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RETHINKING ECONOMIC GROWTH: Towards Productive and Inclusive Arab Societies

EXECUTIVE SUMMARY



Highlights

- The underlying causes for the Arab spring include a **skewed development model** and an **unravelling social contract** in which Arab citizens traded political freedoms for public sector jobs, public services, various subsidies (e.g. for food and energy), low taxes and state handouts.
- The 1990s were marked by a slew of **pro-market reforms** in Arab states. The aim was to tackle stagnant or declining per capita GDP, increasing fiscal burdens, slow productivity growth and low competitiveness.
- **Structural adjustment** aimed to tackle debt and inflation, and growth rates averaged 5 per cent between 2000 and 2010 (which was high by regional standards but low compared to other world regions).
- However the **private sector** failed to produce enough gains that trickled down to the broader economy. Arab states continued to lack sound trade, financial and foreign investment policies and sufficiently developed capital markets and accompanying institutional reforms. The private sector remained significantly constrained.
- **Privatization** was conducted without regard for the income concentration outcomes of handing over public goods to private operators.
- **Government spending was inefficient:** largely devoted to untargeted subsidies and ill-designed public services and social protection while failing to adequately support the domestic economy, including manufacturing and other value-adding industries.
- **Job creation** was concentrated in low productivity sectors and the expanding informal economy. Workers were increasingly educated but most new jobs were low skilled – and the region became a major exporter of skilled workers.
- Though employment increased and poverty was reduced in many cases, the share of consumption as well as the wage share of the national income declined significantly.
- **Social protection** deficits widened in light of a shrinking public sector, reduced access to its accompanying welfare benefits, and expenditure cuts targeting subsidies.
- The Arab region combined the lowest per capita income growth with the **lowest rates of voice and accountability**. This meant that citizens had no say in policymaking. Governments remained oblivious to the social impact of economic reforms and demands for accountable systems of governance.
- The ongoing Arab transitions underscore that trade off between economic and political rights was a false one – political and economic reforms must go hand in hand.
- Economic growth should be balanced, creating quality jobs and social services to guarantee the dignity of working women and men. These processes will only be sustainable if they are participatory and inclusive, i.e. developed through effective dialogue between workers, employers and governments.



Chapter 1

Output & Employment Growth

Over the past two decades, on a per capita basis, the increase in Arab incomes has been among the lowest in the world while the quality of governance has deteriorated over time. The Arab region also continues to have the lowest rates of citizen voice and government accountability globally. Economic policies, combined with poor structures of democratic and economic governance, have led to distorted economic incentives and patterns of structural transformation that are resistant to decent employment creation.

Figure 1.11: Income growth and voice and accountability have been low in the Arab states

Per capita income growth 2000-2010 (%) versus index of voice and accountability



Sources: The Worldwide Governance Indicators Database; IMF World Economic Outlook Database (WEO).

Slow growth but fast employment creation

After the so-called “lost decade” of the 1980s, which witnessed a recession caused by tumbling oil prices, the rate of economic growth in the region averaged 3.5 per cent per annum and surpassed 4.5 per cent in the decade leading up to the Arab Spring. **While unprecedented for the region, these growth rates remained the lowest of all world regions with the exception of Latin America.**

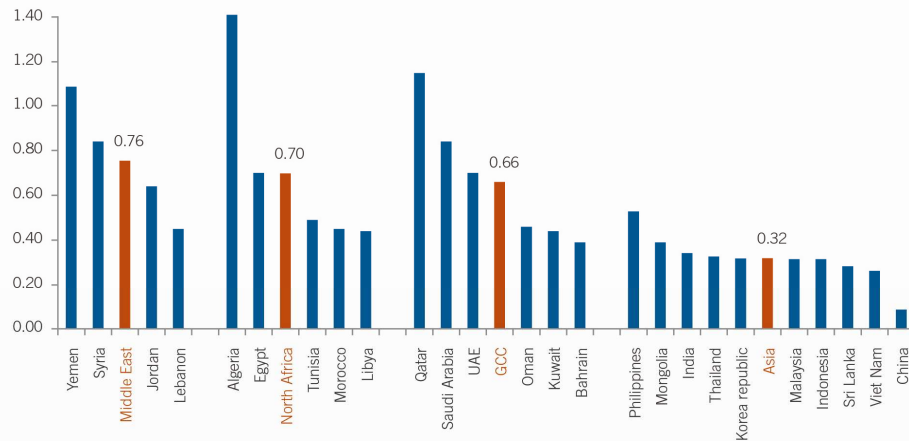
Productivity growth has also lagged behind. **Between 2000 and 2010, the Arab region had the lowest productivity growth of any region except Latin America.** North Africa achieved slightly higher productivity growth than the Middle East, with the respective annual rates being 1.5 per cent and 1.2 per



cent, against a world average of nearly 2 per cent. On the other hand, **employment growth was substantial**. The ratio of the percentage change in employment to the percentage change in output (employment/output elasticity) averaged nearly 0.7 between 2000 and 2010, which is more than double the expected rates during a typical course of economic development.

Figure 1.3: The employment response to output growth was significant

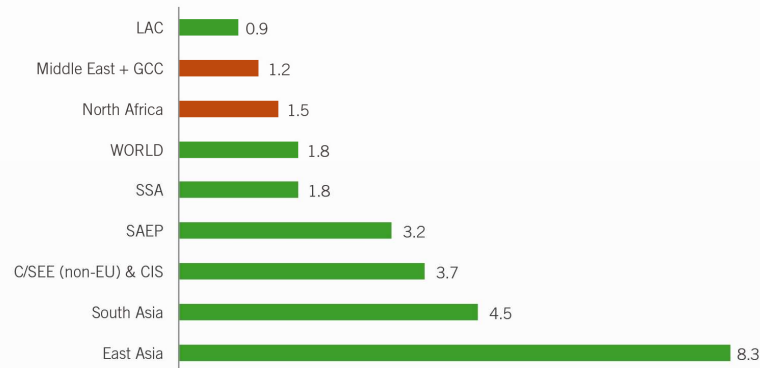
Employment/Output Elasticity, 2000 - 2010



Source: ILO (2010a).

Figure 1.4: Productivity gains have been small in the Arab region

Average annual productivity growth (%), 2000 - 2010



Source: ILO (2010a).

Sectoral changes in employment

Agriculture's employment share has declined by an average 20 per cent in the last twenty years. That said, in North Africa, agriculture continues to employ 30 per cent of workers, compared to 22 per cent in the Middle East.

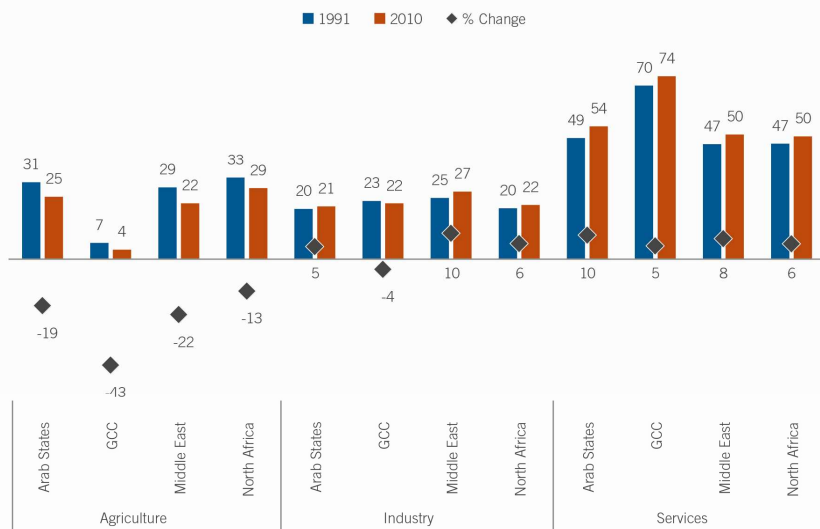
The combined share of employment in the mining, manufacturing and utilities sectors has increased in the Middle East by 10 per cent and North

Africa by 6 per cent, but stayed relatively constant in the GCC (a decline of only 4 per cent).

Most employment gains have been in the service sector, with a 10 per cent increase in the employment share of services in the last twenty years. That said, the public sector still accounts for a large portion of formal employment in the region.

Figure 1.7: Most employment gains were in the services sector

Employment shares and their changes by sector, 1991 - 2010



Notes: (1) The world average shares for employment in industry and services are 22 and 43 per cent respectively; (2) A decline in sector share does not mean that employment in that sector declined. For example, in the last 20 years in MENA, employment in agriculture increased by 9 million, in industry by just over 14 million and in services by 33 million.
Sources: ILO (2011b and 2012).

Private sector: still constrained after the reforms

Despite efforts to make the private sector more effective, the Arab region remains among the least competitive globally. Reforms mostly failed to provide **equality of opportunity in market and employment transitions** or in terms of **access to markets, resources and an unbiased regulatory environment** for business and individuals. **Investment rates remained low** and the **formal private sector remained under the control of a few firms.**

Chapter 2

Population, Labour Supply, Employment & Unemployment

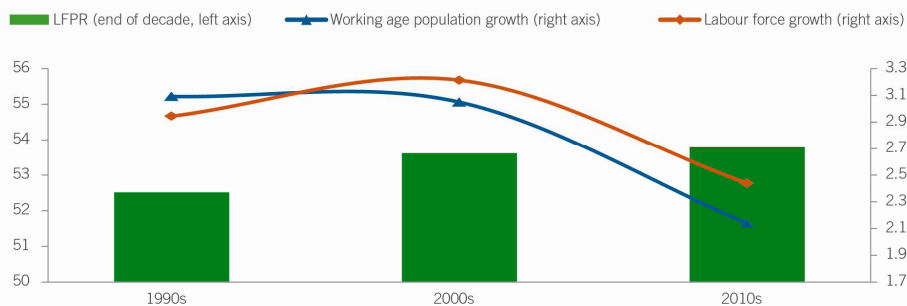
There has been a sharp decline in regional fertility rates and a corresponding decline in the share of youth in the population and, consequently, in the labour market. In terms of the labour force, three characteristics are shared across the region: (1) low labour force participation rates (primarily due to the low labour force participation rates of women); (2) highest unemployment rate worldwide, including for youth (and especially women); and (3) striking gender differences.

Population and labour force growth in decline

The **total population in the Arab states increased by 53 per cent** between 1991 and 2010 from 224 million to 343 million (or annually by 2.2 per cent). Children aged 0 to 14 constituted 43 per cent of the total population in 1991 but contributed only 16 per cent to total population growth, their numbers growing by less than 1 per cent per annum.

Figure 2.1: Population and labour force pressures have declined in the last 20 years

Labour force trends, 1990s - 2010s



Note: LFPR corresponds to country average

Sources: ILO LABORSTA and Key Indicators of the Labour Market (KILM) Databases.

Male employment grew by 89 per cent and female employment by 126 per cent. The number of employed as a share of the total population went from 19.4 per cent to almost 25 per cent, and the ratio of female/male employment from one-in-five to one-in-four.

Male and female youth employment increased at similar annual rates but their combined share of the population fell from 5.2 to 4.7, partly aided by increased enrolment in schools and universities.

The numbers of male (female) youth in school increased by 77 per cent (116 per cent) or annually by 2.9 per cent (and 3.9 per cent).



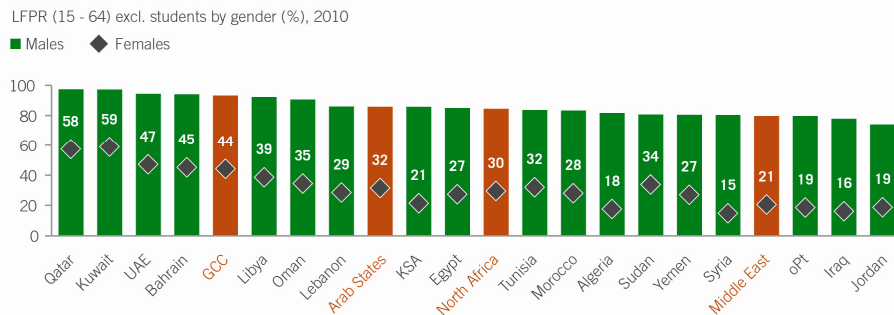
The share of male youth “not in school, not in the labour force” in the total population was 0.3 per cent both in 1991 and 2010; the share of young women of the same category declined from 4.5 per cent to 3.4 per cent.

The regional unemployment rate declined mainly due to a decline in North Africa (by nearly 30 per cent between 1990 and 2010). It remained almost constant in the Middle East but the **youth-to-adult unemployment rate declined by almost 25 per cent in both sub-regions.**

Labour force participation rates low – mainly for women

Despite increases, female labour market participation is still relatively low and continues to drive up the overall unemployment rate. **Labour force participation rates for Arab men are more or less on par with the world average, but only one in four Arab women is in the labour force (26 per cent) compared to a world average of 51 per cent.** At 38 per cent, women tend to be most active in the GCC – but only 31 per cent of those women are nationals. The female labour force participation rate for North Africa is 27 per cent, and 19 per cent for the Middle East. **Women in the region maintain the lowest labour participation rates globally even after the exclusion of students from the working age population.**

Figure 2.5: Arab region has low labour force participation rates mainly as a result of low female participation rates



Sources: ILO Key Indicators of the Labour Market (KILM) and UNESCO Institute of Statistics (UIS) Databases.

High unemployment rates, especially for women

The Arab male unemployment rate is high but not exceptional compared to other parts of the world (11.7 per cent in the Middle East, 7.4 per cent in North Africa and 3.1 in the GCC).

As a region, youth unemployment is the highest globally at 23.2 per cent, compared to a world average of 13.9 per cent, and varies significantly within sub-regions. The **Arab female youth unemployment rate is the highest in the world** (37 per cent regionally, 48 per cent Middle East, and 34 per cent for North Africa and also the GCC).

However, the number of unemployed male youth in the region exceeds the number of unemployed female youth: There are **nearly 150 unemployed male youth for every 100 unemployed female youth**.

Unemployment in the Arab region **impacts jobseekers from across the whole income range**.

Figure 2.8: In most Arab countries unemployment decreased



Chapter 3: Quality of Jobs & Living Standards

The rate of economic growth (measured in terms of GDP) has been relatively high in the region over the past decade, and has been accompanied by an increase in employment. But the rate of increase of total output growth (around 4 per cent annually), translated into only half that increase in *per capita* incomes due to concurrent population growth. At the same time, the **wage share of GDP declined drastically** by one-fifth in the Middle East and one-third in North Africa. **Household consumption's share of GDP across the region fell by 9 percentage points** – a significant decline in comparison to other world regions, especially since Arab growth has lagged behind the rest of the world. This suggests that only a small part of the apparently substantial GDP increase was transferred to workers and their households. This explains the modest decline in poverty rates in the region. In parallel, progress in social development was lagging behind economic growth, an indication that public expenditure was falling short of needs and expectations.

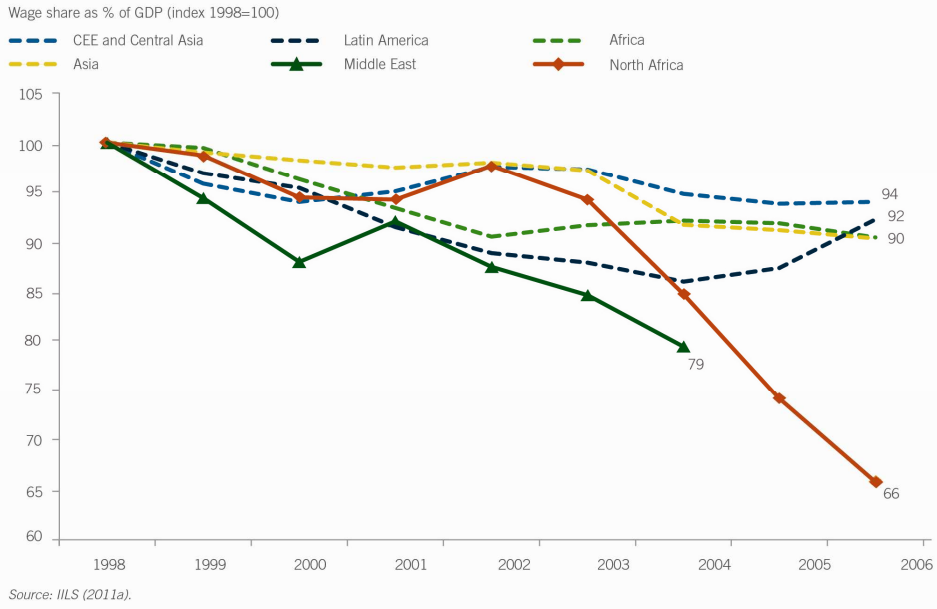
Working poor, vulnerable employment reduced but share of wages to GDP declined faster

The share of working poor has declined in the Arab region. The Middle East and North Africa sub-regions experienced significant declines in the share of working poor, averaging 20 per cent. The share of working poor stood at 35 per cent of total employment in 1991 for each of the Middle East and North Africa. By 2011, the share of working poor had declined by one third in the Middle East and by one fifth in North Africa. In the GCC states, the share of working poor is reported to be practically zero.

The share of Arab workers in vulnerable employment has declined by 20 per cent. This decline was second only to that in East Asia. However, **the share of women in vulnerable employment compared to the share of men in vulnerable employment in the region is the highest in the world and has increased in the last 20 years.**



Figure 3.2: The share of wages in GDP declined faster in the Arab region than in other regions



Chapter 4

Education & Skills

There is evidence of an oversupply of educated jobseekers in the Arab labour market: (1) in many regional economies, the unemployment rates of educated youth are as high as, or even higher than, those of the less educated; (2) wages of educated workers are not much higher than less educated workers; (3) the Arab region has one of the highest rates of educated and skilled emigration worldwide.

The supply of education: educated and jobless

Most Arab countries have achieved universal or near universal primary enrolment since the 1970s. At the **secondary school level, the gross enrolment rate has risen** from just over 20 per cent to nearly 70 per cent (from 4 million to 30 million students). The youth literacy rate is now 92 per cent in North Africa and 99 per cent in the Middle East and the Gulf Cooperation Council.

Female education has almost caught up with male education. From a ratio of female/male enrolments of 40-50 per cent at all levels of education in the 1960s, female-to-male enrolments have now almost reached parity at primary and secondary levels with a few exceptions, such as Morocco and Yemen.

In many countries there are more females than male university students, the ratio being as high as 7:3 in some GCC countries. Today, the total student population is almost 80 million. **One in every four Arabs is in school.** Despite impressive gains in education, Arab students fare poorly in international league tables, particularly in countries where public employment is more or less guaranteed by the state.



Table 4.1: Student learning is below average in Arab countries

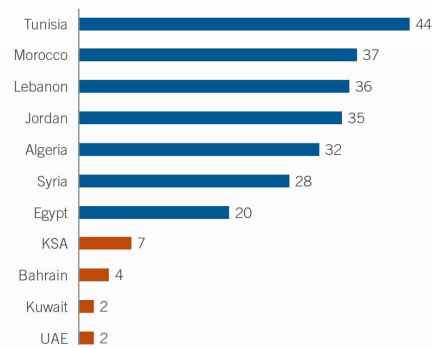
Student achievement in mathematics and science – international country rankings

RANK	COUNTRY	SCORE
1	Chinese Taipei (1st)	598
	International Average	451
28	Lebanon	449
31	Jordan	427
32	Tunisia	420
37	Syria	395
38	Egypt	391
42	Oman	372
45	Kuwait	354
47	Saudi Arabia	329
49	Qatar (Last)	307

Note: Based on TIMSS (2007) results
Source: Gonzales et al (2008).

Figure 4.1: Educational achievement is lowest when there are no incentives to emigrate

% of youth who desire to emigrate permanently



Source: Silatech (2010).

Demand for skills: at what wage and for what jobs?

The problem has less to do with a “skills shortage” and more with the lack of demand for better educated and more skilled workers. Arab employers are the least likely worldwide to offer training and are more concerned with issues of macro instability, corruption, taxes, financing and access to finance than with skills shortages. Employer perceptions about the education quality of the workforce differ between oil-rich and oil-poor Arab economies. Oil-based economies provide few educational incentives for jobseekers given the importance of nationality for obtaining employment. In non-oil based economies, education is critical for jobseekers to find a job locally or to emigrate and, therefore, students have relatively higher rates of educational achievement. **The Arab region has one of the highest skilled emigration rates worldwide.**

Chapter 5

Social Protection

Social security coverage in the region remains inadequate and untargeted.

Most social insurance systems cater to public and formal private sector workers with long-term contracts, excluding other categories of workers. High rates of informality, low female labour market participation rates and high levels of unemployment further contribute to low coverage. When other schemes were available, such as various subsidies, they were often poorly targeted and required substantial budgetary resources.

Pensions: only for the formal sector, still fiscally unsustainable

Countries in the region have mandatory pension schemes but only for a limited number of workers. For example, **pensions in the Arab region cover only one third of workers** and are as low as 8 per cent in Yemen. Current **structures and pay-outs of pension schemes are no longer viable**. For example, the benefits formula for the pension level was set at 70 to 80 per cent of the pensioner's salary at the end of his/her career in several countries. The average vesting period (years required to qualify for benefits) was 13 years in the Arab region in the 1990s, compared to 18 years in OECD countries and 25 in Eastern Europe.

Unemployment insurance: limited but expanding

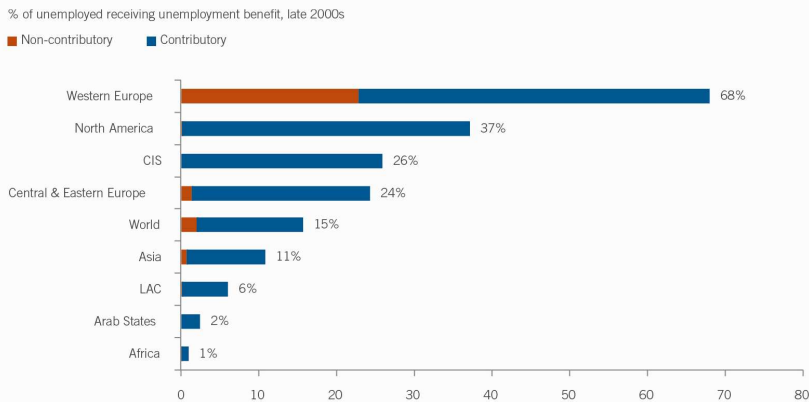
Few Arab states offered unemployment benefits and coverage was extremely limited before 2010. But even those systems that were available often failed to meet the objectives of typical unemployment protection schemes: insurance against the risk of workers losing their jobs (funded by payroll contributions) or social assistance based on an income test (funded by general revenues).

Figure 5.1: Schematic structure of social protection

FORMAL SOCIAL PROTECTION: Unemployment, Family, Maternity, Health, Sickness, Injury, Invalidity, Old-age, Survivors' and Employment Benefits		No Formal Protection				
Public Sector Employees	Private Sector		Children	Self-Employment and Informal Economy	Working Age Non-Employed	Elderly
	Formal					

Note: The non-shaded boxes on the left refer to the focus of policies in the Arab region.

Figure 5.3: Before the financial crisis, few Arab countries provided unemployment benefits



Source: ILO Social Security Inquiry Database.

Healthcare: uneven with high out-of-pocket expenses

The GCC economies have markedly increased their per capita health spending over time and have facilities offering healthcare to international standards. For many other Arab countries, however, access of the broader population to health insurance **has not been commensurate with the high levels of economic growth** achieved in recent years. In fact, there have been declining shares of public health expenditures as a proportion of GDP in parts of the region. In some Arab countries, such as Egypt, Lebanon, Sudan, Syria and Yemen, more than half of total health expenditure is covered from out-of-pocket payments.

Post-2010 changes in social protection

Pensions in the GCC have been increased on average by more than 50 per cent since the start of the Arab Spring. The increase in pensions outside the GCC was generally more modest, albeit still significant. For example, in Egypt, minimum pensions increased by 15 per cent, in Algeria by 30 per cent. In Morocco, the Government announced an increase in the minimum pension of almost 70 per cent for both the public and private sectors. Unemployment benefits were introduced or were expanded. Most GCC states as well as Algeria, Egypt, Morocco and Tunisia also increased their bills for food subsidies.

Chapter 6

Prospects & Policy Directions

Economic growth in the Arab region up to 2015 is projected to be the lowest of all world regions, after Latin America (3.8 per cent North Africa and 4.5 per cent Middle East). Given the still growing population, these rates will make only a modest impact in per capita real incomes while they are projected to be clearly inadequate to reduce unemployment at any significant rate in the future.

Arab governments adopted various labour market and social protection measures in response to the uprisings, but these were mostly reactive, unsustainable in the long term and introduced in a top-down manner.

Moving forward, general policy directions to create an inclusive, more sustainable path toward economic growth include: (1) **macroeconomic policy coherence** aimed at improved aggregate productivity gains and increases in average wages; (2) **participatory and inclusive social dialogue** between governments, workers and employers achieved through a fundamental reform of labour relations; and (3) **expanded and more effective social protection** that provides income and employment security.

Arab governments are also encouraged to (4) enhance **migration management**; (5) employ well-designed **employment policies and active labour market programmes**; (6) improve **access to quality education** by all income groups and encourage demand-driven **training** that is relevant **to labour market needs**; and (7) establish **up-to-date and reliable information systems**, produce **better statistics** and effectively **monitor and evaluate policies and programmes**.



Chapter 7

Workers' Perspective

Critical elements for the promotion of decent work for all women and men:

1. **The promotion, ratification and implementation of international labour standards**
2. Respect for **freedom of association, collective bargaining and social dialogue**
3. **Creating jobs, structural transformation, industrial development and productive employment.** This can be achieved through a sound industrial development, trade liberalization, and investment policies, as well as the building of **free democratic and independent trade unions** and the promotion of **collective bargaining**.



Chapter 8

Employers' Perspective

Creating an enabling environment for enterprise-led growth and job creation requires trade, competition and investment policies for growth, innovation, wealth and employment creation; inclusive labour market regulatory frameworks that support innovation and promote competition; tackling corruption and promoting good governance; increasing efforts for more efficient and more equitable distributive mechanisms; and a greater role for private sector organizations in policy dialogue.

Recommendations for chambers and Employers' Organizations in the region

- **Reinforce the policy role:** act as bridge between private sector and public officials
- **Be more inclusive:** speak for all sectors of the business community, large and small
- **Reach out** to civil society actors and trade unions
- **Be visible:** Use the media and communicate effectively
- **Credibility is critical:** act as a truly representative voice for business, without fear or favour

