

PROJECT DEVELOPMENT & FINANCE | 10 June, 2016

Transforming Saudi Arabia: National Transformation Program 2020 Approved

On 6 June 2016, the “National Transformation Program 2020” was approved by the Saudi Cabinet. This caps a frenetic few months of activity in the Kingdom that began with the approval of “Saudi Vision 2030” at the end of April, saw Ministerial changes and questions as to the role that Saudi Aramco and the Public Investment Fund (“**PIF**”) would play in the country’s plans to reduce its dependency on oil and diversify its economy by encouraging greater private sector participation, reducing public spending and promoting newly-established industries that would create new opportunities for the people of the Kingdom. Below we take an initial look at the National Transformation Program 2020 and the opportunities that may result in the Kingdom.

Background

The National Transformation Program 2020 has been developed to help fulfill Saudi Vision 2030 by establishing strategic objectives and identifying the initiatives necessary for achieving specific interim targets in 2020. It is therefore important to first understand what the “vision” of Saudi Vision 2030 is.

Saudi Vision 2030 is a wide-ranging privatisation and economic reform program that aims to reposition the Kingdom’s economy away from its dependence on oil export revenues and Government spending. It encompasses strategic objectives, targets, outcome-oriented indicators and commitments that are to be achieved by the public, private and non-profit sectors in the Kingdom. Some of the more ambitious targets cited in Saudi Vision 2030 include:

- cutting the Kingdom’s dependence on sale of hydrocarbons by 2020 through the development of non-oil sectors;
- increasing the Kingdom’s overall non-oil government revenue from SR163 billion (\$43.5 billion) to SR600 billion by 2020, increasing it further to SR1 trillion by 2030;
- increasing the private sector’s contribution from 40% to 65% of GDP; and
- raising the Kingdom’s share of non-oil exports in non-oil GDP from the current 16% to 50%.

Key highlights from Saudi Vision 2030 include the following:

- *Saudi Aramco IPO*—Up to 5% of Saudi Aramco will be listed in the Kingdom, with foreign investors entitled to subscribe and with the remainder of Saudi Aramco’s ownership to be held by PIF. Although not confirmed, it is rumored in the market that any IPO will likely incorporate an ADR/GDR listing in New York and/or, possibly, Hong Kong.
- *PIF*—The proceeds of the Saudi Aramco IPO will go to PIF, which is intended to become a sovereign wealth fund with a value up to \$3 trillion, making it a global investment powerhouse. PIF recently made headlines through its

\$3.5bn investment into Uber, which is seen by many as a statement of intent. PIF will have a mandate to kick-start domestic investment and encourage major Saudi corporations to expand across borders and compete in global markets.

- *Privatisation*—Government assets (up to 146 state-owned entities have been mooted), from Saudi Aramco to healthcare and education, will be privatised to help meet the Kingdom's target of diversifying the economy away from oil and to enable the Government's role to shift from providing services to regulating and monitoring the provision of the services by the private sector.
- *Investment by the Private Sector*—Private sector investments, both local and international, will be sought in healthcare, municipal services, housing, finance and energy sectors.
- *Mining Sector*—Structural reforms will be made to the mining sector to ensure that it reaches SR97 billion by 2020, creating 90,000 job opportunities in the process.
- *Defence Sector*—By 2030, 50% of defence spending is intended to be sourced locally by 2030, meaning that local military and defence capabilities will be established, including building aircraft.
- *Renewable Energy*—A competitive renewable energy sector will be established through the gradual liberalisation of the fuels market. The King Salman Renewable Energy Initiative will be launched, which will include the implementation of a legal and regulatory framework that allows the private sector (via public-private partnerships) to buy and invest in the renewable energy sector. A local renewable energy industry will also be developed.
- *Other*—Access to investing and trading in the stock markets, and the process of listing private Saudi companies and state-owned enterprises, will be simplified and liquidity in capital markets will be deepened, the role of debt markets will be fortified and derivatives markets will be developed.

National Transformation Program 2020

Background

The National Transformation Program 2020 has been launched across 24 different Government bodies to help build the institutional capacity and capability required to fulfill Saudi Vision 2030. The first phase of initiative implementation will be launched this year and in the following years, more Government bodies will participate in the implementation. The National Transformation Program 2020 document sets out the strategic objectives, key performance targets and benchmarks of the different Government bodies and links them to Saudi Vision 2030. The appendix to the document sets out the initiatives to be undertaken by the different Government bodies that have been approved by the Council of Economic and Development Affairs and it is worth noting that:

- the National Transformation Program 2020's initiatives should result in the creation of more than 450,000 jobs in the non-Government sector and the localization of more than SR270 billion of content, each by 2020; and
- the private sector will fund 40% of the cost of the National Transformation Program 2020's initiatives.

Energy, Mineral Resources & Industry

Targets to be achieved by 2020: These targets include:

- Decreasing water and electricity subsidies by SR200 billion.

- Boosting annual non-oil commodity exports to SR330 billion from SR185 billion.
- Lifting the percentage of power plant electricity generation through “strategic partners” to 100% from 27%.
- Boosting dry gas production capacity from 12 billion to 17.8 billion standard cubic feet per day.
- Increasing the mining sector’s contribution to GDP from 64% to 97%.
- Increasing local content in total expenditure of private and public sectors from 36% to 50%.
- Increasing the volume of private sector investments in high-potential less-developed regions from zero to SR28 billion.
- Increasing local pharmaceutical manufacturing percentage of total market value from 20% to 40%.

Notable Initiatives: The Ministry of Energy, Industry and Mineral Resources will spend over SR2.5 billion on new initiatives over the next five fiscal years, including coordinating with relevant authorities to build production centres for manufacturing and light industries in Raas Abu-Gamis, Bani-Tamim and Debaa to benefit from the local natural resources that are available.

Transport

Targets to be achieved by 2020: These targets include increasing private sector contribution to developing and operating railways projects (from 5% to 50%) and ports projects from 30% to 70%.

Notable Initiatives: The Ministry of Transport will spend over SR5.5 billion on new initiatives over the next five fiscal years, including the establishment of private sector operation and maintenance concession contracts and development of an integrated program to increase the efficiency of ports.

Health

Targets to be achieved by 2020: These targets include increasing private healthcare expenditure (from 25% to 35%) and total revenue generated by the private sector (from SR300 million to SR4 billion).

Notable Initiatives: The Ministry of Health will spend over SR23 billion on new initiatives over the next five fiscal years, including reform and restructuring of primary health care, the establishment of private public partnerships, the privatization of one of the medical cities and the localization of the pharmaceutical industry;

Saudi Arabian General Investment Authority

Targets to be achieved by 2020: These targets include:

- Raising direct foreign investment from SR30 billion to SR70 billion.
- Implementing 218 administrative and procedural reforms aimed at improving the business environment.
- Developing a unified national investment vision to promote and direct investments supporting the national economy, resulting in SR2.3 trillion in new investment opportunities.
- Reducing time needed to issue new business permits from 19 days to one day.

Notable Initiatives: The Saudi Arabian General Investment Authority will spend over SR1 billion on new initiatives over the next five fiscal years, including the development and execution of plans for localizing construction material and equipment industries and the transportation and logistical services sector, establishment of a government agency to manage and execute mega projects, launching the unified permits for foreign investors and the execution of the “National Investment Plan.”

Haj, Umrah and Tourism

Targets to be achieved by 2020: These targets include:

- Increasing total new tourism investment from SR145 billion to SR171.5 billion.
- Increasing total revenues from partnerships with the private sector from SR80 million to SR19 billion.

Notable Initiatives: The Saudi Commission for Tourism & National Heritage will spend over SR10 billion on new initiatives over the next five fiscal years, including the development of Ola City, Uqair, Farasan Islands and Okaz City.

Royal Commission for Jubail and Yanbu

Targets to be achieved by 2020: These targets include:

- Increasing the number of value-added basic manufacturing and transformation products from 432 to 516.
- Increasing total RCJY cities’ industrial production from 252 million tons to 309 million tons.
- Increasing the size of the private sector’s new investments from SR681 billion to SR1.065 trillion.

Notable Initiatives: The Royal Commission for Jubail and Yanbu will spend over SR41.5 billion on new initiatives over the next five fiscal years, including the development of new infrastructure in Yanbu Industrial City (including the localization of the renewable energy industry and rubber industry and establishment of industrial gases and steam networks), Jubail Industrial City, Ras Al-Khair Industrial City and Jazan Economic City.

King Abdullah City for Atomic and Renewable Energy

Targets to be achieved by 2020: These targets include:

- Enabling atomic energy to contribute to the national energy mix.
- Enabling renewable energy to contribute to the national energy mix in the amount of 3.45GW.
- Increasing the local content in the industrial and service value chains and localization of expertise in the renewable energy sector (from 25% to 35%) and the atomic energy sector (from 25% to 30%).

Notable Initiatives: King Abdullah City for Atomic and Renewable Energy will spend over SR5 billion on new initiatives over the next five fiscal years, including in relation to:

- the atomic energy sector, identification and preparation of the construction locations of the first nuclear power plant sites and provision of necessary infrastructure, development of necessary human capabilities, localization of small nuclear reactors and industry, localization of nuclear fuel cycle in uranium production to achieve investment returns and development of necessary legislation; and

- the renewable energy sector, the launch of the “King Salman Renewable Energy Initiative,” development of necessary human capabilities, localization of renewable energy technology to support the Kingdom’s power and water desalination sectors and development of necessary legislation.

Water

Targets to be achieved by 2020: These targets include:

- Percentage of desalinated water production through strategic partners to increase from 16% to 52%.
- Percentage of treated water production through strategic partners to increase from zero to 20%.
- Percentage of cities covered with water and sewage services through The National Water Company to increase from 42% to 70%.

Notable Initiatives: The Ministry of Environment, Water and Agriculture will spend over SR12.9 billion on new initiatives over the next five fiscal years, including the expansion of the number of the cities covered by the services of The National Water Company in collaboration with the private sector.

Housing

Targets to be achieved by 2020: These targets include:

- Percentage of real estate sector contribution to the GDP to increase from 5% to 10%.
- Percentage of available housing units (new and unoccupied) to total number of subsidy-eligible citizens to increase from 10% to 50%.

Notable Initiatives: The Ministry of Housing will spend over SR59 billion on new initiatives over the next five fiscal years, including savings programs to enable financing applicants to save a portion of the cost of owning their own home, encouraging private sector real estate developers to invest in housing projects (including the use of fast track licences and special finance packages) and establishing partnerships with private sector developers to develop government lands into large-scale housing projects.

Education

Target to be achieved by 2020: These targets include increasing the percentage of students in non government higher education from 6% to 15%.

Notable Initiatives: The Ministry of Education will spend over SR24 billion on new initiatives over the next five fiscal years, including encouraging private sector investment in public education in the Kingdom.

Technology

Targets to be achieved by 2020: These targets include:

- Number of establishments created to develop local content to increase from 17 to 8.
- Number of technology companies emerging from universities through the “Innovative Companies Program” to increase to 800.
- Number of localized and developed technologies in targeted sectors to increase to 125.

- Number of patents issued by the Kingdom to increase from 700 to 5,000.

Notable Initiatives: The King Abdulaziz City for Science and Technology will spend over SR8.3 billion on new initiatives over the next five fiscal years, including the localization and transfer of technology in building and construction, mining and advanced materials, health, energy, information and communication, water, oil and gas and transport and logistics.

Opportunities

Two recent transactions suggest that foreign and local investors should be optimistic that Saudi Vision 2030 and the National Transformation Program 2020 will result in significant opportunities both within the Kingdom and in connection with Saudi entities looking to do business outside of the Kingdom.

Recently, General Electric agreed with Saudi Arabian Industrial Investments Company to participate in as much as \$3 billion of investments across industries in the Kingdom, evidencing the Kingdom's commitment to developing local industry through joint ventures with foreign companies, facilitating direct foreign investment and increasing the participation of the private sector in the Kingdom's economy. We expect to see many more transactions of this nature (which may also take the form of public private partnerships) involving foreign partners in sectors like mining, manufacturing, defence, health, education, real estate, tourism, technology, finance, social services, transport, energy and petrochemical sectors. With increased private sector investment, we would also expect to see an increased demand for debt finance which will be one of the challenges for investors given the current squeeze on liquidity of local banks.

PIF's recent \$3.5 billion investment in Uber should also be seen as confirmation of the Kingdom's commitment to looking beyond the Kingdom for ways of accessing technology and know-how, boosting employment opportunities and encouraging entrepreneurship of Saudi entities, as well as earning strong equity returns. We expect PIF to be quite active over the coming years as it pursues further foreign investments, especially when the proceeds of the Saudi Aramco IPO become available. We do expect, however, that PIF may look to tap debt markets to finance some of its investments, which was rumoured to be the case on the Uber investment.

Given the Kingdom's commitment to increasing private sector investment and reducing Government expenditure, we expect to see a flurry of privatization activity, which should present many opportunities for lenders, local investors and foreign investors in connection with Government asset sales and sales of shares in Government-owned companies. We also expect increased levels of IPO activity through the implementation of the Government's privatisation program.

We expect that over the coming months, many more new initiatives will be announced in the Kingdom in connection with Saudi Vision 2030 and the National Transformation Program 2020 and we will continue to monitor developments with great interest.

Shearman & Sterling LLP has worked in the Middle East for over 40 years on some of the region's most significant transactions. In the Kingdom, Shearman & Sterling LLP has offices in Riyadh, Jeddah and Al-Khobar through its association with Dr. Sultan Almasoud & Partners and our practice in the Kingdom is fully integrated with Shearman & Sterling LLP's global network of 20 offices in the Middle East, Asia, Europe and the Americas. This

gives our Saudi Arabian clients and our international clients doing business in the Kingdom direct access to a top tier Saudi law practice that is backed by the skills and experience of every expert in our global network.

CONTACTS



Marwan Elaraby
Co-Regional Managing Partner of
Europe, Middle East & Africa
T +971.2.410.8123
marwan.elaraby@shearman.com



Dr. Sultan Almasoud
Partner
Saudi Arabia
T +966.11.211.2000
sultan.almasoud@sa.shearman.com



Sanjarbek Abdukhalilov
Partner
Saudi Arabia
T +966.11.211.2000
sanjarbek.abdukhalilov@sa.shearman.com



Iain Elder
Partner
London
T +44.20.7655.5125
iain.elder@shearman.com



Brendan Hundt
Counsel
Saudi Arabia
T: +966.11.211.2000
brendan.hundt@shearman.com



Matthew Powell
Partner
London
T: +44.20.7655.5910
matthew.powell@shearman.com

ABU DHABI | BEIJING | BRUSSELS | DUBAI | FRANKFURT | HONG KONG | LONDON | MENLO PARK | MILAN | NEW YORK
PARIS | ROME | SAN FRANCISCO | SÃO PAULO | SAUDI ARABIA* | SHANGHAI | SINGAPORE | TOKYO | TORONTO | WASHINGTON, DC

This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

9 APPOLD STREET | LONDON | EC2A 2AP | UNITED KINGDOM

Copyright © 2016 Shearman & Sterling LLP. Shearman & Sterling LLP is a limited liability partnership organized under the laws of the State of Delaware, with an affiliated limited liability partnership organized for the practice of law in the United Kingdom and Italy and an affiliated partnership organized for the practice of law in Hong Kong.

*Dr. Sultan Almasoud & Partners in association with Shearman & Sterling LLP