

May 11, 2015

## **The Next Generation**

On April 29<sup>th</sup>, Saudi King Salman announced a set of changes to his cabinet and to the order of royal succession. We believe these changes are very significant, perhaps the most critical since the first royal succession in 1953.

In this report, we will detail the changes announced by King Salman. To put these changes in context, we will provide a short history of the important succession plan that was established in 1964. With this background, we will show how the king's announcement represents the first change in the program and discuss how these changes could affect the future stability of the kingdom. As always, we will conclude with potential market ramifications.

## **The Changes**

At 4:00 am Arabia Standard Time, King Salman made a series of announcements regarding the administration of the Kingdom of Saudi Arabia. They are as follows:

- Prince Muqrin was demoted from the line of succession and is no longer crown prince. He is considered the last competent and able-bodied son of Ibn Saud, the founder of the kingdom.
- Prince Mohammed bin Nayef was named crown prince, putting him in line to the throne. He is the son of the late Crown Prince Nayef, who was a high-ranking son of Ibn Saud and one of the Sudairi Seven, the sons of Ibn Saud's favorite wife. The new crown prince has been in charge of internal security, along with foreign and domestic politics for the kingdom.
- Prince Mohammed bin Salman was named deputy crown prince, putting him second in line to the throne. He is the first son from King Salman's third marriage; King Salman has older sons but reports indicate that the 30-year-old prince is his favorite. The deputy crown prince is the minister of defense and chief of royal court; in Western terms, that is similar to the role of chief of staff. He is also in charge of economic affairs. Prince Salman is in charge of external defense and will act as "gatekeeper" for access to the king.
- Adel Faqih was appointed to economy and planning minister. He had previously worked in the labor ministry. He is a commoner.
- Adel al-Jubeir was appointed minister of foreign affairs. He is a career diplomat who has mostly served in Washington. He is also a commoner.
- Prince Saud al-Faisal was relieved from his role as foreign minister, a position he has held for 40 years. At age 75, he has been in ill health for some time and had asked to be removed.
- Nora al-Fayez, the deputy minister for the education of girls and the highest ranking woman in government, was relieved of her duties.

- Khalid al-Falih was named health minister. He was in charge of the state oil company Saudi Aramco. He has a reputation of being a very capable manager. He is also a commoner.
- Ali al-Naimi remains as the Saudi minister of petroleum and natural resources, although we would expect him to retire from this position in the coming months. Keeping al-Naimi in place probably suggests that the kingdom's current oil policy will remain unchanged.

In addition to these changes, King Salman has been making structural changes to the government to improve its efficiency. The state oil company, Saudi Aramco, was formally separated from the oil ministry. The king abolished 17 councils that managed the government's affairs and streamlined the bureaucracy into two national committees. The crown prince oversees the political and security areas and the deputy crown prince is in charge of the economic and social spheres. Thus, these two will be responsible for most aspects of Saudi Arabia.

### Historical Context

King Ibn Saud, the founder of modern-day Saudi Arabia, didn't formally create a plan of succession. The king selected his eldest (and, reportedly, favorite) son, Saud, to be crown prince. When Ibn Saud died in 1953, Crown Prince Saud became king.

King Saud, unfortunately, proved to be a weak ruler. He was a spendthrift and treated the kingdom as his personal asset. He seriously damaged the kingdom's finances. His foreign policy was mercurial. For example, Saud sided with Egyptian President Gamal Nasser during the Suez Crisis in 1956, sending \$10 mm to Egypt

and implementing oil embargos on Britain and France. In 1958, the king, horrified that Syria and Egypt had created the United Arab Republic (UAR), engaged in a rather harebrained scheme to assassinate Nasser by shooting down his airplane. Saud opposed the growing anti-monarchy sentiment that Nasser represented. But the plot to kill Nasser was ill-conceived, shocked Saud's brothers and damaged the kingdom's international reputation. With relations between Egypt and Saudi Arabia thoroughly severed after this event, the two countries squared off in the early 1960s in a proxy war, both supporting factions in a civil conflict in Yemen.

The combination of profligate spending habits and an unpredictable foreign policy led to dissent within the royal family. There were serious concerns about King Saud's competency. Perhaps the most divisive issue was that of unresolved kingly succession. Ibn Saud had 30 sons; so did King Saud. As King Saud began appointing his sons to positions of authority, the sons of Ibn Saud saw this trend as a way to supplant their opportunity to take power.

In response to the king's incompetent behavior, the royal family and the Saudi *ulama* (clergy) pressed Saud to have his more competent brother, Faisal, appointed to a position of authority. Prince Faisal was in and out of various positions of authority from 1958 until Saud was deposed in 1964. When given executive authority, Faisal would implement austerity measures, which the king opposed. The king would then press Faisal to resign; soon after, fiscal and foreign conditions would deteriorate and Prince Faisal would be moved back into government. Finally, assisted by a *fatwa* (Islamic legal opinion) by the *ulama* and support from three key brothers (Princes Khalid, Fahd and Abdullah, all future

kings), King Saud was deposed and Prince Faisal was named king.

The ouster of King Saud also resolved the succession issue. The sons of Ibn Saud opposed King Saud's attempt to create his own line of succession that went to his sons. Instead, the kingly line ran through the sons of Ibn Saud. The decision to keep the throne among the sons of Ibn Saud instead of passing it to the sons of the incumbent king has become a social contract within the royal family. By keeping the kingship among the brothers instead of shifting the line to sons, peace and stability has been maintained. There have been numerous tumultuous events in the region since 1964—major wars, oil embargos, oil price volatility, regional instability, the rise of Islamic jihadism—and through it all, the Saudi royal family has remained in power. A key factor in that stability is that the sons of Ibn Saud have generally selected good candidates for king and have avoided internal power struggles that occur when succession becomes uncertain.

Another element of the Saudi family social contract was that power was generally distributed among the brothers. Even if a prince was not in line for the throne, he could become influential by good performance in government. Thus, being a competent administrator in a province or ministry gave power to a lesser prince. Part of this social contract also meant that princes were given preference in positions of authority. As we note below, this pattern appears to be changing as well.

### **An Era Ends...What Now?**

By selecting a crown prince from the third generation, the grandsons of Ibn Saud, King Salman has ended the system that has been in place since King Faisal. Of course, at some point, it was going to end. Prince

Muqrin could have taken power but there were no further sons of Ibn Saud available. And, Muqrin was too young to have any involvement or recollection of the issues surrounding the decision to depose King Saud. King Salman will be the last Saudi king to operate under the current social contract.

Although there were other candidates for future king among the grandsons, there isn't much quarrel with the selection of 55-year-old Crown Prince Nayef. He is considered a diligent and competent administrator, presiding over the kingdom's anti-terrorism efforts over the past decade. He is also well known and generally liked in the U.S., a religious conservative and a bulwark against secular or religious extremism. Perhaps most importantly, Nayef has no sons, only daughters. So, it will be impossible for him to select a son to replace him, which would reopen the problems of the King Saud/Prince Faisal period and call the current social contract into question.

The selection of Deputy Crown Prince Mohammed bin Salman is much more controversial. He has older, more accomplished brothers. Mohammed is very young; most sources place his age at 30, but there doesn't appear to be any definitive date of birth. Some have speculated he could be as young as 27. Unlike many of the royals of his generation, he did not study abroad; instead, he has a law degree from King Saud University. Most reports suggest that Mohammed is a hard worker. At the same time, he has been given great responsibility; the young prince is managing the war in Yemen and is also in charge of managing the economy during a period of low oil prices.

It is clear that King Salman has given great power and authority to both the crown

prince and the deputy crown prince. They will be forced to collaborate in order to run the country. According to reports, the Allegiance Council approved the king's decision by a large majority—28 out of 34 supported the decision, which likely means both will be given the opportunity to succeed.

Given the appointments of Crown Prince Nayef and Deputy Crown Prince Salman, a large number of grandsons, many of whom are older than Mohammed bin Salman, now realize they are not in line to be king. These same grandsons have likely noted the selection of commoners to key positions, such as foreign minister. In one sense, selecting administrators beyond the royal family could mean that the king is more interested in creating a meritocracy. On the other hand, these commoners will not have a power base within the royal family. Although it appears they will be competent, they will also be more prone to follow the direction of the crown prince and deputy crown prince; after all, they will be serving at their discretion.

Given King Salman's advanced age of 80 years and deteriorating health,<sup>1</sup> King Nayef may be appointed sooner rather than later. It is quite possible Nayef could take power before turning 60, which means he could be king for a long time. Assuming King Salman remains mortal for a few years, both Crown Prince Nayef and Deputy Crown Prince Salman will amass significant power. According to Saudi succession rules, if Nayef becomes king, he could choose another crown prince, bypassing Salman. However, barring a serious failure in his duties, the current deputy crown prince should become quite powerful and

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<sup>1</sup> A medical record which includes spinal surgery in 2010, at least one stroke and reports he may be suffering from dementia

influential in the next few years. It may be very difficult to remove him from the path of succession without causing dissension within the royal family and increasing the likelihood of a power struggle. An internal power struggle in Saudi Arabia could lead to major instability in the region.

### **Ramifications**

When we wrote about Saudi succession in January,<sup>2</sup> we noted that the issue was probably not imminent. In one sense, that position is still true. King Salman will likely be with us for a while, and we doubt there will be any challenges to his selection of crown prince. The real problem is with the deputy crown prince. The litany of issues are long. He is young, there isn't evidence that he is well educated, his responsibilities are huge and lots of other grandsons of Ibn Saud are wondering why, other than being the son of the king, this man was chosen for this important position.

Fortunately, the deputy crown prince will probably have years of on-the-job training to prepare him for future challenges. Both of the new appointees appear to be hard working, are conservative and seem to have the support of the royal family. Deputy Crown Prince Salman's best ally is time. The longer he is in office, assuming he performs well, the better the odds are that the kingdom will avoid a messy succession problem when Nayef becomes king.

We see three primary risks. The first, and most important, is if Nayef becomes king and names a different crown prince. If the current deputy crown prince forms a strong enough power base, he could challenge the new king's decision and create the chaos seen in the early 1960s. If that were to occur, we would expect oil prices to rise and safety assets (gold, Treasuries) to benefit.

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<sup>2</sup> See WGR, 1/20/2015, [Saudi Succession](#).

That outcome probably isn't imminent, but clearly bears watching. This is a new risk to the security of oil supply.

A key secondary risk is that the social contract that has led to stability in the kingdom is now being rewritten. How the rest of the royal family will accept these changes is not known. However, we should expect some discontent if anything goes awry.

The third risk is that the concentration of power in two leaders will allow for more aggressive policies. When power was distributed among the royal brothers, and actions were taken mostly on consensus, policy changes occurred rather slowly. That will not be the case going forward. In a region where a power vacuum is developing due to America's decision to reduce its "footprint," consensus decision-making may

not be appropriate. On the other hand, this condition will also increase the odds of mistakes due to aggression.

Overall, the primary concern from regional instability would be higher oil prices. We do not expect higher oil prices for the next few months. The Saudis are trying to capture market share, and history shows when that is occurring oil prices tend to remain under pressure. However, less American influence in the region is almost certain to raise instability in the region and, at some point, that condition will likely be expressed in higher and more volatile oil prices.

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May 11, 2015

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