

# Chapter 9

## Foreign Trade: Changing Composition and Direction

*Commerce is the equalizer of the wealth of nations.*

Gladstone

### Learning Outcomes

*By the end of this section, you would understand:*

- *The need to trade for Saudi Arabia*
- *The composition and evolving patterns of imports*
- *The changing origins of imports*
- *The importance of the export sector*
- *The dominance of the oil sector*
- *The need for efficiency and competitiveness in the export market*
- *Saudi Arabia's trade and balance of payments*
- *The need to establish trade competitiveness best practices*

### Introduction

Saudi Arabia leads the Arab world in exports and imports, and ranks among the top five in the Islamic world, along with Malaysia, Turkey, Indonesia and the UAE (Wilson, 2003). This chapter discusses the various aspects of foreign commerce, principally imports and exports; we will look at how the composition has changed over time as well as their impact on the Kingdom's balance of payments. We will closely examine Saudi exports to assess the success of the economic diversification programme to date, as well as to analyse Saudi product export competitiveness. The final section of the chapter sets out model guidelines for a more effective export promotion programme to help the private sector achieve the country's economic diversification goal.

Why does Saudi Arabia need to trade? Economic theory postulates that countries trade with each other based on either absolute or comparative advantage. In trade,

countries specialize in exporting commodities where specialization gives them cost-of-production advantage. Saudi Arabia, with large, homogeneous and low-cost oil fields, undoubtedly has a comparative advantage over other high-cost oil producers. But it does not have an absolute advantage, for the Kingdom never had to make the choice of producing non-oil products, and as such there was no opportunity cost or alternatives forgone (Wilson, 2003). There was no trade-off between oil and non-oil production, but rather a positive relationship between oil exports and revenues and imports, with imports rising during oil booms and remaining static or declining in oil depressions. The next major challenge for the Kingdom is the expansion of Saudi Arabia's export base into other finished and semi-finished products not directly related to oil. It will be based on production efficiency and specialization, in competition with similar products produced worldwide. This will not be easy. According to the World Trade Organization (WTO), the Middle East and North African countries have seen their share of global trade diminish. This is illustrated in Table 9.1 for the period 2005–2007.

**Table 9.1** GDP and merchandise trade by region, 2005–2007 (Annual percentage change at constant prices)

	GDP			Exports			Imports		
	2005	2006	2007	2005	2006	2007	2005	2006	2007
World	3.3	3.7	3.4	6.5	8.5	5.5	6.5	8.0	5.5
North America	3.1	3.0	2.3	6.0	8.5	5.5	6.5	6.0	2.5
United States	3.1	2.9	2.2	7.0	10.5	7.0	5.5	5.5	1.0
South and Central America	5.6	6.0	6.3	8.0	4.0	5.0	14.0	15.0	20.0
Europe	1.9	2.9	2.8	4.0	7.5	3.5	4.5	7.5	3.5
European Union (27)	1.8	3.0	2.7	4.5	7.5	3.0	4.0	7.0	3.0
Commonwealth of Independent States	6.7	7.5	8.4	3.5	6.0	6.0	18.0	21.5	18.0
Africa and Middle East	5.6	5.5	5.5	4.5	1.5	0.5	14.5	6.5	12.5
Asia	4.2	4.7	4.7	11.0	13.0	11.5	8.0	8.5	8.5
China	10.4	11.1	11.4	25.0	22.0	19.5	11.5	16.5	13.5
Japan	1.9	2.4	2.1	5.0	10.0	9.0	2.5	2.5	1.0
India	9.0	9.7	9.1	21.5	11.0	10.5	28.5	9.5	13.0
Newly industrialized economies <sup>a</sup>	4.9	5.5	5.6	8.0	12.5	8.5	5.0	8.5	7.0

<sup>a</sup>Hong Kong, China; Republic of Korea; Singapore and Chinese Taipei

Source: WTO Secretariat

Exports from North America declined, as did those from Europe, but imports rose for the Middle East and India.

## The Causes of Trade

From an economic perspective, the case for freer trade rests on the existence of gains from trade and most economists typically agree that there are gains from trade. In recent years, however, free trade has increasingly come under fire and it is not uncommon to hear trade sceptics say that economists' arguments in favour of

free trade and in particular comparative advantage may have been valid at the time of Ricardo (in the early 19th century) but that they are no longer valid in today's globalized world. Most trade models are designed to answer two closely related questions: what goods do countries trade and why?

The idea that there are gains from trade is the central proposition of normative trade theory. The gains from trade theorem states that if a country can trade at any price ratio other than its domestic prices, it will be better off than in *autarky* – or self-sufficiency. More generally, the basic gains from trade propositions are that (i) free trade is better than autarky; (ii) restricted trade (i.e. trade restricted by trade barriers) is better than autarky; and (iii) for a small country (i.e. a country too small to influence world prices) free trade is better than restricted trade. Samuelson (1939) showed that there are potential gains from trade for small countries provided world prices diverge from autarky prices. Kemp (1962) showed that restricted trade is better than no trade. He also extended the argument to the large country case, proving that free trade is potentially superior to autarky, in the case when there are many commodities and factors and with variable factor supplies. As noted by Deardorff (1979), most treatments of the gains from trade say that if trade could potentially benefit all members of a country's population (assuming their preferences and income were identical), it is regarded as benefiting the country because some form of income redistribution among the country's consumers is assumed to be feasible.

These basic propositions about the gains from trade, however, are not the end of the story. First, as pointed out by Corden (1984), the divergence between autarky and free trade prices is only an approximate explanation of the gains from trade. A full explanation of those gains should link them to the causes of trade – that is, to the elements that give rise to divergence between autarky or self-sufficiency and free trade prices. Those elements are the ones that lie behind the sources of comparative advantage. They would include differences in technology or differences in endowments. Second, economic theory points at other forms of gains from trade that are not linked to differences between countries. In particular, countries trade to achieve economies of scale in production or to have access to a broader variety of goods. Also, if the opening up of trade reduces or eliminates monopoly power or enhances productivity, there will be gains from trade additional to the usual ones. Finally, trade may have positive growth effects.

Table 9.2 provides a simplified summary of some of the basic characteristics of different trade models to illustrate the diversity of opinions on the subject.

Traditional trade theory emphasizes the gains from specialization made possible by differences among countries. The main contribution of this strand of thought is that opportunities for mutually beneficial trade exist by virtue of specialization on the basis of relative efficiency – a country does not have to be better at producing something than its trading partners to benefit from trade (absolute advantage). It is sufficient that it is relatively more efficient than its trading partners (comparative advantage). This insight explains why so many more opportunities to gain from trade exist than would be the case if only absolute advantage counted. More recent theories point to other sources of gains from trade not linked to differences among

**Table 9.2** Trade model theories

	Traditional trade theory Ricardo, Heckscher–Ohlin	New trade theory Krugman	Heterogeneous-firms model Melitz
<b>Gains from trade (causes)</b>			
Specialization	Yes	No	No
Economies of scale	No	Yes	Yes
Pro-competitive	No	Yes	No
Variety	No	Yes	No
Aggregate productivity (through selection/ reallocation)	No	No <sup>a</sup>	Yes
<b>Trade patterns</b>			
Inter-industry	Yes	No	No
Intra-industry	No	Yes	Yes
Exporters and non-exporters within industries	No	No	Yes
<b>Distribution</b>			
Trade liberalization affects relative factor rewards	Yes	No	No

<sup>a</sup>In the Krugman model, “productivity” in the integrated market also increases in the sense that the same total amount is produced at lower average cost due to exploitation of scale economies. However, the Krugman model is silent about which firms remain in business, since it does not include differences among firms. Once firms are distinguished according to their productivity level, as in the Melitz model, the exit of less productive firms itself leads to improvements in overall industry productivity

Source: WTO

countries, such as economies of scale in production, enhanced competition, access to a broader variety of goods and improved productivity.

International trade can affect the growth process through its effects on the accumulation of capital and on technological change. In a standard “neoclassical” growth framework, where technological change is determined externally (*exogenously*), international trade affects factor and product prices and, through this channel, incentives to accumulate capital. Within this framework, the effect of international trade on growth depends on the nature of trade taking place (Grubel, 1967, Porter, 1990).

Many studies that have focused on how trade might stimulate firms to innovate have uncovered several new mechanisms that could associate trade liberalization with higher growth rates. Examples of such mechanisms include increased market size, knowledge spillovers, greater competition and the improved quality of the institutional framework. Several studies have pointed to possible offsetting effects resulting from differences in human capital across countries, imitation of foreign technologies, a worsening of policies affecting trade and so on.

Nevertheless, many studies focusing on knowledge spillovers and firm productivity demonstrate a high correlation between growth rates and trade volumes. But

this does not necessarily imply that trade leads to growth. Does trade cause faster growth or do economies that grow quickly also trade more (Cohen and Levinthal, 1989, Hoekman et al., 2004b)?

An alternative strategy is to estimate the importance of international knowledge spillovers, which are crucial for the realization of dynamic gains from trade. Recent studies point to the presence of “direct” (i.e. bilateral) research and development (R&D) spillovers, which are related to the level of R&D produced by the trading partner, and “indirect” knowledge spillovers, which result from participating in international trade more generally (Branstetter, 2001, Bottazzi and Peri, 2007, Young, 1991).

Finally recent studies that use firm-level data find that trade liberalization has a positive effect on firm productivity and that “learning by exporting” effects (externalities) exists in several emerging market economies (Gould and Gruben, 1996, Falvey et al., 2006a).

Studies that focus on international knowledge spillovers find that knowledge developed in one country has positive effects on other countries through trade. Trade leads to the spread of international technology for three major reasons. First, technologically more sophisticated intermediate goods become available for production. Second, the technological specifications of intermediate and final goods developed abroad can be studied and the intrinsic knowledge can be acquired. Finally, trade favours person-to-person communication as an important vehicle of knowledge transfer (Branstetter, 2001, Hoekman et al., 2004b). This type of international learning by doing was examined in the previous chapter in relation to the wide range of foreign companies operating in the Saudi energy sector.

Studies have emphasized several factors determining whether technology is successfully absorbed across countries. These factors are associated with the idea that a country needs to have certain types of skills (e.g. human capital) and institutions in order to be able to adopt foreign technological knowledge (Ventura, 1997).

Policies to improve a country’s ability to adopt technological innovations must be targeted at its educational system as well as its business and regulatory environment. One particular problem related to the transfer of technology is that innovations produced in advanced economies may not respond to the needs of developing countries (Bhagwati and Brecher, 1980).

Such a mismatch may result from insufficient property rights protection. This suggests a role for international organizations in promoting international technology diffusion through adequate property rights enforcement. Other areas where international organizations can help include the coordination of development aid to build infrastructure and human capital (Young, 1991).

## **Saudi Industrial and Export Strategy**

Since the launch of Saudi Arabia’s industrialization strategy in the early 1970s, the key debate was on what type of strategy to adopt: an import substitution strategy or an export-led strategy (Johany, 1986). While both are not mutually exclusive and

can coexist for a certain period of a nation's economic development, both have some inherent appeal for national planners, as follows:

- *Import substitution strategy*: This type of strategy can be characterized as being an industrial development policy whose aim is to encourage investment in both the private and public sectors so as to establish a viable domestic industrial base that gradually replaces foreign imports. The perceived advantages of following such a policy are a reduction in the amount of foreign exchange outflow and pressure on the balance of payment current account; the chaneling of investment opportunities domestically instead of capital outflows; the creation of new jobs in such import substitution industries and the building up of an expertise in the labour force; reduction in foreign country dependency, especially for strategically deemed products, and enabling a higher degree of self-sufficiency in such products.

There are some disadvantages associated with a prolonged import substitution policy. These centre around the opportunity cost of a continued protection policy for so-called "infant industries," which might become powerful domestic business lobby groups demanding continued government subsidies and protection against foreign competition. Also, the successful establishment of an import substitution industrial base might shift and change the structure of imported goods and services from consumer goods to one dominated by raw materials and highly specialized capital goods and foreign labour. Such import substitution policies usually do not succeed if the domestic demand base is small and fragmented.

- *Export-oriented industrial strategy*: This type of policy is more proactive and involves fundamental structural, administrative and capacity changes in the domestic economy for it to succeed. The aim of such a strategy is to encourage the production of competitive industrial domestic goods and services to be exported to other countries on equal terms. As discussed earlier, for this strategy to be successful, a country primarily focuses on the production of goods and services in which it has a comparative advantage. Similar to the import substitution strategy, the export-oriented industrial strategy has imbedded advantages and disadvantages. The advantages relate to the reduction of foreign currency outflows and replacing this with foreign currency inflows helping to build up current account surpluses; an effective export-oriented policy will help to promote domestic competition and efficiency as higher standards are often required for export goods to meet internationally accepted International Organization for Standardization (ISO) benchmarks. Finally, a high-quality export-led industrial policy may open up new foreign markets for the domestic producers owing to economies of scale, instead of relying on a more limited domestic demand and market.

The disadvantages of an export-oriented industrial policy can also be significant and relate to the intensity and level of international competition for initial market entry and if the foreign companies react by "dumping" their products at lower prices in the developing countries' market in order to kill off competition. Also, this export-led strategy may lead to increased levels of imports for high-value capital goods and

reliance on foreign skilled workers to run the newly established export industries, causing a deterioration in the balance of payment position in the short run, as well as dependence on foreign skilled labour and foreign technology dependence and know-how in the long run.

Over the next few chapters, we will examine how Saudi Arabia tried to overcome these constraints and balance both objectives and whether they have been successful to date. In summary, some of these obstacles are set out in Table 9.3.

**Table 9.3** Obstacles facing Saudi industrial sector development and solutions

Obstacles	Possible solution
<ul style="list-style-type: none"> <li>• Skilled manpower shortage at both technical and managerial levels</li> </ul>	<ul style="list-style-type: none"> <li>• Expansion of specialized vocational and technical institutions, development of market-led courses at universities, international scholarships for areas deemed to be of national priority, on-the-job training</li> </ul>
<ul style="list-style-type: none"> <li>• Transfer of technology and its continuous application, and maintenance of such new technology</li> </ul>	<ul style="list-style-type: none"> <li>• Establishment of joint venture companies with access to foreign companies' R&amp;D processes, establishment of internal R&amp;D centres and specialized research institutions at universities, supports for commercialization and new patent applications</li> </ul>
<ul style="list-style-type: none"> <li>• Potential dumping of foreign goods</li> </ul>	<ul style="list-style-type: none"> <li>• Application to international bodies such as WTO for redress and imposition of penalties on such foreign companies</li> </ul>

## Saudi Arabia's Trading Patterns: Exports

From a humble beginning in the early 1970s, Saudi Arabia's imports and exports have risen dramatically over the past decades as illustrated in Table 9.4.

What is noticeable from the above table is that while oil exports tended to fluctuate, there was a gradual increase in non-oil exports to around SR 120 billion by 2008, compared with under 1 billion in 1970. The driving force for exports has been

**Table 9.4** Saudi trading patterns 1970–2008 (SR billion)

Year	Imports	Total exports	Non-oil exports
1970	3.197	10.907	0.800
1975	14.823	104.412	1.160
1981	119.298	405.481	4.635
1991	108.934	178.636	15.328
2001	116.931	254.898	30.182
2005	222.985	677.144	71.263
2007	338.088	874.403	104.468
2008	431.753	1,175.354	120.182

Source: SAMA

**Table 9.5** Composition of Saudi exports 1984–2008 (SR billion)

Composition	1984	1993	2000	2008
• Foodstuff	0.166	1.656	1.700	8.875
• Petrochemicals	1.489	8.348	15.930	62.738
• Base Metals	0.185	0.869	1.982	10.503
• Electrical Equipment/Machines	0.008	0.460	0.951	6.388
• Construction material	Nil	1.273	2.357	10.206
• Re-exports	2.505	1.527	1.886	21.472
• Total	4.353	14.134	24.806	120.182

Source: SAMA

the petrochemical sector, which now accounts for around 52% of total exports in 2008 as broken down in Table 9.5.

Besides petrochemicals, there has also been noticeable success in non-energy-related Saudi exports in the foodstuffs sector and general machinery and construction material. These are the results of the establishment of modern agro-business enterprises such as the Saudi Al Marei group, which is the largest in the Middle East, and the various Saudi cement companies and other industrial groups. This non-oil export trend was assisted by several initiatives that the Kingdom undertook to assist the private sector, by creating a number of entities such as the Saudi Exports Programme of the Saudi Fund for Development, the Saudi Export Development Centre and the Saudi Exports Development Authority. Each is analysed in Table 9.6.

**Table 9.6** Saudi export assistance agencies

Agency	Function
• Saudi Exports Programme of Saudi Fund for Development (SFD)	• Established in 1999 to provide finance and insurance for non-oil exports. Helps Saudi exporters to receive export proceeds due to importers' inability to pay, by providing 90% non-payment risk. In 2008 the programme provided SR 838 million in export finance and SR 3.525 billion in guarantees
• Saudi Export Development Centre (SEDC)	• Established in 1985 under the auspices of the Chambers of Commerce and assists exporters by making proposals and studies, conducting research on export potential and new markets, assisting with marketing plans and assisting with internal and external trade missions, as well as providing import regulations of designated target countries to Saudi members
• Saudi Exports Development Authority (SEDA)	• Established in 2007 by the Council of Ministers. The SEDA's objectives are in setting the State's policies of developing non-oil exports, increasing the export sector's competitive capacity, developing policies and legislation and improving the export environment and providing incentives. SEDA also prepares studies on export opportunities and organizing symposia and conferences



## Import Diversity

Imports saw the largest sustained rises, with this sector growing at an annual compounded rate of over 33% during the first boom period of 1974–1982 (Johany, 1986). Even more striking are the marked changes in the composition of imports and their points of origin, along with relative changes in sectoral demands. Table 9.7 illustrates the evolution of the composition of imports for the period 1970–2008. Imports of goods and services are virtually unrestricted to the Kingdom, with the exception of those goods and services that are deemed *haram* or forbidden by Islam (such as pork and alcohol products), as well as immoral or security-related commodities. Goods from countries that the Kingdom is still boycotting, such as Israel, are also forbidden.

**Table 9.7** Saudi Arabia – imports by major commodity groups (1970–2008) (SR billion)

Commodity group	1970	1984	2000	2006	2008
• Machines, appliances	0.590	28.410	24.982	67.302	117.318
• Foodstuffs	1.011	18.739	20.258	35.547	62.199
• Chemicals	0.355	11.625	14.716	33.394	53.039
• Textiles/clothing	0.157	3.605	7.573	10.281	13.875
• Metals and their products	0.300	14.183	8.895	38.626	66.012
• Wood and jewellery	0.416	7.790	8.769	4.256	8.355
• Transport equipment	0.428	15.916	19.996	50.453	77.619
• Other goods	0.042	3.716	3.072	21.543	33.336
• Total SR billion	3.299	103.984	108.261	261.402	431.753

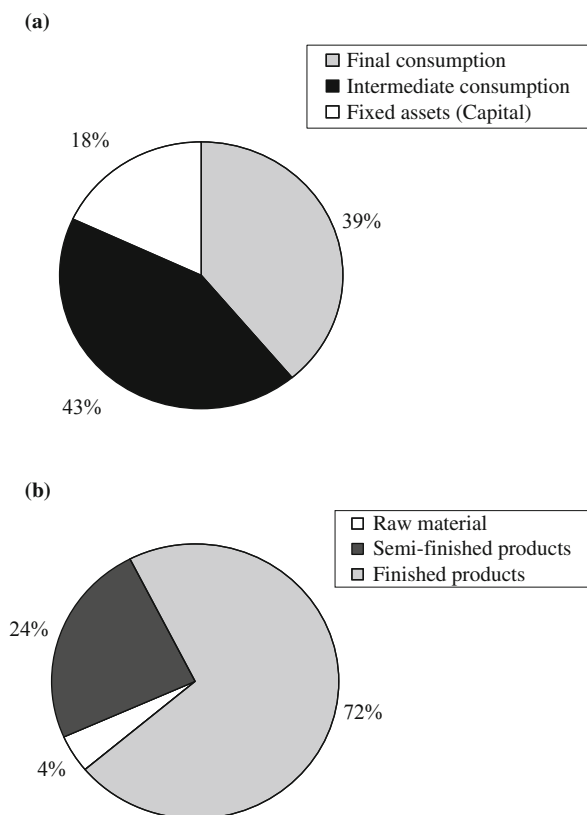
Source: SAMA

In 1970, the import of foodstuffs accounted for around 31% of total imports, but the oil-led boom of the mid-1970s changed the composition of imports, with machinery, transport equipment and mineral and chemical products becoming nearly 60% of imports until the mid-1980s. With the decline in government capital expenditure, discussed in earlier chapters, the private sector increasingly drove import demand. Today, in addition to foodstuffs that account for around 15–16% of total imports, textiles, machinery and vehicle imports account for a significant portion of imports that meet domestic and expatriate consumer needs.

Despite the growth of the domestic petrochemical industry as analysed in previous chapters, Saudi Arabia still imports significant amounts of chemical products, representing around 12% of total import value for 2008, with such chemicals being final consumption items to meet shortfalls in domestic production.

As Saudi Arabia's industrial base expands and matures, the composition of imports will move towards intermediate and fixed assets as illustrated by Fig. 9.1. For the year 2005, fixed assets made up around 18% of total imports, with final and intermediate consumption goods at 39 and 43%, respectively, as illustrated in Fig. 9.1(a).

Figure 9.1(b) illustrates that raw material imports average around 5%, while the bulk of imports (72%) are composed of finished products in value terms. Semi-finished products stood at around 24% of total imports. This high proportion



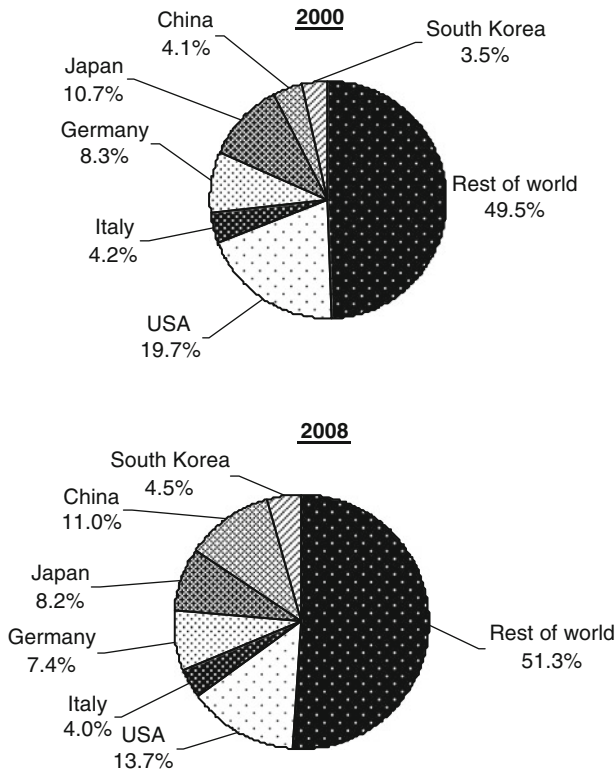
**Fig. 9.1** (a) Import by utilization of items, 2008 (SR billion); (b) Imports by nature of items (Source: SAMA)

of finished product imports for the Kingdom is a function of the open economy. It also reflects the degree to which consumer demand has been influenced by international consumption habits. Relatively sophisticated local advertising and marketing campaigns have also developed brand awareness, especially for high-value luxury items.

Saudi Arabia now has large, flourishing shopping malls, catering to a younger generation. We have seen earlier that non-oil GDP has been gradually rising over the past few decades, contributing to some import demand stability. Earlier studies carried out on the level of the Saudi marginal propensity to import (MPM) indicated a fairly high level of MPM, almost 75% (Bashir, 1977), as well as a high level of correlation between imports and non-oil GDP. By marginal propensity to import, we mean the fraction of each increment or addition to income that is spent on imports. In the earlier research, 0.75 of each additional 1 riyal income was spent on imports. It will be interesting to note whether, in the long run, this high-level MPM will continue in the face of domestic Saudi manufacturing expansion, especially in the food sector, where Saudi products have established brand recognition and international standards.

## Origins of Imports Are Changing

It is not just the composition of imports that has changed over time for Saudi Arabia, but also the origins of these imports. This reflects an interesting mixture of economic relations, consumer taste and political realities. Figure 9.2 sets out the share of total imports accounted for by the top six exporting nations to Saudi Arabia for the years 2000 and 2008.



**Fig. 9.2** Saudi imports by origin (2000 and 2008) (Source: SAMA)

On the whole, the Kingdom’s trade direction is largely determined by the private sector; it is based on commercial relations, the agencies held and the level of comfort in dealing with their international counterparts, rather than being based on political considerations. While some government-to-government lobbying does certainly exist to obtain government-related contracts, such contracts have become less important over time as the Saudi government has emphasized the role of the private sector in economic decisions.

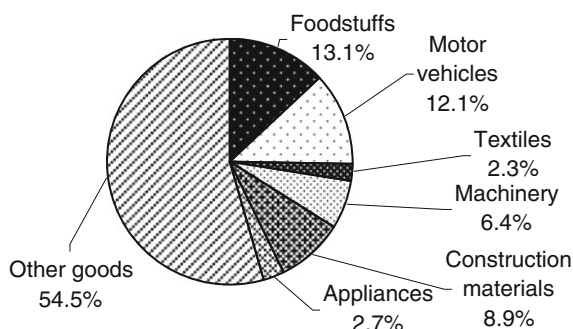
Figure 9.2 shows the pre-eminent position of the USA as the Kingdom’s major import trading partner. This is not surprising, considering that the USA is, in turn,

the largest importer of Saudi oil. Following the September 11, 2001 events, the premier position of the USA has been eroded to around 14% in 2008, down from 20 to 21%. Political sensitivities and travel problems to the USA for Saudi citizens have also been issues. What the figure further demonstrates is that Saudi Arabia's import relations are mainly carried out with non-Arab and non-Muslim countries. This supports our earlier observations that Saudi buyers are generally knowledgeable of, and sensitive to, market conditions, especially when it comes to the import of "quality" or "brand name" items that are lacking in the wider Arab or Muslim world (Johany, 1986).

Currently, imports from all the Arab and Muslim countries account for around 11% of the total imports. The presence of Lebanon in 1972 amongst the top five exporting countries to the Kingdom is an interesting historical aside. It came about because of Lebanon's position as a trans-shipment centre in the early 1970s for Saudi goods; Saudi Arabia used Lebanese ports because of its own limited port facilities in that early boom era. In 1970, the handling capacity of the combined Saudi ports stood at around 2000 tons, rising to 3,700 in 1974. By 2000, Saudi port capacity had risen to 252,000 tons. It is interesting to note the rising market share from China, with imports accounting for around 4.1% of total imports in 2000 and rising fast.

The almost doubling of Chinese exports to Saudi Arabia in a decade to become the second largest importing trading partner after the USA by 2008 is a reflection of the sharp increase in Saudi oil exports to that country, raising China's importance to the Kingdom as a major trading partner for the future. As noted from [Chapter 8](#), 2008's high oil prices have been largely underpinned by strong demand from China. This is expected to remain robust over the next few years according to oil industry analysts. Over the next decade, the origin of Saudi imports could continue to shift towards the Asian markets, given that Japan has also been the second most consistent exporter to Saudi Arabia, while imports from the USA could see further volatility, despite competitive U.S. product prices, due to the fall in the value of the U.S. dollar during 2007–2009.

Most Saudi imports are financed by Saudi commercial banks through letters of credit opened in favour of overseas beneficiaries. The major financing is applied to motor vehicles and foodstuffs, followed by textile and clothing, as illustrated in [Fig. 9.3](#).



**Fig. 9.3** Private sector imports financed through commercial banks 2008 (Source: SAMA)

Overall, around 65–70% of total imports are financed through banks. The remaining imports use different forms of direct payments or supplier credit arrangements. With the growth of local Saudi industries and a wider manufacturing base, the level and composition of future imports to Saudi Arabia could yet undergo fundamental change. There could be more machinery, spare parts and raw material imports, and fewer imports in foodstuffs, appliances, construction material and textiles.

## The Export Sector: Oil Is Still King

Despite efforts to diversify the country's production base, and specifically its export base, oil exports continue to dominate the Kingdom's foreign export trade. As such, any overview of Saudi Arabia's exports is much simpler than that of its imports.

The lack of meaningful export diversification could have implications for the Kingdom following entry into the World Trade Organization (Azzam, 2002, Husseini, 2002). According to the WTO, the Arab world in general has fallen behind in the export race relative to world growth in exports; one key reason is the lack of diversification of export products.

From a peak of around 12% of total world exports in 1980, the Arab world's share is now fluctuating between 5 and 8%, despite a 300% increase in world export value over the period 1980–2008.

Significantly, the expansion of exports in the Arab world has not kept pace with world export growth, but rather it has mostly correlated with changes in oil prices.

Crude oil exports currently account for around 75–80% of total Saudi exports, down from 94 to 96% during the period 1979–1984, but still giving a one-dimensional emphasis on a single commodity. If one adds petroleum-related finished and semi-finished products, exports from this sector accounted for around 95% of the total in 2008 as illustrated in Table 9.8.

**Table 9.8** Oil-related merchandise exports 1979–2008 (SR billion)

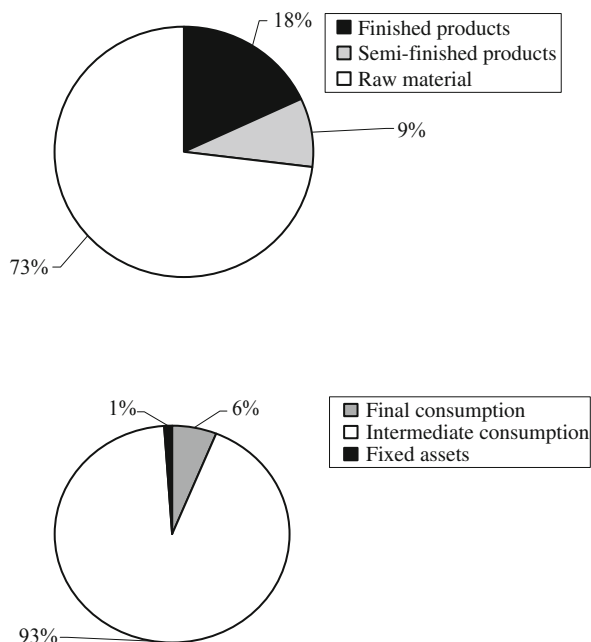
Export segment	1979	1984	2005	2008
Total exports	213.183	132.220	677.144	1,175.354
• Crude petroleum	200.225	127.867	513.939	926.613
• Refined products	0.600	1.750	91.942	127.119
• Petrochemicals	1.939	1.489	42.055	62.464
Oil-related exports	202.764	131.106	647.936	1,116.196

Source: SAMA

Saudi Arabia's other petroleum-related product exports are important sources of revenue, especially refined oil products, including bunker fuel.

Saudi manufacturing and processing industry is slowly coming of age, with steady export rises in foodstuffs, equipment and base metals, in addition to plastic and construction materials. The Saudi government aims to ensure faster growth of such exports so that they will constitute a larger share of overall Saudi exports,

achieving diversification within non-oil-based economic structure (Zarouk, 2002, Khemani, 2002). This will be a long-term task. In the meantime, the Kingdom will continue to be primarily a raw material, intermediate consumption goods exporter (goods which still need value-added input), as illustrated in Fig. 9.4(a) and (b).



**Fig. 9.4** (a) Export by nature of items (2008); (b) Export by utilization of items (2002) (Source: SAMAA)

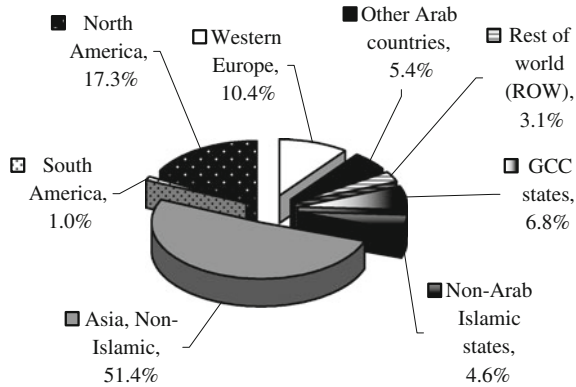
In 2008, according to Fig. 9.4(a), some 73% of Saudi exports were composed of raw materials, with finished products accounting for 18% and semi-finished for 9%. It is the second category that needs to be encouraged to grow, as it is a high-value export category. Similarly, Fig. 9.4(b) points out that only 1% of total exports were in fixed assets and 6% in final consumption goods. An increase in finished product exports will assist in the growth of exports in the value of final consumption goods, that is, goods that have final use. Developing these export sectors will reduce the instability of export earnings that result from oil dependency.

## Asian Exports Predominate

Saudi Arabia's main export market is Asia, which accounted for some 51% during 2008 as illustrated in Fig. 9.5.

These were followed by North America and Western Europe, while the GCC states took 7% of exports. Saudi exports to other Arab countries were a meagre

**Fig. 9.5** Geographic distribution of average Saudi exports 2008 (Source: SAMA)



5%, and the non-Arab Islamic states took 4%. Once again, it was the predominantly industrialized Western and Asian economies that received the bulk of Saudi oil exports and petroleum-related products.

Given the strong performance of primarily Asian countries such as China and India during the 2007–2009 financial crisis, the trend for Saudi exports to Asia is set to grow.

Saudi Arabia’s relatively narrow export base is also a reflection of the government’s development strategy during the first planning periods, discussed in [Chapter 2](#). This strategy emphasized import substitution as an explicit goal, as well as investment in petrochemical-related industries. The result of import substitution policies was the creation of protected domestic manufacturing industries that looked to the lucrative domestic consumer market as their first choice for expansion and sales (Jalal, 1985). An export-oriented, non-oil manufacturing base was not emphasized, and Saudi Arabia is now trying to find its niche in this competitive sector to create some stability in exports, as compared with oil. This could take several decades, and significant steps have been achieved, and it is not impossible, given the financial resources that are available to the private sector as evidenced from earlier chapters. This leads us to a discussion on the required change in the operational environment of the non-oil export sector.

## Efficiency and Competitiveness

Over the period 2006–2010, the Saudi investment environment and private sector operating framework has benefited from significant progress from the structural reforms examined in [Chapter 2](#), which involves liberalization, greater transparency and the reduction of red tape and bureaucracy. The result has been a gradual improvement in Saudi Arabia’s global ranking in the World Bank’s “ease of doing business” index, which is illustrated below and has placed the Kingdom in 16th position, ahead of some western European countries.

Saudi Arabia: Ease of doing business World Bank ranking

	2006	2007	2008	2009
Global Rank	35	38	23	16

This improvement in Saudi Arabia's global ranking has largely been driven by the Saudi Arabian General Investment Authority (SAGIA), which was created to overcome red tape and bureaucracy and make Saudi Arabia an "investment-friendly" destination for foreign and domestic companies. SAGIA's objective is even more ambitious – to rank Saudi Arabia in the top 10 countries of the world in terms of competitiveness by the end of 2010, through SAGIA's so-called 10×10 vision (SAGIA, 2009).

Aspiring to be in the top 10 countries is one thing, while achieving it is another, as it involves some fundamental structural changes in the competitiveness-enabling environment. There are many methods for enhancing a nation's competitive position, and we summarize the main concepts below.

Competitiveness can be broadly defined as the ability of a nation to create sustainable value through its enterprise, and to maintain a high standard of living for its citizens. In addition, countries are placed in three broad categories:

- *Factor-driven*: relying heavily on natural resources and basic production.
- *Investment-driven*: increasing investment to make production more efficient and enabling the economy to move up the "value chain" from basic manufacturing towards product design, distribution and marketing.
- *Innovation-driven*: producing unique goods and service that demand high prices on the global market.

As analysed in the previous chapters, Saudi Arabia's competitiveness has been primarily factor-driven, but with more emphasis now on investment-driven, due to the emergence of a high-value petrochemical sector.

Whichever competitiveness measures are taken, there is one common factor that drives competitiveness, i.e. productivity or the level of output per unit of input used to produce something of value. The main drivers of a nation's prosperity and hence its competitiveness vis-à-vis other nations are as follows:

- The proportion of the labour force engaged in productive economic activity
- The efficiency with which goods and services are produced
- The value these goods and services can demand on the world markets

A nation's competitiveness depends on its ability to capitalize on these three factors to create new sources of wealth over time. However, Saudi Arabia must ultimately define competitiveness for itself that suits its own unique operating environment as there is no single standard or blueprint for success and such strategies need to be tailored to reflect a country's unique character. For example, natural



resources such as oil may bestow Saudi Arabia with an “inherited prosperity” that makes generating a momentum for change that much more challenging compared with other less favourably nature endowed countries but which seek out new challenges to give them a competitive edge. The example of Singapore in the latter category suffices.

### *Achieving Competitiveness*

More than one factor is essential to achieve a sustained level of competitiveness. These involve broad strategic issues such as

- (i) the quality of macro-economic, social, political and legal policy;
- (ii) the quality of the business environment and
- (iii) the sophistication of company strategy and operations.

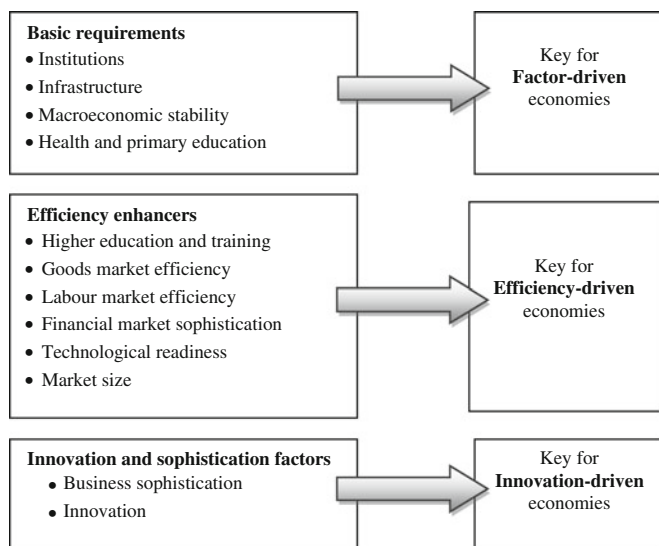
The overall macroeconomic, social, political and legal policies create the potential for greater company productivity by providing access to capital and foreign markets. However, actual wealth generation takes place at a microeconomic level through the creation of unique and innovative goods and services that can demand high prices on world markets. Wealth can be inherited, whether for individuals, or through endowed factors such as oil for a country like Saudi Arabia, but ultimately it needs to be created to achieve sustainable prosperity. Competing on cost or low wages or an abundance of natural resources is not a basis for a sustainable competitive advantage.

Countries that have high rankings and/or have shown significant gain have done so by showing consistently superior performance in key macro- and microeconomic areas:

- *Macroeconomic environment*: high budget surpluses, low government waste, strong country credit rating, low inflation
- *Strong public and private institutions*: absence of corruption, business and governmental transparency, judicial independence, enforcement of property rights
- *Technology and innovation*: high spending on research and development (R&D), aggressive adoption of new technologies, university and industry research collaborations, active use of technology
- *Education and training*: high educational enrolment rates, excellent educational establishments, skilled labour force

The World Competitiveness Report (World Economic Forum, 2009) has identified 12 “pillars” of competitiveness and Fig. 9.6 sets them out by groupings relating to the factor-driven, efficiency-driven and innovation-driven economies.

How has Saudi Arabia performed against the above pillars and what are the perceived obstacles achieving a higher level of competitiveness in the Kingdom?



**Fig. 9.6** The 12 pillars of competitiveness (Source: Global Economic Forum (2009))

### *Saudi Competitiveness Performance*

Saudi Arabia has steadily improved its world ranking in both ease of doing business as discussed earlier, and also in the global competitiveness index as illustrated in Table 9.9, which indicates that Saudi Arabia's rank as 28 out of 133 surveyed countries.

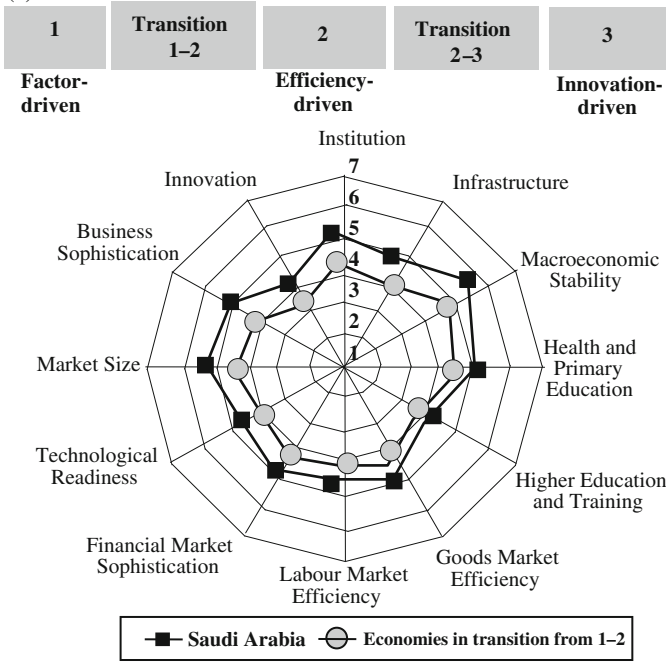
**Table 9.9** Global competitiveness index: Saudi Arabia ranking

	Rank (out of 133)	Score (1–7)
GCI 2009–2010	28	4.7
<i>Basic requirements</i>	30	5.2
1st pillar: Institutions	28	4.8
2nd pillar: Infrastructure	36	4.6
3rd pillar: Macroeconomic stability	9	5.9
4th pillar: Health and primary education	71	5.4
<i>Efficiency enhancers</i>	38	4.5
5th pillar: Higher education and training	53	4.3
6th pillar: Goods market efficiency	29	4.8
7th pillar: Labour market efficiency	71	4.3
8th pillar: Financial market sophistication	53	4.4
9th pillar: Technological readiness	44	4.2
10th pillar: Market size	22	4.9
<i>Innovation and sophistication factors</i>	33	4.2
11th pillar: Business sophistication	35	4.6
12th pillar: Innovation	32	3.7

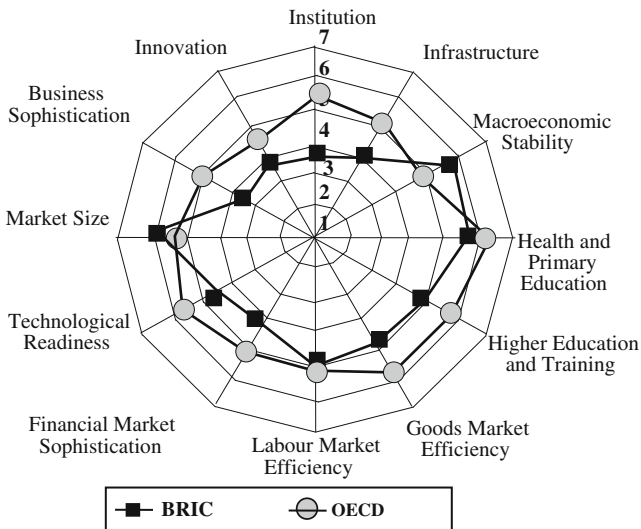
Note: Score 1 defines the lowest and 7 defines the highest rankings

Source: Global Economic Forum (2009)

(a) Saudi Arabia



(b) BRIC and OECD average scores



**Fig. 9.7** Stages of development across 12 pillars of Global Competitiveness Index (a) Saudi Arabia; (b) BRIC and OECD average scores. Source: Global Economic Forum (2009)

Table 9.9 reveals varied differences in the competitiveness index pillars for the Kingdom. Saudi Arabia’s macroeconomic stability ranked it 9th out of 133 countries, and the Global Economic Forum gives the Kingdom special praise about progress being made with respect to upgrading its public institutions, which were ranked at 28 for 2009. According to the Global Economic Forum, Saudi Arabia is in a state of transition from being a factor-driven economy towards an efficiency-driven economy, but still has some way to go before being an innovation-driven economy. This is illustrated in Fig. 9.7, which compares Saudi Arabia to similar economies in transition as well as with the Organisation for Economic Co-operation and Development (OECD) countries and the so-called BRIC (Brazil, Russia, India and China) economies.

From Fig. 9.7(a) we note that Saudi Arabia has done relatively better for all 12 pillars compared to other similar transition countries, especially in macroeconomic stability, institutions, market size and business sophistication, but does less well on labour market efficiency and health and primary education. Saudi business sophistication is also ranked higher with its peers. Analysis of Fig. 9.7(b) illustrates that the BRICs do well in terms of market size in comparison with the OECD block, as well as receive a high score for labour market efficiency, macroeconomic stability and health and primary education. Comparing Saudi Arabia with the BRIC economies, the Kingdom does well on most scores with the exception of innovation. There seems to be a correlation between countries with a higher efficiency and innovation-driven economy than those in the factor-driven phase. Figure 9.8 maps out a global prosperity index using purchasing power parity (PPP) adjusted GDP per capita and growth of real GDP per capita for the period 1998–2007.

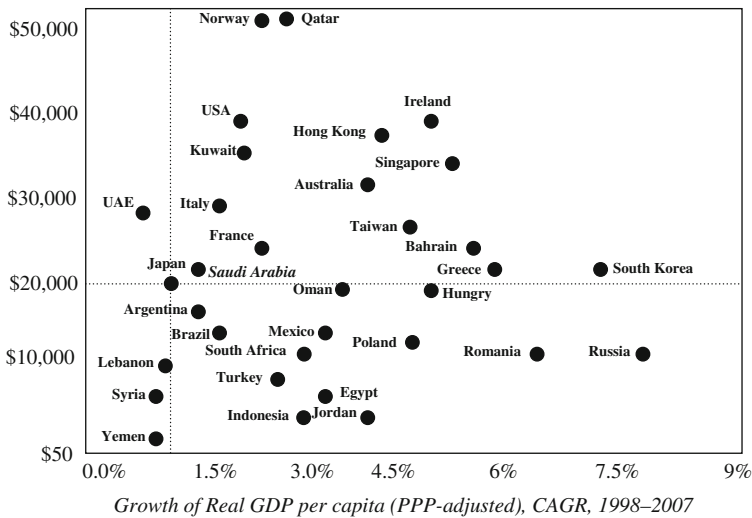
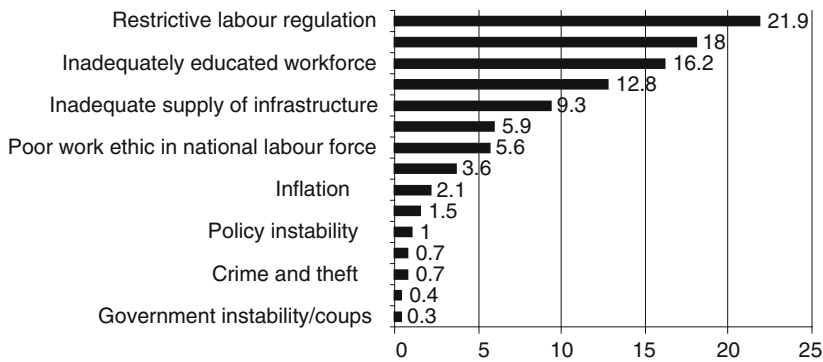


Fig. 9.8 Global prosperity performance growth of real GDP per capita adjusted in PPP terms (1998–2007) (Source: EIU (2008), Porter (2010))

From Fig. 9.8, we note that Saudi Arabia, although doing better than most Arab and other developing countries in terms of PPP adjusted GDP per capita growth, did not outperform the other GCC member states and was slightly ahead of Oman. From the GCC block, Qatar was the highest at \$73,000 ahead of the USA and on par with Norway, while Saudi average was around \$22,000.

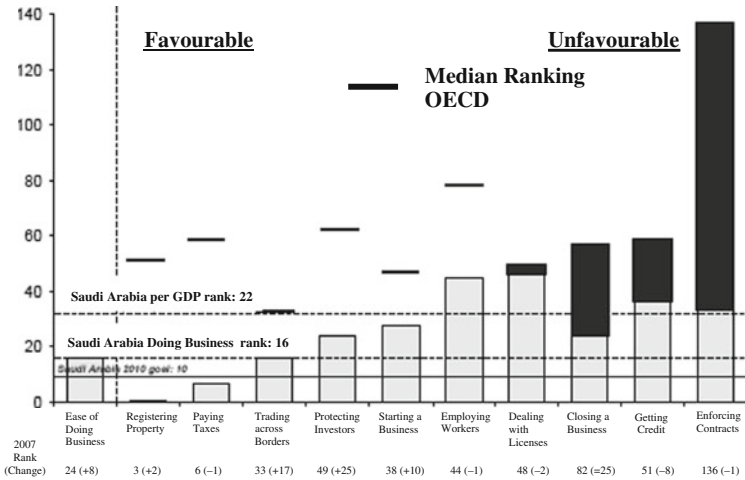
### Reducing Competitiveness Obstacles

Despite the progress noted above, obstacles still remain in achieving higher competitiveness levels for the Kingdom. These can be measured in the manner by which businesses operate and the relative ease of doing business and by asking respondents to list the factors they feel the most problematic for doing business. Both issues are illustrated in Figs. 9.9 and 9.10.



**Fig. 9.9** The most problematic factors for doing business: Saudi respondents (2009). Note: From a list of 15 factors, respondents were asked to select the five most problematic for doing business in their country/economy and to rank them between 1 (most problematic) and 5 (least problematic). The bars in the figure show the responses weighted according to their rankings (Source: Global Economic Forum (2009))

According to respondents, Fig. 9.9 indicates that most agree that Saudi competitiveness is hampered by restrictive labour regulations, followed by access to financing. The labour issue will be covered in a later chapter, but the high negative response concerning restrictive financing reflects the generally tighter credit terms imposed by Saudi banks in general following the 2007–2009 global financial crisis as discussed in a previous chapter. An inadequately educated labour force was also listed as a high impediment, as well as inefficient government bureaucracy, despite the higher positive rating given by the Global Economic Forum survey to Saudi Arabia for institution building examined earlier in Fig. 9.7(a). Analysis of Fig. 9.10 seems to confirm some of the respondents’ unfavourable findings in obtaining credit, but employing workers in general seems to get a higher positive rating.



**Fig. 9.10** Saudi Arabia ease of doing business (2008) (Source: World Bank Report: Doing Business (2008))

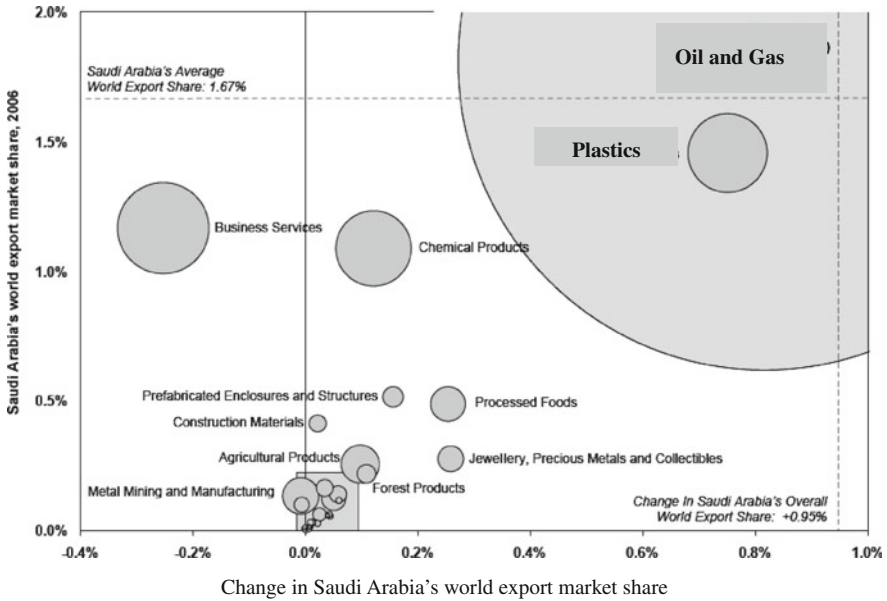
Figure 9.10 sets out the OECD median ranking for most favourable ease of doing business benchmarking, and the Saudi ranking changes over the period 2007 and 2008. The most positive changes have occurred in trading across borders, protection of investors, starting a business and closing a business as well as general ease of doing business. All these factors had been targeted by SAGIA as discussed before, and seem to demonstrate the relative success of that government organization in reducing bureaucracy. The factors which saw unfavourable rankings were in employing workers, dealing with licences, getting credit and enforcing contracts. All these factors involved government legislation and laws and lay outside the direct control of institutions such as SAGIA, but within legislative decision-making bodies. As discussed in Chapter 2, there has been some movement towards legislative and legal reforms, but more is needed if Saudi Arabia aspires to reach OECD levels.

### *Saudi Arabia’s Competitive Advantages*

Saudi Arabia needs to adopt a new export promotion strategy that focuses on efficiency and competitiveness and which encompasses both oil- and non-oil-related products (Nojaidi, 2002, Richard, 2002). Broad macroeconomic data such as export volumes or values do not reflect individual sectors’ export performance based on competitive efficiencies. The *Arab Competitiveness Report of 2008* has conducted intensive studies in this area and has ranked 16 countries of the Arab world amongst 100 exporting countries based on their Trade Performance Index (TPI). The composite rankings of the TPI were supposed to capture many dimensions of export performance for various commodities based on competitiveness and efficiency.

Trade Performance Indexes were classified as *current TPI* and *change TPI* and countries were ranked from 1 (the most efficient and competitive) to 100 (the least efficient and competitive).

The findings of the report established that the Kingdom has five sectors in which it competes with mixed results on the international level, including oil and gas, plastic, chemical products and processed foods. Figure 9.11 sets out these areas of dominant Saudi export portfolios.



**Fig. 9.11** Saudi Arabia’s “Champion” export cluster portfolios (Source: UNCTAD, IMF, Global Economic Forum, Porter 2010) (1998–2006)

Figure 9.11 illustrates the overwhelming dominance of the oil and gas sector and the increase in market share in this cluster but also the decrease in Saudi business services over the period 1998–2006.

Trading based on advantages in resources will lead to depletion of such resources in the long run and make a country hostage to fluctuations in world commodity prices. What should the strategy be then? In practice, it is not necessary to move away from resource-based exports completely, but it is important to build alternatives, especially high-value-added export alternatives. In order to achieve a higher level of sustainable growth, Saudi Arabia needs to shift from trading on resource-based advantages towards trades based on products, skills, processes, quality and innovation. This requires improved productivity, upgrading existing technology and increasing the efficiency of the use and allocation of resources. It is only in this manner that countries like Saudi Arabia can meet the challenges of gaining an increasing share of a growing world export market.

## Foreign Sector Trade Development

The Kingdom is conscious of the wealth-generating effect of export promotion; the world has observed the remarkable growth in the GDP of the so-called “Asian Tiger” economies, as well as that of China in more recent years. Studies have indicated that the traditional development strategies of import substitution that were adopted by many developing countries in the post-Second World War period have been ineffective for long-term sustained economic growth (World Bank, 1993, Solow, 1970, Romer, 1994). A shift towards export-led growth has taken place, with many developing countries seeking to establish supremacy over competitors in niche areas, based on productivity and efficiency. Saudi exporters face both opportunities and challenges, evidence of which is the broad range of products exported by the Saudi Arabian Basic Industries Corporation (SABIC).

However, there are some areas of institutional support that are needed to make Saudi exports more competitive, as in the final analysis it is firms that compete, and not nations, and the focus of the Kingdom should be to assist individual exporters as they tackle concrete problems of market entry, while protecting them from unfair competition and dumping practices. This support can take different forms:

### *Direct Assistance for Exporting Firms*

As exporting is generally new to the Saudi Arabian private sector, exporters might require assistance at each stage of the export process, including customer and market identification, product development and client adaptation, pilot testing in the target market and finally developing a detailed marketing strategy. Further stages involve process development, productivity and quality improvement, production launch and sales. There needs to be follow-up performance analysis and modification of the marketing strategy.

Very few Saudi private sector companies have carried out all or some of the above processes. Instead, they have concentrated on the domestic market, securing sales through “net-back” discounts and special offers. It was left to the government-owned and joint venture companies in the petrochemical sector, along with well-established and well managed Saudi private sector companies, to enter the export market. There have been some notable private sector successes in this field. Table 9.10 lists some selected private sector companies operating in the export sector that have also established an international presence.

Table 9.10 highlights the major emphasis on food products by Saudi exporters with the majority of companies concentrating on the nearby Gulf Cooperation Council (GCC) markets due to shorter communication routes, logistics and GCC trade harmonization policies. A few companies such as Al Zamil, Amiantit and Fakieh have ventured into Europe, Asia and North America. On the whole, Saudi exporting experience has been confined to tried and well-tested regional markets.



**Table 9.10** Selected prime Saudi private sector exporting companies

Group	Product range	International presence
Al Babbain	Household appliances	No
Amiantit	Pipes, storage tanks	Yes
Halawani	Food products	No
Al-Qahtani Pipes	Coated pipes, equipment	Yes
Savola Snack Food Co.	Snacks, general confectionary	No
Abdulateef Jameel	Car accessories	Yes
Al Zamil	Air conditioners, steel fabrication, aluminium, plastics	Yes
Arasco	Fertilizers, feedstock	No
Abdulhadi Qahtani Co.	Oilfield equipments, machinery	No
Al Marai	Dairy products	No
Al Rajhi	Foodstuffs, juices, shrimps	No
Bahrawi	Cosmetics, perfumes, food	No
Al Jomaih	Beverages, cans	No
Nissah	Bottled water	No
Jeraisy	Smart cards, PC equipment	Yes
Fakieh	Poultry, fast food	Yes
Hail Agriculture Dev. Co.	Food product	No
Saudi Cement Co.	Cement	No
Saudi Cable Co.	Cables, electrical wires	Yes
Fitaihi	Jewellery, perfumes	Yes
Savola Group	Ghee, edible oils, foodstuff	Yes

Source: Top 1000 Saudi Companies, 6th Edition, 2000–2001, IIT Publishing, Khobar

### *Assist All Sizes of Firms to Export*

Most of the Saudi company names listed in Table 9.10 belong to the top-tier family businesses, often in the top 100 companies of the Kingdom. For exports to succeed at the national level, neither size nor ownership should be criteria. The Saudi government should be able to assist those smaller companies that are willing to help themselves enter the export market, if they are willing to take the associated risks. Resources of like-minded smaller companies could be pooled to share export risks and the government could be more generous in providing financial support in the form of larger export guarantee insurance to this sector.

### *Establish Institutional Development Programmes*

An export development agency will be able to develop strategy and coordinate amongst members, besides having a powerful “lobbying” voice to discuss specific export issues of concern with the government.

## ***Develop International Trade in Services***

During the past two decades, the provision of services has become the major economic activity of many countries in the world. Within the region, the economies of Bahrain and Dubai in the United Arab Emirates have shifted towards international and domestic services, whether in the transportation of goods and people, banking and insurance services, communications, leisure industry or entertainment. Other economies have established expertise in legal services, education and health. For Saudi Arabia, the service sector accounted for around 28.0% of GDP in 2008 (SAMA). The Saudi government has begun to make some serious plans to expand its domestic tourism industry so as to attract year-round visitors to the holy Muslim sites of *Makkah* and *Madinah* and to other tourist areas of interest. While the overall Saudi GDP percentage of services is lower than that of the USA, which stood at around 75% in 2001, in Saudi Arabia the service sector accounted for 78% of the labour force compared to 71% for the USA. If in the future the provision of services becomes a more “knowledge-based” activity, with information and ideas as the most precious resources, the Kingdom would have to adapt accordingly if it is not to be left behind in this sector (Zarouk, 2002).

## ***Adopt Best Practices***

Nations do not need to “reinvent the wheel” as there are many best practice models available around the world to draw upon and to adapt to domestic conditions. Saudi Arabia can benefit from the experiences of those countries that have transformed themselves to outward-looking, export-oriented economies, and can choose models that best suit the Kingdom’s current human, technological and capital resources. The aim is to give Saudi exporters some comparative advantage over competitors by adapting selected “best practices.” Table 9.11 outlines a best practice export promotion programme for Saudi Arabia that draws upon the experiences and practices adopted by countries such as Malaysia, Ireland, Singapore, India and Tunisia (Khemani, 2002). Table 9.11 also highlights the current Saudi status in implementing such a proposed programme. In some areas the government has taken action, especially in funding and lead agency assistance, but so far the assistance has not been wide enough to make a significant impact.

The promotion of Saudi exports and opening of new markets can be very beneficial to Saudi Arabia in terms of revenue diversification and job creation. According to reports, it estimates that every SR 1 billion of new exports will generate some 25,000 new jobs (Saudi Commerce and Economic Review, February 2003). In the final analysis, however, government support is needed not only to ensure market access and market development but also to create an integrated trade support programme that deals with the central issue of export *competitiveness*. Export promotion should not be conceived in isolation. The creation of new supervisory institutions, however good, cannot alone bring about needed institutional change

**Table 9.11** Saudi Arabia: An export promotion programme model

Programme	Required action	Current status
Marketing	Market promotion, strategies, internet marketing, market development	Internet marketing is still not fully developed; market research tends to be product-driven rather than customer-driven
Technological	Quality assurance, product and technology development, skills development, information technology, tooling, productivity	Uneven quality assurance and internal R&D development, productivity low
Investment and working capital	Export credits and guarantees, bonded warehouses, marketing finance, seed capital, R&D finance/incentives, export insurance cover	Available but limited in amount and only recently extended to non-oil exports. Limited bonded warehouses, limited R&D finance from commercial banks and government
Collective promotion programmes	Research, marketing and trade missions, group promotional programmes, comprehensive system of marketing, information collection, global sourcing	Effected through the regional chambers of commerce and industry, some national trade missions; comprehensive database at national level not yet developed, global sourcing on a pooled basis
Funding and cost sharing	Government funds, 50% cost sharing	Saudi export credit programme exists, using the Saudi Fund for Development (SFD)
Lead agencies	Export promotion authority; export centres, industry associations and insurance corporation	Export non-payment risk coverage exists through SFD using the French COFACE as partner; amounts are limited; no national insurance corporation

in an export climate that involves all organizational sectors of society: universities, research institutes and government departments. There is a need for dedicated and qualified personnel, databases and an entrepreneurial spirit to venture into new markets.

## Conclusion

Saudi Arabia is a country with an unusually large foreign sector and a particular reliance on exports from a narrow commodity base to fund its developments needs. The composition and origins of its international trade have changed over the past three decades and Saudi Arabia today stands on the eve of new trade relationships.

The accession to the World Trade Organization by Saudi Arabia, preceded by bilateral trade agreements with WTO member states, has created a new set of internal dynamics. There is now a greater sense of urgency to position the Kingdom's trading relations on more competitive terms than ever before.

WTO entry is expected to benefit the Saudi petrochemical industry, whose exports to western European markets in particular have been hit by an imposition of tariffs against Saudi petrochemical products. WTO entry would ensure a fair and level playing field for Saudi exports in this market. Similarly the private sector is also beginning to position itself for greater competition following Saudi accession, despite some reservations from vested interests that saw WTO entry as a threat to their domestic markets.

It is not that Saudi Arabia has limited experience in establishing multilateral trade partnerships. The Gulf Cooperation Council (GCC) has achieved some success in harmonizing the six member countries' trading policies with a reduction in tariffs to 5% in January 2003, and with duty-free access to products originating in the GCC, if 40% of value added is from the GCC region.

It is no wonder that Saudi exporters have tended to concentrate on the GCC market, as we explained earlier, but the size of the GCC market is small compared to the potential economies of scale for Saudi exports to larger non-GCC markets. The Kingdom is also a member of the *Greater Arab Free Trade Area* (GAFTA), which extends from the Gulf to North Africa and includes 18 member states. It was established in 1997 with the objective of eliminating all tariffs and taxes but with specific items exempt from tariff reduction in health, security and religious areas.

## Summary of Key Points

- *Saudi Arabia is the Arab world's leading exporter and importer and trade plays a vital role in the economic development of the country.*
- *Imports have risen in quantitative terms since the early 1970s, fuelled by oil revenues, but the composition of imports has changed over the past decades. Imports are now more diversified towards consumer goods orientated compared to equipment, machinery and infrastructural demand of the earlier period. Import origins have also begun to change, with China becoming a major trading partner.*
- *Exports are still dominated by oil and oil-related products which account for around 90% of total exports despite attempts at export diversification. Foodstuffs and chemical products are the major non-oil exports followed by base metals and electrical equipment.*
- *Saudi Arabia, in common with other exporting nations, is focusing on efficiency and competitive advantage for its exported products.*
- *Saudi Arabia has made significant strides in global ranking in areas such as ease of doing business and global competitiveness, but obstacles still remain in areas such as labour issues and access to finance by the private sector.*

- *Saudi Arabia is moving from being a factor-driven (resource-based) economy towards an efficiency-driven economy.*
- *Foreign sector trade development could benefit from several institutional programmes. These include direct assistance for exporting firms, establishment of institutional development programmes through an export development agency, development of international trade in services sector and adoption of best practices.*