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## Current Progress in the Nationalisation Programmes in Saudi Arabia

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**EXPLANATORY NOTE**

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# Current Progress in the Nationalisation Programmes in Saudi Arabia

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**Abstract:** For the past 14 years, Saudi Arabia has been struggling to reduce its dependence on foreign labour and increase the participation of Saudi nationals in the private sector. Policies of Saudization adopted in the last twenty years have not achieved what they set out to do, falling far short in combating unemployment, accommodating the increasing numbers of Saudi job seekers, and decreasing dependence on foreign labour. This explanatory note discusses the latest Saudization scheme “Nitaqat” and evaluates it as a national policy. The note addresses three dimensions: Output of the programme, mainly planned and implemented activities; Outcome or what the policy achieved (intermediate policy results); and finally, the Objective of the programme, i.e., the general impact the policy might have in the long run.

**Keywords:** (Un)Employment, Nationals and Foreign Labour, National Labour, Nationalisation, Workforce, Saudization.

## Introduction

For the past 14 years, Saudi Arabia has been struggling to reduce its dependence on foreign labour and increase the participation of Saudi nationals in the private sector. Policies of Saudization adopted in the last twenty years have not achieved what they set out to do and fell short in combating unemployment, creating jobs for the increasing numbers of Saudi job seekers, and decreasing dependence on foreign labour. Despite the slight increase in the percentage of Saudis employed in the private sector from 10.4 percent in 2011 to 14.4 percent in 2013,<sup>1</sup> the country is still experiencing

the highest influx of foreign labour at any point of time<sup>2</sup> and outgoing remittances remain one of the highest in the world, second only to the United States. Foreign workers are sending out over SR26.6 billion a year and, more importantly, unemployment among Saudis remains very high.<sup>3</sup> Considering these figures, this explanatory note discusses the latest Saudization scheme “Nitaqat” and evaluates it as a national policy. It mainly addresses three dimensions: Output of the programme; mainly planned and implemented activities; Outcome or what the policy achieved (intermediate policy results); and finally, the Objective of the programme, that is, the general impact the policy might have in the long run.

## Background

Since the early 70s, the Saudi economy has been one of the fastest growing economies in the region due to ample oil resources.<sup>4</sup> To carry out the ambitious development plans and build the country’s infrastructure, the government relied on foreign workers to overcome the lack of national human resources and to satisfy the huge demand for labour starting with the first oil boom in the mid-seventies to the present. The ambitious development approach that was adopted by the government resulted in over-dependence on an expatriate workforce to satisfy the labour shortage in the private sector. However, policymakers were aware of the importance of reducing the economy’s dependence on foreign labour and increasing national labour market participation and therefore several initiatives were introduced to nationalise private sector jobs.

The government addressed Saudization as early as 1969 when it drafted its Third Workers and Labour Law.<sup>5</sup> Article 45 of the law stated that 75 percent of private sector workers must be Saudis and their wages should not be less than 51 percent of the total salaries paid; but such a decree has never been implemented or enforced. A few years later, the first oil boom caused a surge in labour demand exceeding the available supply even in the public sector; therefore, there was no pressure to pursue the Saudization policy. However, the government’s attempts continued, and in 1974, it was decreed that priority should be granted to recruitment of Saudis when hiring in the private sector. The law was not enforced at that time because almost all of the Saudis were interested in working only for the public sector, and for the following two decades, the fast growing government sector was able to absorb the national workforce. It was not until the late 1980s that Saudization became a matter of concern due to the sharp increase in the Saudi population from 5,772 million in 1970 to 16,139 million in 1990.<sup>6</sup> Improvement in the population’s educational attainments and saturation in the public sector also pressured decision makers to pursue Saudization more vigorously. Private sector employment elasticity over the past decade was only 1.1, leaving Saudis with no option but to wait for an opening in the public sector. Saudi nationals faced unemployment while the dependence on foreign labour continued. Therefore, Saudization became a priority on the policy agenda at the end of 1990s when the Saudi labour market started recording increasing unemployment rates among nationals, and over 90 percent of private sector employees were foreigners.

In the late 1990s, a number of programmes and targets were launched to reach one goal, which was to increase the Saudi workers’ employment share in the private sector by substituting foreign workers with Saudis. In 1995, an annual increase of 5 percent in the employment share for Saudi nationals in all companies with more than 20 employees was also decreed but this aim remains far from being achieved. The 75 percent target was not realistic because the population was small and demand for labour was

extremely high as a result of the ambitious development projects of the government. The Seventh Development Plan 2000–2005 set a more feasible target of a 25 percent Saudization rate in the private sector by 2002. Later, in the Eighth Development Plan, the target was increased to 30 percent. Along with the quota system, many measures were decreed to expedite nationalisation efforts, such as the reservation of specific job categories for Saudis, such as security, administrative/clerical, sales, and taxi drivers. Visas for such occupations are not being issued. In addition, many sanctions such as exclusion from government tenders and loans and a ban on labour card renewals were introduced for those who failed to comply with the new regulations. However, quotas remain far from being achieved and the Saudis' employment share in the private sector remains low at only 10.4 percent in 2010. Nationalisation strategies are now firmly embedded in Saudi Arabia like in all other Gulf Cooperation Council (GCC) countries to tackle present and potential unemployment problems.<sup>7</sup> Nevertheless, results have not matched the level of government efforts to Saudize; when the country's population of 27 million contains 8.4 million expatriates, it is safe to say that Saudization is under huge pressure to achieve better results than those already attained. Therefore, because of continuing pressure, in 2011 the Saudi policymakers came up with a new and improved programme "Nitaqat," which was launched by the Ministry of Labour and enforced by the Ministry of the Interior. The programme is the focus of our discussion in this paper, bearing in mind that nationalisation tops the economic and political agenda of the Saudi government.

## Nitaqat Output

Nitaqat is a national Saudization programme designed to boost the Saudis' share of private sector employment opportunities. The Nitaqat system evaluates private sector entities based on their nationalisation achievements and classifies them into groups, Excellent, Green, Yellow, and Red, according to their Saudization performance.

As per the Nitaqat programme, companies are classified into four groups:

|   |   |
|---|---|
| Entities achieving an excellent quota performance with the highest percentage of national recruitment | Entities achieving a good quota performance with a good percentage of nationalisation |
| Entities achieving below average performance with a low percentage of Saudization                     | Non-compliant entities  |

The Saudization rate is calculated using a moving average basis over a successive period of 26 weeks, with the number of Saudi workers registered with the Kingdom's national insurance scheme (GOSI). Unlike previous nationalisation schemes which required a unified quota for all companies, under Nitaqat the size of the company and the nature of the economic activities set the minimal requirement for their compliance with the quota system.<sup>8</sup>

The Labour Ministry also claimed that the Nitaqat programme includes many other short-term and long-term objectives like providing more opportunities for less privileged groups such as women, people with special needs, and individuals born with a maternal Saudi heritage. The new scheme also offers greater mobility to expatriates if they are working in non-compliant companies. Saudization targets given in Table 1 are adjusted, upwards or downwards, to fit the prevailing economic situation and outlook. Organisations that meet their targets are given rewards with preferential treatment, mainly facilitating visa renewal for existing visas and granting/issuing new visas if desired. Classification depends upon the number of Saudi jobseekers demanding opportunities in that corresponding field. Companies are again classified into 45 economic activities and categorized into five groups based on the number of their employees. The main tool of the system is visa control: suspending the privileges of issuing, renewing or transferring visas for non-compliant companies and granting all privileges to those who comply.

**Table 1. Nitaqat system**

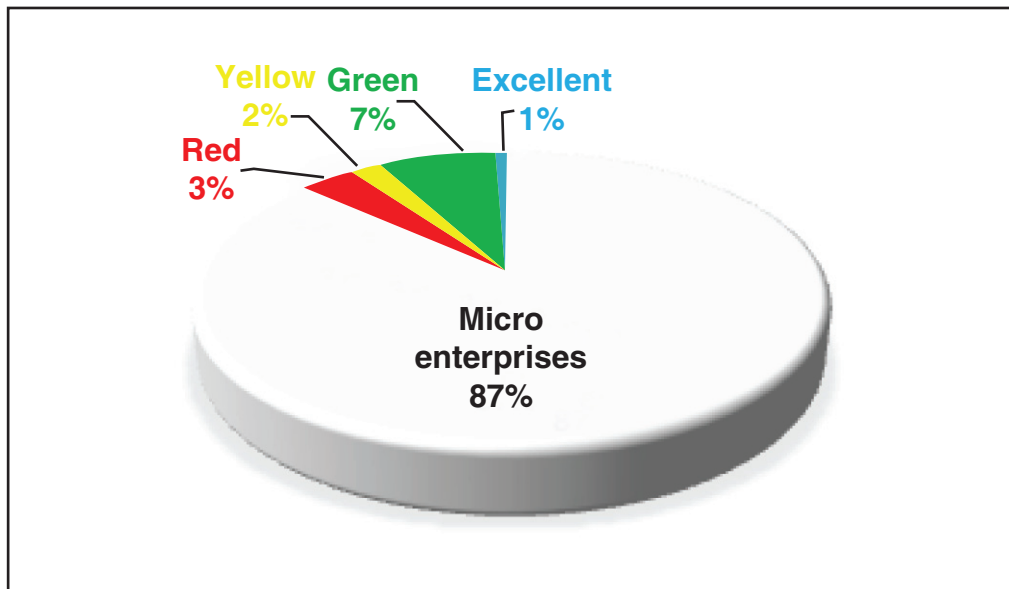
| <b>Number of employees</b> | <b>Size</b>      | <b>Saudization requirement</b> |
|----------------------------|------------------|--------------------------------|
| 1 - 9                      | Micro Enterprise | Exempt from Nitaqat            |
| 10 - 49                    | Small            | 5 - 24%                        |
| 50 - 499                   | Medium           | 6 - 27%                        |
| 500 - 2,999                | Large            | 7 - 30%                        |
| + 3,000                    | Big              | 8 - 30%                        |

Under this system, the Saudization quota that the firm has to satisfy varies by industry and size. Economic activities are allocated into 52 different categories such as tourism, banking, communications and petrochemicals. Each category is divided into five groups based on number of employees, as shown in Table 1. Therefore, firms are distributed among 260 categories. All private entities are classified within each industry by size, economic activity, and the number of employees.

## Nitaqat Outcome

In 2011 when Nitaqat was first introduced, the registered private sector enterprises accounted for 1,805,875. By the end of 2012, their number had increased to 1,979,103. Only 13 percent of the total firms are subject to Nitaqat, because entities operating with less than 10 employees are exempt. The data reveals that about 87 percent of the private sector falls into the white category and is exempt from the quota system.

**Figure 1. Distribution of private sector entities by Nitaqat zone in Saudi Arabia 2011, 2012**



Source: Ministry of Labour Statistical Yearbook, 2012.

As shown in Figure 1, the share of micro enterprises which employs less than 10 people grew between 2011 and 2012 by 9 percent. Growth of micro enterprises is expected in a dynamic growing economy. However, the overall change in each category's share reflects the result of enforcing Nitaqat. Private sector entities are trying to escape penalties and this is evident in the sharp decrease in the red zone's share and, to a lesser degree, the yellow zone's share too. A recent empirical study concluded that about 68 percent of red zone firms improved their status, with over half moving to the green or platinum zone.<sup>9</sup> Moreover, almost 80 percent of the firms in the yellow zone improved their status and moved to a higher zone. In both categories, enterprises try to escape penalties either by reducing the number of employees (if they are small enterprises) or employing more Saudis. In the latter case, the outcome is very positive.

**Table 2: Private sector enterprises by Nitaqat zone 2011-2012**

|                 | Excellent | Good    | Below average | Non-compliant | Exempt    |
|-----------------|-----------|---------|---------------|---------------|-----------|
| <b>2011</b>     | 6,641     | 8,0247  | 40,341        | 120,599       | 1,558,047 |
| <b>2012</b>     | 12,899    | 14,6548 | 37,611        | 67,769        | 171,4276  |
| <b>% Change</b> | 49%       | 45%     | -7%           | -78%          | 9%        |

Source: Ministry of Labour Statistical Yearbook, 2012.

The Saudi labour market is still dominated by foreign workers; they account for about 85.6 percent of the total workers in the private sector, as Table 3 shows. This represents a fall from 89 percent in 2011. This modest improvement is a direct result of the policies that the Saudi government has adopted recently, including Nitaqat. However, it is important to note that the second largest proportion of foreign labour is not in the red or yellow zones, but in the green and white zones. Both of these are safe zones; the green is safe because they have an equivalent workforce share of Saudis, and the white is safe because firms are exempt from the previously mentioned regulations. Therefore, it is very important to look at the overall effect.

**Table 3: Distribution of Saudis and non-Saudis in the private sector by zone, 2012**

|                  | Excellent | Good      | Below average | Non-compliant | Exempt    |
|------------------|-----------|-----------|---------------|---------------|-----------|
| <b>Saudi</b>     | 325,125   | 602,509   | 67,537        | 40,727        | 98,735    |
| <b>%</b>         | 29%       | 53%       | 6%            | 4%            | 9%        |
| <b>Non-Saudi</b> | 210,168   | 3,914,853 | 653,467       | 680,862       | 1,893,550 |
| <b>%</b>         | 3%        | 53%       | 9%            | 9%            | 26%       |

Source: Ministry of Labour Statistical Yearbook, 2012.

Did the new programme increase the number of Saudis in private sector employment? Table 4 shows the composition of the workforce by nationality and gender. It shows that the Saudi males' share in employment, increased in one year by 23.3 percent; on the other hand, there was an increase in foreign male workers but to a lesser degree of 6.16 percent. Combining that with another indicator, which is the number of issued visas for the same period, a noticeable increase can be seen in the number of expatriate workers. The approved visas increased by 33 percent in 2012 as compared to 2011, and the Ministry of Labour explained that the increase was due to a high demand for labour in construction projects (visas issued to the construction sector alone increased by 51 percent, compared to the visas issued in 2011). Therefore, it seems that the substitution of foreign workers did not take place. Instead, more Saudis were employed to satisfy the requirements and more foreigners were used to do the work, especially in sectors that depend heavily on foreign labour such as construction. The easy availability of cheap, low skilled foreign labour made this sector unattractive to Saudis.

The data given in Table 4 shows a noticeable increase (almost 117 percent) in the number of Saudi women employed in the private sector. There were a number of reasons for this increase assuming the reliability of the data and the actual employment of these women as opposed to "phantom Saudization."<sup>10</sup> The increase is due mainly to the large number of Saudi women willing to work,<sup>11</sup> in line with the set of policies and regulations that the Ministry of Labour has implemented to "feminize" a number of retail sales jobs and suitable industrial jobs, and, more importantly, the generous support provided by the Human Resources Fund to subsidise up to half the salary paid to a national employee. The decline



in the non-Saudi females share in employment by -4.21 percent reflects a substitution effect (by Saudi females) especially in retail sales jobs.

**Table 4: Private sector registered employees by nationality 2011-2012**

|          | Saudis  |         | Non-Saudi |          |
|----------|---------|---------|-----------|----------|
|          | Males   | Females | Males     | Females  |
| 2011     | 744,990 | 99,486  | 6,823     | 1,134,66 |
| 2012     | 918,793 | 215,840 | 7,244,206 | 108,694  |
| % change | 23.33%  | 116.96% | 6.16%     | -4.21%   |

Source: Ministry of Labour Statistical Yearbook, 2012.

The data given previously demonstrates an increase in the number of Saudis being employed following the implementation of Nitaqat. Demand for Saudis went up immediately after the implementation of the programme especially as companies sought to avoid non-compliance penalties. The wages for Saudi workers have also gone up by 7.5 percent.<sup>12</sup> Some of this is probably the outcome of regulatory pressure and sanctions from the government. Some of it, however, is attributed to the increasing cost of living in the course of the high fiscal spending.<sup>13</sup> To sustain the increase in wages, nationalisation schemes must not ignore the existing market segmentation and must facilitate and enforce market mechanisms, especially employment based on productivity. Nitaqat has increased Saudi employment as data shows, but such results also come at a heavy cost. A recent empirical evaluation of the programme concluded that the compliance rates were very high.<sup>14</sup> Firms hired an additional 96,000 Saudi workers over an initial period of 16 months, but the programme also caused approximately 11,000 firms to close down, raising the exit rate by nearly 50 per cent. The programme also brought down total employment numbers among surviving firms, and overall private sector employment declined by 418,000 workers. However, correction measures are expected to have some negative impact in the short term.

## Discussion

The focus of our discussion is on whether or not the programme's targets have been achieved. Firstly, the new programme addressed some shortcomings of previous nationalisation schemes, especially at the operational level. It abandoned the blanket quotas of Saudization in different sectors and occupations and adopted more flexible quotas based on needs and demands. One important target of this programme is to increase the employment share of Saudis in the private sector, and it actually did help in this regard, especially in relation to female employment. Many argue that Nitaqat is constructed around a very contradictory philosophy: it aims at rationalising the use of foreign labour to ensure more opportunities for Saudis, yet its incentive system facilitates the use of more foreign labour<sup>15</sup> as compliant companies are granted more visas to hire more foreign labour.<sup>16</sup> Another shortcoming of Nitaqat is revealed by the fact that 87 percent of the private sector enterprises employ a quarter of the foreign labour; more than two million foreign employees are employed by firms in the white zone which are exempt from Nitaqat. Such exemption might encourage employers to restrict employee numbers below nine in order to es-

cape the Saudization requirement and that undermines the effectiveness of the programme in reducing dependence on foreign labour and increasing opportunities for Saudis. On the other hand, the business community is concerned that in the absence of qualified and skilled employees, the productivity of the business and industrial sector might be undermined. This, in my opinion, is a short-term effect and business could adjust in the long term if nationalisation programmes tackle the supply and demand issues. Recent evaluations of Nitaqat's impact on increasing the Saudi nationals' share of private sector jobs has not been positive<sup>17</sup> as it showed that the share of the nationals in private sector employment increased at a very modest rate. Also, the implementation of Nitaqat has been very difficult, and the programme has had only a modest impact so far in boosting private sector employment and reducing foreign dependence.<sup>18</sup>

The modest effects recorded so far, despite the government's long term commitment to Saudization, are a result of the failure to tackle the issue comprehensively. The schemes adopted were not, and are still not, part of a strategic process where all government policies are aligned and synergized to reach a common goal and where all stakeholders are involved. Nationalisation still faces two obstacles: first, it obligates the private sector to employ more Saudis but has no means of motivating nationals to participate actively in the private sector, especially considering the ongoing competition from the government sector. Then, the growing wage disparity and the expansion in government recruitment further intensifies the preference for government sector jobs.<sup>19</sup> Government investment decisions have a long term impact on employability. In recent years, growth in Saudi Arabia has been driven by government spending on large infrastructure projects which in turn is facilitated by easy access to low wage foreign labour. Consequently, sectors such as construction and general services have been the main engine of private sector growth.<sup>20</sup> However, these sectors have not contributed to an increase in Saudi employment and are not expected to do so in the future because of the low wage levels and low skill requirement. Therefore, strategic investment decisions should take into account employability implication on local human resources and the level of required skills. Nitaqat cannot stand alone and have an optimal impact without the necessary changes being made to the labour market eco-systems. This would also mean focusing on administrative intervention rather than on market mechanisms, which would then pose major constraints to an effective labour policy.

Like all previous programmes and initiatives, Nitaqat has had some degree of success as discussed previously but has also brought along significant costs and inefficiencies that a market-oriented policy could have minimised. In addition, quotas and occupational bans, such as Nitaqat, are policies of micro-management, which demand a monitoring capability that is beyond even the most modern of bureaucracies.<sup>21</sup> They create incentives for manipulation, fake employment, and corruption. Inspection capacities have been criticised as insufficient on the basis that bureaucratic discretion reduces the legal security of business and creates opportunities for corruption. Labour offices have limited information about the actual needs and structures of the hundreds of thousands of businesses operating in the Kingdom, which can result in misallocation of visas and Saudization requirements. The Ministry of Labour claimed that its new controlling body for labour inspections will significantly increase its monitoring capabilities, but this remains to be seen as the policy is still in a transition stage and requires more monitoring and evaluation.

## Conclusion

The paper provides an overview of the current progress towards Saudization. Nationalisation policies are proceeding briskly as labour markets undergo huge adjustments driven by demographic changes in the Kingdom, along with an improvement in the quality and quantity of the local labour supply. However, for policies to be successfully implemented, active coordination between the government and the private sector is required. Therefore, we can draw two broad but related conclusions: on the supply side, there is an ample pool of skilled Saudi labour, but there is still a mismatch between supply and demand that needs to be addressed by introducing complementary policies beyond Nitaqat. On the demand side, the segmented labour market still exists and the Nitaqat programme actually further reinforces the segmentation by creating a bigger gap between Saudi and non-Saudi salaries as a result of which private employers are expected to favour expatriates because of their lower wages. Quantitative measures of nationalisation might encourage an increase in phantom Saudization. Expatriate labour continues to be vital to support certain sectors such as construction and localising these sectors is neither possible nor advisable.<sup>22</sup> This situation is compounded by conflicting government strategies, influencing both supply and demand. For example, the expansion in higher education institutions push youth away from vocational training, further widening the skills gap in the long run. Besides, the government has initiated an expansion in public sector recruitment to ease social and political pressures. If these two issues are addressed, a sustainable outcome and positive progress in the nationalisation process is expected. In the long term, effective nationalisation policies require structural reform in many areas, including coordination and synergy between labour policies and macroeconomic policies, addressing nationalisation concerns when making strategic investment decisions, and modifying the prevailing social contract.<sup>23</sup>

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## Endnotes

1. Ministry of Labour, Workers Statistics Division, 2013.
2. According to Ministry of Labour statistics, the number of foreign workers increased from 4.74 million in 2005 to 6.937million in 2011 and to 7.352 million in 2012.
3. Unemployment rates among Saudi nationals rose from 5.4 percent in 2000 to 12.1 percent in 2012 and if we look at unemployment rates by gender it rose from 15.8 percent to 35.7 percent among women.
4. IMF 2013.
5. The first Workers and Labour Law was issued in 1941, the second Law was issued in 1946, and the third Workers and Labour Law was issued in 1969, the last Labour Law was issued in 2006.
6. Fertility rate during that period was on average 7.2 (number of children per women)
7. I. Forstenlechner, "Workforce Localization in Emerging Gulf Countries: the Need to Fine-tune HRM," *Personnel Review*, 39, no. 1(2010): 135-152.
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10. This expression is widely used to explain statistical employment to meet nationalisation requirements.
11. According to job search assistant benefit "Hafiz" data, 86 percent of Saudis looking for jobs are women.
12. Saudi Hollandi Capital Report, "Labor and Nitaqat Program."
13. S. Hertog, "A Comparative Assessment of Labour Market Nationalization Policies in the GCC." In *The Gulf Region: Economic Development and Diversification*, 4. (Berlin, Germany: Gerlach Press, 2012). Also available at: LSE Research Online <http://eprint.lse.ac.uk/46746/>.

14. J. Peck, "Can Hiring Quotas Work?"
15. This is one of the most prominent shortcomings of the program, but policy makers are arguing such an incentive is necessary in the short run in order not to hinder private sector growth.
16. Riyadh Economic Forum, "Labor Policies and Nationalization of Private Sector Jobs," December 2013.
17. Hertog, "A Comparative Assessment of Labour Market Nationalization Policies in the GCC."
18. See IMF Country Report 13/230.
19. H. Alsheikh and Erbus, "Labor Income and Oil Wealth: A Border Sustainability Framework for Saudi Arabia," Middle East Development Journal (MEDJ), Vol. 05, no. 2, June 2013, <http://www.worldscientific.com/toc/medj/05/02>.
20. See IMF Country Report 12/272'.
21. Hertog, "A Comparative Assessment of Labour Market Nationalization Policies in the GCC."
22. Most of the construction jobs require low skilled and manual workers, and such workers are not available among the Saudi workforce. In addition, wages are very low which hampers the welfare of the individuals and Saudi society in the long run. Low skilled workers are more likely to live in the lowest socioeconomic group; there is no career path for these jobs and their earnings peak while expenses continue to rise, both because of inflation and increasing family responsibilities. These economic consequences are compounded by lack of status and a feeling of inferiority, making these jobs undesirable among Saudi nationals.
23. As a rentier economy, citizens of Saudi Arabia are more dependent on state employment than most other countries in the world and often expect their government to cater for their employment needs by creating more jobs in the public sector.

## About the Author



**Hend M. Alsheikh**, Ph.D, is a Professor of Economics at the Institute of Public Administration and currently is the director general of the female branch of IPA. She started her academic career at King Faisal University. During her service at IPA, she was in secondment at the International Monetary Fund (IMF) and also was policy and strategy consultant at King Abdullah University for Science and Technology (KAUST) in the economic development unit. As a labour economist, her publications focus on labor market challenges: female labour allocation, wage differentials, and the sustainability of the Saudi growth model taking into account labour market imbalance.

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