

# Saudi-American Forum

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SAF Essay #23

October 31, 2003

## **Saudization: Development and Expectations Management**

By Grant F. Smith

### **Executive Summary**

The Saudization program is striving to increase workforce participation of Saudi nationals in the Kingdom. The goal is 70% Saudi workforce participation by the end of the decade, although the Saudization of some industries has been accelerated.

In this environment, opportunities for American investors continue to be attractive, though more complex. Paradoxically, U.S.-Saudi relations will most likely improve as Saudi employees experience increasing employment in American and joint venture firms operating throughout the region.

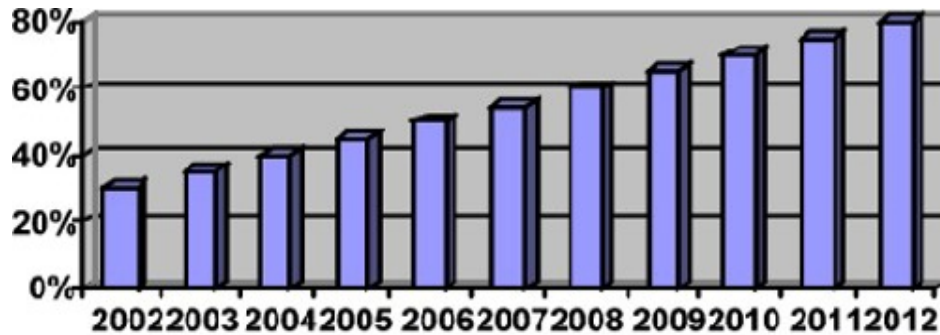
As the recently announced municipal elections underscore, the pace of change and development is proceeding at Saudi Arabia's unique tempo. Saudization is a net gain for both Saudi Arabia and the United States in spite of the transition costs.

### **What is Saudization?**

Saudization is a development strategy that seeks to train Saudi workers and replace foreign workers in Saudi Arabia. Saudi Arabia relied heavily upon foreign workers during accelerated development projects since the early part of the past century. The program to reverse this historic reliance is gradual. According to the guidelines of the Shura Council (a consultative body), by 2007, 70% of the workforce will have to be Saudi, although Saudization is accelerated in some industry sectors. (See Exhibit #1)

## Exhibit 1 Target Saudization Benchmarks

(Source: Shura Council, 2002)



Workforce Saudization (companies with 20+ employees)

Saudization is driven by three important goals:

1. Increase employment for Saudi nationals across all sectors of the domestic economy.
2. Reduce and reverse over-reliance on overseas foreign workers.
3. Recapture and reinvest income which otherwise would have flowed overseas as remittances to foreign worker home countries.

The merits of the process have been analyzed in depth by both internal and external stakeholders. Many Saudi business people point out the higher costs associated with increased percentages of Saudi workers who typically demand higher salaries and benefits. Leading expatriate recipients of remittances, such as Filipinos, argue that their long-term service to the Kingdom demands some special recognition and protection. Specialist workers from the United States and Europe, especially those in financial services and energy sectors, also believe that their technical skills merit some level of continued access.

As a worker replacement development strategy, Saudization clearly creates some disturbances. The pain of transition resembles tremors caused by the development strategies of the Asian "Tigers" South Korea, Taiwan and Singapore. Their "top-down" development strategies retooled entire economies to emphasize exports, education policy integrated with economic development policy, the free market with some protection and subsidization of key domestic industries, and advocacy for work ethic and meritocracy.

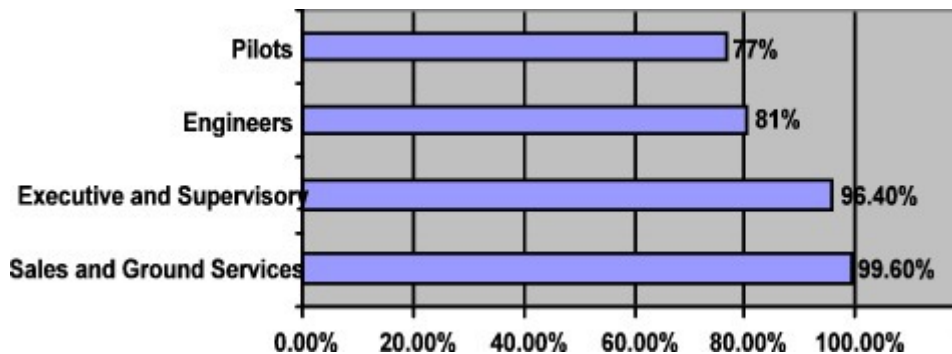
Like the economic policy of the Asian "Tigers," Saudization's ultimate goal is development at the cost of short term transitional disruption. The fruits of the program have already been realized in some industries.

## Saudization Implementation

Air transport reveals that Saudization works. Saudi Arabian Airlines began life as an integrated regional partner of Trans World Airlines (TWA) in 1946. By the late 1960s, the airline pilots were about 60% Saudi and 40% American. Female flight attendants hailed from Lebanon, France, Egypt, and various Asian countries. Saudi Arabian Airlines outlived TWA as a wholly Saudi owned regional powerhouse. The Saudi Airlines current national labor force participation levels demonstrate that Saudization can be achieved in highly complex industries. (See Exhibit #2)

### Exhibit 2 - Workforce Saudization at Saudi Arabian Airlines

(Source: Saudi Arabian Airlines)



The airline now runs its own training programs and has more certifications for aircraft mechanical overhaul and servicing than any other regional airline.

Saudization is not a grassroots phenomenon. Aramco's original oil concessions with the King specified that the company "shall employ Saudi nationals as far as practicable, and in so far as the company can find suitable Saudi employees it will not employ other nationals."

In January of 2003, the Shura Council began to apply Saudization metrics to companies working in the Kingdom that are directly owned by Saudi Aramco as well as those implementing Aramco projects. The Saudization level of contractors must now be included in annual performance reports submitted by the ministry of petroleum and mineral resources. While this may increase the complexity of foreign competitive bids for oil and gas projects, from the Council's perspective the measure moves bid selection toward achieving the country's national labor force interests.

### Implications for Foreign Workers

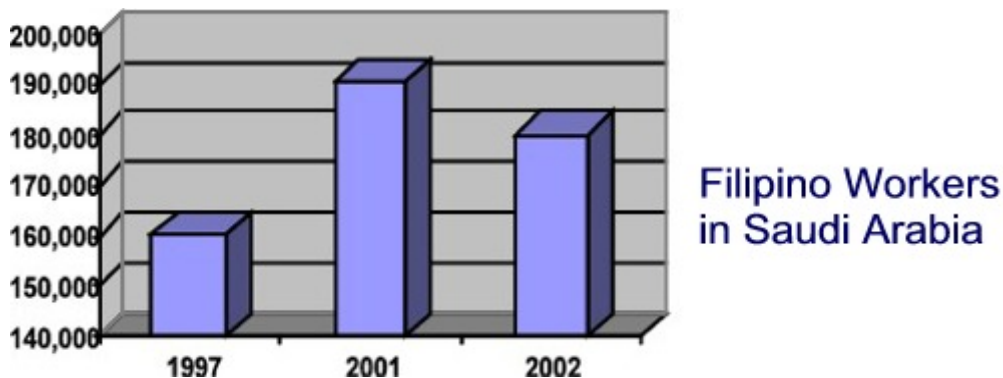
According to the CIA, Saudi Arabia's estimated population in July, 2003 was 24,293,844 including 5,576,076 non-nationals. The nation's high population growth rate of 3.27% per year and young median age of 20.9 for males and 16.8 years for females generates an insatiable demand for new jobs. The Saudi labor force numbers 7 million with 35% of the jobs held by non-nationals. According to the Saudi Bureau of Labor, 501,000 Saudis work in the private

sector. Unemployment in 2002 was 25%. Saudization has not proceeded uniformly across all industries. The huge demand for immediate jobs has led to acceleration of Saudization in some sectors that offer lower barriers to transition.

In September of 2002, Saudi officials decreed that within six months, foreign workers would be barred from driving taxis. That meant replacing about 50,000 drivers accounting for 90 percent of the nation's cab drivers. Other Saudization efforts are more challenging. Early in 2003, the Saudi labor ministry ordered the accelerated Saudization of the 9,771 bank jobs held by expatriates. Many bankers spoke out that Saudization of all banking jobs would likely to cause a brain drain and loss of business to other regional banking centers, particularly Dubai.

In response, some Saudization benchmarks have been relaxed in cases where accelerated transitions threaten economic disruption. Saudization of fruit and vegetable vendors was slowed as accelerated replacement of small foreign vendors proved disruptive and impractical. Even though Saudi Arabia continued to be a top destination for overseas Filipino workers over the past five years, the gradual "Saudization" of jobs in the Kingdom has led to declining numbers of workers according to figures from the Philippine Department of Labor and Employment. (See Exhibit 3)

**Exhibit 3 - Overseas Filipino Workers deployed in Saudi Arabia**  
(Philippine Overseas Employment Administration, 2003)



The application of Saudization thus far indicates an approach that while clearly “top-down” is pragmatic in preserving stability and continuity of industrial operations. However, financial stakes of Saudization as a development strategy are clear. By some estimates, Filipinos, Indians, Bangladeshis and other expatriates remit \$16 billion each year from the Kingdom. If Saudi Arabia can efficiently recapture this wage income, particularly from service sector occupations that accounted for 43.6% of the Gross Domestic Product (GDP) in 2001, it will accelerate the creation of wealth.

**Conclusion: A Matter of Expectations Management**

A pragmatic approach to Saudization, from the perspective of employees, employers and other stakeholders is expectations management. For the wave of Saudis entering the job market, a

willingness to accept jobs within a new system of meritocracy is key. A Saudi leader recently urged young Saudis to consider all categories of employment. "We should take into consideration that our Prophet Mohammed, (peace be on him), was grazing sheep, and Prophet David, (peace be on him), was a carpenter, and so the Saudi youth should not hesitate in doing any job."

For American entrepreneurs, future projects in the Kingdom will require more effective engagement of local talent. One Saudi observer, Omar Bahlaiwa the Secretary General for the Saudi Committee for the Development of International Trade in Riyadh, stated that Saudization is an important tool for U.S. companies as they invest in KSA. When Saudis are well-trained and employed they will be an asset to U.S. investors which must, none the less, be present in the market to capitalize on changing business opportunities.

Saudi executives, worried that increased Saudization will lead to pressures on earnings as salary and benefits increase, may take comfort from the wage strategy of Henry Ford. Henry Ford paid a \$5-a-day minimum-wage at a time the average wage in the auto industry was \$2.34 for a 9-hr. shift. Although the Wall Street Journal opinion at that time labeled the plan "an economic crime," the higher wage made the automobile accessible to Ford workers and strengthened the U.S. middle class. Many Saudi service industries that cannot be efficiently outsourced to offshore operations would benefit from the same strategy. As information technology and other innovations increase operational efficiency, increased wages to Saudi nationals will not be a significant burden to employers.

It is clear that Saudi Arabia has historically marched to the beat of its own drum. Now these percussions are loudly rippling through both business and government circles. The recently announced elections for 14 municipal councils in 2004 culminating in partial elections for the consultative council (Shura) are only the most recent manifestation.

The tempo of Saudization is also increasing. The benefits are likely to outweigh the costs of traditional business practices and produce a net gain for both Saudi and U.S. stakeholders.

### **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

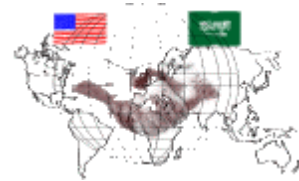
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management consulting firm. While there, he consulted clients in the insurance, banking and industrial sectors on business process improvement, business planning and information systems technology strategies. Before that, he was marketing manager at 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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