

Saudi Arabia's Emerging Energy Policy:

The Role for U.S. Firms

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Brief Analysis

Spurred by comments made by Crown Prince Abdullah during his October visit to the United States, U.S. oil firms have high hopes that they may be able to become more active in Saudi Arabia. Last week, Secretary of Energy Bill Richardson visited the kingdom to discuss the issue, with mixed results. The future foreign role in Saudi energy will depend upon two significant trends underway in Saudi Arabia -- namely, the transfer of power to the crown prince and the plummeting revenue caused by lower oil prices.

The Royal Family Listens to Experts

Energy policy provides an important example of the professionalism that has characterized the crown prince's regency. In stark contrast to the favoritism and accommodation that symbolized the awarding of contracts in the late 1970s under former Saudi Oil Minister Zaki Yamani, Crown Prince Abdullah has delegated power to an oil committee stacked with energy, economics, and legal experts. The heir to the throne seems prepared to abide by its recommendations. He has won the support of a majority of the influential senior princes -- such as Prince Sultan, Prince Nayef, Prince Salman, and Prince Ahmad -- for allowing this committee much authority.

In some ways, the new special committee revives the concept of consultation embodied in the Higher Petroleum Council that was established by the late King Faisal in 1973 to supervise the then-burgeoning petroleum community and to formulate national policy. The council, although it still exists, has been moribund for the past decade. The new committee's membership is broader than that of the still-existing council, as it includes two ministers of state -- one who represents the conservative religious establishment, the other, the emerging generation of public servants. Furthermore, the appointment of the minister of industry and electricity to the committee demonstrates the government's willingness to open up the electric industry -- which needs \$120 billion in new capital projects before 2015 -- to foreign investment.

The signs are, however, that the new committee is not so excited about foreign investment in oil production in the short term. With 2 million barrels per day (bpd) of spare Saudi production capacity and an extremely weak market, there is little reason for any large petroleum development projects. Moreover, during his recent visit, Secretary Richardson was treated to a day-long journey to the kingdom's empty quarter to see how Saudi Aramco engineers had developed the 14.3-billion-barrel Shaybah oil field without any foreign expertise. The message was crystal clear: no foreign investments in petroleum production for the foreseeable future.

Prospects for Foreign Investment in Non-Oil Energy

Whereas foreign investment in oil production may not be in the cards, Saudi attitudes are entirely different about foreign financing for the tens of billions of dollars in needed downstream petroleum projects and natural gas, power, and desalination plant expansion. The principal reason that foreign firms may be interested is that the Saudis are holding out the tantalizing possibility of future contracts in the oil sector. "Those who invest in developing the industrial base of Saudi Arabia," Oil Minister Ali Al-Naimi said last week, "will probably be the ones who will be

invited when and if the upstream [oil sector] is available." The stakes are so high -- Saudi Arabia has by far the world's largest proven oil reserves, worth over \$2.7 trillion at the current depressed prices -- that, as one senior American oil executive remarked, "No one could say no."

Of course, if demand for oil begins to outpace supply, then the kingdom will undoubtedly seek outside investments to finance developing its vast petroleum fields. Those companies most deeply entrenched in natural gas production and downstream petroleum operations will be best positioned to win these extremely lucrative contracts. The Exxon Corporation -- after having absorbed Mobil, with its \$8 billion already invested in the kingdom's petrochemical industry -- is the most likely candidate to grab the lion's share of any future offerings.

The strategic relationship between the United States and Saudi Arabia has not always been rosy and trouble-free. A major impediment has always been misconceptions about each others' political culture. A case in point: Two weeks ago, Chevron chairman Kenneth Derr, on a tour of the Gulf, opined, "It would be in the interest of Kuwait to move on this [accepting U.S. oil upstream investments] as promptly as possible so that companies can make their decisions." Although this remark went unnoticed in Kuwait, it raised numerous eyebrows in Riyadh, because it implied that a Gulf country should alter its political processes to meet the needs of U.S. firms. Were the Saudi government to perceive itself as being under pressure from U.S. firms, the Saudi leadership might very well then have a change of heart about the U.S. role, deciding instead to award the bulk of any future contracts to European firms.

MEMBERS OF THE OIL COMMITTEE

NAME	POSITION	RANK
Crown Prince Abdullah	Regent	Chairman
Prince Saud Al-Faisal	Minister of Foreign Affairs	Secretary-General
Dr. Ibrahim Al-Assaf	Minister of Finance & Economy	Member
Eng. Ali Al-Naimi	Minister of Oil & Natural Resources	Member
Dr. Hashim Yamani	Minister of Industry & Electricity	Member
Dr. Mohammad Al-Sheikh	Minister of State	Member
Dr. Musaed Al-Ayban	Minister of State	Member

Nawaf Obaid, a graduate student at Harvard University, is a visiting fellow at The Washington Institute, preparing a study on Saudi petroleum policy.

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