

Saudi-American Forum



SAF Essay #20

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At Your Service: Future U.S. Service Exports to Saudi Arabia

By Grant F. Smith

Executive Summary

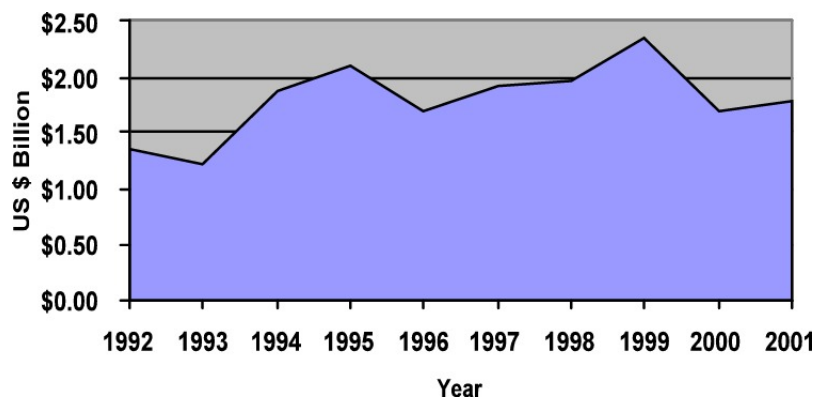
U.S. service exports over the past ten years have achieved steady successes in the Saudi market, growing on average 5.31% per year. Government sponsored changes in the Kingdom including privatization, Saudization, exploration and infrastructure projects that will accelerate service demand over the coming decade. Many barriers to foreign service providers such as majority ownership requirements, onerous taxation, and import tariffs have been reduced or eliminated. Now, American service providers must effectively confront supply side obstacles that could diminish a \$41.8 billion export opportunity over the coming decade.

U.S. Service Exports to Saudi Arabia

Over the past decade the United States has achieved stunning successes exporting services to Saudi Arabia. Between 1992 and 2001 U.S. service exports to the Kingdom grew on average 5.31% per year. This provided steadily increasing and renewable revenues totaling US \$18 billion to American corporations serving the market. (See exhibit #1).

Exhibit 1 U.S. Service Exports to Saudi Arabia 1992-2001

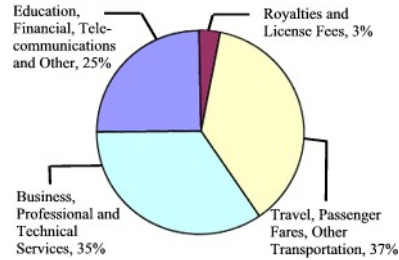
(Source: U.S. Bureau of Economic Analysis, 2002 and IRmep)



U.S. service exports over the four year period 1998-2001 totaled US \$7.8 billion. The major categories of service exports during this period are relatively evenly distributed between travel and transportation, business and technical, and the "other" category which includes education, financial, and telecommunications services. (See exhibit #2)

Exhibit 2 Major U.S. Service Export Categories to Saudi Arabia 1998-2001

(Source: Bureau of Economic Analysis, 2002 and IRmep)



Kingdom of Change

Saudi Arabia's economy is expected to grow 5.7% in 2003. Even so, Saudi Arabia is increasing the rate of state-owned industry privatization. The Kingdom is training and retraining the Saudi workforce, opening new energy reserves, and upgrading the Saudi defense forces. A US \$25 billion package of regional infrastructure and exploration projects, temporarily placed on hold in June of 2003, was put back on the table in July. This is only the tip of an iceberg of new demand floating toward the world market.

In the coming three years, up to 15% of the economy is slated for privatization. In May, 2003, Saudi Arabia divested 30% of the leading telecommunications service provider to the public. Saudi Telecom was the largest single Arab initial public offering in 15 years. The benefit was immediate for U.S. database software and IT service providers charged with upgrading Saudi Telecom. Capacity demand is likely to continue as explosive Internet usage growth rates of 300% generate additional demand for robust modern telecommunications infrastructure and international bandwidth.

Ultimately, the Kingdom's entire transportation and telecommunications sectors will be privatized, although the government will commit passive financial support through ongoing investment. Private sector service providers will receive contracts for upgrades and maintenance of newly privatized electric, water, sewage and other municipal services. Demand for electricity alone is forecast to increase 250% over the next two decades.

Foreign corporate service providers are better positioned than ever before to participate. New laws have removed the requirement for companies based in the Kingdom to be majority owned by Saudi nationals. The tax regime for foreign nationals has decreased. Import tariffs have been reduced from 12% to 5%. Although some obstacles remain, the country is reforming to compete for increased foreign direct investment. Prince Abdullah bin Faisal bin Turki Al Saudi, governor of the Saudi Arabian General Investment Authority, publicly criticized an imposition of a 25% tax on foreign companies fearing that the flow of foreign investment would be negatively affected. Saudi business leadership in opening up the domestic services market to competition mirrors a predicted global trend of lowered barriers to foreign service providers. The World Bank recently estimated that this kind of barrier removal could create new global services opportunities adding \$900 billion a year in wealth to developing economies.

Opportunities for management consulting and training services are likely to skyrocket. Demand for highly trained Saudis continues to exceed the available supply. The "Saudization" program charged with placing more Saudis in high value added jobs guarantees an increase in training

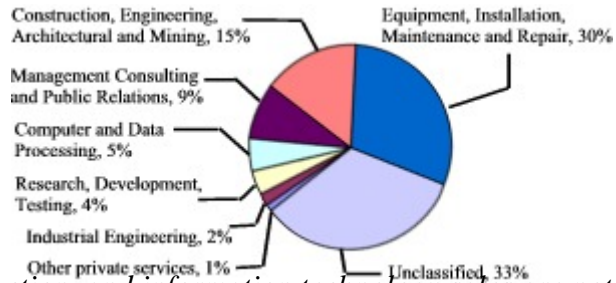
requirements now and in coming years. The list of jobs and positions that can no longer be held by non-Saudis is expanding, creating a clear segmentation for interested training and performance management consulting firms.

U.S. Service Export Demand and Supply Challenges

As U.S. troops formerly based in the Kingdom deploy elsewhere, demand for transition and upgrade services to the Saudi defense forces has increased. Booz Allen Hamilton Inc., in McLean, Virginia recently won a \$7.9 million contract for technical advisory and assistance support services to the Royal Saudi Naval Forces. Engineered Support Systems, Inc. of St. Louis, Missouri has been awarded a \$26.1 million task order by the Royal Saudi Air Force (RSAF) under a new Rapid Response contract.

The mix of services delivered by U.S. providers to Saudi corporate and government customers and internally to their own local U.S. affiliates has been relatively stable. This reflects long term repeat business opportunities many service business relationships generate. During 1998-2001 the sub-category of installation, maintenance and repair of equipment represented on average 30% of total U.S. business services exports. Management consulting and public relations services were just under 9% of the total during the same time frame. (See exhibit 3)

Exhibit 3 U.S. Business Service Exports to Saudi Arabia 1998-2001
(Source Bureau of Economic Analysis, 2002 and IRmep)



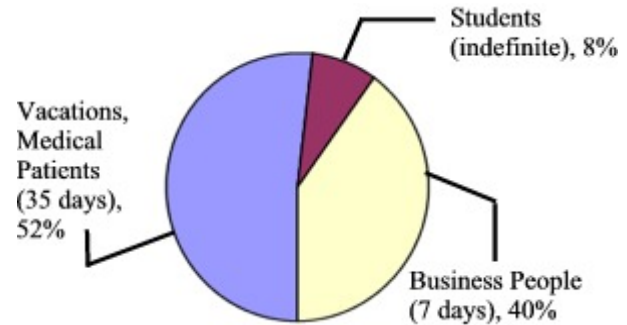
Note: Some revenues from software, construction, and information technology sales are not categorized by BEA to protect confidential corporate data. IRmep includes these revenues in the "Unclassified" category.

Non-industrial services delivered to consumers reveal some expected supply-side obstacles that must be overcome. Travel services provide one example. U.S. travel and tourism services have traditionally been the most important of all U.S. service exports to Saudis, accounting for 37% of the total.

The U.S. Department of Commerce estimated that 85,000 visitors came to the United States from Saudi Arabia in 2001. The key difference between Saudis and other groups of international visitors is that their longer average visit duration and travel in large family groups compounds the effect of higher-than-average daily spending per visitor. Vacationers and healthcare visitors have typically outnumbered businesspeople and students. (See Exhibit #4)

**Exhibit 4 Saudi Visits to the United States:
Visitor Category and Average U.S. Stay
(2001)**

(Source U.S. Department of Commerce 2003
and IRmep)



With average spending of US \$400 per person per day (not including airfare) Saudi visitors spent an estimated \$390 million in the USA in 2001.

The number of Saudi Arabians traveling to the United States dropped to almost zero following the tragic events of September 11, 2001. Recently visitor count began to recover. Current estimates for Saudi business travel to the United States are 15% below expected levels, and tourism/medical visits are down 40%.

Unfortunately, U.S. healthcare delivery to Saudis in the United States has suffered slightly more. One of the nation's leading healthcare providers, Mayo Clinic in Rochester, Minnesota reported that patients from the region dropped 50% to 1,098 in the year 2002 down from 2,195 patients in 2001. Lengthy delays in visa application approval, a nuisance for tourist and business travelers, can be harmful and even fatal to traveling foreign patients.

U.S. education service delivery to Saudis has also been vulnerable to visa delays and reentry uncertainties. U.S. education service exports to Saudi Arabia, which grew on average 9% per year between 1998-2001 fell in 2002-2003. Enrollment in U.S. universities is likely to erode further if visa delays, reentry uncertainties and students' personal safety concerns cut remaining Saudi demand for U.S. higher education services. A growing atmosphere of xenophobia on campus is also harming Saudi enrollment at U.S. universities to the detriment of student body diversity and international cultural exchange. (See the SAF essay "Getting Back on Track: Saudi Study in the United States")

U.S.-Saudi Relationship "Tune-up"

The machinery of U.S. service export categories need a major "overhaul" in order to meet future demand. Top clinics, hospitals and health service providers need to engage more effectively with the new Bureau of Citizenship and Immigration Services. Efforts are needed to streamline U.S. visa processes for traveling patients in a way that guarantees homeland security concerns while permitting accelerated preferential access to U.S. medical care facilities. Student visitors must be assured that visa processing won't delay their entry into academic programs. After enrollment, students need special assurances and that they will be allowed to reenter the United States if they should return to Saudi Arabia for vacations or short visits. Shifting U.S. visa procedures and unpredictable re-entry processes currently result in students applying elsewhere.

Business service export categories with some of the brightest prospects for growth are installation/ maintenance/and repair services, management consulting, and telecommunications

services as well as public relations. However, leaders within these industries should also assume a larger role in "tuning up" the broader U.S.-Saudi relationship. This may require U.S. management consulting and PR firms to focus on U.S.-Saudi relationship issues that are larger than their primary business concerns.

Other industry and civic leaders can do much to reverse the damage caused by miscommunication, misunderstanding and politically motivated smear campaigns. Noble on its merits, in the long run, repairing the relationship can be considered enlightened self-interest. Plummeting Saudi U.S. business school enrollment driven by xenophobia does not bode well for the long range health of U.S. consulting services to Saudi corporations. Obstacles to patient access to U.S. facilities may mean that U.S. hospital administrative processes, pharmaceuticals, and equipment are no longer considered an ideal model for Saudi healthcare. By treating the U.S.-Saudi relationship as a larger complex system and acting independently to understand and communicate American perspectives and insights about Saudi Arabia back to key U.S. government, lobbying and citizen groups, high profile consultancies in particular can efficiently repair broken and damaged links. This lays the groundwork for restored cultural, academic and business exchanges between the United States and Saudi Arabia.

U.S. software and IT service firms can also take on more important roles. They must do more than localize their software and services to be more competitive against European, Indian and Lebanese firms now successfully entering the market. They must also reposition themselves as good American corporate citizens serving customers in neglected sectors. Demonstrating their commitment to Saudi Arabia by publicized software and service contributions to lower margin education and social service sector IT projects even as they harvest the plums of privatization is key. U.S. service trade must become an even more potent force in Saudi modernization. We believe that the enormous Saudi transformation currently underway will accelerate the average annual service demand growth rate to 15% over the next 10 years. This creates a U.S. service market potential of US \$41.8 billion. However, the proactivity of U.S. business leaders and policy makers will largely determine whether American companies continue to be "at your service" to the global marketplace in general and the Kingdom of Saudi Arabia in particular.

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ABOUT THE AUTHOR

Grant F. Smith is the Director of the Institute for Research: Middle Eastern Policy (IRMEP) in Washington , D.C. (<http://www.irmep.org>). Before joining the Institute, Smith served for three years as senior analyst and later program manager of international research at The Yankee Group Research, Inc., a Boston based research and consulting firm owned by the Reuters PLC group. He worked closely managing business plan development and financing due diligence with the International Finance Corporation of the World Bank, Inter-American Development Bank, and many consortium investors and corporations on over \$3.0 billion in investment projects in over 40 countries.

Preceding his tenure at Yankee Group, Smith taught graduate level finance and marketing courses for five years at Colombia's most prestigious business school, the Colegio de Estudios

Superiores de Administración (CESA). He coordinated executive seminars, exchanges, simulations and programs between CESA and Harvard, Berkeley, and other U.S. universities. He also served as president of Smith & Sefair Zaher Ltda., a Bogota based technology and management consulting firm. While there, he consulted clients in the insurance, banking and industrial sectors on business process improvement, business planning and information systems technology strategies. Before that, he was marketing manager at American Express Financial Advisors corporate headquarters.

Smith received his Master's degree in International Management from the University of St. Thomas in St. Paul, Minnesota. He has a B.A. in International Relations from the University of Minnesota and has completed postgraduate certificate work in information systems at New York University.

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The Institute for Research Middle Eastern Policy (IRmep) is a Washington D.C. based think tank working to research, define, communicate and promote America's real interests in the Middle East. Founded in 2002, the Institute became an independent non-profit IRS recognized tax-exempt organization in 2003. IRmep promotes the peaceful settlement of regional and international disputes by returning the U.S. to a higher foreign policy role: that of a just, secular, and development oriented regional influence.

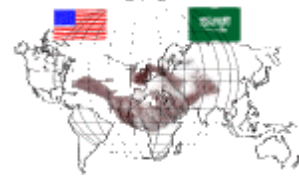
IRmep produces research, publications, commentary, focused policymaker educational events and research tour programs to the Middle East. The heart of the IRmep's work is academically, not ideologically, driven research. The Institute's network of analysts is composed of experienced university research academics with reviewers in the international business and diplomatic communities.

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The Saudi-American Forum is an information service designed to provide you timely information -- background and current issues - - impacting the Saudi-U.S. relationship.



The Forum is a resource for Americans who value the relationship between the United States and Saudi Arabia and who want to act in response to erroneous and misleading depictions of the relationship in the media and elsewhere. The Forum is a vehicle for stakeholders in the Saudi-U.S. relationship to contribute their experiences and their ideas and opinions on the issues of the day.

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Thank you for your support of the Saudi-U.S. relationship and the Saudi-American Forum.