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Redefining the social contract

Policy options for economic inclusion and fiscal sustainability

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EXECUTIVE SUMMARY

Following the 1970s oil boom, the Gulf Cooperation Council (GCC)[1] countries developed a generous welfare model offering a wide range of benefits to nationals, including public-sector employment, energy subsidies, a variety of non-means-tested categorical benefits,[2] and free public services such as education and healthcare. Governments now understand that this implicit social contract needs reform, given fiscal constraints and demographic pressures.

Although GCC governments are responding to this challenge, thus far reforms have been piecemeal. Creating a new social contract requires simultaneous fiscal reform, welfare modernization, and labor policy changes. Moreover, governments need to design and implement the contract components specifically for each country's needs.

There are five policy tools that GCC governments can consider as they redesign their social contracts, described below:

- Permanent income supplements for lower earners can make private-sector employment more attractive to nationals. Such income support ensures that the shift away from public-sector employment does not result in "working poor."
- Active labor market policies, including lifelong learning, job services, and training, can support nationals' integration into the private sector.
- Universal basic income (UBI) can provide all nationals with income security, while maintaining incentives for private-sector entrepreneurship and work.
- Means-tested social benefits can support those that need it most, while reducing welfare dependency and fraud.
- Integration of foreign residents through dedicated welfare tools, such as a modest minimum wage, can attract and ensure a ready workforce of foreigners, while reducing the differential in labor rights and costs that discourages employers from hiring nationals.

A new social contract in GCC countries can provide opportunities to all nationals, guarantee basic welfare for all, incentivize and improve the rewards for private economic activity, ensure fiscal sustainability, and minimize economic distortions.

THE NEED FOR A NEW SOCIAL CONTRACT IN GCC COUNTRIES

To illustrate the problems in the established social contract in GCC countries, consider Fulan bin Fulan, a Saudi national in his late 30s. Fulan has a government job. His monthly salary is SAR14,000 (US$3,732). That is average for the public sector, but substantially higher than the average monthly salary of SAR11,400 (US$3,039) earned by Saudi men working in the private sector.[3]

Fulan's family has a SAR500,000 (US$133,268) home mortgage, which it obtained from a private bank. Saudi Arabia's Real Estate Development Fund provides a partial subsidy of the loan and its interest rate. The government also subsidizes the first 6,000 kWh of electricity that the family uses each month and the gasoline to run the family cars.[4]

Before he landed his first job, Fulan received SAR2,000 (US$533) per month in Hafiz unemployment benefits. Saudi Arabia's Citizen Account Program paid his family SAR1,400 (US$373) per month until he was promoted to his current, higher-earning job.[5] Fulan's family enjoys free healthcare and schooling, including university education.

Although Fulan and his family do not exist, the generous government-provided benefits described above are typical of the employment support, free public services, and subsidies that Saudi Arabia and other GCC countries provide to their nationals. They are integral to an implicit social contract that is extensive compared with the welfare systems of other high-income countries—and, critically, that is delivered through quite different channels. GCC countries spend far more on salaries and energy subsidies than do advanced economies in the Organisation for Economic Co-operation and Development (OECD), but far less on support mechanisms such as unemployment benefits, income supplements for low-income citizens in the private sector, and non-contributory state pensions.

Although the social contract in the GCC countries has created, and supported, a large and prosperous middle class in the past 50 years, some of its core components have resulted in economic distortions. In Kuwait, Qatar, and the United Arab Emirates (UAE), for example, more than two-thirds of nationals in employment are in the public sector. Such government overemployment encourages bureaucratic sluggishness, lowers accountability, uses talent inefficiently, and distorts labor market incentives for nationals. Fuel subsidies also have undesired consequences: They encourage overconsumption of fossil energy and foment regressive consumption patterns in which richer households benefit more from state resources than poorer households.

GCC governments recognize that their established social contracts are not sustainable. Fiscal constraints, demographic growth, and the inability of public sectors to absorb employment and serve as a social safety net are eroding the social contract. Fortunately, GCC governments are responding to these changes. They have reduced or eliminated subsidies, for example, replacing some of them with less distortive and regressive cash grant systems, such as the Citizen Account Program that Saudi Arabia introduced in 2017. However, it is not easy to reform all aspects of the established social contract, and some cuts to old entitlements can have unintended consequences.

Reducing subsidies and public-sector hiring without careful analysis and considered action can exclude some nationals from the social contract. These nationals do not have access to the principal channels through which GCC governments have historically shared wealth. For instance, nationals in the low- to mid-skilled segments of the private labor market must contend with strong competition from lower-cost expatriates, a competition that depresses wages in comparison with what GCC nationals earn in the public sector. Of the 2.3 million Saudis employed in the private sector in the third quarter of 2023, 1.3 million earned less than SAR5,000 (US$1,333) per month; the average public-sector wages for Saudis are more than SAR13,000 (US$3,465).[6]

Welfare systems that could benefit such nationals stranded in the private sector are underdeveloped. Consequently, in some GCC countries, a divide is growing. On one side are (often older) nationals with well-paid government jobs. On the other side are younger nationals with lower private-sector incomes (excepting the managerial and entrepreneurial elite). Although some GCC governments have deployed temporary grants and support systems for nationals outside public employment, these efforts are insufficient to bridge this income gap and maintain the old guarantee of middle-class life.

GCC countries need to go beyond partial reforms toward a new social contract. They need to do so in a comprehensive and systematic manner that eliminates the excessive costs and distortions of the established model, while providing young nationals with opportunities similar to those enjoyed by their older peers.

THE ESTABLISHED SOCIAL CONTRACT HAS WORN THIN

Following the 1970s oil boom, the GCC monarchies developed a welfare model based on a de facto public employment guarantee for most male citizens, subsidized energy, a varying range of welfare benefits that were not means-tested, and free public services (*see Exhibit 1*). A more detailed statistical analysis of the established social contract is available on coauthor Professor Steffen Hertog's website.[7]

As the implicit guarantee of public employment suggests, the ratio of GCC nationals in public-sector jobs is higher than in comparable countries. Consequently, government wage spending across the region is also greater than in similar economies. The most recent data available shows that 40 percent or more of government spending in Bahrain, Kuwait, and Saudi Arabia was devoted to employee compensation.[8] These figures are at least double the average share of wage spending in OECD countries' budgets of 20 percent.[9]

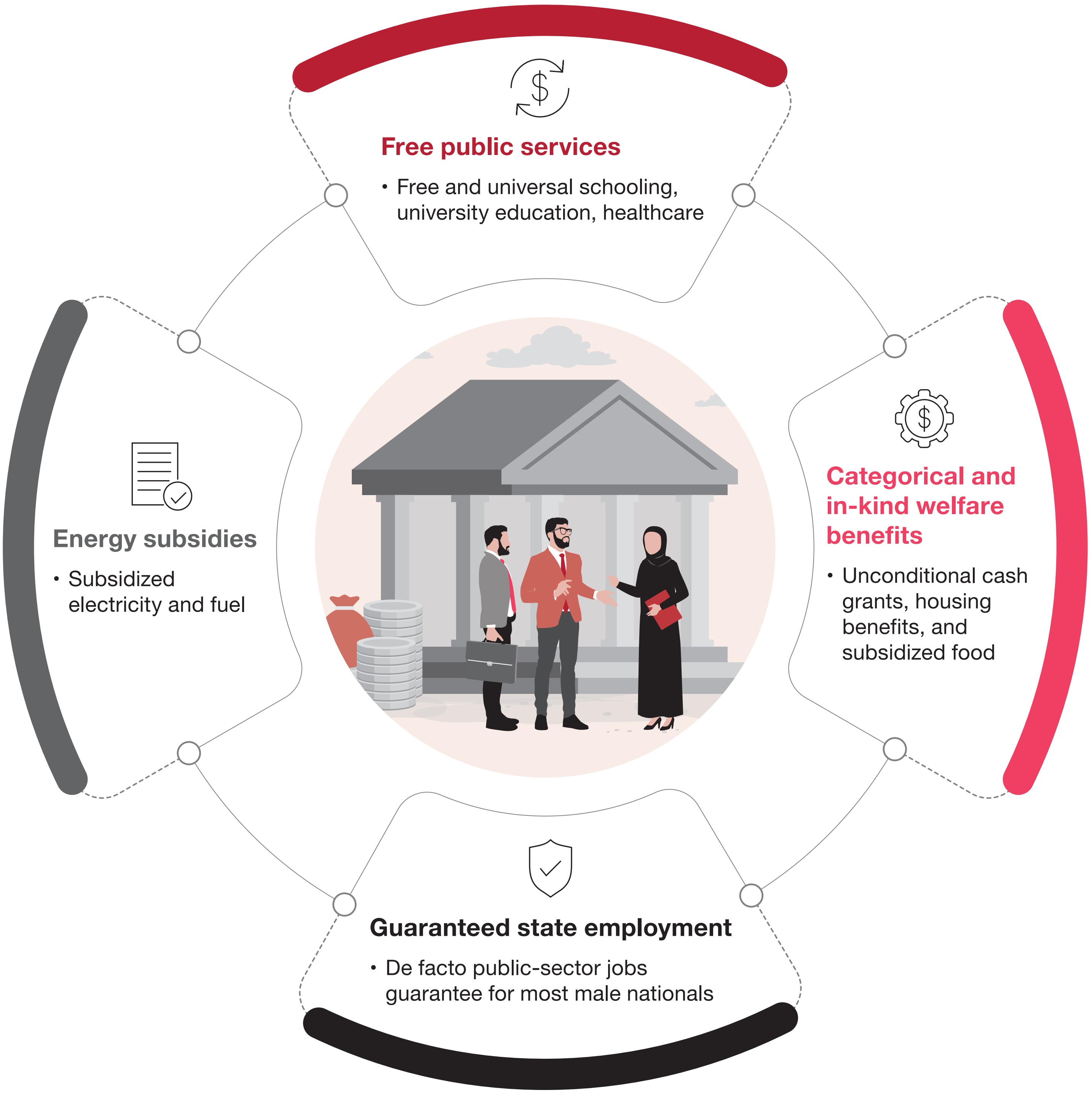
In addition to its fiscal burden, mass public employment has created administrative inefficiencies, making it harder to hold the bureaucracy accountable for performance. Mass public employment has also distorted labor market expectations. Nationals who work in the private sector sometimes expect unrealistically short working hours or expect the same level of job security they would possess in the public sector.

There has been some change on the public employment front, as new hiring has been much reduced during the last decade or so in several GCC countries. In Saudi Arabia, where public hiring has stalled and private employment has grown fast, the share of publicly employed citizens as a share of all employed citizens, although still over 50 percent, has dropped substantially since 2017.[10] However, this process has not been planned and integrated with general welfare modernization.

The shift to private-sector employment has resulted in a substantial group of low-income workers among nationals in some GCC countries. Their wages are higher than those of most of their expatriate competitors, but far below nationals' earnings in the public sector. The most common monthly wage bracket of Bahrainis newly entering the private labor market in 2021 was US$800 to US$925.[11] In Oman, 79,000 out of 267,000 Omanis employed in the private sector in 2021 earned between US$840 and US$1,040 per month.[12]

Compared with the implicit transfers built into traditional public employment, the volume of assistance provided to nationals working in the private sector is limited.[13] Benefits tend to be temporary, and they do little to bridge the gap with the wages and job conditions available in the public sector. The Nafis Program in the UAE is probably the most generous, but also competes with more lucrative public-sector packages.[14]

EXHIBIT 1
The established social contract



Source: Strategy&

Many young nationals are struggling to achieve the middle-class living standards that the social contract in the region has historically provided. When nationals are in private employment, they typically earn lower incomes than their peers in the public sector, work longer hours, and have less job security. Nationals on low private wages struggle to acquire property, marry, and start families, all of which affects their quality of life and social development.

Available to all nationals, the GCC countries provide domestic energy subsidies, another major component of the established social contract, which produce substantial opportunity costs and economic distortions.[15] Cheap fossil energy incentivizes inefficiency and overconsumption. It has negative environmental externalities. Overuse of subsidized energy at home means less oil will be available for export at global market prices, which deprives governments of fiscal revenues. Such subsidies are also inequitable because they tend to benefit richer households, which often consume more energy than poorer households.

GCC governments have lifted some energy prices during the last decade or so, and in some cases have replaced them with less distortive cash grants. Yet the incidence of energy subsidies remains high and the cost considerable.[16]

“Many young nationals are struggling to achieve the middle-class living standards that the social contract in the region has historically provided.

HOW TO CREATE A NEW SOCIAL CONTRACT

GCC governments possess the ingredients required for a new social contract. They have the fiscal resources, growing regulatory capacities, long-term economic planning capabilities, and desire to make the necessary economic adjustments.

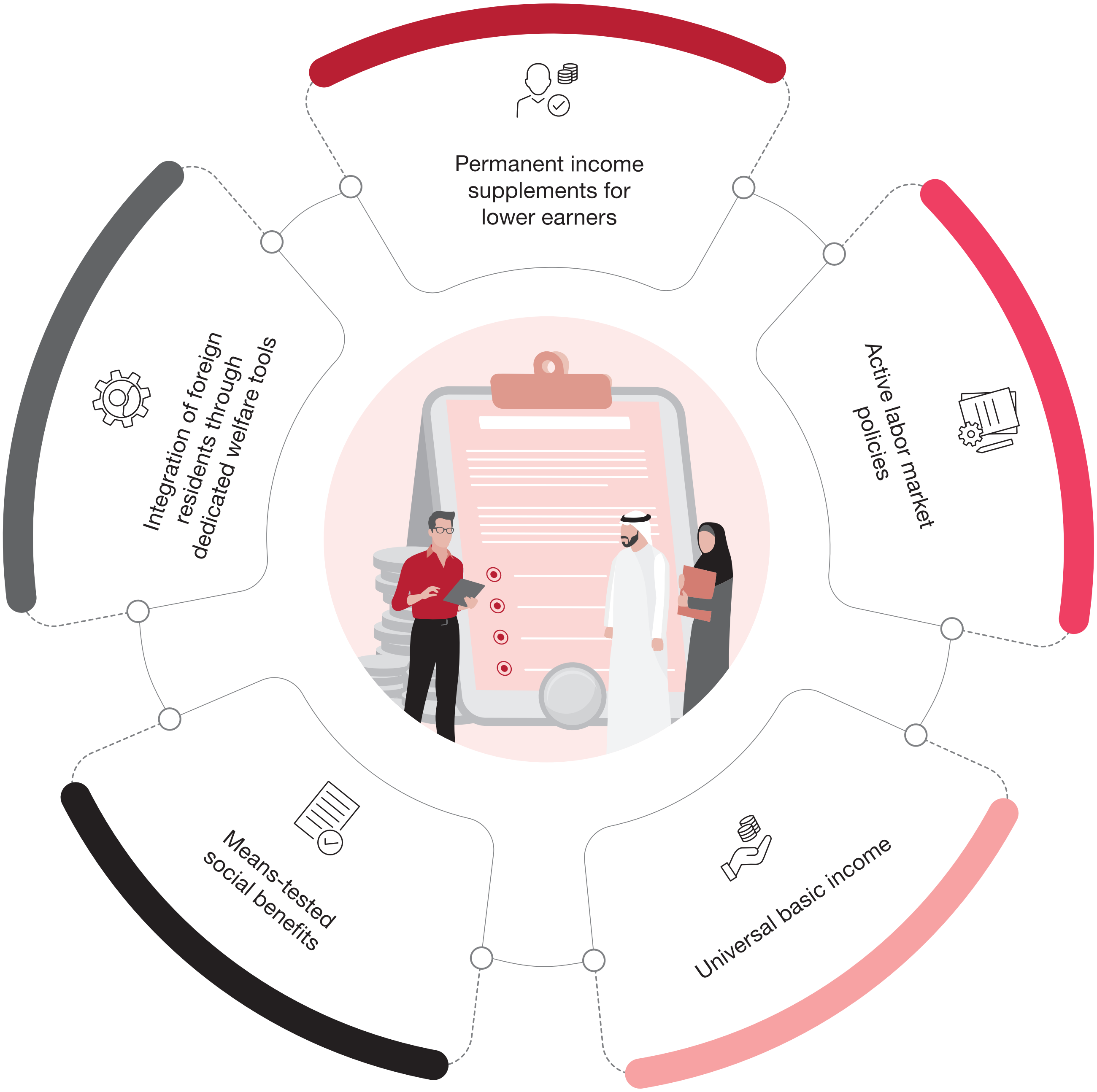
GCC countries can build on existing policy efforts to build this new social contract. Some are already moving toward comprehensive, activation-oriented welfare and income support systems.[17] Kuwait's permanent private-sector wage subsidies for nationals have increased the number of Kuwaitis in private employment and narrowed the wage gap with those in the public sector (although the support is not means-tested and repeat increases in public-sector wages have undercut their efficiency). Abu Dhabi's income top-up program for families guarantees an adequate standard of living.[18]

To succeed, however, GCC countries need to add some risk-taking, creativity, and lateral thinking to the mix. Elaborating a new social contract involves simultaneous fiscal reform, welfare modernization, and labor policy changes. Most of the solutions these countries adopt must be GCC-specific, as there are few international models that directly address the region's challenges.

The main objectives of a new social contract should be to integrate nationals into the private labor market and incentivize entrepreneurship, while maintaining acceptable standards of living and material security. Toward this end, government leaders should retain the basic principle of providing free education and healthcare, while modernizing other policies to make the social contract fairer, more inclusive, and more market-compatible. They can use the following policy tools (*see Exhibit 2*):

- Permanent income supplements for lower earners
- Active labor market policies
- Universal basic income (UBI)
- Means-tested social benefits
- Integration of foreign residents through dedicated welfare tools

EXHIBIT 2
The new social contract for GCC countries



Source: Strategy& analysis

Permanent income supplements for lower earners

Income support policies should go beyond the mostly time-limited wage subsidy schemes currently in existence. The challenge in GCC countries is that the large presence of low-wage expatriate workers exerts a strong and persistent downward pressure on wages in the low- to mid-skilled labor market segments. Long-term income support for low-earning citizens in the private sector can counteract this, preventing the emergence of working poor among GCC nationals.

Income support policies would increase take-home incomes and allow GCC nationals to compete effectively with expatriates in all but the lowest-skilled professions. Although skills improvement policies can help nationals earn more money, there will always be some nationals who are unable to join highly skilled occupations, and who therefore are exposed to expatriate competition.

The specific design of income support policies depends on national circumstances, including consideration of fiscal constraints, what constitutes a living wage for citizens, and the relative wage gaps between nationals and foreign workers. However, the general design principle should be to supplement, on a sliding scale, any wage below a certain level. The gradient of the scale would determine the rate at which low-earning individuals lose supplementary payments when their wages increase. Generally, this taxing away of benefits should not be too steep, to avoid dissuading nationals from seeking better jobs with higher pay.

Successful international models are available for such support, including the Earned Income Tax Credit in the U.S. and the Workfare Income Supplement in Singapore.[19] These are negative taxes in which government grants top up wages that are below a certain threshold. They are market-conforming and avoid discouraging work, as can happen with many conventional welfare benefits. Instead, these models incentivize work: As take-home incomes in the private sector increase, more nationals will seek jobs there. Critically, negative taxes also reduce wage inequality among nationals by narrowing the gap between public and private employment, as well as between high-paid and low-paid work.

The availability of income support could make private employment attractive to at least lower-earning workers in the public sector, potentially streamlining large government bureaucracies. Public-sector workers moving into private employment would both liberate additional labor for productive use in the private sector and create fiscal savings.

Buttressing a new social contract with income supplement policies also could justify, and support, broader civil service reforms. Recruitment and promotion could become increasingly selective and purely merit-based, leading to a leaner, more capable, more responsive, and more coherent state apparatus. Thus, as public employment and wealth sharing become progressively disconnected, the performance of public-sector workers could improve due to stronger performance incentives and penalties for weak performance.

Income supplements in action

Implementing income support would cost money. Nevertheless, the burden of even a generous system would be modest compared with the current expense of public-sector overemployment. In Saudi Arabia, for example, we estimate that a relatively generous income supplement policy would benefit close to 1.9 million of the 2.3 million Saudi nationals currently in private employment at an annual cost of SAR57 billion (US$15.2 billion). In 2023 terms, that would have constituted less than 5 percent of total state spending and barely over 10 percent of public-sector salary spending.[20]

Under this plan, Saudis earning below SAR10,000 (US$2,666) per month in the private sector would receive a supplement of SAR0.5 (US$0.13) for each SAR1 (US$0.26) of market wage income below that threshold. The maximum supplement would be SAR3,000 (US$800). So, if Fulan were making SAR6,000 (US$1,597) per month, he would receive a supplement of SAR2,000 (US$533), which is half of the wage gap below the SAR10,000 (US$2,666) per month set for nationals in the private sector. The full supplement would be paid to nationals with a wage of SAR4,000 (US$1,066), which is the minimum qualifying wage to be considered fully employed under the Nitaqat (Saudization) quota system—the current de facto minimum wage, because very few Saudis in full-time employment earn less. Such a plan would guarantee a minimum take-home income of at least SAR7,000 (US$1,866) for the vast majority of privately employed Saudis (*see Exhibit 3*).[21] This automatic support system would differ from existing Human Resources Development Fund wage subsidy systems, which require substantial administrative paperwork and, critically, are time-limited. Time-limited support systems are insufficient to address low-income levels in low- to mid-skilled professions, which are a permanent, structural feature of GCC labor markets.

EXHIBIT 3

How an in-work wage support system works

Solid line: Income with support

Dotted line: Income without support

Source: Strategy&

> Income support policies would increase take-home incomes and allow GCC nationals to compete effectively with expatriates in all but the lowest-skilled professions.

How to pay for income supplements

GCC countries could easily finance a general income supplement system through reforms to their wealth distribution systems. One avenue could be public employment reform, including "golden handshake" options for incumbent civil servants.

Bahrain, for example, has already created a voluntary retirement plan for state workers, introduced in the US$10 billion budget support agreement with its GCC neighbors in 2018.[22] Cutting the public payroll in Bahrain by 10 percent through gradual attrition and incentivized exits could free US$370 million in spending per year. This corresponds to a potential income supplement of approximately US$3,700 for each of its 100,000 privately employed nationals—and higher supplements for lower-earning Bahrainis if the support were means-tested.

Another method of financing income support programs could be the continued reduction, or removal, of remaining energy subsidies, which are regressive and inefficient means of wealth sharing. For example, Bahrain could alternatively finance the income support system proposed above in its entirety by eliminating the household electricity subsidy, saving around US$370 million.

Income support for lower-earning GCC nationals also could come from new or increased fees for employing expatriate workers. Saudi Arabia already levies such fees, although they flow into the general budget. These fees offer the additional benefit of narrowing the employment cost gap between nationals and foreigners, thereby incentivizing firms to hire nationals, a declared policy aim across GCC countries.

Such fees on expatriates will be particularly effective if they target occupations or skill levels in which it is relatively easy to substitute nationals for expatriates and the existing wage gap is small. A fee-based policy can complement, and eventually replace, nationalization quotas, which have increased the employment of nationals in the private sector, but also have spawned market distortions, high costs, and tactics to evade the regulations such as "phantom" employment of nationals.[23]

Governments should accompany expatriate fees with the simultaneous creation of a minimum wage for expatriates. This minimum wage will ensure that employers do not recoup the cost of the fees by lowering wages, which would reduce expatriates' welfare and defeat efforts to narrow the wage gap with nationals (*see "Integration of foreign residents through dedicated welfare tools," page 18*).

Similarly, it is important to enforce minimum wages for nationals. Governments should ensure that workers, not employers, receive the direct benefit of pay supplements at the lower end of the income spectrum. The situation in the wage bands above the minimum wage for nationals would be different: For higher wages, employers would enjoy an indirect benefit from the supplement in the form of moderated wage demands by nationals. That is because nationals receiving income support would typically lower their wage demands somewhat given their higher income from benefits. These more moderate wage claims would make the fees on expatriates more acceptable to employers and, by leveling the playing field, provide an incentive to hire nationals.

Administrative enforcement

An important aspect of income supplements and fees is administrative enforcement. Governments across the region already have many of the administrative enablers in place to deploy new, means-tested income support systems. E-government capabilities are advanced and have functioned well for Saudi Arabia's Citizen Account Program. Governments have also begun digitizing labor contracts and monitoring wage payments on a monthly basis, reducing fraud.

Big data analytics that draw on linked employer, worker, and household data can minimize welfare misuse. Such data analysis, which should be undertaken under strict data privacy standards, enables comprehensive fraud monitoring and sanctioning systems. It requires the expansion of existing databases used for means-testing to include both individual- and household-level assets and non-work income streams. Governments need household-level data if they are to adjust wage supplement systems to consider household income and reduce support for individuals in high-income families. Data analysis also allows governments to pinpoint suspicious patterns, which would reduce the incidence of "phantom" employment of nationals and spot consumption and asset ownership levels that exceed officially declared incomes.

Active labor market policies

GCC governments can increase their investment in active labor market policies to increase citizens' integration in the private sector. These policies include lifelong learning arrangements, job advice and matching services, and support for training in the private sector. Such policies complement income support as they improve the quality of employment outcomes for nationals, providing particular benefit to the less privileged. International experience shows that wage supplements are most effective when combined with other labor market programs, such as on-the-job training, counseling, information sessions, and employment search assistance.[24]

GCC governments should invest in monitoring and evaluation tools to assess the impact of their current labor market activation policies, and identify how they can adjust them to produce more effective outcomes. Many activation programs already exist across the GCC, such as Nafis in the UAE, and the Tamheer (on-the-job training) and Doroob (e-training) programs in Saudi Arabia.[25] However, government investment in these programs is comparatively limited, their quality can be uneven, and their impact has not been studied systematically. Further, governments should update these policies in close collaboration with private-sector stakeholders, which are discovering the benefits of adjusting their training and employment strategies to the needs and capabilities of the growing national workforce. Experience with advanced active labor market policies in OECD countries demonstrates that high-quality programs require considerable fiscal investment and ongoing impact evaluation.

Further reforms of the general education system, particularly at the primary and secondary levels, can integrate citizens productively into the private labor market. Important changes are already happening in this realm, such as the shift toward science, technology, engineering, and mathematics (STEM) subjects in higher education. However, more needs to be done. In particular, there should be more selective recruitment and better incentivization of teachers—a complex subject, because teaching has guaranteed public employment, which has benefited women in particular. Governments will find it easier to implement education reforms when they extend the modern HR practices and golden handshakes needed in the public sector, as suggested above, to the education system. These changes can help governments strengthen accountability on the part of schools and teachers, and increase transparency in the reporting of educational outcomes.

How a universal basic income could work in Kuwait

A UBI could work in Kuwait by redirecting current energy subsidies into monthly grants for nationals.[26] Suppressing energy subsidies would create enough savings to pay every adult national outside the public sector a monthly grant of about US$700, with a supplement paid for every child of around US$230. Existing public-sector employees could receive a grant of US$195 to include them in the new system and compensate them for somewhat higher energy costs.

The reform would be strongly progressive. All major income categories of Kuwaiti households would be net beneficiaries, with poorer households gaining significantly more, given their lesser use of current energy subsidies. A UBI in Kuwait also would narrow the income gap between the public and private sectors.

Cash grants could be significantly higher than suggested if the government cofinanced them from savings generated by the gradual attrition of Kuwaiti public employment. The government could socially justify less public employment with the UBI as a new basis for the Kuwaiti social contract. A 10 percent reduction of the public payroll could finance an increase of about US$650 per month in UBI payments to adults outside government. Kuwaitis could decide to leave government employment to receive the UBI, thereby generating further savings for the government.

Universal basic income (UBI)

GCC countries should consider adding UBI to their new social contract. It would, in effect, serve as an unconditional, fixed dividend generated by a country's hydrocarbon and investment revenues. Although UBI has generated much debate in advanced economies, in the context of the GCC countries it would be less economically distortive than much of the current wealth sharing.

A UBI would provide all adult nationals with basic income security, while retaining sufficient incentives to earn supplementary income in the private sector (*see "How a universal basic income could work in Kuwait"*). Governments would pay UBI to all adult nationals monthly, with a possible top-up for those with children. As part of its public-sector reform, a government could either exclude public-sector employees or pay them a reduced amount.

Reforms that eliminate, or reduce, the least effective and most costly elements of the established social contract, including energy subsidies and excess public employment, could easily finance a UBI system. Indeed, the cost of a UBI per individual would be drastically lower than the direct expenses (salaries) and indirect expenses (non-wage and infrastructure) of public employment. Moreover, a UBI in GCC countries would have none of the problems that bedevil such proposals in OECD countries: It would neither require new taxes nor create work disincentives compared with the status quo (because excess public employment already creates worse economic distortions).

A UBI is a serious option, especially for Kuwait, Qatar, and the UAE, which have looser fiscal constraints and more generous legacy social contracts to accommodate than other GCC countries. It could be financed out of savings and new income sources, similar to the suggestions above for wage supplements.

An important effect of a UBI would be to provide nationals with stronger incentives to seek skills relevant to the private sector. The unconditional nature of a UBI means that recipients would not lose it as their private incomes rise, thereby avoiding the work disincentives that can occur with conventional means-tested welfare programs. Indeed, the security of a UBI would encourage nationals to take entrepreneurial risks and exploit their talents.

A further advantage of a UBI is the quid pro quo it would offer nationals in exchange for reductions in public-sector hiring and energy subsidies, thereby making such adjustments more palatable. It would powerfully change expectations in countries in which there are deeply ingrained claims to the benefits of the established social contract.

UBI and wage supplements are not mutually exclusive. Governments can combine them. Such a mixed system could provide a modest UBI to all nationals, while some nationals would also be eligible for wage supplements for private employment. Pairing UBI and wage support would ensure basic income security while also guaranteeing improved material rewards for private-sector activity. Each country could adapt the details to its own needs when determining the ratio of the two payments, their size, and the treatment of incumbent public-sector workers and employees in partially or wholly state-owned companies.

Means-tested social benefits

Governments can reform benefits through means-testing or by replacing them with administratively unified cash benefits. Saudi Arabia's Citizen Account Program, for example, provides household cash grants instead of inefficient energy subsidies.

Governments should combine such means-testing with the systematic labor market activation policies discussed above (*see "Active labor market policies," page 14*). The combination can reduce the risk of welfare dependency and increase the integration of nationals into the private sector.[27] Similarly, GCC governments can introduce a general, means-tested, non-contributory state pension. Such a pension would minimize the risk of old-age poverty for nationals who have been unable to contribute to formal pension systems.

A key result of overall benefit reforms should be a minimum income guarantee that also extends to non-working nationals, of the type that many advanced economies have already introduced. The minimum income should be sufficient to avoid poverty, but not so generous as to reduce work incentives (which wage supplements would strengthen). A UBI could be part of such a guarantee.

Integration of foreign residents through dedicated welfare tools

Governments should ensure that reforms to the social contract do not inadvertently make expatriates worse off. Foreign residents in GCC countries are not part of the established social contract. They cannot have the same social entitlement as nationals unless they become permanent residents or naturalize themselves. Nonetheless, they are an important element of GCC economies and societies. They can be materially vulnerable, especially workers at the lower end of the private-sector wage spectrum.

GCC governments should consider introducing a modest minimum wage for foreigners to prevent employers from passing on foreign labor fees by cutting wages at the bottom of the market. Such minimum wages, where already implemented, have had no serious effect on firm profitability or competitiveness.[28] Governments could also adjust any minimum wage if, for instance, energy subsidy reforms—a key component of wider social contract changes—increased the cost of living for expatriates.

GCC governments also should continue to modernize the limited welfare arrangements for expatriates, as the UAE has already done. Such changes might include the provision of independently regulated pension arrangements beyond the customary employer-provided “end of service” benefits. These can be difficult to claim in practice and can disappear when employers go bankrupt. Governments should also address the limited ability of expatriates to change jobs (which can lead to employers’ preference for them over nationals) by further relaxing “sponsorship” rules and facilitating labor market services such as job platforms and matching services. Further, they should consider providing unemployment insurance for longer-term foreign residents.

Guaranteeing expatriate welfare in the labor market also benefits nationals because the ability to exploit foreign workers undermines the employment chances of nationals in the private sector. Additionally, it would improve productivity because workers with better labor and social rights tend to be more productive. Indeed, there is a strong argument that GCC countries can attract high-potential individuals only if they have a reputation for fair treatment and good opportunities for foreign workers.

CONCLUSION

The GCC countries have already achieved a measure of welfare reform. The next step is to build on these achievements to create a new social contract that provides for the equitable well-being and labor market inclusion of nationals in a sustainable and productive manner. A new generation of nationals would benefit from a simplified, more transparent, and more market-conforming welfare system. Under such a system, they would receive stronger incentives to enter the private sector while also enjoying welfare guarantees and improved opportunities for a middle-class income.

GCC countries can achieve an attractive, inclusive, and productive new social contract because they enjoy a unique endowment. They have considerable fiscal resources for welfare and employment policies, an ability to plan for the long term, and a young citizen population increasingly willing to engage in private economic activity. The challenge is to use this endowment in a fiscally sustainable way to ensure basic welfare for all nationals and maximize productive economic opportunities for all.

ENDNOTES

1. The GCC countries are Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

2. Categorical benefits are benefits that are not means-tested but are provided on the basis of recipients' general social status (students, orphans, widows, elderly, etc.).

3. The difference in average income between public-sector and private-sector employees is likely closer to SAR5,000 (US$1,333) per month because the private-sector average is skewed upward by a relatively small group of top executive salaries.

4. The International Monetary Fund estimated the value of per capita energy subsidies in 2022 in Saudi Arabia at US$3,600. The subsidy received by citizens in effect is likely somewhat lower because the full range of subsidies includes the gas, electricity, and diesel subsidies received by agriculture and industry.

5. Citizen Account Program website (https://tinyurl.com/mpexctkd).

6. Wage data from the General Organization for Social Insurance, Saudi Arabia, Q3, 2023.

7. Steffen Hertog, "Backgrounder: The Old GCC Social Contract," October 2024 (https://tinyurl.com/bdhs7jjp).

8. In 2023, wage spending in Saudi Arabia dropped to 42% of overall spending, largely a reflection of non-wage spending on Vision 2030 projects.

9. N. Tamirisa and C. Duenwald, "Public Wage Bills in the Middle East and Central Asia," IMF, January 9, 2018 (https://tinyurl.com/2yc4me6r).

10. Annual absolute figures are not available on a consistent basis for Saudi Arabia.

11. Data from Bahrain's Labor Market Regulatory Authority.

12. "Statistical Yearbook, 2022," Sultanate of Oman National Centre for Statistics and Information, Table 11-4 (https://tinyurl.com/5mvpxjcu).

13. "The Jobs Agenda for the Gulf Cooperation Council Countries," World Bank Group, 2018 (https://tinyurl.com/mwzhd2r9).

14. See https://nafis.gov.ae/.

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16. Steffen Hertog, “Backgrounder: The Old GCC Social Contract,” October 2024 (https://tinyurl.com/bdhs7jjp).

17. Sami Zaki, Rasha Salem, and Nour Oueidat, “A New Social Welfare Model: Encouraging Economic Participation,” Strategy&, 2024 (https://www.strategyand.pwc.com/m1/en/strategic-foresight/sector-strategies/public-sector-management/social-welfare-model.html).

18. Steffen Hertog, “Reforming Wealth Distribution in Kuwait: Estimating Costs and Impacts,” LSE Middle East Centre Kuwait Programme Paper Series, July 5, 2020 (https://tinyurl.com/m3e84p7u).

19. Earned Income Tax Credit, U.S. (https://tinyurl.com/mwwzbzv5); “Boost Your Savings with Workfare Income Supplement,” Central Provident Fund Board, Singapore (https://tinyurl.com/3mhpsdb6).

20. Due to the positive labor supply reaction that such a policy would generate, the actual number of beneficiaries would likely be somewhat larger.

21. The proposed system would be fundamentally different from the open-ended “da’m al-‘amala” wage supplement system available for privately employed Kuwaitis, which is not means-tested and is regressive in that nationals with higher formal qualifications receive larger grants.

22. Fiscal Balance web page, Kingdom of Bahrain Ministry of Finance and National Economy (https://tinyurl.com/37f7j7er); “Bahrain Agrees USD 10 Billion Financial Support Agreement with Saudi Arabia, UAE and Kuwait,” Bahrain News Agency, October 4, 2018 (https://tinyurl.com/pt9m9pt3).

23. Steffen Hertog, “Arab Gulf States: An Assessment of Nationalisation Policies,” GLMM Research Paper, January 2014 (https://tinyurl.com/6x53cx3e). Phantom employment is when employers put nationals on their payroll to meet nationalization requirements, but do not ask these nationals to actually work.

24. I. Walker, D.A. Robalino, and H. Ribe, “From Right to Reality: Incentives, Labor Markets, and the Challenge of Universal Social Protection in Latin America and the Caribbean,” Washington, D.C.: World Bank, 2021, p. 281.

25. For example, “Electronic Training (Doroob)” webpage, Human Resources Development Fund, Saudi Arabia (https://tinyurl.com/2knvymby).

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27. Sami Zaki, Rasha Salem, and Nour Oueidat, “A New Social Welfare Model: Encouraging Economic Participation,” Strategy&, 2024 (https://www.strategyand.pwc.com/m1/en/strategic-foresight/sector-strategies/public-sector-management/social-welfare-model.html).

28. Arindrajit Dube, “Impacts of Minimum Wages: Review of the International Evidence,” HM Treasury, November 2019 (https://tinyurl.com/4k8j37xb).

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