

# Week in China

## Talking Point

### A Shenzhen for Arabia

## Saudi plans \$500 billion new city – expect China to play a key role

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A month ago the government of Saudi Arabia made a historic decision to allow women to drive. Last week it also announced that females will be allowed into sports stadiums for the first time too.

But the female who has been given the most groundbreaking rights in the kingdom is Sophia, a robot.

The humanoid never covers her face with a niqab. Nevertheless, during the Future Investment Initiative (FII) in Riyadh last week Sophia was granted citizenship by Saudi Arabia, the first country in the world to give a robot this right.

Sophia was created by American firm Hanson Robotics. Yet her new status has garnered attention in China, where she is considered to be a made-in-China product: Hanson relocated to Hong Kong three years ago, attracted by the city's proximity to tech suppliers in Shenzhen. "This is the pride of Hong Kong," news portal HK01 proclaimed, reporting that Hanson is applying for a Saudi passport for Sophia so that she can travel on planes as a passenger rather than cargo.

The humanlike robot appears to epitomise a deeper trend: closer ties between China and Saudi Arabia. Among the 170-plus speakers at the FII event, only eight came from China. However, like Hong Kong-based Hanson, the feeling is that business dealings with China are becoming a compelling pull factor for the oil-rich nation. Yes, the US remains Saudi's most important ally but there are signs that the kingdom could be tempted to shift some of its strategic direction eastward to China.

That's because Riyadh and Beijing increasingly share common interests.

### Reforms along the Silk Road...

Since Mohammed bin Salman was appointed as Saudi Arabia's Crown Prince in June he has been talking about social and economic reforms to modernise the Sunni Islamic state. And according to Fan Bao, the chief executive of China Renaissance, an independent investment bank, the Chinese have a lot to offer in aiding the transition. In particular, Fan says that Chinese tech firms are better equipped than the American giants such as Google and Facebook to capture a lucrative share of the Saudi internet industry.

"A critical aspect of the Chinese business model is the ability to work with the government," Bao told CNBC last week. Because Chinese firms are more comfortable working in close contact with

the state, the banker reckons they “can be particularly effective in countries like Saudi Arabia and the Middle East”.

Bao was one of the Chinese speakers at the FII, a three-day investment conference attended by more than 3,500 guests. Dubbed “Davos in the desert”, the lavish event is an annual gathering promoting Vision 2030, a masterplan to transform Saudi Arabia into a global investment powerhouse and cut the kingdom’s reliance on oil revenues.

This long-term ambition has a similar timeframe to Xi Jinping’s “China Dream”. In a two-stage development plan, the Chinese leader said last month that he would lead the country into an era of socialist modernisation by 2035 (see WiC385).

Chinese state media has also been highlighting the positive reception for Xi’s Belt and Road Initiative, another of his signature policies. Saudi Arabia sits close to the centre of a plan that connects Asia, Africa and Europe, Xinhua notes, and this strategic location means Saudi’s Vision 2030 could fuse perfectly with Xi’s Belt and Road plan.

### **A tale of two mega cities...**

The most eye-catching story to emerge from the FII last week – besides Sophia, of course – was Neom, a futuristic city that the Saudi government wants to build from scratch. According to the proposals, the city will be bigger than Dubai, powered entirely by renewable energy, and have a larger number of robots than humans in its local population.

The word Neom means “new future” in a combination of Greek (aka neo) and Arabic abbreviations. The project will be built on 26,000 square kilometres of uninhabited land along the Red Sea coastline near Egypt and Jordan. Mohammed bin Salman hopes it could pull in more than \$500 billion of investment and contribute \$100 billion to the Saudi Arabian economy by 2030.

The Saudis also plan to turn Neom into a new economic zone that operates under separate rules from the rest of the kingdom (hoping perhaps to ape the success of Shenzhen which became a special economic zone in 1980 and next year will overtake Hong Kong in GDP terms).

Sceptics scoff that the ‘Neom dream’ will never become a reality. The Economist notes that a similar exercise – the King Abdullah Financial District – has ended up becoming “a \$10 billion white camel”. But Neom could be different, the magazine said, because it will start with the credibility that comes from big-name supporters such as Softbank’s Masayoshi Son and Stephen Schwarzman’s Blackstone.

Both Son and Schwarzman might prove excellent at getting the Chinese involved too (Softbank is a major shareholder in Alibaba and Blackstone has deep China connections, see WiC369). But regardless of those individuals, Beijing policymakers will be keen for Chinese companies to bid for business in Neom. After all, China is a veteran when it comes to building special economic zones and new cities from scratch. Indeed, in Xiongan, the authorities are pouring hundreds of billions of dollars into building a new megacity of their own (see WiC361) which is expected to be completed by 2030 too.

### **How could China help in Neom?**

Chinese state firms must fancy their chances of securing big contracts for Neom’s buildout, probably under the auspices of infrastructure projects in Xi’s Belt and Road Initiative.

“The beauty of Neom is that it neatly fits into another grand geo-economic design: China’s ‘One Belt, One Road’ vision,” Cornelia Meyer, an economist and energy industry consultant, wrote on Arab News.

That said, infrastructure heavyweights such as China Railway Construction Corp (CRCC) will be mindful of the challenges of mega projects of this type.

In 2009, CRCC won a \$1.8 billion contract to build a new railway line in Saudi. The 18-kilometre light rail line now links the Red Sea port city of Jeddah to Mecca and Medina – Islam’s two holiest sites. But a year after winning the tender, CRCC shocked its investors by flagging that it could lose Rmb4.1 billion (\$630 million) on the deal. The state firm initially planned to seek compensation from the Saudi government, Chinese media suggested, but eventually absorbed the loss after heeding advice from Beijing.

Why so? The central government wanted CRCC to set a good example in China’s first major infrastructure project in the Arab world, especially as millions of pilgrims would travel on the Mecca Light Rail every year.

CRCC’s sacrifice appears to have paid off. “With Muslims from all over the world taking the new Chinese trains between five stations in Mecca, the Chinese company [CRCC] was overwhelmed with praise from the media and Saudis,” Xinhua pointed out in March during a state visit to Beijing by King Salman bin Abdulaziz Al Saud.

During the Saudi monarch’s trip, China and Saudi Arabia signed further trade and investment deals worth \$60 billion.

The two countries have also agreed to set up a joint \$20 billion investment fund, and according to Xinhua, there are now nearly 150 Chinese firms operating on Saudi projects worth a total of \$25 billion.

### **How about financial investments?**

In issue 276 we reported that China Communication Construction Corp (CCCC) is well-positioned to benefit from the Belt and Road roadmap. Al-Waleed Bin Talal, a member of Saudi’s royal family, spotted the firm’s potential even earlier than we did. When CCCC went public in Hong Kong in 2006, the billionaire Saudi prince invested \$700 million in the state-controlled infrastructure firm. He has since invested in private-sector companies such as Fosun and e-commerce giant JD.com.

Chinese firms now look ready to invest in the other direction and Reuters reported last month that state oil majors PetroChina and Sinopec have written to the Saudi authorities to express an interest in buying a 5% stake in Saudi Aramco, a company that produces one in eight barrels of the world’s oil supply.

Initial media attention focused on which of the world’s stock exchanges will host Aramco’s upcoming IPO, set to be the biggest in history. With the rumoured interest from the Chinese oil majors, the speculation shifted to price tags: it’s rumoured the Chinese firms are prepared to pay \$100 billion for a 5% stake that would value the oil firm at \$2 trillion.

Last month Aramco’s chief executive Amin Nasser downplayed suggestions that the Saudis are talking to the Chinese about a bid, while the country’s energy minister Khalid al-Filah has maintained that a broader IPO will happen in the second half of next year.

Charles Li, chief executive of Hong Kong Exchanges and Clearing, also said this week that his bourse (which also owns the London Metal Exchange) has been working overtime to secure the Aramco listing.

But the benefit of a Chinese bid is that it could set a benchmark for Aramco's equity at a time when other investors are said to be baulking at the price. It might also delay the need for a fuller IPO until oil prices are higher. Any deal with the Chinese might also include co-investment in China's refining and chemical sectors, which would help Aramco reduce some of its reliance on crude exports.

Sohu.com says the Chinese regard an investment in Aramco as a long-term play, particularly in cementing political ties with Crown Prince Muhammad bin Salman, the driving force behind the float.

China imports about a quarter of its oil from the Saudis, the third-largest suppliers after Russia and Angola. Of course, a stake in Aramco might also offer guarantees of future supply. CEFC China Energy has done something similar in Russia, acquiring 14% of Rosneft for \$9 billion, and locking in delivery of up to 260,000 barrels a day (we profiled China's newest oil major in WiC381).

### **From petrodollars to petroyuan?**

Also on the agenda, says Hexun.com, is that China wants to purchase oil from Aramco with yuan, rather than dollars.

Beijing has been looking for ways to boost acceptance of the renminbi and there are already yuan-denominated contracts for crude (with the sweetener that they are transferrable into gold) on the Shanghai Futures Exchange (see WiC380). Persuading Riyadh to invoice in yuan would be seen as signalling a fracture of Richard Nixon's 1973 pact with the Saudis that established the greenback as the currency of choice in the oil industry.

With a traditional role as OPEC's swing producer, if the Saudis agreed to accept the yuan, other oil nations might do the same.

Closer ties between China and Saudi Arabia may also extend to the international debt markets as Riyadh is considering selling yuan-denominated bonds.

But Saudi is likely hedging its geopolitical relationships. After all, its ties with the United States go back a long way. The clue is in Aramco's name – the Arabian-American Oil Company, which was formed in the 1930s and headquartered in San Francisco and New York for much of its early existence.

Most analysts have cautioned that it is too early to announce an end to the petrodollar era. For a start, China doesn't have the same levels of pricing power in oil that it enjoys in some other commodities (it consumes about 13% of the world's crude). Restrictions on how the yuan is traded internationally also make it a less liquid currency, which could deter oil producers from accepting it more.

But the planned development of Neom is a reminder that both China and Saudi are planning for a future more focused on renewable energy. Aramco's production generates about 90% of Saudi Arabia's revenues and most of its foreign earnings. But the Saudis know they can't be so dependent on oil and in this regard Beijing has something to offer, thanks to its aggressive push into sectors like solar power.

In an early sign of cooperation between the two countries, Dubai's state energy utility announced in September that it had awarded a \$3.9 billion contract for a 700 megawatt solar power plant to a consortium comprising Shanghai Electric and Saudi Arabia's ACWA Power.

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