

Energy, Economic Growth and Islamic and Developing Societies

By

Ali I. Al-Naimi Minister of Petroleum and Mineral Resources Kingdom of
Saudi Arabia

2nd World Islamic Economic Forum
Islamabad - Pakistan
5 - 7 November 2006

Your Excellency, Mr. Shaukat Aziz, Prime Minister of Pakistan, Excellencies, Distinguished delegates to this second World Islamic Economic Conference. I would like to begin by expressing my sincere thanks to the government of Pakistan for sponsoring this important conference and to H.E. Mr. Shaukat Aziz, Prime Minister of Pakistan, for inviting me to address you. I am honored to speak to you today about energy, its role in the economies of developing countries and Saudi Arabia's Oil Policy.

It is clear that the world around us is rapidly changing and that these changes will have profound implications for the future. The information technology revolution, the lowering of trade barriers and the widespread adoption of market principles are shrinking the world and creating a global market place. Traditional national barriers to the free movement of capital, trade and knowledge have already fallen. Capital now flows to the best opportunities, and new ideas and approaches are not limited by geographical boundaries.

Some feel threatened by these changes. I am not one of them. I see the future as one of great promise - where the potential for economic prosperity is greater and more widespread than at any time in history.

I believe this conference is very timely. We are at an important crossroad in our histories. Global change is creating significant new opportunities and challenges for Islamic countries. We must not miss our chance to benefit from this change. Forums like this are important vehicles for exploring new ideas and approaches to cooperation and partnership. We must work together to unleash the economic potential of Islamic nations.

The subject of this session is Managing Energy Demand. I would like to make four points which I believe can be useful for setting the stage for the discussions which will follow this presentation. They are:

First, we should not be intimidated by the prospect of growing energy demand. Rising energy demand goes hand-in-hand with growing prosperity and is a positive indication of our successes, not of failure.

Second, conventional energy resources - oil, gas and coal -- are plentiful and sufficient to meet the world's energy needs for the foreseeable future.

Third, there are huge quantities of non-conventional hydro-carbon resources of very heavy and viscous oils all around the world which can be called upon to meet projected energy demand for the remainder of this century.

Fourth, technology and price will be crucial factors in expanding the available resource base. Technological advances will provide us with increasing innovative and sophisticated means to find and develop the earth's energy resources. However, to ensure this happens, prices must provide sufficient returns to encourage adequate investment.

Robust economic activity will have profound implications for future energy demand. Without energy, economies can not grow to their potential and the aspirations of the world's people for a better way of life can not be fulfilled.

During the last century, the OECD countries effectively harnessed hydrocarbon resources to become major economic powers and to achieve the prosperity they enjoy today. I believe that in this, the 21st century, developing countries will flex their economic muscles, and once again hydrocarbons will play a key role.

Meeting the aspirations of the world's people for increased prosperity can only be achieved through the cooperative efforts of both consumers and producers. The world must find, develop and produce large new quantities of energy on a scale unprecedented in the history of mankind. I believe it can and will be done, but it will not be easy. Our growing world economy will need many different and new sources of energy in the coming decades.

The world's rapidly growing appetite for energy will require greater contributions from a growing number of fuels and technologies such as biofuels, gas-to-liquids, hybrid vehicles and fuel cells. I see great opportunities for entrepreneurial individuals and companies to research, develop and commercialize new sources of energy which can help supplement conventional energy resources.

While I have no doubt that the world is up to the challenge of producing large additional quantities of energy, the key to a successful energy future lies not only in the production of more energy, but also in conservation and efficiency gains.

Conservation and efficiency will contribute to meeting future demand because a BTU saved is equivalent to a BTU produced. Saving energy extends the life of the earth's resource base, thereby helping to ensure that there will be fuel for continued economic expansion many decades into the future.

We all must use energy wisely and as efficiently as possible, in order to achieve the economic benefits derived from our precious natural resources.

Under the right circumstances, alternatives to traditional hydrocarbon fuels, along with conservation and improved efficiency can make an important contribution to the energy supply mix of developing countries. These alternatives will also provide new economic opportunities for Islamic countries in particular and developing countries in general. They can be a catalyst for the creation of new companies and industries, attracting foreign investment, increasing employment and contributing to a more diversified economy.

While non-hydrocarbon fuels will play a growing role in meeting future energy demand, their importance in meeting the world's energy needs should not be oversold. They will be at best complementary and will not significantly diminish the share of traditional hydrocarbon fuels - petroleum, natural gas and coal -- for the foreseeable future.

This is particularly true for petroleum, which will remain the fuel of choice for transportation. This fact has important implications for developing countries where demand for transportation fuels is expected to account for a major portion of the growth energy demand. Viewed in the context of the world's current technology base, petroleum is, and will continue to be, the superior energy choice in terms of ease-of-use and cost effectiveness. The simple reality is petroleum's share of the overall energy mix is unlikely to diminish significantly from today's levels for at least the next 30 to 50 years.

The world's continuing reliance on hydrocarbons will create significant economic opportunities for

resource-endowed developing countries. Almost 80 percent of the world's petroleum reserves and 65 percent of its natural gas reserves are found in developing countries, especially within the Islamic Countries represented here today.

These reserves numbers are only half of the story, however. Just as significant are the resources that remain undiscovered. The extent and intensity of hydrocarbon exploration in developing countries as a whole is relatively low. We know from past experience that as technology advances, and we gain better knowledge of the subsurface, we will find, develop and produce even more energy in developing countries.

The world's expanding need for energy will be an engine of growth for developing countries with energy resources. However, experience shows us that reliance on resource exports can be a double-edged sword, leaving the economies of exporters vulnerable to the inherent volatility of commodity prices.

Recently, we have seen energy exporting countries step out of the old model of over-reliance on resource exports. Instead, developing countries are creating their own models that leverage energy resources, add value, diversify and maximize the benefits to their economies.

There are many possible approaches. Local conditions dictate which is best for any individual country. Where appropriate some countries are choosing to add value by processing petroleum into usable finished products through the construction of refineries and petrochemical plants.

Some are also attempting to leverage their resources by starting companies and developing industries that provide support services to the resource industry. By leveraging their valuable energy resources in this manner, resource rich developing countries can maximize the value of those resources. In doing so, they can create a more robust and diversified economy that produces skilled, high-paying opportunities for their citizens.

Saudi Arabia is a developing country just like the countries represented in this gathering. The peoples of our respective countries have much in common and share many of the same aspirations. Meeting these aspirations requires that we create vibrant economies which offer our young people the opportunity for meaningful employment and financial security.

In the Kingdom, we have taken important steps to reform our economy and we have undertaken initiatives designed to leverage our natural endowment of petroleum resources to create a stronger and more vibrant economy.

We have entered into partnerships with international companies to build new refineries inside the Kingdom while increasing capacity at other plants at home and in joint ventures abroad. We are also expanding our petrochemical industry by building new capacity. Our aim in undertaking these projects is to capture the value added when our oil and natural gas resources are turned into finished products.

We are also creating new opportunities for growth and diversity through the development of industries to provide the support services that are vital to our energy resource industry across the entire spectrum from exploration, to production, to refining and finally marketing for exports. We are currently focused on energy-intensive industries such as iron and aluminum smelters. But we are also expanding the exploitation of our mineral wealth to increase the diversification of our national

economy. Distinguished Delegates, Ladies and Gentlemen;

Now, I would like to discuss the issues of oil supply, price and the policies of Saudi Arabia. We in Saudi Arabia are well-aware that the availability of sufficient quantities of reasonably priced energy is a crucial issue for all countries, but particularly for developing countries. We also know that reliable supply and stable prices are imperatives for sustained economic growth.

Promoting reliable supply and stable prices are the cornerstones of Saudi Arabia's oil policy. Our interests and the interests of all countries are best served when these two conditions are met.

We can not talk about the adequacy or the reliability of future oil supplies without a discussion of oil prices, because therein lies the biggest potential threat to our efforts to ensure reliable energy supplies in the future.

Some say that the preeminent goal of energy policy should be to keep oil prices as cheap as possible in the mistaken belief that low oil prices are a precondition for stability and sustainable economic growth. Experience taught us that in fact, the opposite is true. Allow me to explain.

We have seen that there is a strong negative correlation between low oil prices and the ability of producers to continue supplying energy to growing economies. The low oil prices of the 1980s and 1990s offered little incentive to invest in the energy industry and, as a result, capital was drawn to other industries that offered higher returns. With capital flows into the industry choked off, its capacity to supply energy to consumers stagnated and even declined in some instances. What made matters worse was that low prices were encouraging greater consumption of energy. In retrospect, it was clear that these trends were not sustainable. The higher prices we have seen recently are a direct result of underinvestment during the previous two decades.

Some individuals also mistakenly believe that economic growth is inversely related to the price of oil or to the amount of oil a country imports. Recent experience has shown this is not true. There are many outstanding recent examples of energy import dependent countries achieving impressive economic growth rates during periods of rising oil prices.

Neither high prices nor substantial energy import dependence has been a major impediment for these dynamic economies. We must not think of energy import levels as a negative indicator. They are not a sign of failure; but rather an indicator of success. The more their economies grew the more energy they needed. And, the more energy they used the more their economies grew.

The reality is very low oil prices are not sustainable. In fact, they invariably lead to volatility and subsequently higher prices for the reasons I have just outlined. Sustainable economic growth requires reliable energy supplies and stable prices. These two conditions are only achieved when the needs of both producers and consumers are met. Prices must be high enough to offer an adequate return to producers without hurting consumers. Only then, do the necessary conditions exist for sustainable economic growth.

Reliable supply and stable prices are the metrics by which we measure our oil policy. We do so because they are good for the world economy, and as such, they are good for the long-term health of Saudi Arabia's economy.

Next, I would like to summarize the key elements of Saudi Arabia's oil policy. It includes:

- 1.) A willingness to supply markets with additional oil in times of need to maintain short-term price stability. To this end, we are committed to maintaining at significant cost to ourselves, at least 1.5-2.0 million bid of spare capacity to act as a cushion against unforeseen supply interruptions or surges in demand. This is a powerful tool which helps Saudi Arabia stabilize oil markets in times when dislocations occur;
- 2.) A practice of pricing our crudes according to local market conditions using regional benchmark crudes that reflect the underlying market demand and supply conditions;
- 3.) A belief that market stability is enhanced by greater knowledge of markets and greater market transparency. To this end, Saudi Arabia, under the direction of the Custodian of the Two Holy Mosques, King Abdullah bin Abdulaziz, has established the International Energy Forum Secretariat, which is headquartered in Riyadh. The International Energy Forum provides an opportunity for producers, consumers and industry to work toward the common goal of improving our understanding of markets and how they work;
- 4.) As I discussed earlier, our policy recognizes the need for oil prices to offer an adequate return to producers while protecting consumers, thus providing an environment conducive to long-term stability for oil markets;
- 5.) A recognition that Saudi Arabia has a crucial role to play in expanding energy supplies to meet the world's growing energy needs. Saudi Arabia takes its role as preeminent supplier of energy to the world seriously, and we are undertaking major new initiatives to increase future energy supplies. These initiatives will raise our production capacity to 12.5 million bid by 2009.

We are also investing heavily to increase our capacity in the down-stream where there is a critical shortage of capacity to meet the projected future demand for finished products.

Through these investments, Saudi Arabia hopes to make a significant contribution toward maintaining reliable supplies of energy in the coming decades.

At this point, I want to address Saudi oil policy as it relates to Islamic and developing countries. The Custodian of the Two Holy Mosques, King Abdullah bin Abdulaziz has mandated that Saudi Arabia's oil policies give special attention to developing countries.

We believe that the most important thing that we can do for developing countries is to help create an environment conducive to sustainable economic growth with an oil policy that promotes adequate supplies at reasonable prices. We believe this policy serves the best interests of all developing countries.

Saudi Arabia is committed to an on-going exchange of visits and increasing dialogue with officials from other developing countries in general, and Islamic countries, in particular. We have an active program of helping the oil industries in our fellow developing countries.

To this end, our policy is to encourage relationships with oil and oil service companies from developing countries that desire to work in Saudi Arabia and that have a competitive edge. We also have an active program for sharing our decades of experience through advice, training, exchanging of experts and more.

Distinguished Delegates, Ladies and Gentlemen, in closing I want to thank you again for the opportunity to address you today. As representatives of developing nations, we all aspire to greater prosperity. Reliable energy supplies and stable energy prices are keys to that prosperity.

We in Saudi Arabia know that if the economies of developing and Islamic countries grow, our economy will also grow. We share the same goals and our futures are intertwined. With enlightened policies and realistic expectations from both energy producers and consumers, we can bring about a brighter future for mankind.

Thank you.