seven years of research, data collection and interviews with leaders in the public and private sectors in Saudi Arabia. It was carried out during numerous visits to that country. More than 120 statistical tables of varying degrees of usefulness and accuracy are offered to describe the dramatic structural transformation of the Saudi economy.

Professor El Mallakh’s approach is to look at the distribution of GNP, according to economic activities. The five year plans of 1970-75 and 1975-80 are thus examined and the outcomes as compared to the stated goals below are evaluated favourably.

1. To increase the growth rate of GDP and enhance the conditions for a sustained growth.

2. To diversify the economy and diminish dependence on oil.

3. To develop the physical infrastructure and human sources and increase the well-being of all groups.

The ruling elite is also very sensitive to the declared or undeclared demands of the ruled, especially demands that are economic. But in spite of all these qualifications and the actual political stability that prevails in Saudi Arabia. The Saudization of economy may prove more challenging than it appears. Professor Mallakh does not make the question of political development an important issue and object of his inquiry. Income distribution

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as an important aspect of welfare is not handled with the same care as economic growth. Perhaps lack of statistical data on the issue has prevailed. The twin problems of extreme inequality in income distribution and the lack of provision for political development point to a deeper problem and give rise to a new question of who is the proprietor of the oil wealth in Saudi Arabia? This book does not raise those fundamental questions of normative economic that appear most appropriate.

9. Saudi Arabia: Energy, Development Planning and Industrialization by Ragaei El Mallakh and Dorothea H. El Mallakh,⁹ (eds.), is a book moving from the general to the particular. Ali Johany provides and excellent overview of the Saudi economy in the first chapter. He sets the stage for further essays on varied topics related to Saudi economic development. Such as Saudi industrial development, philosophy ad aspirations, technical transfer, manpower resources, oil, gas, the petrochemical industry, inflation and Saudi international economic relations.

The weakness in the book are those endemic to multi authored volumes: an unevenness in presentation and level of analysis. The level of analysis of some of the essays, while appropriate for oral presentation, occasionally appears some what superficial in written form. An example of unevenness is the inclusion of two chapters on the transition from tribal society to nation state. In a book that is essential about economic development, it would seem to

this reviewer that one such chapter would have been sufficient and that it should focus less on cultural anthropology and social change than on developing manpower resources. Another endemic problem is topicality and timeliness. The papers were presented just before the full brunt of the world recession and the oil glut of the early 1980s. Thus, a number of the operating assumptions about oil revenues and production policies, industrialization goals appear somewhat outdated. Given the cyclical nature of world oil market in particular, however, some of these operating assumptions are bound to come back into vogue before too very long.

10. *Saudi Arabia’s economy: Oil and Search for Economic Development* by Hossein Askari and Babak Dastmalschi, covers the period of the massive growth in oil revenues during the 1970s and early 1980s, followed by the steep decline. Askari emphasizes that “The underlying basis of Saudi Arabia’s GDP is the depletion of a non-renewable resource. If the proceeds of the sale of this resources are not prudently spent or invested, they are, in essence, wasted and unrecoverable. The sale of this resource fuels the entire economy. In other words, Saudi Arabia should be saving a large proportion of its oil revenues for investment and the development of alternative sources of revenue as oil resources are steadily exhausted. Askari’s discussion of Saudi economic policies are detailed. He briefly alludes to the differences between Saudi and Kuwaiti policies in so far as the latter put the greatest emphasis on foreign

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rather than domestic investment. The Kuwaiti rate of return on foreign investment is far higher than what is realized by Saudi Arabia on its domestic investment, which in many cases had a negative rate of return. Because of the elaborate system of producer subsidies in industries and especially in agriculture. In those years Saudi Arabia had been exporting wheat at the international price, usually a fraction of the real cost of production. Moreover, this policy was rapidly depleting the country’s non-renewable underground water supply. Looney quotes the US Secretary of Agriculture who during a visit to that country rather undiplomatically called the Saudi wheat program ‘Crazy’. But the Saudi official position was that it has been ‘a thrilling story of real success.’

Askari’s study, while detailed in many other respects, is rather less than necessary in its analysis of the labour force and productivity. Looney’s study fills in some of the gap. He notes that labour productivity growth was negative during the period of third five year plan. However, he offers little explanation for this phenomenon, and might also have elaborated on its policy implication.

11. Economic development in Saudi Arabia: Consequences of the oil price decline by Robert E. Looney, states that lower military expenditure might adversely affect Saudi Arabia’s rate of economic growth. But he was not sure that these were relevant for Saudi Arabia. In most developing countries unemployment was a major problem. Saudi Arabia imported a large number of

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labour force. Of particular interest is the Looney’s analysis of the power of OPEC and of the Saudi role in the cartel. He states that the rise of tenfold crude oil prices during the 1970s, can be explained by major changes in market forces, not by the power of OPEC.

12. Mohammad A Bakr, A Model in Privatization Successful Changes Management in the Ports of Saudi Arabia,\textsuperscript{12} states that privatization is an important issue that has been tackled by many researchers both in developed and developing countries. A surge of literature of privatization suggests that it promotes economic growth, stimulates productive efficiency, expands the role of private sector, reduces the size of the government sector, attracts foreign investment, and helps in the development of capital market programs especially in the developing countries. The book under review presents a case study of privatization and economic transformation in Saudi Arabia. The author combines both theoretical analysis and personal experience to describe the privatization of ports in Saudi Arabia.

From reading this book, it seems that the author considers the privatization of the Saudi ports to have been a successful experience that ought to be encouraged and emulated in other places. However, privatization is a complex process involving a host of political and economic factors that needs to be addressed and empirically tasted. Assessing the economic and social impact of privatization is not always straight forward.

\textsuperscript{12} Mohammad A Bakr, A Model in Privatization: Successful Change Management in the Ports of Saudi Arabia, Centre of Arab Studies, London, 2001
13. "Oil and Power: Political Dynamics in the Middle East," by Sheikh R. Ali, attempts to cover too much ground in a relatively short book, as well as trying to address both the general readers and the specialists. The structural problems are compounded by simplistic assertions, speculative assertions and blatantly wrong assertion (The oil exporting Arab countries are the most militant, posing a serious threats to the flow of oil to other nation).

In addition to these difficulties the books suffers from two fundamental shortcomings. First, it fails to deal with some of the more serious historical changes, which have taken place in recent years, as for example, the implications of rising economy and political power of Saudi Arabia, the consequences of the Iraq-Iran war for regional and global configurations of power, and the significance of the formation of oil based gulf cooperation council.

14. *Regime and Elites, Conflict and Collaboration* by Mordechai Abir discovers the formation of Saudi elites. According to him two important sources of change brought about the formation of elite groups in Saudi Arabia i.e. education and oil. After consolidated position of power Ibn Saud realized that a centralized system of government was necessary to retain his power. He needed a system of education to train bureaucrats. By the time oil began to play a role in the life of the kingdom in the 1930s, the ruling oligarchy was

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composed of three groups i.e. the royal family, the religious establishment and the tribal sheikhs. The creation of Israel and its relation with the Arab world, growing dependency of the west on Arab oil, and the increase of oil revenues and the emergence of United States have forced the Saudi ruling class to deal with the perceived threat of the forces of Arab nationalism and to tackle demands of modern military and civilian bureaucracies and technocracies. To deal with these complex issues the royal family balanced the interest of those who wanted to modernize the kingdom and those who opposed the change.

Dr. Abir divides the period after Faisal’s assassination in 1975 into two stages i.e. an economic boom up to 1982 and a period of economic recession thereafter. Heavy development spending characterized the first phase whereas the drastic cutbacks, the second. The ruling class however has sufficient arm forces and intelligence network to help the house of Saud withstand the consequences of the economic decline. The author also fails to analyze the role of US influence on all aspects of Saudi life.

15. *Arab Nationalism, Oil, and the Political Economy of Dependency*, by Abbas Alnasrawi,\(^{15}\) discusses the dependency of Arab states on others and sees oil interests in conflict with Arab nationalism and Arab nationalism in conflict with state nationalism. Arab dependence, first imposed by the ottomans and then by western powers, has resulted from oil interest and revenues. It has also been strengthened by reactionary Arab regimes and by forces of the world

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market in which the Arab countries have been presumably integrated. Dependency on oil, however, has exposed the “myth” of Arab oil power. Which is clear from the failure to resolve the Arab-Israel conflict. The future of middle east countries is not promising, according to the author, because the conditions leading to dependency still include dependence on oil, large external debts and intra regional conflicts that undermine Arab nationalism. It is suggested that privatization and restructuring may influence the future of these countries, but is not clear that how a change in the economic system would affect the degree of dependence. According to the author, by virtue of its oil, Saudi Arabia has influence, little power, but certainly no leadership. The Arab countries are young as independent nation state. A certain degree of maturity is necessary before, they are able or willing to surrender some of their sovereignty to a federal form of Arab unity. The reasons for the lack of motivation to Arab unity and the continued dependency lie also in the poverty and economic underdevelopment of the region, and in the fateful impression of wealth in the oil countries. In Saudi Arabia per capita income is lower than that of Israel, which is not a rich country by modern standard. Finally, the study would have been richer had it addressed the basic cause of underdevelopment and dependency i.e. explosive population growth, relatively low quality education, confessionalism and absence of rational analytical policy making, poor infrastructure and segmented market.
16. Jahangir Amuzegar, "Managing the oil Wealth: OPEC's windfalls and Pitfalls." Examines the success of the member countries in the organizations of petroleum exporting countries in managing their oil wealth. It provides an insightful review of the development, pitfalls and structural changes that OPEC member countries have faced since the mid 1970s. The book provides tools to understand the process better. As OPEC nations accumulated their large, new foreign exchange receipts, both the world community and OPEC itself expected a different outcome. The world community saw the transfer of petrodollars from the developed nations and many poor countries to a group of oil rich countries as a destabilizing influence that would change the balance of economic power and cause worldwide recession. OPEC nations saw their new wealth not only as the engine of development and growth, but also as a tool of social welfare. Amuzegar points out that things turned out very different from expectations. The oil importers did quite well, and oil exporters did poorly. Once the initial shocks was observed, the oil importers used fiscal and monetary policy tools to protect themselves. The massive inflation of the early 1980s ate through OPEC nations revenues and reduced their purchasing power at a time that they had become addicted to waste and inefficiency. Amuzegar uses both theoretical tools and detailed information from country studies to measure the success and failure of the different oil exporting countries. In all

cases the oil money cracked the fabric of the society, changed government behaviour and brought about social change.

The cases examined in this study offered the author an opportunity to test several development hypothesis. These include impact of the resource based wealth and the validity of Dutch disease syndrome. The results indicated that none of the group members enjoyed all the positive elements. All OPEC members were engaged in hasty and ill-conceived spending of their boom earnings. One of OPEC’s stated goals was to diversify the member country’s, economy away from oil. Many OPEC members ended up as dependent or even more dependent on oil revenues than they were before the increase in oil prices and oil revenues.

In the late 1990s, OPEC was still alive and well. Indeed, it staged a recovery in early 1999 as it moved to re-establish itself through cooperation with member states. By 2001, OPEC had the best run of its history i.e. about thirty months of high prices, controlled cheating on quotas, and a spirit of cooperation never seen before in OPEC’s history. Indeed the pain and fear of the 1998 price crash made for a very united OPEC. When oil revenues rose, there was no rush to increase subsidies or to spend the money quickly on projects. Some OPEC members opened their doors to foreign investment and introduced reforms in their economics. OPEC seemed ready to enter yet another down phase. Weak global economic performance and exceptionally weak demand was exerting downward pressure on prices. The turbulent story
of OPEC may continue for many more years. The complexities require careful and continued analysis. This book helps the students understand and categorize the factors that affect this important organization and its members.

17. "The new Economy of Oil: Impacts on Business, Geopolitics and Society" by John V. Mitchell with Koji Morita, Norman Selley and Jonathan Stern, does an excellent overview of the fundamentals of energy market and the issues that need to be considered in developing sensible energy policies. The authors approach is not only comprehensive but remarkably free from bias in the world. Where ideology often overcomes analysis. The role and power of the free market throughout the history of the industry is emphasized properly. But the areas where markets may occasionally fail are recognized as well. To give emphasis on oil, the book provides an overview of all energy markets and defines the challenges facing natural gas. The authors properly warned that the continued growth in market share of natural gas is contingent on competitive pricing versus competing fuels, which in no way is guaranteed. The author in his book emphasized on two changes that will dominate energy pricing over the next era. First, the author argues that competition from other fuel and technology in transportation and power generation would set an upper limit on prices in the long run but that long run rapidly became shorter. Second, the author asserts that massive structural surpluses of oil production capacity have been reduced and this would simplify the task of maintaining prices at

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minimum level. There is no doubt that inter fuel competition will limit oil prices. But their limits may be no tighter in the future than they have been in the past. Oil has been losing market share in power generation for many years. Power generation is an increasingly less relevant market for oil products. Unless gas price rises sharply relative to oil, most of the future competition will be between gas and coal. Several years ago, when the book was authored, it appeared that in the long period spare capacity was about to be over. While the authors analysis is insightful. The question remains how many of their conclusions truly represents a break from long standing energy market trends.

18. Sharif Sabri, *The House of Saud in Commerce: A Study of Royal Entrepreneurship in Saudi Arabia* 18 The study of Sharif Sabri’s Role of the House of Saud in Commerce is contemporary. It has involved equally painstaking and focused research. Sabri has provided detail data for analysis that has hitherto not been compiled systematically. It provides long lists of members of different branches of Al Saud family, giving details of their equity investment in Saudi Arabian companies. It also gives the details of the capital structure of the companies as well as investment stakes of the royal family members, most of these businesses being in private sector. The market value of these shareholdings can not be estimated.

Sabri provides a general analysis that shows that it is the third generation of the house of the Saud, who are actively involved in business both

as investors and as active owners. Other merchants do not appear to have been adversely affected by the business aspirations of royal family members. Indeed Sabri suggests they have benefited, both directly being involved as partners to princes. Sabri suggests that there is a general positive attitude to economic liberalization and reform by royal entrepreneurs, including World Trade Organisation (WTO) membership. But some caution that their own domestic business interest should not be undermined by globalization. The increasing oil wealth presented the opportunities to the younger Princes with money to invest. It is almost a religious imperative given the tradition of profit sharing, that was seen as being more legitimate than simply making money from money through interest. Sabri refers to some of the concept of Islamic economics and finance, but does not discuss them in detail.

19. Paul Rivlin, "Economic Policy and Performance in the Arab World." This book is much less specifically focused than the other studies, being an assessment of the recent economic performance of a member of Arab countries. The author compares the earlier import substitution policies with the economic stabilization and structural adjustment policy introduced at the order of IMF. This book introduces contemporary Arab economic issues. There are interesting contrasts drawn between the Arab and East Asia development experience, but the treatment lacks depth, largely because the range is so wide.

Paul Rivlin follows the world bank Washington consensus in prescription for policy makers.

20. "A Structural Econometric Model of the Saudi Arabian Economy" by Faisal Safooq al Bashir. presents a quantitative analysis of the Saudi economy's structure. Which should be studied in order to understand the recent events of the country into world financial and monetary attention. Al-Bashir informs in this book that there has been substantial economic changes compared to the 1960s, specially in the oil price increases. Which were during the Arab oil embargo of 1973-74, and resulted in accumulation of capital surplus. In his book the author finds large standard errors in one instance, the coefficients of government revenues and personal income in the consumption function. Moreover, he warns that the forecasting ability of the model is restricted, as variables were not included to capture economic changes over time. This is a technical econometric work and not for general consultation. The social factors impeding ultimate development of Saudi economy have not been taken sufficiently into account.

21. "Demand for oil products in Developing Countries" by Dermot Gately and Shane S. Streifel, points out that growth in demand for oil products has been more concentrated in the developing countries, than in the industrial world since 1971. The authors of this book consider the changes that have

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occurred in the developing world and use their analysis to project what will happen in the coming decades. They include in their definition as developing all non-member countries of the Organization of Economic Cooperation and Development (OECD) except those of former Soviet block. In a qualitative discussion of the factors affecting oil demand they conclude that income and population are more important factors than price. While indigenous energy supply, energy policy and traditional fuel use are relevant. They use a variety of specifications that includes income and crude oil prices, static and dynamic formulation. They find that results are satisfactory for gasoline, diesel, LPG and other oil products, are variable for jet fuel and kerosene, are unsatisfactory for naphtha and kerosene. Income elasticities are larger in absolute value than price elasticities and are more often significant. Asymmetries in income and price response were found in some countries but not in others. This analysis was quite an ambitious task and it is a pity that separate product prices were not available by country. Given the variable tax regimes and changing exchange rates, it is not clear how highly correlated world crude oil is to domestic product prices.

22. “The paradox of plenty: Oil Booms and Petro-states” by Terry Lynn Karl, presents a model of the political and economic development of ‘petro states’ across regions. That model is strongly path-dependent. If the development of the petroleum industry is contemporaneous with the building of

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the modern state, a country's political economic trajectory is largely predetermined. The petro-state is characterized by government control over oil resources, leading to a broadly politicized economy in a state. Patron-client ties will dominate the political field. Boom times will lead to a vast expansion of the size of government. When the boom ends, hard choices will be deferred as leaders use oil money, and ability to borrow internationally against oil reserves. Even though Karl's path dependency argument differs from the more contingent conclusion about rentier states. The author emphasized the fact that oil revenues lead to weaker states. Without the need to tax, 'Petro-state elites will allow extractive and information gathering capacities. When the boom ends the state will be unable to tax or regulate effectively its economy. While oil might contribute to state strength in other areas. Karl's comparative cases are not developed extensively, but they generally support her conclusion. The book is not without flaws. The most serious one is methodological. Not a single non-oil case is considered.

23. Girijesh Pant in his article “Saudi Arabia: From Oil Kingdom to Market,” marks out the Saudi accession to the World Trade Organisation (WTO) in December 2005. According to him this accession is marking a new phase in the country's economic management. From this entry the state will have to retreat and the market will have to step in. The social settlement between the state and the society will have to be revised. And the interference,

between the domestic and global market will have to be made transparent. This leap forward is not an absolute benefit. The market led boom has increased the price of land, especially as watering the land is costlier. The food security in the circumstances, as an obvious casualty. The issues of subsidized services and infrastructure support are acquiring added urgency in view of the growing demand and aspiration. In spite of rent-derived resources, the contradiction between the regional global interface will be sharp. The Saudi Arabia initiated a political and social agenda to correspond with the economic transformation but the threshold where the state would be expected to make leap forward to able to the needs of market economy still remains a matter of conjecture. It critically depends upon how Saudi state is going to pursue the delicate act of revising the social contract of the rentier economy without jeopardising the legitimacy.

24. “Political economy of Saudi Arabia” by Tim Niblock with Monica Malik, focused on the internal dynamics of the Saudi economy and the changing role of the state. The ultimate criteria of success is whether the kingdom can advance or at least maintain, its position in the global economic order. For the author the picture is mixed. The development strategy of Saudi Arabia is coherent and sound, but implementation poses major challenges. Saudi Arabia was of course long classified as a rentier state. However, Niblock points out the short comings of this categorization specially because Saudi

Arabia has developed a significant industrial sector. Furthermore, Niblock points out that the private sector has played a significant role in the kingdom's development. Niblock provides some new insights, notably on the articulation of development strategy and economic policy. It would have been helpful. The book ends on an optimistic note with the legal reforms resulting from WTO membership bringing considerable benefits and the creation of the Saudi Arabia General Investment Authority resulting in significant Foreign Direct Investment inflows. Some of the negative factors also identified by Tim Niblock i.e. mass education in the kingdom leaves much scope for improvement. Employment remains an issue linked to the low productivity of some Saudi workers. Privatization is also proceeding after many years of delay. Although the stock market suffered a major correction. But the crisis was contained and investor confidence soon restored.

25. Adne Cappelen and Robin Choudhury in their article "The Future of Saudi Arabian Economy: Possible effects on the Oil Market."25 This article focuses on alternative economic and political developments that could reshape the future of Saudi Arabia. In the article the authors start with a brief summary of the historical, political and economic background followed by description of two scenarios for the Saudi economy. First we outline a future based upon the continuance of the current policies for another decades. The first alternative scenario explores possible effects from policy reforms in taxation and

privatization. The second explores possible effects from changing oil policies. And finally discusses what these domestic scenarios might imply for the relations between Saudi Arabia and the Organization of Petroleum Exporting Countries (OPEC). Although it is not likely that Saudi Arabia will act on its own within OPEC. There are both economic and political arguments that lead us to conclude that Saudi Arabia is likely to maintain its support for OPEC.

The Conceptual Framework:

The issue of diversification became prominent in the world since the discovery of gas in Netherlands and it consequent over dependence on the export of this primary commodity. In economic literature this phenomenon is also referred as the Dutch Disease. The Dutch Disease refers to deindustrialization of a nation’s economy that occurs, when the discovery of a natural resource raises the value of that nation’s currency, making manufactured goods less competitive with other nations, increasing imports and decreasing exports. The term originated in Holland after the discovery of North Sea Gas.  

Dutch Disease is an economic concept that tries to explain the seeming relationship between the exploration of natural resources and decline in the manufacturing sector. The theory explaining that an increase in revenues from natural resources will deindustrialize a  

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nation's economy by raising the exchange rate. Which makes the manufacturing sector less competitive. However, it is difficult to definitively say that Dutch Disease is the lone cause of the decreasing manufacturing sector, since there are many other factors at play in the economy. While it refers to natural resource discovery. It can also refer to "any development that results in a large inflow of foreign currency, including a sharp flow in natural resource prices, foreign assistance, and foreign direct investment." Further, it is said that Dutch Disease is an economic phenomenon that effects countries upon the discovery, extraction and exportation of large amount of natural resources. It specifically tends to effect countries that find large amount of oil and gas. The finding of large amount of oil would have both positive and negative consequences for a country. The term Dutch Disease refers to the impact of those consequences that was noticed in the Netherlands during the period after the Dutch started to sell their natural gas. The manufacturing exports were no longer marketable given an increase in the exchange rate and this marked an economic crisis. At present Netherlands is not the only country associated with Dutch Disease. Nearly every country that find natural gas, oil or valuable amount of a tradable natural resources should concern itself with the possibility of "Dutch Disease" and the impact that extraction of that resource will

27. "The Dutch Disease", The Economist, (Nov 26, 1977), pp.82-83
have on their economy. An examination of Dutch Disease and how different countries have dealt with this influx of revenue from oil resources is presented to illustrate the impact on a country of large oil resources like Saudi Arabia.

The discovery and exportation of a natural resource causes an increase in income of a country, both to the government through royalties and to the people who live through their employment in the new industry. The increase in income and the exchange rate due to production of a large amount of natural resource can quickly cause the domestic economy of resource exporting country to slow down. This is somewhat complex since both the large value of the currency and increase in income are very positive occurrences. Thus a close examination is required to explain why the combination of these two events can result in negative consequences.\(^{29}\)

Three important sectors of the economy need to be examined in this analysis; traded resources, traded manufacturing and non-traded services. Manufacturing is important to employment in any country and it is also important to the development of human capital. Human capital refers to the skills accumulated in the workers of a country. The net human capital of a country is the combined knowledge of workers in

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\(^{29}\) Corden, M., "The Dutch Disease", *The Economist*, London, Nov 26, 1977
that country. As workers experience new tasks, gain new skills and innovate while on the job, human capital increases.

This is ultimate expression of how a country and the capitalist world moves forward over time; human capital in constantly growing and pushing industries and innovation ahead. Thus unemployment is detrimental to a country's total development of wealth as well as to individuals that are unemployed.

Essentially what occurs during Dutch Disease is that the discovery and export of natural resource, most commonly oil, causes an initial increase in income to the workers in a country. However, this increase in employment has been noted to be minimum as oil sector is very capital intensive industry. The skills required for the oil industry can also be unavailable from within the country, thereby encouraging the use of foreign workers and limiting the growth of human capital through yet another means. Given these circumstances consumers spend their income in two ways; on non traded services, which suffer no loss from this increase in income and on imports.

The applicability of Dutch Disease is therefore limited. Some countries may experience situations very similar to this explanation and some countries may differ from the model extensively. The period in which OPEC countries including Saudi Arabia experienced the largest influx of oil revenue was during the price increase in the seventies and
early eighties. So this period will be explored whether Saudi Arabia found itself vulnerable to the negative impact of Dutch Disease or not. This discussion is currently relative because of the high price of oil in present times. A better understanding of how large increase in the price of oil affected countries in the past may shed some light on how a country may protect itself.30

The discovery of oil in 1938 came only six years after the emergence of the Kingdom of Saudi Arabia (United States Library of Congress online). This is significant for a number of reasons, not to mention that a kingdom is quite different from a democracy. It is also said that many Saudis believe in their king being ultimate authority while politics, political parties and labour unions were not allowed. Saudi Arabia was relatively poor prior to the increase in the price of oil during the seventies which substantially increased its oil revenues inflow. The revenues from oil jumped from US$ 4.3 billion in 1973 to US$ 101.8 billion in 1980.31 In 1974 the government attempted to only extract oil at moderate pace in order to ensure a steady, lasting income but the ever increasing international demand and the high price forced Saudis to formulate a new strategy.32 Industrial development, with an emphasis on processing of hydrocarbon was the revised plan. Saudi

31 Pike, David, “Special Report, Saudi Arabia”, MEED, 34(46); 23 Nov 1990, pp.18 & 19
Arabia by using oil revenue would establish valuable industry and stimulate the growth of its economy. Several foreign international companies were invited to joint venture with the government to develop these plants. Infrastructure was also developed during 1980s mainly to support oil industries.

During the same period the government doled huge subsidies, the purpose of which were three fold; encourage non-oil development, distribute income and meet social goals. While these subsidies supported Saudi population they became increasingly difficult to maintain and justify cost of many programs were greater than the overall benefits. When the price of oil began to fall in 1982 Saudi Arabia was forced to change its focus from managing budget surplus to dealing with deficit. Due to this, Saudi Arabia’s enormous share of oil fell mainly to reduce the oil supply in order to reconcile with OPEC’s production quota. Saudi Arabia faced two economic challenges:

1. The reduction in the price of oil.
2. The reduction in the production.

In response to the declining oil revenues Saudi Arabia increased oil production which led to a second price crash for oil in 1986. Saudi
Arabia mitigated these damages through the proceeds of the earlier oil revenues.  

In Saudi Arabia traded manufacturing industries is very limited. The rate of imports is very closely tied to the rate of income from oil. Saudi Arabia's entire economy is dependent on this resource. While attempts were made to develop industry outside of oil but cost were unjustifiably high. Also the massive quantities of oil in Saudi Arabia ensure that an economy based on oil is more viable in Saudi Arabia than anywhere in the world. The government made several successful attempts to work with foreign business in developing the oil sector. The true challenges for the Saudi government will be for it to develop a non-oil traded sector before oil resources are depleted. Quite simply, Dutch Disease has not been a factor in this nation due to a general lack of manufacturing before the dependence on oil. The development of refineries in Saudi Arabia and other value added-steps involving hydrocarbons has been an effective means through which Saudi Arabia has increased the value of its industry. The increase in revenue in the seventies was managed relatively wisely and did not lead to the same kind of deficit that were created in Mexico and Venezuela. In Mexico the effect of Dutch Disease were immediate and no solution was

attempted. In Venezuela protectionism and subsidies stalled the effect but the eventuality of market prices prevailed.

In Saudi Arabia there is so much oil that the concerns represented by Dutch Disease were not always relevant. The reflections presented here are pertinent to the situation in the world today because of the current spike in oil prices. An inflow of revenue will grace oil producing nations. The most viable solution to the negative consequences of a large inflow of revenue is the creation of value. Thus the question becomes not one of Dutch Disease and how to avoid the adjustment period, but how to manage inflow of wealth, so as to create industries capable of creating lasting value. This is the situation faced by all developing countries. The reason that they flounder is because there are no viable industries. The transitional effect that Dutch Disease describes let to structural problems that through mismanagement sent Mexico & Venezuela into recession. The question of what proper management would be is a matter of investigation.

Nonetheless, the framework of the concept of the Dutch Disease is most suited to analyse the policy of diversification in Saudi Arabia.

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Hypothesis:

The research study would proceed with the following hypothesis.

1. Has the structure of economy changed?
2. Has policy of diversification paved the way for the development of Petrochemical industries?
3. Is there any improvement realized in the development of communication and infrastructural facilities?
4. Has the process of reforms diversified the economy?
5. Has the process of diversification of Saudi economy made it less dependent on oil.

Objectives:

1. The study aims to analyze the diversification of Saudi economy. For a diversified economy would provide her with reduced dependence on the oil revenues, which in turn would further strengthen its bargaining space in the global oil market.
2. The diversification involves restructuring of the economic structure. It’s necessary to know the changing trends in Saudi economy.
3. Changing economic structure would result in changing economic relations for Saudi Arabia. The study aims to study this for assessing any future impact of this diversification.

4. The study also aims to study the possible impact of reducing the direct role of the public sector as an agent of economic growth by promoting the private sector.

5. It also aims to study the policy of encouragement to Foreign Direct Investment by creating an attractive investment climate.

Methodology:

The research work would mostly be based on secondary data obtained from various sources, published work including plan documents. The review of available published work on the subject has also been undertaken for the purpose of the study. The study has used data collection mainly from annual reports of the Ministry of Commerce, Economic Survey of the Government of Saudi Arabia, Census Reports of different years, Commission Reports and other Annual Reports, which are published by government of Saudi Arabia. Data available from international sources like United Nations, OPEC, OAPEC, Middle East Economic Survey (MEES), Middle East Economic Digest (MEED), Middle East Eastern Study, Journal of Energy and Development, Saudi Arabia Monetary Agency and other agencies have also been used.
The methodology used in simple, analytical and involves calculation of percentages, arithmetical averages etc. Contacts and discussions with experts and scholars who are engaged in similar work was also performed. For the depth of analysis simple statistical tools have been used.