

SPEECH BY

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Ladies and Gentlemen,

It gives me great pleasure to address this distinguished gathering. I would like to thank the Middle East and Central Asia Department, the IMF Institute, and Mr. George Abed for arranging the meeting. I am confident that this occasion will contribute to a greater understanding of the financial and developmental issues affecting the MENA region and its economic potential.

Since Saudi Arabia is the largest economy of the MENA region, I thought it would be interesting to focus my comments on the development experience in Saudi Arabia and draw some lessons. While oil receipts, which we view as a blessing and not a curse, have greatly reduced the financing constraint, experience in other countries has shown that the availability of oil receipts is neither necessary nor sufficient for a successful development. Indeed, the success of the

Saudi development strategy reflects a well-sequenced comprehensive set of policies that spans all sectors of the economy. It was predicated on the following imperatives:

First, the effective use, of oil revenues to **build a modern infrastructure** and develop the country's human capital. Oil revenues were also used to finance a number of large industrial projects, some as joint ventures with international companies. This was necessary to help diversify the production base especially given the lack of capital and managerial skills in the Saudi private sector in the 1970's and early 1980's.

Second, the maintenance of **a market-based economy with liberal exchange and trade systems.** Indeed, despite the oil shocks and a number of wars in the region, there has never been any attempt to impose any restrictions on the exchange and trade systems. This has helped greatly in enhancing confidence and encouraging private sector investment in the Saudi economy.

Third, **a stable macroeconomic structure** that is anchored by a solid exchange rate peg with appropriate fiscal and monetary policies. Saudi Arabia has been successful in maintaining low inflation and a **sound and well-capitalized banking system**. This performance has been facilitated by prudent monetary policies, a state of the art payments system, and strong supervision and prudential regulations. Moreover, government debt is fully denominated in domestic currency and a large portion is held by public sector institutions.

Fourth, the pace and sequencing of the reforms have been implemented in a manner that ensured that **social stability** is not disrupted.

As a result, Saudi Arabia has undergone **a major transformation**, with highways, water, electricity, hospitals, and schools reaching all regions of the country. Indeed, only people who are familiar with Saudi Arabia in the early 1970's can fully appreciate the progress that has been made. The role of the private sector has also increased substantially with its GDP rising by 28-folds in real terms from 1973 to 2002. Over the same period, non-oil exports increased from a mere US\$26 million to more than US\$10 billion. The social development indicators have also improved by leaps and bounds during that period as

documented by the recently published UNDP/MOE&P report on Human Development in Saudi Arabia. These accomplishments are all the more notable in view of the region's geopolitical uncertainties.

While drawing comfort from these achievements, we are fully aware of the challenges that remain. First and foremost is the need to **increase employment opportunities** for the rapidly growing Saudi population. As an aside, in the early 1970's the complaint was over shortage of Saudi labor. Now the challenge is the opposite. To this end, we have embarked on a multi pronged approach which aims to raise the economy's growth to a higher plateau, reduce the skills mismatch in the economy, and improve the flexibility of the labor market.

To achieve these objectives, the government has embarked since the late 1990's on a second generation of reforms. The **Supreme Economic Council** was established to better address economic issues, enhance coordination among relevant agencies, and accelerate decision-making and implementation. Also the **Saudi Arabian General Investment Authority** (SAGIA) was created as a one-stop shop to further promote domestic and foreign investment. In addition, a **Tourism Authority** has been founded to develop this sector as an important new source of growth, and a **Supreme Council for Petroleum and Mineral Affairs**

has been established in order to streamline the decision-making process in the energy sector and increase efficiency. Moreover, a number of laws and regulations that will enhance transparency and competition are now in place. The **laws on the legal practice** and the **penal code** should further improve the functioning of the judicial system and streamline the legal process.

More recently, the Council of Ministers has passed **the tax law**, which reduces the tax rate on foreign investment from 45 percent to 20 percent. In addition, substantial progress has been made in a number of other areas, including **company law**, **agency law**, and **labor law**. We are also pressing ahead with **privatization**. In this connection, the very successful sale of 30 percent of the telecommunications company to the public is a major milestone. Indeed, it was the second largest Initial Public Offering (IPO) in the world during 2002. We are continuing to increase private sector involvement in **utilities and infrastructure** development. To speed up development of the utilities, enhance efficiency, and streamline procedures, the Water, Electricity and desalination responsibilities, were merged under one Ministry.

In the **financial** area, measures have been taken to enhance the growth of **mortgage financing** by commercial banks, which are privately owned and run

with significant international participation. Furthermore, approval to open branches has been granted to a number of GCC banks and more licenses to international banks are pending. The Council of Ministers has also passed the **insurance law** which provides the legal framework for the development of this sector. Moreover, the recently passed **Capital Markets Law** (CML) should facilitate the floatation of more IPO's as well as the development of a corporate bond market and other instruments. The CML should also strengthen the operations and efficiency of the stock market, and encourage investment and growth. By the way, the capitalization of the Saudi market has exceeded \$180 billion.

As part of ongoing efforts to expand and diversify the productive base, **the gas initiative** has been launched to expand foreign investment in our hydrocarbon sector. So far, an agreement has been signed with 4 consortia of international companies to undertake investment in non-associated upstream gas projects. Investment is expanding in the mineral sector. Projects to extract Phosphate and Bauxite are already in place.

To further enhance the economy's efficiency and competitiveness, we have made significant progress in **trade liberalization** and **regional integration** under

the GCC and the wider Arab area. Import duty cuts under the Greater Arab Free Trade Area have been accelerated and, with the introduction of the GCC's Common External Tariff, the tariff rates in Saudi Arabia have been reduced for most items from 12 percent to 5 percent and the customs union of the GCC was launched. We also hope a final agreement will soon follow from our continuing negotiations for accession to the **World Trade Organization** (WTO).

Colleagues & Friends,

Expanding employment opportunities for Saudis requires not only faster growth but also the assured availability of a well-educated and trained national labor force. To this end, the **Human Resource Development Fund** has been established to finance the training of Saudi Arabian nationals for jobs in demand by the private sector. The recent separation of social affairs from the **Ministry of Labor** is designed to sharpen the focus on labor issues. Efforts are also continuing to deepen the **education system's** capacity to help bridge the skills gap in the economy. A database to help match Saudis seeking employment in the private sector with job openings has also been developed. A flexible application of the **Saudization policy** aims at increasing the proportion of Saudis in the new

jobs created by the expanding economy while maintaining the competitiveness of the private sector.

Looking back, the progress we have made over the past three decades has lessons that are indeed general and not limited to Saudi Arabia. There is clearly no magic wand to strike underdevelopment with nor is there a simple or simplistic formula for development. As other speakers have shown, economic development is only achievable through complementary sets of fiscal, monetary, banking, and structural policies. The combination and sequencing of these policies have to be developed with unwavering commitment at the highest levels, and in sync with the prevailing socio-economic conditions of each country.

Thank you for your attention.