Opportunities in the Saudi Defense Sector and the Impact of U.S.-Saudi Defense Spending

Tuesday August 8, 2017

In collaboration with:
## About the USSABC

### Deep Roots
- Established in 1993 from the U.S.-Saudi Arabian Joint Economic Commission
- Benefits from distinguished and experienced Saudi and U.S. Board of Directors
- Experienced staff in Washington, D.C. /Riyadh

### Unique Profile
- Only bilateral organization **solely** focused on the commercial relationship between Saudi Arabia and the U.S.
- Private sector, non-profit, objective, membership organization

### Goal
- Facilitate **new partnerships** between the U.S. and Saudi public and private sectors

### Clear Deliverables
- 24+ years advising Fortune 500 and SMEs from 48 U.S. States and Saudi entities market receptivity in both countries
- U.S. companies **look to us** for clarification and understanding of Saudi policies and Saudi companies consult us on the U.S.

### Unique Experience
- Actual and recorded business transactions and technology transfers successes
- Delivery of actionable business information
- Successful planning and execution of networking events
- Organization of delegations of American investors to Saudi Arabia
USSABC Programs and Services

**Programs**
- Business Development Missions
- Sector-Focused Conferences
- Business Opportunities Forum

**Publications**
- A Business Guide to Saudi Arabia
- U.S.-Saudi Business Brief
- Industry Sector Reports

**Business Advisory Services**
- Market Entry Strategy
- Partner Identification and Introduction
- In Country Appointments
What Makes Us Different

We are not... an \textbf{IMPLEMENTER} of business partnerships

but we are...
Alliances Across Borders

Our relationships have refined our ability to understand the needs of American and Saudi companies and government agencies and improve our tools to best respond to their requirements.

**Strategic Alliances**

**Saudi Stakeholders**
- MOU for Strategic Promotional Collaboration with Royal Commission for Jubail and Yanbu
- Marketing Agreement with King Abdullah Economic City

**U.S. States and Government Agencies**
- State of Pennsylvania
- State of Virginia
- State of Washington
- State of Oregon
- State of Florida
- U.S. Department of Commerce

**U.S. and Saudi Private Sector Players**

*Images of strategic alliances.*
USSABC Success Highlights

Known USSABC Success by Company Size, 2012-2017

- Small: 14%
- Medium: 25%
- Large: 61%

86% are SMEs

Known USSABC Success By Company Presence In KSA, 2012-2017

- New to market: 39
- Recent entrant: 48
- Veteran: 49

Total recorded successes: 136
USSABC - Conduit to the Saudi Market

Secure Access to U.S. Executives

- Webinars, Roundtables, Seminars at Tradeshows
- High profile Business Conferences
- Business Development Missions

Promote Saudi Industry-Specific Opportunities

Build Market Commitment

Strengthening Bilateral Business Relations through Trade and Investment
Defense in Saudi Arabia

- Saudi Arabia is the world’s third largest military spender behind the U.S. and China and the largest importer of arms.

- Ministry of Defense and Aviation (MoDA) Structure:
  - The Saudi Arabian National Guard (SANG) is an independent entity reporting directly through the Minister of the National Guard.

- In 2016, Saudi Arabia spent $82 billion on defense, not including military operations.

- The 2017 budget allocated $50.9 billion to military and security services.

- Security has emerged as a theme – homeland security in securing northern and southern borders, counter-terrorism, cybersecurity.
Increasing Sector Demand

- There is a strong outlook for the security and defense sector as Saudi Arabia continues investment, signs contracts with international firms, and increases JVs for the design, assembly, manufacturing and maintenance of military equipment.

- The Saudi defense sector has a 1.8 percent forecasted compound annual growth rate (CAGR).

- Local employment in this sector related to government expenditure is expected to grow steadily at a 1.3 percent CAGR.

- Continued growth of the sector reflects the region’s geopolitical situation.

Source: USSABC, REMI
Defense Priorities and Initiatives Under Vision 2030

- **Localization**: Vision 2030 calls for localizing 50 percent of procurement for Saudi Arabia’s military requirements. This target is in line with KSA goals for self-sufficiency and growth by directing spending toward in-country suppliers. At the creation of Vision 2030, only around 2 percent of all military purchase are produced in Kingdom.

- **Creation of Saudi Arabian Military Industries (SAMI) in May 2017**: Vision 2030 called for a government-owned holding company for military industries. SAMI seeks to be one of the world’s top 25 defense companies by 2030.

- **Defense industrialization**: Saudi Arabia has begun to develop less complex industries like spare parts, armored vehicles, and basic ammunition.

- **Applying offsets and contract mechanisms**: Saudi Arabia aims to promote “direct” offset projects where the selling country will join in co-production, licensing, and supply arrangements for the purchased products.
Localizing Defense

• Looking forward, contracts with foreign suppliers, strategic partnerships, and funding of research facilities will be key focuses for development of the defense sector.

• In the short term, localization will require setting up JVs between international defense equipment manufacturers and Saudi firms, especially for assembly and repair.

• Saudi Arabia can achieve localization in the long-run by requiring that Saudi companies manufacture domestically, including the design and production of hardware.

• Goal to develop the domestic aeronautics sector, including civil aviation, aimed at military capabilities.

• There will be a need for human capital and continued training to maintain expertise to effectively operate military systems and technology in Kingdom.
Saudi Arabian Offset Programs

• Saudi Arabia established an Offset Program in 1984, and was the first country in the Gulf Cooperation Council (GCC) to do so. The program began with the Peace Shield programs with the U.S.

• **Indirect offset projects**: (previous arms agreements)
  o The country making the sale assists the importing country with investment strategies and general development, unrelated to the contract item.

• **Direct offsets**: (promoted under Vision 2030)
  o Licensing, co-production, technology licenses, other supply arrangements between the purchasing and selling countries to supplement elements of the purchased product.

• **Offset models**:
  o **Co-production overseas**: government-to-government or producer agreements permitting acquisition of the technical information and tooling to manufacture all or part of a defense contract. While the most advanced offset and localization, is dependent on a high degree of local technology and R&D expertise.
  
  o **Technology transfer**: assistance in establishing defense industry capabilities by providing valuable technology and manufacturing expertise.
  
  o **Directed subcontracting**: procurement of components made domestically for incorporating or installation of items sold under direct contracts.
Saudi Arabian Military Industries (SAMI)

• Formed in May 2017 as a subsidiary of the Public Investment Fund.
• SAMI to change procurement procedures for the Ministry of Defense.
• The goal is for SAMI to become the offset partner for Western defense groups and the backbone of Saudi Arabia’s military-industrial complex.
• Establishment of companies through JVs with global equipment manufacturers.
• Manufactures products and provides services across business units that complement KSA’s future military requirements.
• Cooperates with local military companies and is charged with creating new business units to ensure alignment with latest developments in military industries.
• The creation of SAMI is a move to consolidate the military industry.
Key Players in the Saudi Defense Sector

Leading Saudi companies and institutions in defense:

• **Military Industries Corporation (MIC):** Currently largest defense company in Saudi Arabia. Supports national security through the creation of a sophisticated military industry – purchase of arms, ammunition, military equipment.

• **Advanced Electronic Company (AEC)**

• **Alsalam Aircraft**

• **Middle East Propulsion Company (MEPC)**

• **International Systems Engineering (ISE)**

• **Saudi Arabian Military Industries (SAMI)**
Selling to the Market and Restrictions

- U.S. companies may work alongside U.S. and Saudi Government to find partnerships that are permissible with regulations and commercially viable.

- CEDA maintains a ‘negative list’ of sectors in which foreign investors have limitations. The list prevents defense contractors from participating in certain activities in the military sector (manufacturing of military equipment, devices, uniforms). Within the service sector, it has included a restriction on catering to military sectors.

- The local client, normally the Saudi government, oversees the importation of products and customs clearance as part of the sale and purchase of armaments and other military equipment.

- Non-Saudi companies that are registered in GCC countries may obtain SAGIA licenses to undertake the activities in sectors with restrictions on a case-by-case basis.

- Before applying for a SAGIA license, it may be beneficial for defense contractors to arrange meetings with the Ministry of Defense or with branches of the Saudi Arabian Armed Forces to gain support in the process.
U.S. Support to Develop Saudi Arabia’s Local Defense Industry

- **Boeing** announced in Aug. 2015 that it would open an in-country helicopter MRO facility, joint venture with Alsalam Aircraft Co. and Saudia Aerospace Engineering Industries.


- **Raytheon** signed agreement with Saudi Arabia Military Industries Company in 2017 during state visit of President Trump, also announced formation of Raytheon Arabia subsidiary to develop defense, aerospace and security capabilities in Kingdom.
Emerging Opportunities Summary

- Strategic partnerships between research institutions and companies aligned with Vision 2030, including JV’s intended to localize military spending

- Security needs for the oil & gas industries, including offshore facilities (Saudi Aramco bids to increase security – July 2017)

- Investment in military hardware

- Non-Saudi companies registered in GCC countries may in some cases obtain SAGIA licenses for military manufacturing and other activities on ‘negatives list’

- IT protection – cyber security needs:
  - Cyber Security Summit (Riyadh 2016) – KSA’s cybersecurity market will grow to over $3.5 billion by 2019 with an annual growth rate of 14.5%
  - Active foreign companies – Includes Microsoft, IBM, Lockheed Martin, BAE Systems, Raytheon, Selex ES, Symantec

- Development of industrial and manufacturing capabilities
  - Meeting industrialization goals as part of Vision 2030 will require building local expertise through training and building a supporting infrastructure, such as IT
U.S.-Saudi Defense Deals

• The United States remains a major defense supplier to Saudi Arabia, with $97 billion in active and open Foreign Military sales cases.

• New defense spending as of the May 2017 visit to Saudi Arabia by U.S. President Donald Trump:
  
  • Boeing reported $50 billion worth of deals, expected to support Saudi Arabia’s goals of localizing spending.
  • Saudi Arabia expression of interest in acquiring over $28 billion in weapons from Lockheed Martin.
  • JV between TAQNIA Aeronautics and Lockheed Martin for final assembly and completion of 150 S-70 Black Hawk utility helicopters for the Saudi government.
  • General Dynamics letter of intent to localize the engineering design and manufacturing of armored combat vehicles.
  • Nearly $18 billion of spending discussed to upgrade Saudi Arabia’s military command and control.
  • A $6 billion deal for Saudi Arabia to purchase Littoral Combat Ships.
  • As part of the arms deal, the U.S. State Department approved the potential sale of over $1.4 billion of military training equipment to Saudi Arabia. This included Lockheed Martin radar systems ($662 million) and a training program for the Royal Saudi Air Force ($750 million).
  • As much as $110 billion of defense commitments announced.
About REMI

Regional Economic Models, Inc. (REMI) is a World Leader in Economic Policy Modeling

<table>
<thead>
<tr>
<th>Software</th>
<th>Support</th>
<th>Services</th>
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<tbody>
<tr>
<td>• REMI tools are the industry standard for rigorous policy analysis.</td>
<td>• REMI licenses include access to full remote technical support and model assistance.</td>
<td>• Macroeconomic impact consulting</td>
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<td>• PI+</td>
<td>• REMI users have myriad resources to enhance their understanding and skill in the model.</td>
<td>• Analysis of prominent state and federal legislation</td>
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<td>• TranSight</td>
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<td>• Led by REMI’s team of highly experienced and qualified research economists</td>
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what does REMI say?™
About REMI

REMI’s 35-year history of rigorous academic research and software development has led to the development of the industry standard in macroeconomic research methodology:

**Input-Output**
Close analysis of inter-industry relationships

**General Equilibrium**
Estimate of long-run stability of the economy allows for analysis of policy decisions

**Econometrics**
Advanced statistical analyses underpinning the model

**Economic Geography**
Effects of geographic concentration of labor and industry

**Integrated REMI economic modelling approach**
Prior Analyses

REMI’s flagship product, PI+, is the industry standard for comprehensive analysis of the economic and demographic consequences of military spending.

- Utah’s Defense Sector: Economic Impacts of the Military and Veterans (2017)
- Economic Impact of DoD Activity in Maryland (2017)
- Economic impact of the military in North Carolina (2015)
Military Spending and the Economy

The top five supply chain suppliers make up over 94% of intermediate demand. High concentration in skilled/technical labor; high-tech components; and vehicle parts.

Input-output supply chain linkages specific to federal defense purchases.

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<tr>
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<tbody>
<tr>
<td>69</td>
<td>Federal Military</td>
<td>0.79481</td>
<td>0.00753</td>
<td>0.0000</td>
</tr>
<tr>
<td>49</td>
<td>Professional, scientific, and technical services</td>
<td>0.05792</td>
<td>0.12083</td>
<td>0.0101</td>
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<tr>
<td>16</td>
<td>Other transportation equipment manufacturing</td>
<td>0.04215</td>
<td>0.00770</td>
<td>0.0001</td>
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<tr>
<td>13</td>
<td>Computer and electronic product manufacturing</td>
<td>0.02332</td>
<td>0.05578</td>
<td>0.0024</td>
</tr>
<tr>
<td>15</td>
<td>Motor vehicles, bodies and trailers, and parts manufacturing</td>
<td>0.02378</td>
<td>0.02386</td>
<td>0.0118</td>
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<tr>
<td>28</td>
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Military Spending and the Economy (cont’d)

Labor intensiveness: Military spending creates a large number of direct US jobs

Table: Labor intensiveness

- Capital: 0.5244
- Labor: 0.41684
Defense Spending and Economic Development

Defense Spending

- Military Personnel
  - Consumer spending; demographic shifts
  - Impact of dependents

- Equipment and weapons purchases
  - Manufacturing jobs and output

- Investment in bases and facilities
  - Construction, installation, repair/maintenance and operations
Current Distribution of US Defense Spending
Impact Simulation Scenarios

- Scenario 1: $10B defense spending
- Scenario 2: $30B defense spending
- Scenario 3: $50B defense spending
- Scenario 4: $110B defense spending

**Variable:** Federal Military Spending
- Spread according to current distribution of defense spending across states
### Employment – by State (2025)

<table>
<thead>
<tr>
<th>Absolute Terms</th>
<th>Percentage Terms</th>
</tr>
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<tbody>
<tr>
<td>1. California</td>
<td>1. Hawaii</td>
</tr>
<tr>
<td>2. Texas</td>
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</tr>
<tr>
<td>3. Virginia</td>
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</tr>
<tr>
<td>5. Florida</td>
<td>5. South Carolina</td>
</tr>
<tr>
<td>8. Colorado</td>
<td>8. Georgia</td>
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This table shows the top 10 states by employment in terms of absolute numbers and percentage terms for the year 2025.
## Critical Results

### Employment – by Industry (2025)

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<tr>
<td>2. Administrative and Support Services</td>
<td>2. Water Transportation</td>
</tr>
<tr>
<td>3. Professional, Scientific and Technical Services</td>
<td>3. Other Transportation Equipment Manufacturing</td>
</tr>
<tr>
<td>4. State and Local Government</td>
<td>4. Air Transportation</td>
</tr>
<tr>
<td>5. Retail Trade</td>
<td>5. Support Activities for Mining</td>
</tr>
<tr>
<td>6. Construction</td>
<td>6. Administrative and Support Services</td>
</tr>
</tbody>
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what does REMI say?sm
# Critical Results

## Output – by State (2025)

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</tr>
<tr>
<td>9. Colorado</td>
<td>9. New Mexico</td>
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*what does REMI say?*
Output – by State (2025) – Percentage Terms
## Critical Results

### Output – by Industry (2025)

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<td>2. Water Transportation</td>
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<tr>
<td>3. Real Estate</td>
<td>3. Other Transportation Equipment Manufacturing</td>
</tr>
<tr>
<td>4. Wholesale Trade</td>
<td>4. Air Transportation</td>
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<td>5. Support Activities for Mining</td>
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*what does REMI say?*
## Critical Results

### US International Imports Demand – by Industry (2025)

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<tbody>
<tr>
<td>1. Computer and Electronic Product Manufacturing</td>
<td>1. Other Transportation Equipment Manufacturing</td>
</tr>
<tr>
<td>2. Other Transportation Equipment Manufacturing</td>
<td>2. Petroleum and Coal Products Manufacturing</td>
</tr>
<tr>
<td>3. Petroleum and Coal Products Manufacturing</td>
<td>3. Air Transportation</td>
</tr>
<tr>
<td>5. Oil and Gas Extraction</td>
<td>5. Truck Transportation</td>
</tr>
</tbody>
</table>
Model Demonstration
Questions

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