SAUDI ARABIA: GAMBLING ON DEEP POCKET POWER

(An analysis of the opportunities and threats involved in the Saudi decision to expand oil production in the face of falling prices.)

Written By
Edward J. Dodson

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Dr. Sandra Featherman
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A WALL STREET JOURNAL report in mid-March characterized the economic impact of recent falling oil prices as follows:

> After a decade of painful price increases blamed on the Organization of Petroleum Exporting Countries, the recent plunge in oil prices has come as a welcome relief to oil consuming nations.
>
> But according to many oil economists and analysts, the price collapse could be setting the stage for another oil crisis far more severe than the ones following the 1973-1974 Arab oil embargo and the 1979 Iranian revolution.[1]

What WSJ and many other observers have similarly described are the complexities of a tremendous gamble being taken by those in control of national policy over oil production and sales in Saudi Arabia. Saudi decisions to increase production and direct a drop in oil prices came about because of impatience and frustration with other O.P.E.C. member nations, from whom they had attempted to secure an agreement to limit production and thus reduce the intrusion on the Saudis' share of the world's oil market.

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Greater production by both O.P.E.C. and other producers (particularly Britain and Norway) created an oversupply of oil in a market hit by energy conservation-consciousness in the industrialized "West" and debt-produced recession in the developing nations. While the Saudis were cutting oil production from around 10 milion barrels a day to 2 million (losing three-quarters of its income), the British increased production to near full capacity. Late in 1985 the Saudis finally made their move, increasing their own production and forcing prices down even further in an effort to recapture its market share and at the same time drive out competitors whose cost of production is much higher.

The question to be analyzed is whether this was, in fact, a wise long-run decision for the Saudis. What are the immediate costs and benefits and the risks involved? Are they in a "win win," "win now/lose later" or a "no win" situation? The strengths and weaknesses of the Saudi political economy result in a decision-making structure that is in many ways unique and have a strong impact on the course of its domestic and foreign policies; it is therefore relevant to examine Saudi society and how it functions if we are to reach any conclusions about these decisions.

GEOPOLITICAL POWER IN THE DESERT

The Saud family has maintained tight control over Saudi Arabia's 8 million people and land, its rise to power going back to the eighteenth century and an alliance with the Islamic reformer, Mohammed ibn-Abd-al-Wahab. Surviving brief periods of domination by the Egyptians and Turks, by 1926 the Saud family under King Ibn Saud had regained control of the Arabian peninsula and expanded the nation's territory to its present boundaries. The appearance of oil as an important element in Saudi geopolitics occurred during the 1930s, when the the ruling family entered into a 50-50 joint partnership with several American oil companies. By 1965 the ruling family was receiving oil royalties of $300 million annually.[2]

Within Saudi society this oil-derived revenue has historically been valuable as a source of tribute for distribution to important tribal chieftains and sheikhs in return for continued allegiance. Members of the Saud family have themselves gained reputations as lavish spenders and consumers of great amounts of wealth. Their exploits have been the subject of much media coverage and criticism during the last half century.

Until the late 1940s the Saudis were essentially isolated from the lifestyle produced by the industrialization their oil resources had fueled. Then came the recognition in 1948 of the state of Israel in the very heart of the Middle East. The Saudis broke with other members of the Arab League, who (lead by Syria, Iraq and Jordan) wanted to cut off oil production in reaction to the partitioning of Palestine and the creationof the Jewish state. Saudi loyalty to United States business interests was acquired by secret agreements "whereby the taxes formerly paid [by international companies] were transferred between the companies and the U.S. government to the treasuries of the House of Saud."[3] Oil production and Saudi revenues during these early post-war years was substantial enough to fulfill the desires of those who held power, but were nothing like that required to bring the Saudi nation into the modern world. By 1944 total oil production reached 7.8 million barrels (less than the daily production of the late 1970s) and brought the Saudi "government" $1.7 million in royalties. This grew to 174 million barrels in 1949 and a more significant inflow of $50 million in revenue. Only a year later the revenue take had more than doubled to $111.7 million and production would rise and fall as the world economy experienced boom or contraction.

There were apparently two reasons why American oil companies agreed to a significant increase in royalty payments to the Saudis. The first was dictated by U.S. foreign policy designs, as expressed by George McGhee (at the time the Assistant Secretary of State for Near Eastern, South Asian, and African Affairs) in testimony before the U.S. Congress:

> At this time, the principal threat to the Middle East lay in the possibility of nationalist leaders moving to upset regimes which were relatively inept and corrupt, and not attuned to the modern world.[4]

Because U.S. political strategies deemed it necessary to promote stability in this area, the corporations were permitted to deduct royalty payments not as business expenses but as direct tax credits, which brought oil company taxes paid to the U.S. Treasury to "nearly zero."

What is perhaps most amazing is that the Saudis somehow survived what in past centuries or even recent decades would have been a sure takeover attempt by the more powerful nations, whose track records for concern over rights of native peoples has never been a serious foreign policy consideration. The following view reflects a fairly common expression of viewpoint by Westerners:

> The worldwide energy crisis is not a problem of absolute shortages of resources. It is a political crisis over who shall control these resources; who shall decide where, when, and how they are to be distributed; and who shall share in the enormous revenues. The struggle for control of the world's resources is just beginning. The emerging consciousness that the riches of the earth are not infinitely exploitable, that the cost of producing, distributing, and consuming them can no longer be set by the industrial nations, and that indeed such nations must compete with one another for natural resources to maintain their increasingly similar standards and styles of living marks a new stage in world politics. It is a time of danger because the capitalist countries may well be tempted to use military power to offset their declining economic power. But it is also a time of possibility. It is now clear that a death sentence hangs over millions unless there is a radical redistribution of the riches of the earth in this generation. It would be naive to underestimate the power and determination of the old cartelists -- the energy companies, and the military establishments that protect them -- or of the new cartelists -- the shahs, sheikhs, and the bankers who serve them -- to preserve their hold on world resources. But it would be more naive to underestimate the pwoer and determination of those who struggle for survival.[5]

Saudi power seems to have survived and expanded at the expense of those who have desired to forever manipulate Middle East politics and economics for self-interest. In return for guaranteeing a uninterrupted supply of oil to Western industry, the entrenched oligarchy of the Saud family would be supported and catered to -- because it was in the interest of U.S. national security. Perhaps. The question of where national interest and special interest began and ended has been more difficult to determine. The Saudis would not have to wait long to receive a taste of the potential consequences should they decide not to play the game as the Western powers desired.

The first great shockwave in the Middle East occured in 1956. Egypt, under Gamal Abdel Nasser had been working since 1952 to build a unified Arab movement of neutrality in the war of nerves between the Soviet bloc and the West. As part of this strategy, Nasser ordered Britain out of its Suez base and, when Egypt was attacked by Israel (Israel's forces backed by both Britain and France), Nasser was forced into a position of dependency on Soviet arms and assistance when the terms of United States aid came with conditions Nassar could not accept and maintain his vision of Arab independence. The United States retaliated by withdrawing aid for the construction of the Aswan dam; Nasser retaliated by nationalizing the Suez Canal. Arab nationalism was growing rapidly.

Elsewhere, Arab workers began to strike against the oil companies. Saudi Arabia had its share of labor unrest, and the disruptions were put to an end by the use of troops (arms coming from the United States). King Saud acted swiftly, suppressing all trade union or political activity.

In this volitile environment President Eisenhower opposed military intervention against Nasser because he saw this would only enhance Nasser's power with those in the Arab nationalist movement. Thus, in a certain twist of historical trend, Eisenhower publicly opposed British and France efforts to restore colonial domination in the Suez; this political move worked well for the United States. As a result, American dominated oil companies essentially inherited control from England and France over Middle East oil.[6] (Not much later, Eisenhower and his advisers would take a very different stance with regard to the crumbling French empire in Southeast Asia.) American foreign policy efforts now were shifted to uniting Saudi Arabia and Iraq against international communism, which (whether real or contrived) put the Saudis in a role of dependence on the United States for arms and economic aid.

At the same time, the Israeli leadership -- faced with severe financial and economic pressures -- contemplated expansion of its territory at the expense of Arab lands. The anticipation of a solution achieved by force was growing stronger on both sides. In 1958 Nasser engineered the formation of the United Arab

Republic, further increasing Arab nationalistic prestige; and, in 1960, the finance ministers of the oil-producing countries met in Baghdad to discuss common problems and Arab foreign policy. OPEC was one result of this meeting.[7]

The Arab nations, and the Saudis in particular, were at the dawn of a new era in which freedom from foreign domination would come with a growing core of Arab technical experts who were receiving engineering, economics and finance educations in the West. One of the most able was Abdullah Tariki who, after a U.S. education at the University of Texas, returned to Saudi Arabia in 1954 to become the first Director General of Petroleum Affairs. In his case, one man certainly made a tremendous difference:

> As the person responsible for government relations with Aramco, Tariki's dedication to work -- to educating the public about oil affairs, to improving the terms of the concessions and opening up positions for Saudis in the company management, to using the country's wealth for the benefit of all the people -- made him stand out in the Saudi regime, where venality and corruption were the rule, where no administrative structure existed, and where power and influence depended on one's lineage in the Royal House of Saud.[8]

Tariki was instrumental in the early formation of OPEC and was an ardent supporter of total nationalization of Saudi Arabia's natural resources. Under Tariki's direction during the 1960s, the method of determining revenue sharing was gradually revised to the benefit of the Saudi government. Saudi Arabia then experienced a struggle for political power between brothers Saud and Faisal; with U.S. backing Faisal staged a successful coup and became prime minister. Tariki was soon dismissed and then exiled from his country (eventually settling in Lebanon to work as an oil consultant). As far as American interests were concerned, the nation was back in safe hands.

Faisal's immediate task was to diffuse his opposition. He began by sharply reducing the royal household budget -- which had historically consumed most of the nation's oil revenues. His method of consolidating his power included public beheadings of political opponents and the purging of the army and air force. He also took steps to build up a modern police state designed to control all political activity. A U.S. House Foreign Affairs Committee report of 1965 looked upon Faisal's activities with considerable satisfaction:

> After a generation in which oil revenues were not turned to proper account, Saudi Arabia now appears to be assuming a responsible attitude toward economic development. Strenuous efforts are being made to diversify the economy.[9]

Then came the 1967 Arab-Israeli War. A strike occurred against Aramco on June 25, 1967. In an effort to control the dissent, a large number of Palestinian workers were deported from Saudi Arabia. Still, a show of Arab unity was required, so all oil shipments were suspended for a time and an embargo placed on shipments to the United States and Britain. The Saudis quickly became worried about the loss the oil revenue and negotiated an end to the embargo, obtaining concurrence from Egypt after agreeing to a $400 million annual aid program for Egypt in return for Nassar's support. Pressure within all the Arab states to nationalize oil production increased with the Israeli victory. Saudi Arabia pushed hard for a different course of action, negotiating an equity interest in Aramco. This was the beginning of Saudi plans to make major improvements in its own infrastructure and to become a net exporter of manufactured goods as well as of oil. In the meantime, the Saudis would channel surplus revenues into profitable foreign investments.

In mid-1972 the Saudi finance minister, Sheikh Zaki al-Yamani, went public with this plan in an address before the Middle East Institute, proposing that "the United States give tariff preference for Saudi oil imports, direct investments in refining, and other oil industry activities," in return for which the Saudis would "commit itself to a production level of at least 20 million barrels per day" (a level equivilent to all Middle East production in 1972). The American companies signed the agreement in October and it was ratified by the Saudis in December.

A number of events in the world economy brought chaos to the oil market in 1973. Early in the year prices began to climb because of rising demand for low-polluting (i.e., low sulphur) crude oil, particularly in the environmentally-conscious United States. The Saudis continued their policy of accommodation because, as Faisal, stated:

> We are thinking in terms of economic cooperation and shared interests in the financial sphere. As is always the case in international relations, whenever mutual

> interests exist between two countries in the economic field very strong political relations immediately develop.[10]

On the other hand, the natural temptation to control markets and, hence, prices has always been a fundamental desire of suppliers and producers. Adam Smith, in THE WEALTH OF NATIONS, warned that "People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices." The Saudis were being accomodating; however, in their relatively brief exposure to international business and geopolitics they had learned the value of tough negotiation. And so, in May 1973 the United States concluded an informal agreement encouraging both Saudi investments in the United States and reciprocal assistance in developing the Saudi economy.

SAUDI INDUSTRIALIZATION

Under the new arrangement, increases in Saudi production were to be tied to "large-scale technical assistance to help industrialize the Saudi economy."[11] However, the U.S. influence over the Saudis in staying out of the Arab-Israeli conflict was lost because of a new Arab unification initiative made by Egypt's new leader, Anwar Sadat. In April 1973 Yamani, the Saudi oil minister, visited the United States in an effort to convince U.S. policymakers not to continue shipping arms to Israel. Yamani let the Americans know that oil production might be used as the Saudis' foreign policy weapon. On October 6, 1973, Egypt and Syria launched their attack against Israeli forces in the Sinai Peninsula. Sadat and the PLO increased pressure on Faisal to initiate an embargo against the United States; the result was an initial, tentative 5 percent cut, then an additional immediate cut of 10 percent. Following the announcement by the U.S. of a $2.2 billion aid bill to Israel, the Saudis followed other Arab countries in the embargo against the United States. To do otherwise might have meant political suicide for Faisal among his Arab neighbors.

The cease fire between the Egyptian and Israeli forces in November brought the problem to the negotiating table. The price of OPEC oil at January 1, 1974 had risen to over $11, a 470 percent increase in just one year. In the United States, oil stocks kept moving upward; however, non-energy consumner spending for began to fall precipitiously and the world economy slipped toward recession. OPEC members then met in March to discuss lifting the embargo and the raising of prices. At this meeting Yamini expressed his view that "prices were already too high and that they should be reduced so as not to jeopardize the economic and political stability of the industrialized capitalist countries."[12] One reason for the Saudi stance was U.S. government assistance in pushing American corporations to assist in Saudi economic development and to channel Saudi oil revenues into U.S. securities and markets. These oil revenues totalled around $17 billion in 1974; while significant, a breakdown in the distribution of revenues on oil products is revealing:

	1974	1973
Producing country	40%	17%
Consuming country (taxes)	36	54
Oil companies	24	29

One immediate impact on the Saudi Arabian people was a doubling of food imports from the United States between 1973-74. Up until 1974, however, the distribution of oil wealth had had little impact on the life of the average Saudi. Military and internal security budgets had greatly expanded, but the nation was not at all equipped to undertake large development projects. The country's economic development was actually in the hands of the Stanford Research Institute; almost nothing had yet been done in terms of real infrastructure.

Saudi society has undergone a rapid rate of change during the last decade. Industrialization and a greatly increased standard of living for the Saudi citizen have occurred, but most of the technical and manual work has been performed by 2.6 million workers brought into the country. The impact of these changes is partially reflected by economic and budgetary figures.

During 1981-84 the Saudis allocated $550 billion for infrastructure and industrialization development. At the same time they retained $100 billion in foreign reserves. A substantial portion of these monies were utilized for the creation of two new industrial cities projected to create 144,000 new jobs for Saudi citizens by the year 2000. The emphasis toward domestic industrial expansion is reflected in restrictions on foreign investment which no longer permits companies to come in for a quick profit and then leave. Foreign companies must now made long-term commitments of time, resources and TECHNOLOGY TRANSFER. One result of these efforts has been an average per capita income in Saudi Arabia of $14,000.

A five-year developmental plan for 1985-90 has been adopted with a projected cost of $277 billion. Around $190 billion is to be allocated to civilian spending and the remainder to defense. This plan also calls for the reduction of government involvement in the economy, replacement of foreign workers with Saudis and absorption of Saudi women into the workforce. Faced with a continuing decline in oil revenues during 1984-85 the Saudi government took various measures to reduce expenditures, including a reduction in the number of subsidies on consumer goods, salary cuts for government employees and the removal or reduction of housing, medical and travel allowances.

The government has also moved to increase the domestic content of business contracts. In early October 1984 it was announced that 30 percent of the value of any single contract had to be subcontracted to companies which were wholly Saudi-owned. A decree issued by King Fahd in mid-June of 1985 subsequently ruled that all non-construction contracts would be awarded to Saudi firms. Tariffs on durable imports were increased from 4 percent to 7 percent beginning with the start of the fiscal 1986 year.[13] These measures seem to reflect an economy in trouble and a government concerned about DEFICITS. An evaluation of the Saudi economy by Daniel Yergin and Martin Hillenbrand a few years ago reached an opposite conclusion:

> Because of low demand for foreign goods compared to earnings, Saudi Arabia is able to scale down its oil production without hurting its own growth.[14]

This seems to be supported by a BUSINESS AMERICA report concluding that "declining Gross Domestic Product growth is less meaningful in the current Saudi context than it would be elsewhere in the world because Saudi Arabai's roads, communications, and basic infrastructure are now largely in place."[15] That is a tremendous achievement within the span of only a decade.

Net foreign assets held by the Saudis rose from $4.2 bilion in 1973 to $67.3 billion in 1978, to $118.2 billion in 1980 and were at $161.6 billion by the end of 1981.[16] In fact, the Saudis held 40 percent of the total net asset position of all the OPEC oil countries combined. Yergin and Hillenbrand have concluded that

> The different demand patterns of the OPEC countries are important for their investment objectives and strategies. The first objective is always to maintain the country's international liquidity under circumstances of fluctuating foreign exchange revenues and expenditures. This is the typical purpose for keeping foreign exchange reserves.
>
> Saudi Arabia will, as a rule, devote only part of its total financial surpluses to monetary reserves. The rest, perhaps the greater part, will be invested with a view to spending the money in the future to import goods and services and/or to secure a continuous stream of income in the face of depleting oil reserves. The actual investment strategy depends on the development strategy pursued. Priority is always given to the development of the domestic economy. Saudi Arabia considers the accumulated foreign assets as a kind of deferred expenditure, to be spent developing their country. With this fairly defined time period, the preference will be towards fixed income instruments.[17]

A number of investments in existing businesses seem to go against the above investment strategy until one understands that many individual Saudis are extrementlly wealthy. Saudi interests have acquired three Hilton Hotels in North Carolina and the brokerage firm of Smith Barney. The nation's investments are managed by the Saudi Arabian Monetary Agency, which (unlike its Kuwait neighbor) has made minimal investments in European or North American real estate and generally keeps its equity participation in United States firms below 5 percent. Although not significant to the Saudi portfolio, a number of other investment choices are interesting because of their diversity:

Industrial Park (Salt Lake City, Utah	$750 million
Arizona Land & Cattle Company, Phoenix, Arizona (15%)	250 million
First National Bank of San Jose, California (33%)	14 million
Security National Bank of Walnut Creek, California (96%)	12 million
Bank of Contra Costa, Calif. (57%)	14 million

SOURCE: Saturday Review, January 25, 1975

Saudi strategy for at least the last decade has thus been to strive for independence from its oil clients by an accelerated devellopment of infrastructure, diversification of its domestic economy and the minimization of risk in foreign investments. There are now two scenarios to pursue. The first is a look at what did not occur and what the probable consequences might have been HAD the Saudis followed a path of least resistance. Second, I will attempt to forecast the future based on the path they have taken.

THE PATH OF LEAST RESISTANCE

From late 1981 until late October of 1985 the price of crude oil settled down to around $28 per barrel. Increased production by Britain, Norway and other producers was putting downward pressure on the price. The Saudis were pumping around 2.2 million barrels/day which, at $28 would generate $22.5 billion in annual revenue. Assuming the Saudis' primary goal would be to sustain this revenue flow at the lowest production level required, and that the weighted average price of oil would drop by $2 each year after 1986, the adjustments to production would be roughly as follows:

TOTAL REVENUE (R) = $22.5 Billion, or
$22,500 Million

VARIABLES: X = millions of barrels/day
Y = price/barrel

Both "R" and "Y" are knowns; we are seeking to determine how many barrels must be produced each day to maintain a constant revenue inflow.

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The formula to find "X" in the base year is Total Revenue (R) divided by 365 [in order to arrive at daily revenue], the result of which is divided by the current price per barrel (Y). Thus, for 1986 the calculation would be as follows:

(1) $X_0 = \frac{22,500/365}{28}$ (3) X_0 = 2.2 million brls/day

(2) X_0 = 61.64/28

From the 1986 base year figures, subsequent production levels can be determined by simply substituting the present year weighted average price per barrel. Given our assumptions this results in a 1987 price of $26, a 1988 price of $24, and so on. Production levels derived under these conditions through 1995 are shown below.

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\begin{array}{llll}
1986: & X_0 = (R/365)/Y & ---- & X_0 = (22{,}500/365)/28 \\
 & & ---- & X_0 = 61.64/28 \\
 & & ---- & X_0 = 2.2 \text{ mb/day} \\
1987: & X_1 = X_0(Y_0/Y_1) & ---- & X_1 = 2.2(28/26) \\
 & & ---- & X_1 = 2.2(1.08) \\
 & & ---- & X_1 = 2.38 \text{ mb/day} \\
1988: & X_2 = X_0(Y_0/Y_2) & ---- & X_2 = 2.2(28/24) \\
 & & ---- & X_2 = 2.2(1.167) \\
 & & ---- & X_2 = 2.567 \text{ mb/day}
\end{array}
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\begin{array}{llll}
1995: & X_9 = X_0(Y_0/Y_9) & ---- & X_9 = 2.2(28/10) \\
 & & ---- & X_9 = 2.2(2.8) \\
 & & ---- & X_9 = 6.16 \text{ mb/day}
\end{array}
$$

Only a few short months ago the suggestion that crude oil prices might drop from around $30 per barrel to as low as $10 per barrel by 1995 would have been given a near zero probability. In hindsight, however, the world's expanded production capacity, discovery of new fields and heightened energy consciousness lend credibility to this scenario. As the Saudis have shown, they are fully capable of pumping well over 6 million barrels a day and, based on current estimates of reserves, would still be able to meet this level in the mid-1990s.

There are several other key variables to be considered in this analysis. At issue is whether the Saudis would be able to generate sufficient revenues to finance the national budget without incurring a deficit (and, hence, eating away existing financial reserves). Again, a number of critical assumptions must be made based on current reported Saudi assets, budget estimates and income from oil and non-oil related production. For 1986 the Saudis have reported a $55 billion budget which is acknowledged will generate a $12 billion deficit. Total foreign investments are estimated to be worth $106 billion, plus a reserve of $60 billion in liquid assets (U.S. government securities, etc.). The Non-oil related sector of the Saudi domestic economy has forecasted revenues of $7.2 billion.

For purposes of estimating Saudi cash flow and national assets, it is assumed that the market value of foreign investments (i.e., real estate, corporate holdings, etc.) will average a 10% annual increase and yield a positive cash flow of 8% return on current value. Saudi reserves are also projected to yield an 8% average return. Although the latest Five Year Plan looks for an average increase in domestic productivity of 5.9% we will use 3% here; however, based on the reduction in infrastructure requirements and expansion of the private sector we will also forecast a constant 3% reduction in the national budget. For purposes of simplicity all figures are assumed to be adjusted for inflation.

	1986	1987	1988	1989	1990	1991	1992	1993	1994
REVENUES:									
Oil	$22.5	$22.5	$22.5	$22.5	$22.5	$22.5	$22.5	$22.5	$22.5
ForInv	8.5	9.3	10.3	11.3	12.5	13.7	15.1	16.6	18.3

FinRes	4.8	3.8	3.0	2.3	1.8	1.5	1.6	1.9	2.4
DomRev	7.2	7.4	7.6	7.8	8.0	10.0	10.3	10.6	10.9
TOTAL REV	43.0	43.0	43.4	43.9	44.8	47.7	49.5	51.6	54.1
(Budget)	-55.0	-53.4	-51.8	-50.2	-48.7	-47.2	-45.8	-44.4	-43.1
NET +/-	-12.0	-10.4	-8.4	-6.3	-3.9	+.5	+3.7	+7.2	+11.0

As the above table reveals, the Saudis would have experienced a gradual loss of financial reserves as a result of five straight years of budget deficits. By the end of 1995, however, reserves would have climbed back to $56.7 billion. The Saudi cash flow and financial reserves/physical capital at year end 1995 would have appeared as below:

(billions of dollars)

REVENUES:			
Oil Production	$ 22.5	Oil Reserves	$1,600*
Foreign Investments	20.1	Foreign Inv.	277
Financial Reserves	3.3	Financial Reserves	57
Nonoil Domestic Inc.	11.2	Domestic Capital	373
TOTAL REVENUE	$ 57.1	TOTAL WEALTH	$2,307
Budget Expenditures	-41.8		
SURPLUS	$ 15.3		

*Saudi Arabia possesses approximately 25% of the world's known oil reserves of some 640 billion barrels, or 160 billion barrels. At the forecasted $10/barrel 1995 prices these reserves would have a market value of $1,600 billion.

The above analysis supports the conclusion that the Saudis' overall economic development is firmly established; therefore, drastic cuts in its domestic program spending were not needed to ensure long-term growth. Lower crude oil prices, gradually obtained as a result of supply/demand relationships in the market were offset by higher oil production. At the same time, the lower energy costs stimulates worldwide economic activity and the Saudis' own return on foreign capital investments. Had they followed this course of action the Saudis would have experienced a "win/win" situation by both preserving oil-generated revenues and maintaining growth elsewhere.

The course actually followed is much more difficult to forecast into the future or to evaluate because of the intense political ramifications involved. Saudi Arabia has very quickly influenced the price of oil by its increase in production from the 2.2 million barrels per day used in the above scenario to around 4.5 million barrels per day presently (April 1986). Moreover, the rapid drop in oil prices has had a complex effect on the world economy. The large money center banks with loans outstanding to Mexico and to international oil firms are threatened by massive defaults (oil revenues have been a primary sources of foreign currency for Mexico, whose economy is now at a standstill). Oil and gas industries that expanded on the assumption of continually rising oil prices are cutting back on exploration, research and development, and are reducing their workforces by the thousands. As unemployment rises in the "oil belts" of the United States and elsewhere, real estate foreclosures are increasing and land values falling; new office buildings remain empty and existing ones drop rents as the competition for tenants increases. In areas where the economic base is highly diversified there is considerable optimism and economic growth. Depending on where you sit the signs look either mighty good or downright terrible. With the rise and fall of OPEC we have probably seen the end of the "national economy." The global economy has flexed its muscles and shown us its might. Thus, at this point whatever assumptions are made about the Saudi economy are fraught with pitfalls. What my research has shown is that Saudi Arabia is far better positioned to weather the storm than many other nations, particularly those who have not had the benefit of sitting on an ocean of oil.

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[3] Joe Stork. MIDDLE EAST OIL AND THE ENERGY CRISIS [London: Monthly Review Press, 1975] p.46.

[4] Ibid., p. 47.

[5] Ibid., pp. ix-x. From the INTRODUCTION written by Richard J. Barnet.

[6] In March 1957, Congress passed legislation authorizing up to $200 million for economic and military aid and a commitment of United States troops to any nation in the Middle East that requested U.S. support against "armed aggression" from "any country controlled by international Communism." The major impact of U.S. policy initiatives was, however, felt by its NATO allies, Britain and France. Source: Blanche Cook. THE DECLASSIFIED EISENHOWER [NY: Doubleday & Co., 1981], p.188.

[7] The original members of the new Organization of Petroleum Exporting Countries included Saudi Arabia, Kuwait, Iraw, Iran, and Venezuela.

[8] Joe Stork. pp. 89-90.

[9] Ibid., p.110.

[10] Ibid., p.207.

[11] Ibid., p.209.

[12] Ibid., p.243.

[13] Kessing's Contemporary Archives [Harlow, England: Longman Group, Ltd., 1985. Vol. XXXI, No. 11], p.34013.

[14] Daniel Yergin and Martin Hillenbrand. GLOBAL INSECURITY [Boston: Houghton Mifflin Co.; 1982], p.313.

[15] Elise Kleinwaks. "Saudi Arabia: Services and Technology in Demand as Market Matures." BUSINESS AMERICA [Washington: U.S. Department of Commerce, Vol.9, No.6, March 17, 1985], p.34.

[16] Susan Bluff. "OPEC's $350 Billion Balance Sheet," EUROMONEY. September 1980.

[17] Yergin and Hillenbrand. p.314. The authors refer to the Saudi state as a "low absorber" because of its controlled spending during the last decade. They also note that under this investment strategy "fixed income securities of longer maturity are used, the liquidity less important than yield. Other non-financial assets, such as property or precious metals, have also been considered as areas of investment.