



THE LABOR MARKET POLICY REFORM AGENDA IN MENA

MNSHD¹

Introduction: What is the problem? Despite positive economic growth in recent years, basic labor market outcomes in the Middle East and North Africa (MENA) remained stagnant and have only improved slightly in the past 10 years. A number of recent and ongoing analyses have stressed the pressing need for many economies in the region to identify new and sustainable sources of growth, create more and higher value-added employment, and absorb the fast growing number of university graduates into the labor market. Structural transformation towards higher productivity and the creation of qualified jobs requires far-reaching reforms in multiple sectors, including innovation, science and technology; education quality; labor market flexibility and mobility; and entrepreneurial incentives allowing investors to innovate, invest, and create higher value added jobs. Within this broad context, this note focuses on labor market policies and the agenda for labor market reform in MENA.

The Context - The Youth Bulge: In the short-run, labor markets in MENA will need to create employment for a large youth bulge. In most MENA countries the population share of 15 to 24 years-old accounts for 20 to 25% of the overall population compared to 18 % globally. Countries in North Africa will need to create over 1,500,000 additional jobs annually over the next 10 years just to keep the current proportion of unemployed unchanged.

Low Levels of Female Employment: Although increasing, *Female labor force participation* in MENA (28% in the Middle East and 25.5% in

North Africa) is the lowest in the world. International experience indicates that getting women into jobs is associated with poverty reduction, higher economic growth, and better governance. Higher levels of female employment allow government investments in education to be used more efficiently as women use their acquired talents productively in the economy. In countries with low levels of female employment, families often under-invest in girl's education with important externalities on children's nutrition and education outcomes.

High Unemployment: Unemployment in MENA - 10.6% across the region² - is higher than in any other region in the world and is particularly high among youth at 24.4% vs. 15% worldwide. In Tunisia and Egypt, unemployment rates are highest among highly educated individuals, 17% in Egypt and 21% in Tunisia. However, in many countries low-skilled individuals still compose the majority of all unemployed. In Tunisia, for example, the majority of all the unemployed, around 71%, are individuals that have completed at most primary education. Many of the unemployed population, especially youth, have been so for long periods of time. The time-dimension of unemployment is an important characteristic of the labor market, as long-term unemployment reduces individuals' propensity to find employment - in Tunisia about one third of the unemployed have been seeking for employment for at least 12 months.

High Levels of Informality: To cope with scarce formal jobs, young-educated workers are opting to work in low-pay/low-productivity jobs the informal sector. Having to rely on informal sector jobs constitutes an important loss of human capital for young entrants as

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² The World Bank, World Development Indicators, 2010.

returns to education (even among those with university education) tend to be very low in the informal sector. Approximately 67 percent of MENA's labor force works in *low-quality low-productivity jobs* with no pension health/unemployment insurance and *producing only 27 percent of regional GDP*. Informal employment, proxied by the share of the population without access to social security, is rising rapidly, especially among the most educated segments of the population. In Egypt and in Tunisia, most net employment creation in recent years has occurred in the informal sector, largely in wholesale, construction, and transport.

Main constraints to Employment Creation:

Despite great improvements in recent years, *private investment* remains low in MENA (Private Investment as % of GDP is 15% in Tunisia and 11% in Egypt vs. 32% and 28% in Malaysia and China). *Skills mismatches* remain an issue. Results from enterprise surveys indicate that firms identify worker skills and education among their top five constraints to business climate in the region, especially in North Africa - share of firms indicating labor skills comes up as a major constraint to business creation - cited by 37% of businesses in North Africa vs. 24% in Latin America (LCR), 14% in Eastern Europe-Central Asia (ECA), 6% in East Asia (EAP).

The relatively large *public sector* in the region still distorts incentives. In many MENA countries, civil service remains large for its levels of development. Since public sector jobs are still associated with relatively generous medical and retirement benefits, relatively short work hours, and transportation benefits, many educated individuals (mainly women) still queue for public sector jobs. This phenomenon undermines entrepreneurship among young educated workers and contributes to long unemployment spells. In Egypt, Syria, Iraq, the public sector still account for 30, 27, and 37% of overall employment (vs. an average of 15 to 20% worldwide).

Labor regulation remains rigid and labor taxes remain high. Firing regulations in MENA remain quite strict and firing costs remain high. In MENA, the cost of advance notice

requirements, severance payments and penalties due at termination, expressed in weeks of salary account for 50 weeks of salary on average vs. 28 in ECA, and 27 among OECD countries. Labor taxes and mandatory contributions by businesses as a percentage of commercial profit are 25 percent in North Africa vs. an average of 10 to 13 percent in EAP and LCR.

What is our Approach and Strategy? Our policy framework considers constraints in labor demand and supply, as well as the meeting of the two (i.e. matching and intermediation) through four policy pillars:

1. **Support Regulatory reforms and capacity building, with a focus on:**
 - Make it easier for firms to hire people
 - Protecting workers in periods of transition with a focus on unemployment insurance;
 - Ensure that labor costs (taxes and wages) are not too high as compared to productivity;
2. **Address the issue of skills:**
 - Train and re-train workers
 - Address skills mismatches
 - Ensuring high quality recognition of learning at all levels, enhancing flexibility, transparency and portability of education credentials for all students
3. **Supporting Rapid Employment Creation:**
 - Modernize public agencies that help workers and firms to get together
 - Foster coordination with private intermediation agencies
 - Prepare /help individuals to obtain employment abroad
4. **Income Support:**
 - Promote employment and provide income support through regional incentives, wage subsidies, entrepreneurship programs, and public works.

Note that the labor market agenda complements a private sector development strategy focused on improving competitiveness and the business environment.

What have we done? Labor market and institutional reform are politically sensitive. Yet, we have been able to further this agenda. The region's engagement in this area is composed of a diverse portfolio that includes regional and country level dialogue (AAA

work³ and technical assistance) and a rapidly growing operational pipeline.

Regional AAA: The region leverages AAA and data generation work to produce solid diagnostics and to build a constituency around the need for reform. These include:

- The upcoming *Regional Informality Report* (FY11) and the cross-sectoral *Employability Flagship Report* will foster the regional dialogue on the needed reforms to promote employment creation.
- Regional dialogue on *migration and social insurance portability* – with a focus on regional issues, including Tunisia, Egypt, and the UAE. The goal is to establish mechanisms to identify demand for labor abroad and improve labor intermediation, and to better link migration and skill development through training policies.

Policy Dialogue and Lending to Support Regulatory Reform: MENA engages in multi-year analytical work on labor markets, skills supply, constraints to labor demand in private sector, and social protection systems. In *Tunisia* and in *Morocco* this work has led to Employment DPLs and to a broad scope DPL in Jordan supporting social security reform. Similar work is ongoing in Lebanon, Syria, and Egypt, and is planned for Yemen. Also, the Bank works closely with counterparts on TA programs on qualifications frameworks for skills training.

Investment lending: The region uses investment lending to facilitate entry of higher quality skills into the labor market with projects underway in Tunisia, Morocco, Yemen, Djibouti and Jordan. In Jordan the employer driven Skills Development Project is aimed at realigning the design of Technical and Vocational Education and Training systems with market needs.

Strengthening Governance and Social Service Delivery: MENA is preparing a Regional Report on Labor Regulation, Active Labor Market Programs (ALMPs), and Public Employment Services. There are also ongoing technical assistance engagement with clients to

modernize and build the capacity of Labor Ministries, public intermediation, and labor offices in Jordan, Syria, Egypt, and Tunisia.

Promoting Employment Creation and Income Support: Workfare programs (Djibouti, Yemen) and school-to-work-transition programs are implemented to create and facilitate employment opportunities for unskilled and skilled workers.

Workfare Programs: Workfare programs provide temporary employment for wages that are lower than market wages. They comprise labor intensive infrastructure works (construction, maintenance, soil conservation, water collection, and green public works). Workfare programs are effective ways to rapidly increase employment, provide income support in the short run, and through this, to achieve poverty reduction and promote social cohesion.

Yemen's Social Fund for Development (SFD) delivers community-driven projects in the poorest and most remote areas of rural *Yemen*. In response to the recent food price crisis a small Bank grant (\$10M) initiated a Labor-Intensive Work (LIW) Program to provide emergency cash-for-work to households most affected by the shock with 36,000 beneficiaries. In *Djibouti* with support from a JSDF emergency window Grant (\$4M), the Bank, in collaboration with the Japanese Social Development Agency designed and is implementing an innovative 'workfare plus' in urban areas. The program combines traditional cash-for-work with nutrition promotion to leverage the effect of the additional income on the family's nutritional status. It targets poor and vulnerable households with 0 to 2 years old children and/or pregnant women.

School to Work Transition Programs: School-to-work transition programs are used to enhance employability and to promote job creation, especially among new entrants to the labor market. The four main types of school to work transition programs are (i) employment services, i.e. intermediation programs to match new entrants with firms domestically and abroad, (ii) labor market training, (iii) wage subsidies, and (iv) self-employment promotion.

³ AAA: Analytical and Advisory Assistance

Tunisia's Reform of Active Labor Market Policies: The Tunisian Ministry of Vocational Education and Employment undertook a reform of the ALMP portfolio in 2009, based on analytical work by the World Bank and supported by the first Employment DPL. The reform bundled over 20 ALMPs into six programs, facilitating management and financial control. All ALMPs have small monthly income-assistance components with strict eligibility rules for job-seekers and employers. The number of new and ongoing program contracts has increased markedly from 85,889 (2008) to 95,415 (2009) to 138,674 in 2010.

Entrepreneurship Promotion: A Business Plan Thesis Competition supported by the EDPL aims to improve students' school-to-work transition by encouraging entrepreneurship and innovative thinking. The intervention provides an integrated package of entrepreneurship training and individual coaching to university students in order to implement business ideas, developed as part of the University thesis. The program is an innovative pilot and impact evaluation has been embedded in the project to assess its effectiveness.

What more could be done? In the *short term* employment response packages (easy to scale-up) composed of a mix of programs/policies for employment generation, temporary employment, and income protection to mitigate the impact of the youth employment crisis could be considered. While far-reaching reforms are challenging, ALMPs and temporary employment programs can help mitigating excess supply in the short run.

- Programs targeted to skilled graduates such as subsidized wages and or social security contributions, training, Labor Intermediation programs, international placement services, business promotion.
- Programs targeted to the unskilled would include public works, Regional development programs, entrepreneurship programs with micro-credit components and training.

In the *medium term*, countries need to establish more dynamic labor markets with appropriate labor market institutions. This means reforming

labor regulations, promoting private intermediation, revising social security systems, including tax wedges, social contributions and pensions. Also useful would be liberalization of professions and a shift from protecting particular jobs to a framework of protecting workers via social support, unemployment insurance, and active measures to assist during periods of transition. Other measures include modernization of labor intermediation and public employment services through investment operations and fee-for-services and working with Labor Ministries and Labor Offices to assess and monitor ongoing employment programs, reform ALMP systems, and develop and design labor market information systems.

Remaining challenges: In recent years governments in MENA have shown some reluctance to engage in projects/core reforms in the social sectors. This partly occurs because some of the needed reforms to improve the operation of the labor market are politically sensitive. Unions in MENA – some of which still have strong political leverage – continue to favor the status-quo as defined by the post-independence social contract, making labor reform a rather complex and far-reaching political process.

Also, access to micro-data for policy design in MENA in the area of employment such as labor force surveys remains restricted, even among government officials and public institutions. This limits the ability of policy makers to formulate evidence-based policies.

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