

WORKFORCE LOCALIZATION POLICIES IN SAUDI ARABIA: THE DETERMINANTS OF SUCCESSFUL IMPLEMENTATION IN MULTI-NATIONAL ENTERPRISES

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Abstract:

Job Localization policy in Saudi Arabia (commonly known as ‘Saudization’) has passed its fourteenth year aiming at replacing foreign employees in the private sector with local employees. This research attempts to identify the determinants of localization success within Multi-National Enterprises (MNEs) in Saudi Arabia. From institutional perspective, the research evaluates the impacts of Institutional determinants, HR practices, role of HR director, and firm characteristics on localization success. The study draws its conclusion from the analysis of quantitative data collected from Human Resource Directors representing 157 MNEs. With regard to the first group of localization determinants, the results completely support the cause and control determinants while supporting only the consistency proposition in the content determinants. In regard to HR determinants, recruitment, training and the role of HR director were found to be powerful determinants of localization success. Finally, the results have shown that determinants related to MNEs’ characteristics, namely MNE size and MNE age, have no significant impact on localization success. We also found that MNEs which operate in the petrochemical sector are more likely to succeed in their localization policies than other industries, namely electronics, food, motor, paper products, real estate, business services, hotel, manufacturing, and agriculture industries.

Keywords: localization policies, Saudization, institutional theory, HR practices, role of HR director.

1. INTRODUCTION

The labor market in the Kingdom of Saudi Arabia has depended heavily on foreign workers. The Expatriate labor constitutes two-thirds of the total workforce in Saudi Arabia (Pakkiasamym, 2004). In the private sector the expatriates found to represent more than 88 % of the workforce according to recent report by the Saudi Arabia Monetary Agency (SAMA) in 2008. The rising number of unemployment rate among Saudis ranging from 10 percent to 30 percent has caused the government to launch a policy of jobs localization so called “Saudization” (Rice, 2004). Moreover, The Saudi government has expanded employment of Saudi nationals, as part of its strategic goal of creating a domestic labor force and preparing solid human capital to meet the needs of skilled labor for the large public and private development projects, and to decrease the huge money fleeing the country by foreign labor estimated 20 Billion SAR annually (Ministry Of Economy and Planning Report, 2008).

2. BACKGROUND ON SAUDIZATION

With an aim of creating new jobs through the process of assimilation, i.e. replacement of foreign workers with Saudi nationals, the Saudi Arabia initiated in 1994 the Saudization program intensively implemented during the Sixth Development Plan of the country (1995–1999). The program focuses on setting quotas for the number of nationals which private firms should hire aiming at increasing the Saudi jobs in the private sector. The concept refers to the replacement of expatriates (sent from the parent company’s native country) with competent and skilled local employees (recruited from the local labour market of the host country) (Law et al., 2009, p. 135). The policy was formulated through a ministerial decree in 1995, which “declared that private firms with over 20 employees should reduce the number of non-Saudis by 5 percent annually, implement penalties for non-compliance including denial of access to certain types of government support, enforce a freeze on applications to hire new workers from abroad and on their renewal of existing permits” (Ministry of Planning, 1995; Said & Al-Buraey, 2009, p.70).

After the initial introduction in 1995, the progress of the Saudization policies was reviewed and revised in the Seventh Development Plan (2000–2004), when targets were set to 25 percent of private sector jobs by 2004 (Al-Dosary and Rahman 2005). However, the activities are not producing the set targets due to a combination of factors which influence the outcomes: (1) the strong public sector where Saudis tend to seek employment as it offers them a three times higher salary compared to the private, (2) the high unemployment benefits and (3) the lower efficiency of the Saudi labour compared to the foreigners (BMI, 2011, p.1; Al-Dosary & Rahman, 2005). BMI (2011, p. 2) reports that in 2011, “the Saudi nationals account for only 10 % of private sector employees”. The persistence of the above mentioned factors makes it unlikely that there could be a significant change in the period to come, unless a larger penetration is not made in the private sector and particularly among the Multinational Enterprises present in the country.

3. RESEARCH PROBLEM

Localization literature lacks theoretical foundations as most research is narrow in scope and descriptive in general. Moreover, Success factors of localization are rarely understood across countries and industries.

4. RESEARCH AIM

The aim of this study is to identify the determinants of successful implementation of the workforce localization policy in Multi-National Enterprises (MNEs) in Saudi Arabia.

5. LITERATURE REVIEW SUMMARY

After conducting an extensive survey of the relevant literature of Saudization, the following gaps have been identified:

- There are no coherent theoretical foundations of the saudization or any workforce localisation process. It seems that most of the studies have been concerned with the practicality of the policy without developing theoretical understanding based on empirical findings.
- There is no conclusive study which investigates the roles and influences of HR practices on the implementation of workforce localisation policy. Most researchers have rather used their common sense and rational thinking to determine that such HR roles and influences exist.
- There is no single study which verifies the different roles of the HR Director on the successful implementation of workforce localisation. Notably, all of the previous studies neglect to examine the role of the HR Director in relation to such a policy.
- There is no extensive study which examines the workforce localisation in MNEs. However, several studies mention that this industry is very promising for researchers interested in the localisation policy. The reasons behind this are two: first, owing to the strong willingness by the Saudi government to support localisation in MNEs for security issues; and secondly, it seems that this industry has mixed success and failure scenarios in regard to localisation. Therefore, it would be very interesting to examine the determinants of localization success MNEs.

6. THEORETICAL FRAMEWORK AND RESEARCH HYPOTHESES

We adopted the institutional theory as the basis for our theoretical framework. The Institutional theory focused on the forces that shape the behaviour of companies provides the best framework for a comprehensive analysis on the forces influencing the Saudization in the MNEs and its success. It is the starting point in the further analysis.

The institutional theory is based on the recognition that institutions either enable or impose limitations on the scope of humans and companies (human agents) “by creating legal, moral and cultural boundaries” (Delbridge & Edwards 2007, p. 192). In the case of Saudi Arabia these are the government laws and regulations and the general expectations of the society based on the culture and accepted values.

According to Scott (2001, p. 49), although there is no debate on the definition of what constitutes and institution, defined as ‘multifaceted, durable social structures, made up of symbolic elements, social activities and material resources’, the literature provides an array of different interpretations about the origin, context and scope of the Institutional theory (Delbridge & Edwards, 2007). These views, according to Scott (1987, pp. 493–501) can be divided into four different categories:

The first, or the earliest institutional view embraced by researchers and practitioners, identifies the institutional pressures as a process of instilling value in the organisational structures creating adaptive mediums that go beyond the technical elements shaped both by the characteristics of participants and by external influences from the environment (Scott, 1987, p. 494). The second view on institutionalisation focuses on the creation of reality described in the work of Berger (1981) (Scott, 1987, p. 497). Berger and later Luckmann's arguments associate the concept of social order to the concept of shared social reality in which organisations operate. The third view of the institutional theory views institutionalisation as a system in relation to a distinctive set of elements important for the existence and justification of organisational structures (Scott, 1987, p. 497). The most important characteristic of this view is the shift of focus from the generalised features of belief systems towards various 'institutionalised' sources (Scott, 1987, p. 497). The new focus encouraged analysts to study other types of processes that shape institutional conformity, such as the coercive, mimetic and normative processes developed by DiMaggio and Powel (1983). This altered focus paved the way for greater attention placed on the nature of belief systems on actors beyond the environmental elements and for the development of the conception of multiple institutional environments (Scott, 1987, pp. 497–498). The fourth view supports the idea of diversity of belief systems and their linkage with the traditional view of social institutions as symbolic and behavioural systems. It emphasises instilling value and stressing the theme of persistence and stability of social institutions as “the major mechanisms for social continuity” (Scott, 1987, p. 499).

As argued by Scott (1987, 2001) and later by the comprehensive review of Delbridge and Edwards (2007) as a general benefit from all of the four institutional theory views described in the preceding paragraphs, the view of the organisation as a simple production system has changed, while institutional theorists have focussed on the importance of the symbolic aspects of organisations and their environments and the fact that all organisations exist in a social context which defines and delimits social reality. Moreover, the literature review of all four views on the institutionalisation theory is rich with description on how the institutional theory restricts the choices of companies. The passive outlook of researchers is mainly focussed on the way value and social meaning is installed in organisations (Berger & Luckmann, 1967; Selznick, 1957), and the types and varieties of these institutional processes (DiMaggio & Powell, 1983). As Scott (1987, pp. 507–509) and Delbridge and Edwards (2007) argue this makes the theory rather passive in an environment where the interests shape the behaviour of the actors and where the actors can recognise its interest, contrary to DiMaggio, who argues that norms and assumptions can make “actors unlikely to recognise or to act upon” them (1988, pp. 4–5). In the process Scott (1987, pp. 507–509) moved the debate further and provided an analysis on the impact of the interests and actors on the organisational structure and systems. As a result, Scott (2001, pp. 51–69) developed a consistent institutional framework, composed of three institutional determinants named as regulative, normative and cognitive forces. The regulative forces represent the organisations' rules, regulatory constraints (forced by regulatory bodies) and penalties for violations. The normative forces identify the values and the social behavioural norms which define how things should be done within the organisation, while the cognitive forces represent the actors' social-cognitive perspective, their formulation about what they are and their logical frame of action in different circumstances.

As the work of DiMaggio and Powell (1983) and Scott (1987, 2001) has been more focused on identifying the pressures on companies, the research in the management begun to seek for ways in which the companies can react to these pressures and protect their interests. As a

result Oliver (1991) further developed the institutional theory by defining the strategic responses of companies to these institutional pressures (Clemens, et al., 2005). What Oliver (1991) begun grew into a substantial body of literature (Greeve, 1998; McNamara, et al., 2003; Oliver, 1997) in the institutional theory focused on predicting the strategic choices of companies when pressured with the institutional forces (Goldstein, 1994).

7. INSTITUTIONAL THEORY AND JOB LOCALIZATION IN MNES IN SAUDI ARABIA

The institutional theory as defined by Scott (2001) defines the forces which pressure the companies and shape their internal and external behaviour, while the framework of Oliver (1991, 1997) provides the logic behind their choices. These frames are of particular importance as they can explain the success, or failure, of the job localization process in general and the Saudization in particular. In the case of Saudi Arabia, the Multinational Enterprises are of particular importance for the success of the localisation. According to August (2004, p. 203), a Multinational Enterprise (MNE) is "an enterprise organised around a parent firm established in one state that operates through branches and subsidiaries in other states." There are more than 250 MNEs present in Saudi Arabia at the moment, while their number is likely to increase in the future having in mind the growth of the national economy. The success of the job localisation among the MNEs is of particular importance for the success of the *Saudization*, as MNEs do not only impact the process through the direct employment, but they as well influence the indirect employment levels through the labour turnover, the movement of employees from one company to another and the engagement of local companies in their supply chains.

The specific framework of this research is related to MNEs responses to institutional pressures as outlined by Oliver (1991). We modified the framework to measure whether MNEs succeed or fail on localization instead of compliance or resistance. We also added to this framework two other groups of determinants; HR determinants, and determinants related MNE characteristics (age, size, industry). We have divided our research hypotheses into three main groups. Each group has a set of related hypotheses that might have an impact on the success of the localization policies. We named the first group institutional determinants, the second group HR determinants, and the last group MNEs' characteristics determinants.

The first group is related to Oliver typology. As outlined in the literature, this typology has received a great deal of attention in the area of institutional theory. Oliver (1991) identified five determinants that could impact MNE decisions when responding to institutional pressure such as localization policies. These determinants are the cause, the context, the constituents, the content and the control of localization policies. Accordingly, we formulated our first set of hypotheses to test the relationship between these institutional determinants and localization success in the context of the country of Saudi Arabia:

1. The Cause:

H1: MNEs who perceive localization pressures as legitimate are more likely to achieve localization success.

H2: The higher the economic gains an MNE attain from localization, the greater the likelihood of localization success.

2. The Context:

H3: The higher the degree of interconnectedness between MNEs, the greater the likelihood of localization success.

H4: The lower the degree of uncertainty within the MNE's environment, the higher the likelihood of localization success.

3. The Constituents:

H5: The higher the degree of government multiplicity as perceived by MNEs, the lower the likelihood of localization success.

H6: The higher the degree of dependence on government by MNEs, the greater the likelihood of localization success.

4. The Content:

H7: The higher the degree of consistency of localization requirements with MNE culture, the greater the likelihood of localization success.

H8: The lower the number of constraints imposed by localization on MNE decisions, the greater the likelihood of localization success.

5. The Control:

H9: The higher the legal coercion to implement localization felt by MNEs the greater likelihood of localization success.

H10: The broader the diffusion of localization rules within MNEs the greater the likelihood of localization success.

The second group is associated with HR issues. It has been argued in the localization literature that some HR practices such as recruitment and training could play an important role in localization success. Additionally, we proposed that the role of HR director might have a major influence on the adoption of localization policies. Further, we consider the nationality of the HR director (being Saudi vs. non-Saudi) as a control variable due to its possible association with HR determinants, in particular, the role of HR director. As a result, we aim to test the effects of these HR determinants in our second set of hypotheses:

H11: MNEs with Saudi national HR directors are more likely to achieve localization success.

H12: Recruitment practice will have a positive impact on localization success.

H13: Training practice will have a positive impact on localization success.

H14: The role of HR director will have a positive impact on localization success.

The third group is related to the characteristics of MNEs. We set out these hypotheses to examine the role that MNEs' age, size, or the type of industry could play in the success of localization policies. Accordingly, we propose the following hypotheses:

H15: The older the age of MNEs, the greater the likelihood of localization success.

H16: The bigger the size of MNEs, the greater the likelihood of localization success.

H17: MNEs that operate in the petrochemical industry are more likely to achieve localization success.

8. RESEARCH DESIGN AND METHODOLOGY

To fulfill the research objectives, the study implemented a quantitative approach through the use of survey questionnaires. The research sample was drawn from a pool of top HR directors in MNEs operating in Saudi Arabia. In the current study, data was collected through for surveys composed of a bundle of open and closed questions are implemented in a real work situation in Saudi Arabia. Out of 246 MNEs contacted, a total of 157 valid and complete surveys were obtained.

9. DATA ANALYSIS

We screened and cleaned up the data from the effects of missing data and outliers, and tested the main assumptions underlying multivariate techniques such as normality, homoscedasticity and linearity. The amount of missing data was very small. Little's MCAR test revealed that patterns of missing data were completely at random. Analysis of outliers indicated few extreme cases in MNE size and MNE age. These cases were retained due to the varying nature of these variables. Results also revealed that the data are normally distributed except for MNE size, which has been transformed by taking the logarithms of MNE size. Data screening also revealed homoscedastic relationships between variables. We also tested the linearity of the research variables and the results indicated that the independent variables are not highly correlated.

To answer the main research question, we have divided our research hypotheses into three main groups. Each group has a set of related hypotheses that might have an impact on the success of the localization polices. We named the first group institutional determinants, the second group HR determinants, and the last group MNEs' characteristics determinants. In the current study, the researcher employed a multiple regression technique to test the research hypotheses. This method is appropriate for analysing the research data because we are attempting to evaluate the relationship between several independent variables (MNE size, MNE age, industry, legitimacy, economic gains, interconnected context, uncertain context, constituent multiplicity, government dependence, consistency, constraints, legal coercion, broad diffusion, HR director nationality, role of HR director, recruitment, and training) and a single dependent variable (localization success).

Following the logical reasoning outlined in the literature, we have presented localization determinants in three different groups. Accordingly, we have tested each group of determinants separately in the previous sections. Results indicated that some determinants in each group have significant impacts on localization success, while others made no unique contributions in their relationships with the outcome variable.

In this section, we conducted another regression test to explore the amount of variance in localization success that each group of determinants could explain independently. Table1 shows the analysis of variance for all localization determinants groups. We entered the institutional determinants in the first step, followed by the HR determinants in the second step, and finally entered the determinants related to MNEs' characteristics in the third step. The results in Table 5.12 show that institutional determinants are strongly related to localization success, ($R^2 = .587$, $F = 20.761$, $p < .001$). Importantly, the results of the analysis of variance also show that HR determinants are able to explain a significant incremental level of variance in localization success above the percentage that the institutional determinants have explained ($\Delta R^2 = .115$, F for $\Delta R^2 = 13.751$, $p < .001$). In other words, HR determinants are able to significantly explain 11.5 % of the variance in localization success beyond what the institutional determinants could explain. In addition, the analysis also revealed that the determinants related to MNEs' characteristics are only able to explain a partially significant incremental amount of localization success beyond what the institutional and HR determinants have explained ($\Delta R^2 = .046$, F for $\Delta R^2 = 1.561$, $p < .10$). In other words, MNEs' characteristics are only able to explain approximately 5 % of the variance in localization success after the contributions of the first and second groups of determinants. The results overall indicate that all groups of determinants are significantly related to localization success. However, when looking at the individual determinants in each group, the results will

differ based on the significance of each single determinant in each group in its relationship with localization success. These results are interesting, especially when we explain them at the individual level, and they add an interesting contribution to the theoretical and practical sides in the context of Saudi Arabia. The results are discussed in detail in the next chapter.

Table 1: Analysis of variance for all determinants of localization success.

	Institutional Determinants	HR Determinants	MNEs Characteristics
	<i>Localisation Success</i>	<i>Localisation Success</i>	<i>Localisation Success</i>
R ²	.587	.702	.749
Adjusted R ²	.559	.673	.691
Δ R ²	.587	.115	.046
F for Δ R ²	20.761	13.751	1.561
Significant for Δ F	.000***	.000***	.094†

Notes: N = 157.

† $p < .10$, * $p < .05$, ** $p < .01$, *** $p < .001$

10. RESEARCH FINDINGS AND DISCUSSION

We tested our hypotheses by using multiple regression analysis. With regard to the first group of localization determinants, the results completely support the cause and control determinants while supporting only the consistency proposition in the content determinants. In regard to HR determinants, recruitment, training and the role of HR director were found to be powerful determinants of localization success. Finally, the results have shown that determinants related to MNEs' characteristics, namely MNE size and MNE age, have no significant impact on localization success. We also found that MNEs which operate in the petrochemical sector are more likely to succeed in their localization policies than other industries, namely electronics, food, motor, paper products, real estate, business services, hotel, manufacturing, and agriculture industries.

The empirical tests for each of the determinants (Institutional, HR, and MNE characteristics) presented in the previous section provide an understanding for the significance and relevance on each of the determinants on the localisation success in Saudi Arabia. Now, it is important to understand the relative impact which each of the determinants has on the localisation success in an extended model. The findings indicate that institutional determinants are strongly related to localisation success, accounting for 58 % of the model's variance. HR determinants are able to explain a significant incremental level of variance in localisation success of 11 %, while MNEs' characteristics are only able to explain a partially significant incremental amount of localisation of 5 %. The findings provide a deeper understanding of the process of saudization and which elements account for its success. The strong impact of the institutional determinants is in line with the previous findings on Law et.al. (2009), Law (2004), and Bjorkman (2007) on the localisation success in other developing countries, and

the findings of Goodstein (1994), Ingram and Simons (1995), Etherington and Richardson (1994), Milken et al. (1998), Clemens et.al. (2005) on the impact of the determinants on the strategies of the companies. Therefore, in this regard, the findings provide little surprise, apart from the findings on the individual impact of each of the factors which were discussed in the preceding sections. The relatively negligent impact of the HR determinants supplements the model, arguing that for the Saudization to be more successful HR strategies and activities must support its introduction among the Saudization of MNEs. Again these findings are in line with the previous empirical research of Law et al. (2009), Law (2004) and Bjorkman (2007) on the localisation success in other developing countries. It is good to mention that an increase of MNE's participation in the design and implementation of the Saudization policy might increase this influence in the future.

The insignificance of the MNE's attributes (age, size, and industry) is the largest surprise in the model, as most of the previous research in the other countries, mentioned above, indicates that MNE's characteristics have an impact on the localisation success. The insignificance of these variables in the model can be explained with the rather unique context of the Saudi society and economy, mainly the inflexible labour market, the impact of the lack of transparency in the system, and the lack of coordination among the participants in implementation of the Saudization policy.

Finally, the findings from the model can contribute in the design of a more effective and efficient Saudization policy in the future, and they as well can serve as a benchmark for the further success of the policies.

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