

# Saudi-French Trade Relations

A long history of *fraternité*

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## Disclaimer

These notes should be read in conjunction with the concluding Disclaimer, which forms part of them.

- ▶ Thanks to oil exports, the balance of trade with France has consistently favoured Saudi Arabia
- ▶ The proposed petroleum processing plant in Jubail will be the largest Saudi-French joint venture
- ▶ France's expertise in nuclear power generation could help the Kingdom diversify its energy sources

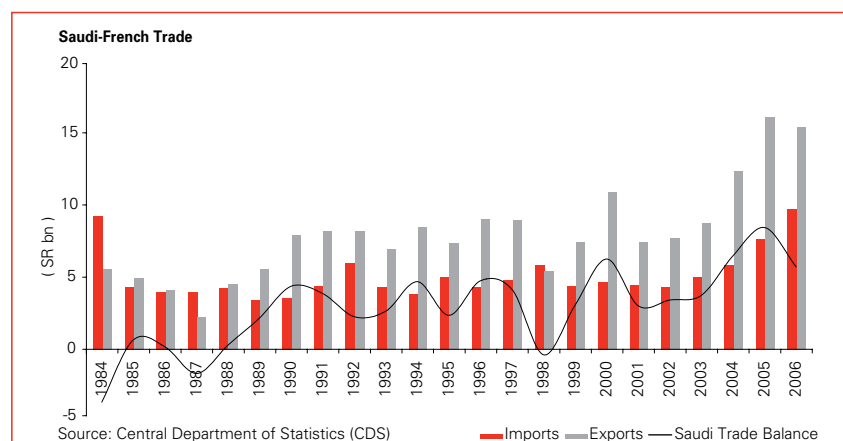
## Diplomatic ties

Formal relations between Saudi Arabia and France date back to the mid-1920s. Indeed, France had maintained a consulate in Jeddah since 1841, prior to becoming one of the first countries to recognise King Abdul Aziz's government in 1926. Ties between the two nations strengthened during the early thirties when France sent an economic delegation to the Kingdom, followed by a diplomatic delegation in 1936.

After the Al-Jazirah Pact in 1931, France established a weapons factory in Al-Kharj – one of the very first in the greater Arabian Peninsula. The foundations of the current strategic partnership were laid by King Faisal and former President Charles de Gaulle in 1967. King Abdullah paid an official visit to Paris in July 2007 and met with the newly elected French President, M. Nicolas Sarkozy.

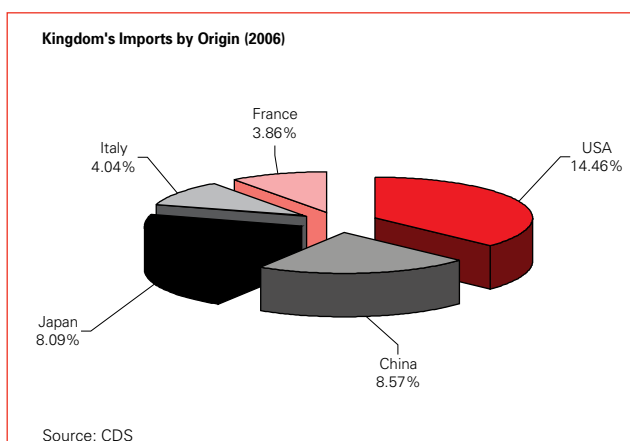
## Competition from the East

In 2007, Saudi Arabia ranked as France's third-largest export market in the Middle East, after Turkey and the UAE. French exports to Turkey in 2006 exceeded SR 26.2bn (\$ 7bn). In 2006, France was the seventh largest exporter to the Kingdom overall, marginally behind the UK with SR 10.3bn (\$ 2.7bn) and Italy with SR 10.5bn (\$ 2.8bn).



Since 2000, the Kingdom's imports from France have grown by 116%, though it was only after 2002 that volumes increased significantly. Imports from France stood at SR 4.3bn (\$ 1.1bn) in 2002 and, by 2006, had reached SR 10.08bn (\$ 2.88bn). A similar increase in exports was witnessed at the same time among France's main competitors: the USA, the UK, Germany, Italy and Japan. However, French exports have not kept pace with the rapid increase in total Saudi imports over the past four years and, as a result, there has been a small decline in France's total share of Saudi markets.

In 2000, French exports comprised 4.1% of all imports to Saudi Arabia, whereas by 2006 it had declined to 3.86%. But a similar decline in market share was experienced by all Saudi Arabia's traditional trading partners, except Germany. This can be attributed to the increasingly competitive positions of Asian countries, such as China, India, Thailand and South Korea. Asian imports have grown consistently, as the pricing and quality of products have helped win greater market share. Low-priced consumer goods from Asia are in tune with the needs of the market, which has been more price-sensitive in recent years.



## Perfume, poultry and passenger planes

In terms of product categories, France's main exports to Saudi Arabia comprise consumer and food products (26%), including clothes, leather goods and perfumes; followed by intermediary goods (25%), such as minerals, paper and metal goods; and lastly, professional equipment (21%), including electrical, electronic and various mechanical items.

In 2006, according to the latest data from the Central Department of Statistics, SR 361m (\$ 96m) worth of French perfumes was exported to the Kingdom. In the same year, various pipes used in the oil and gas sector reached an export value of SR 483m (\$ 129m). Looking forward, we expect agricultural and foodstuff products from France to increase, as well the sale of electronic and electrical equipment. The current increase in French food products is due not so much to the arrival of French hypermarkets such as Carrefour and Géant, but mainly to an increase in frozen poultry meat sales. With the increased global and local incidence of avian influenza (including at some of the Kingdom's 500 poultry farms), imports of French frozen poultry have grown over the past 18 months, despite the appreciation of the Euro against the US Dollar. France's market share in the frozen poultry business (18%) continues to be second to Brazil (c.78% market share in 2007). The imported poultry market is expected to reach SR 1.9bn (\$ 507m) in 2008.

The sale of passenger aircraft is another area in which France is well placed to benefit. One such example is the December 2007 deal between Saudi Arabian Airlines and Airbus to modernise

its fleet with 22 new A320 aircraft. This contract is SAA's first order with Airbus in more than two decades, having previously been the launch customer for the A300-600 range, first delivered in 1984. In addition, at the Paris Air Show in June 2007, National Air Services (NAS) signed a firm agreement for some 20 A320s, with purchase rights for 18 more.<sup>1</sup>

## French firms across the Kingdom

Despite the rise in its exports to Saudi Arabia, France's Foreign Direct Investment (FDI) in the Kingdom has historically remained low. As of 2005, the stock of French FDI had not exceeded SR 4.7bn (\$ 1.2bn), which according to data from the Central Bank of France, gave Saudi Arabia a ranking of 43rd, after Finland.

By 2006, 60 French firms were present in Saudi Arabia, employing over 20,000 people. Calyon's investment in Banque Saudi Fransi (BSF), established in 1977, represents 29% of the total French FDI stock in Saudi Arabia.<sup>2</sup> Indeed, companies in the financial services sector now make up 80% of France's interests in the Kingdom.

There have been several notable French investments since 2000, including the 50% shareholding valued at SR 178m (\$ 47.6m) of Group Danone in the world's largest-capacity integrated dairy farm, Al Safi-Danone. Recently, Saint-Gobain invested SR 90m (\$ 24m) in the local textile-sector business, Al Obeikan. And since 2003, Total has been participating (30%) in a consortium with Shell (40%) and Saudi Aramco (30%) to explore for and produce natural gas in the Empty Quarter.

Other French companies with a significant presence in the Kingdom include Thales (telecommunications), Schneider (advanced materials), BNP Paribas (banking), AXA and AGF (insurance), Argas (seismic projects) and Lactalis (food). As well as expanding in Riyadh, Accor will be the first French hotel group to open outlets in the holy cities of Makkah and Madinah. And Alstom, the world leader in high-speed trains with over 500 TGV trains in service, has made a bid for the 450 km Makkah-Madinah rail-link project.

The largest of all investments, however, would be the proposed joint venture between Saudi Aramco and Total in Jubail, to process 400,000 b/d of heavy/sour crude into premium fuels. Despite the rising engineering, procurement and construction (EPC) costs, it appears that both parties intend to go ahead with this SR 48.7bn (\$ 13bn) plus project. The importance of refining heavy crude oil will grow in coming years, with the increasing availability of heavier crude over lighter grades. The worldwide shortage of refining capacity for heavy crude oil further underlines the importance of building Saudi Arabia's domestic capacity.

## From crude oil to EuroDisney

Since 1984, the balance of trade with France has favoured Saudi Arabia, and only twice (in 1987 and 1998) have the French enjoyed a trade surplus with the Kingdom. But the delivery of military equipment, at various times, has historically helped keep France's trade deficit under control.

<sup>1</sup> NAS currently manages a fleet of 47 aircraft, six of which are Airbus A320s.

<sup>2</sup> Credit Agricole-Indosuez holds a 31.1% stake in Banque Saudi Fransi (BSF).

In terms of the Kingdom's exports, Saudi Arabia was the third largest supplier of crude oil to France in 2006. According to Eurostat, French oil imports totalled 1.57 million bbl/d – the largest source of this being Norway (256,000 bbl/d), followed by Russia (186,000 bbl/d) and Saudi Arabia (166,000 bbl/d). As a result of this trade, 96% of Saudi Arabia's total exports to France in 2006 was crude oil, with the remainder mainly comprising various chemical products.

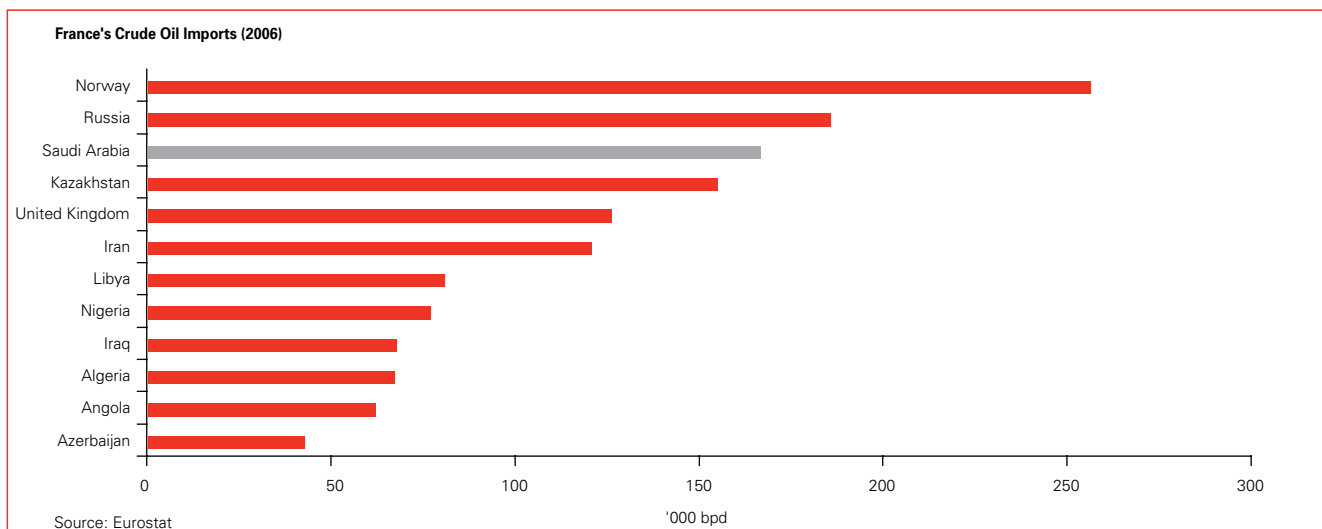
Saudi investment interests in France are focused primarily on entertainment and real estate. As of 2005, Saudi Arabia ranked as the 30th largest investor in France, with total stock of investments amounting to SR 2.6bn (\$ 701m). Kingdom Holdings has a 17% stake in EuroDisney, the company that runs Disneyland Paris and owns one of Paris's most luxurious hotels, the George V. In Paris, property is another popular investment for Saudis, who are well represented in the 7th, 8th and 16th residential districts, as well as the famous Latin Quarter. In 2007, Saudi FDI amounted to just SR 165m (\$ 44m).

## Forty years of defence co-operation

Defence procurement is another key area of French involvement. Currently, around 15-20% of the Saudi procurement needs are met by France.

Military co-operation between the two countries dates back to the late 1960s, when France played an important role in developing the Royal Land Forces. The first Saudi armoured brigade, designated the 4th Armoured Brigade, was structured and trained along French lines. It was equipped with 300 AMX-30 battle tanks and 500 AMX-10P armoured infantry vehicles, both French-made.

In the seventies and eighties, the Kingdom procured armoured vehicles from France to support its four mechanised brigades. The Royal Navy has also expanded with French assistance, known as the Sawari programme. In effect, the Royal Navy's Red Sea fleet is trained and procured by France, whereas the USA and the



UK support the fleet's position in the Gulf. The first phase of the Sawari programme included four ships (Al Madinah-class frigates) based in the Red Sea and built in France in the mid-1980s. Sawari II involved the procurement of a modified version of the Lafayette-class frigate, known as the Al Riyadh class.

Currently pending is the procurement of helicopters for the Kingdom's expanding fleet, with some 150 helicopters expected to be purchased from either France or Russia. Of particular interest to France is also the contract to build a 901km-long security fence along Saudi Arabia's border with Iraq, at a cost of up to SR 4bn (\$ 1.07bn).

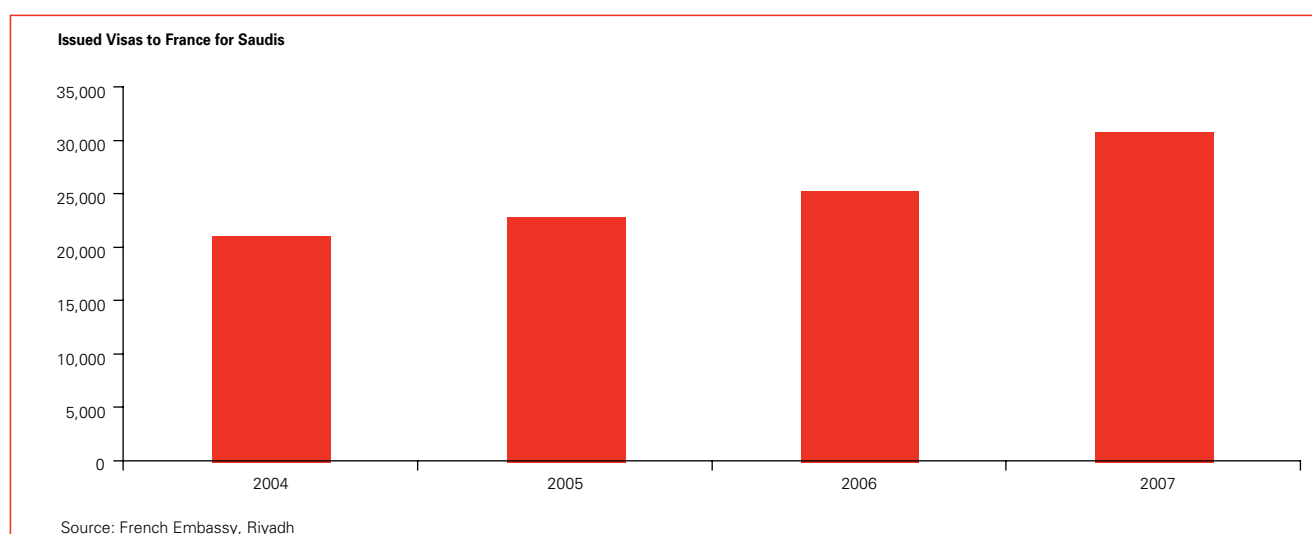
## Language barrier

France itself is a popular destination for Saudis, who represent a major source of foreign currency for French businesses. As the Euro has risen against the US dollar, France has

seen an increasing number of Saudis visiting their country every year. However, currency fluctuation is of little consequence to most of those visiting France, as they generally have a high income profile.

In part, France and other European locations have increasingly replaced the US as travel destinations for the high-income Saudis since 2001. During 2007, 30,911 Saudis visited France, mostly for leisure purposes (92%), which represented a 22% increase over 2006.

Educational exchanges are slowly picking up, but have a long way to go in comparison to other Anglo-Saxon destinations. This is mainly due to the fact that French is not widely learned or spoken in Saudi Arabia. The minimum language training for enrolment at a French university is usually two years, compared to one year for an English-speaking university. Some 450 Saudi students are currently enrolled at French universities.



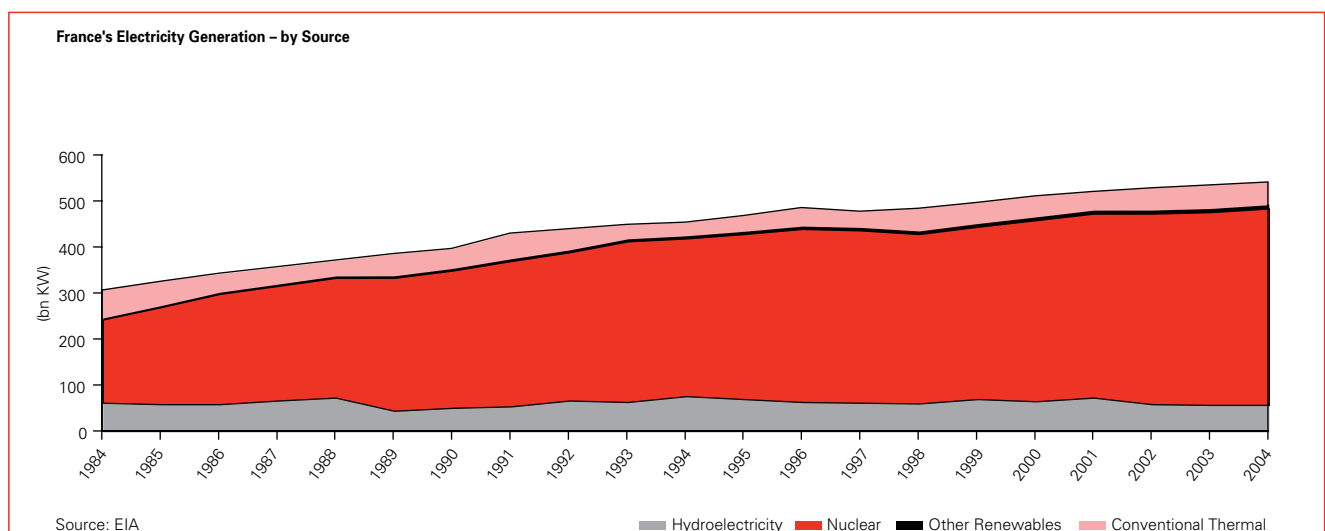
## An opportunity for the Kingdom's future

Behind the USA, France is the world's second-largest generator of nuclear energy. In 2004, France's nuclear reactors supplied 79% of the total national electricity needs – whereas, back in 1973, fossil fuels still accounted for around 65% of gross power output.

French nuclear power is efficient and low-cost – which helps make the country's electricity tariffs the lowest in Europe. Government-owned Areva controls all aspects of the nuclear-power sector in France.<sup>3</sup>

Saudi Arabia needs to diversify its energy sources, reducing current and additional future fossil-fuel power generation. Feedstock for planned capacity increases would primarily be crude oil; and with around 8% of Saudi Arabia's power plants already being oil-fired, the loss of potential gains from oil at \$ 80-90 per barrel is high.

The nuclear electricity sector – and possibly expertise imported from France – may prove an attractive and viable option for the Kingdom. We estimate that Saudi Arabia will require at least 30 gigawatts (gw) of additional power-generating capacity by 2025, nearly double the current capacity. In the decades ahead, Saudi Arabia should depend predominantly on nuclear energy for electricity generation.



<sup>3</sup> France has partnered Germany to develop the European Pressurised Reactor (EPR). The EPR is a third-generation reactor, designed to be safer, more efficient and less susceptible to terrorist attack. Each EPR should produce around 1,600 megawatts (mw) of electricity, against 900mw for most second-generation reactors.

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