

The Price of Oil and the Future of the Saudi Monarchy

By Mamdouh G. Salameh*

The Kingdom of Saudi Arabia is a country of astonishing contrasts where computer print-outs open with the words, "In the name of God," and where men who grew up in goat-hair tents now control more than a quarter of the world's proven crude oil reserves.¹

If it were not for a freak of geology, few people in the world would concern themselves with the well-being of King Fahd, and the United States would not be so closely monitoring internal developments in Saudi Arabia; nor would the Kingdom figure so prominently in the oil geopolitics of the Arabian Gulf.

Under the sands of Saudi Arabia, first conquered by the house of Saud 200 years ago, lie more than 260 billion barrels (bb) of crude oil. More new reserves of very high-quality light crude have recently been discovered in the Hawtah, Hazmiya and Ghinah fields in Central Arabia.²

It is these vast reserves which have enabled Saudi Arabia to emerge as the world's largest producer and exporter of crude oil and there is no reason to expect a change in that position in the foreseeable future.

Upstream and Downstream Capacity Expansion

The Kingdom is currently engaged in what is quite possibly the most expensive oil expansion program in history. Saudi financial sources estimate that wholly state-owned Saudi Aramco, in a program that began in 1988, will have spent \$17 billion by the end of 1995 to raise production and export capacities to 10 million barrels a day (mbd) and 9.12 mbd, respectively. It is projected that by the year 2010, Saudi Arabia will have a production capacity of 12 mbd and an export capacity of 10.45 mbd (see Table 1).

Table 1
Saudi Arabia
Current & Projected Sustainable Production and Export Capacities, 1994-2010
(mbd)

Year	Production Capacity	Export Capacity
1994	9.50	8.65
1995	10.00	9.12
2000	10.70	9.65
2005	11.40	10.12
2007	11.60	10.21
2010	12.00	10.45

Sources: OPEC Statistical Bulletins, Petroleum Intelligence Weekly, Canadian Energy Research Institute (CERI).

Saudi Arabia's strategy is geared toward ensuring that production of Arab heavy crude is kept down to about 15-20% of overall output, thus enabling higher revenue from the much

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¹ See footnotes at end of text.

demand, more expensive and more environmentally acceptable light oil (see Table 2).³

Table 2
Saudi Aramco's Production & Capacity
By Crude Stream, 1995
(mbd)

Type of Crude	Capacity	Current Production
Arab Heavy	1.30	0.60
Arab Light	5.30	5.12
Arab Medium	2.00	1.10
Arab Extra Light	1.10	1.00
Arab Super Light	0.20	0.19
Total	9.90	8.01

Source: Oil Daily's Energy Compass Estimates

The Kingdom is also investing on a global scale. Its long-term target is to acquire up to 3 mbd in overseas refining capacity and outlets, and also an overseas storage capacity of up to 40 million barrels (mb) of crude near the major consuming markets.

The Threat of Financial Shortfall

Meeting these goals will not be easy. Saudi Arabia drew quite heavily on its monetary reserves to finance its share of the 1991 Gulf War to liberate Kuwait, and for the first time in its history had to seek external borrowing and issue domestic treasury instruments to offset budget deficits. The war cost the Kingdom around \$60 billion according to government sources. Saudi budget deficits, made worse by the Gulf War, were fueled by the Kingdom's arms purchases from the United States, estimated at \$25 to \$30 billion, and a reluctance to trim social programs.

There are now considerable doubts over how the expansion program for both production and refining capacities, estimated at \$30 billion, is to be financed. So far, the Kingdom is reported to have borrowed \$5 billion to finance expansion. Further borrowing is to be expected because of the strain on government finances caused by continuing weak oil prices. Earnings from oil exports in 1994 amounted to \$40 billion and were estimated to have risen to \$44 billion in 1995 (see Table 3).⁴

Table 3
Saudi Arabia
Revenue from Crude Oil & Refined Products Exports
1994-95 Actual, 2000-2010 Projected

Year	Price/Barrel U.S. \$	Production mbd	Exports mbd	Revenue \$ billions
1994	15.33	8.04	7.19	40.23
1995	16.88	8.01	7.12	43.87
2000	21.00	9.00	7.95	60.94
2005	23.50	10.00	8.72	74.80
2010	27.00	11.00	9.45	93.13

Sources: OPEC, IEA's World Energy Outlook 1995, Author's Projections.

The Geopolitics of Oil

The political failure of the United States to address the

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Future of the Saudi Monarchy (continued from page 11)

issue of its growing dependence on oil imports from the Gulf has meant that the U.S. had been continuously involved in Gulf politics and its security issues: the key instance is its special relationship with Saudi Arabia.⁵

Today, the U.S. confronts both Iraq and Iran while it is supportive of Saudi Arabia and Kuwait. If, however, Iraq and Iran were both to join hands to counter the U.S. influence in the Gulf, the whole geopolitical situation could change overnight, with very adverse repercussions for both Saudi Arabia and the United States.

These could include a more determined drive to destabilize Saudi Arabia and undermine its royal family through stronger support, particularly by Iran, for the Saudi fundamentalist movement. Iran could also mine or blockade the Straits of Hormuz to stop or hinder Saudi crude oil shipments (as well as United Arab Emirates and Kuwaiti shipments), or join forces with Iraq to mount covert sabotage attacks against Saudi shipping and oil installations in the eastern province.⁶

Another important aspect of the Saudi-U.S. relationship is the succession issue in the House of Saud. The time is coming near when leadership changes could bring to the fore a different set of key princes with difference priorities. If Crown Prince Abdullah becomes the next king, even the new political order in the Gulf could change. The Crown Prince will be less likely to embrace U.S. views on regional politics and may be more willing to mend fences with Iraq, whether or not Saddam Hussein remains in power.

Potential Threats to Saudi Security

The Saudi fundamentalist movement poses the most serious threat to the Saudi ruling family. However, there could also be potential threats to Saudi security from Yemen and possibly Iraq.⁷

Nothing has been more offensive to the sensitivities of the Saudi fundamentalists in recent years than the political fact that Saudi Arabia, the guardian of Islam's holiest places, is itself entirely dependent on a "Christian" nation for its security. Moreover, that "Christian" nation has always been the committed protector of Israel.

But it is the squandering of billions of dollars of oil revenues – and the absence of a system of accountability – that underlies the resurgence of the Saudi fundamentalist movement in recent years and the sharpening of its opposition to the ruling family. Until a few years ago, the Saudi ruling family spent billions of dollars buying off potential enemies; but declining oil prices since 1986 have reduced their export earnings and their ability to fend off enemies and tackle unemployment and other socioeconomic problems facing the country. This situation may not change in the foreseeable future as oil prices are not projected to rise significantly, in real terms, between now and the year 2000.⁸

Then there is the Yemeni threat. In geopolitical terms, Yemen is often referred to as the "soft belly" of Saudi Arabia. If the Saudi-Yemeni territorial dispute is not permanently resolved it will remain a source of conflict between Yemen and Saudi Arabia throughout the 1990s and, in a worst-case scenario, could escalate into a war that could bring Iraq to Yemen's side.⁹

Saudi-Iraqi relations have always been characterized in terms of a struggle for primacy in the Gulf. To Saudi Arabia,

Iraq presents both a potential threat to national security and a rival for supremacy in the Organization of the Petroleum Exporting Countries (OPEC). This uneasy relationship has been complicated by the new political order in the Gulf.¹⁰

Despite these potential threats and financial difficulties, and irrespective of the political orientation of the next Saudi king, the Kingdom will remain the world's oil supplier of last resort and Saudi oil will continue to dominate the global oil markets for at least the rest of this decade.

Footnotes

¹ Robert Lacey, *The Kingdom*, London, Hutchinson & Co. Publishers Ltd., 1981, pp. 4-5.

² *Petroleum Review*, London, July 1992, p. 314.

³ *Platt's Oilgram Newsfax*, 26 April 1994, p. 1.

⁴ *Petroleum Review*, July 1992, pp. 314-416.

⁵ Melvin A. Conant, "The Saudi Dilemma," the *Geopolitics of Energy*, vol. 14, no. 10, 1 October 1992, pp. 1-3.

⁶ Zalmay Khalidzad, "The United States and the Persian Gulf: Preventing Regional Hegemony," *Survival*, vol. 37, no. 2, Summer 1995, pp. 98-99.

⁷ *Financial Times*, Special Report on Saudi Arabia, December 20, 1995.

⁸ Shahram Chubin & Charles Tripp, "Domestic Politics and Territorial Disputes in the Persian Gulf and the Arabian Peninsula," *Survival*, vol. 35, no. 4, Winter 1993-94, pp. 18-21, also *Newsweek*, 27 November 1995, pp. 38-39.

⁹ Mamdouh G. Salameh, "Yemen: A New Oil Frontier or a Flashpoint?," *World Oil Market Analysis*, vol. XII, no. 1, Canadian Energy Research Institute, Calgary, June 1994, pp. 9-14.

¹⁰ Mamdouh G. Salameh, "Iraq: The Emerging Oil Giant," Calgary, Canadian Energy Research Institute, March 1995, pp. 7-8.

News from the Iran Association for Energy Economics, IAEE's Newest Affiliate

IAEE's newest affiliate, the Iran Association for Energy Economics (IRAEE), is off to a fast start. The Affiliate supported *The 1995 International Conference on Oil & Gas Prospects in the Caspian Region* in Teheran, Iran on 10 and 11 December 1995. The conference was organized by the Institute for International Energy Studies (IIES) and the Institute for Political and International Studies.

The conference served as a forum in which the Caspian states and oil and gas organizations explored the grounds for mutual cooperation in the region. More than 400 participants from 40 countries attended.

IRAEE regularly holds educational seminars on energy management. These seminars deal mostly with energy economics in the industries of Iran with the aim of raising energy efficiency and conservation to international levels.

The affiliate is also in the process of implementing an Energy Audit program for the industries of Iran with the aim of determining the optimum energy usage for specific plants.

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