Dubai School of Government

POLICY BRIEF

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SUMMARY

During the recent oil boom, the MENA region has seen job creation accelerate. Unemployment fell from 15 percent in 2000 to at estimated 12.7 percent in 2005. Employment growth averaged nearly 4.2 percent a year during this time, while labor force growth averaged 3.6 percent a year.

Given favorable economic prospects going forward, the region could see unemployment decline to nearly 7 percent by 2010. But this positive forecast depends on the region's ability to continue creating jobs at current rates. Achieving this will prove difficult, especially since MENA economies are still marked by high labor market rigidities and the public sector continues to play a dominant role in these economies.

Moreover, positive labor outcomes do not apply uniformly across MENA. Many non-oil economies have seen unemployment increase in recent years. While oil producers may have the choice to manage job creation on the back of oil revenues, other countries have few choices but to press forward on reforms.

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WILL THE OIL BOOM SOLVE THE MIDDLE EAST EMPLOYMENT CRISIS?

by Paul Dyer — Research Associate

At the 2003 Annual Meetings in Dubai, the World Bank released its flagship report on labor markets in the Middle East and North Africa (MENA).[1] The report described unprecedented job creation challenges facing the region and outlined the reforms needed to navigate these challenges. According to the report, an estimated 100 million jobs would have to be created by 2020 to employ new entrants and reduce unemployment to sustainable levels. To do so, the MENA region would have to maintain average annual economic growth rates of 6 to 8 percent between 2000 and 2020, far higher than the average 3.6 percent growth witnessed over the 1990s. Such growth would require regional policy makers to move beyond graduated, sector-specific interventions and launch comprehensive reform measures aimed at opening the region to trade, diversifying economies away from oil, reducing the dominant role of the public sector and improving governance.

Since the report's publication, however, much has changed in the region. Oil prices rose from $29 a barrel in 2003 (and an average $19 during the 1990s) to $53 a barrel in 2005. The rise in oil prices bolstered regional budgets and stimulated economic growth, with regional GDP growth rising from 2.9 percent in 2002 to an estimated 6.0 percent in 2005. Growth in 2006 is expected to reach 5.6 percent and could remain higher than 5.0 percent over the next few years. In turn, the region has seen higher rates of job creation and declining rates of unemployment. Furthermore, estimates of regional labor supply have been revised, with overall labor force estimates and projections having been reduced. Given these changes, the relevant question becomes whether labor market pressures have suddenly become manageable. Has the oil boom solved the job creation challenge in MENA?[2, 3]

LABOR FORCE GROWTH REMAINS HIGH

As of 2005, the labor force in MENA stood at nearly 120 million persons, accounting for some 56 percent of the working-age population (ages 15-64) and 35 percent of the total population. Average annual growth rates for the regional labor force between 2000 and 2005 averaged 3.6 percent a year. The current rate of labor force growth in MENA is higher than other developing regions. In fact, it is higher than labor force growth rates in such regions as Latin America and East Asia since 1950. Labor force pressures in MENA are indeed unprecedented.

While labor force growth remains high, rates of growth are declining. Having experienced substantial fertility declines in the 1980s, much of the region witnessed peak labor force growth rates in the 1990s. Rates of growth will continue to decline to an average of 3.1 percent a year between 2005 and 2010 and 2.1 percent a year between 2010 and 2020. Absolute numbers of new entrants are currently peaking, at just above 4.0 million new entrants a year, a number that will decline – albeit slowly – to nearly 3.9 million by 2010 and 3.1 million by 2020.

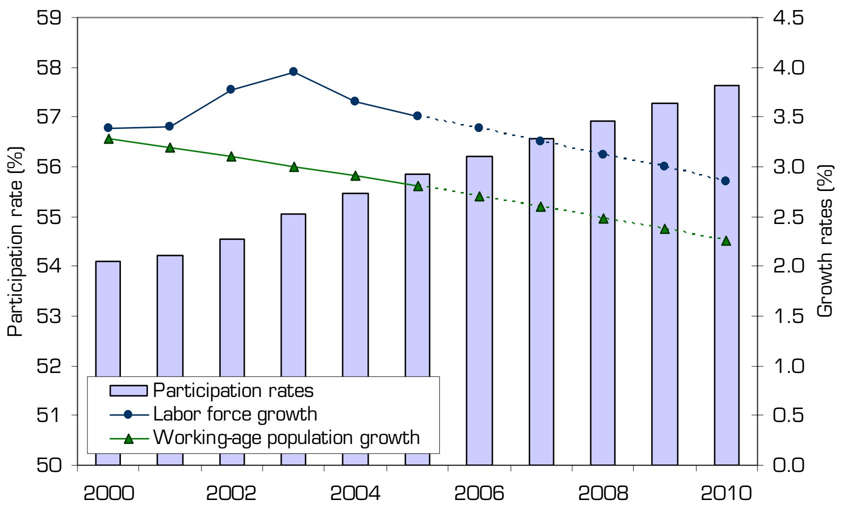
Participation Rates Are Increasing

Labor supply trends in MENA are driven largely by demographics, with the working-age population growing at a rate of nearly 3.0 percent a year between 2000 and 2005. However, changes in participation, particularly among women, have also driven its growth. In 2000, the participation rate among women in MENA was about 27.5 percent. By 2005, it had increased to nearly 30.5 percent. The participation rate among men, on the other hand, has remained fairly consistent, rising from 79.3 percent in 2000 to 79.8 percent in 2005. Participation by young people has followed a similar pattern. Young women's participation in the labor force increased from 23.5 percent in 2000 to nearly 24.9 percent in 2005, while that of young men has declined from 54.9 percent to 54.4 percent, reflective of the fact that larger numbers of young men are remaining longer in school.

Regional Job Creation Has Expanded

With recent economic growth in the region, there has been an increase in job creation and a resultant decline in the overall rate of unemployment. The World Bank estimated unemployment in the region in 2000 at nearly 15 percent. Currently available figures put the regional rate of unemployment in 2005 at about 12.7 percent. This decline suggests that economies are not only increasingly able to absorb new labor market entrants, but they are making progress in reducing overall unemployment as well. Implied regional employment growth between 2000 and 2005 averaged 4.2 percent a year or nearly 20 million new jobs in all.

Labor Supply Trends in MENA: 2000-2010



Source: ILO 2005

Despite rising employment growth, however, the unemployment rate in the region remains high, and reducing rates of unemployment while continuing to absorb new workers remains a critical challenge for regional policy makers. Furthermore, evidence suggests that the bulk of job creation in MENA in recent years has been temporary in nature and has depended largely on public sector expenditure. The elasticity of employment (the percentage change in employment with every percentage change in GDP growth) between 2000 and 2005 averaged nearly 0.9, quite high when compared with international norms. This suggests that much of the job creation in MENA has emphasized short-term, government-supported solutions to a long-term, systemic problem. These have not necessarily been productive jobs. It is questionable whether recent advances in job creation are sustainable in the long run, even given continued high rates of economic growth.

Specific problem areas continue to plague regional labor markets. Evidence suggests that public sector employment continues to account for a large share of employment in the region. The central role of the public sector reinforces incentives for unemployed workers to wait for public sector jobs, with the wages and benefits that accrue to these positions, rather than seeking out work in the private sector. Also, despite some reforms intent on giving more flexibility to firms in regard to hiring workers, regional economies remain among the most restrictive in regard to labor market regulations. This has inhibited the proactive role private business might have played in job creation by elevating the perceived costs associated with labor-intensive production.

MIXED RESULTS BY COUNTRY

Regional aggregates mask the variety of experiences in MENA, both in terms of labor force growth and job creation. As might be expected, the oil economies of the region have been able to channel increased oil returns into job creation. Iran, a country facing relatively high labor force growth (at 4.3 percent a year), has brought the unemployment rate down to 11.0 percent from 13.8 percent in 2000. Implied employment growth has averaged 4.9 percent a year. Likewise, Algeria has witnessed substantial changes in labor outcomes. With labor force growth at nearly 3.9 percent a year, the country has seen reported unemployment rates fall from 29.8 percent in 2000 to nearly 15.3 percent in 2005. It should be noted, however, that recent reported rates might not reflect the true rate of unemployment in the country, as the government statistics agency has adopted a revised methodology for measuring unemployment in recent years.[4]

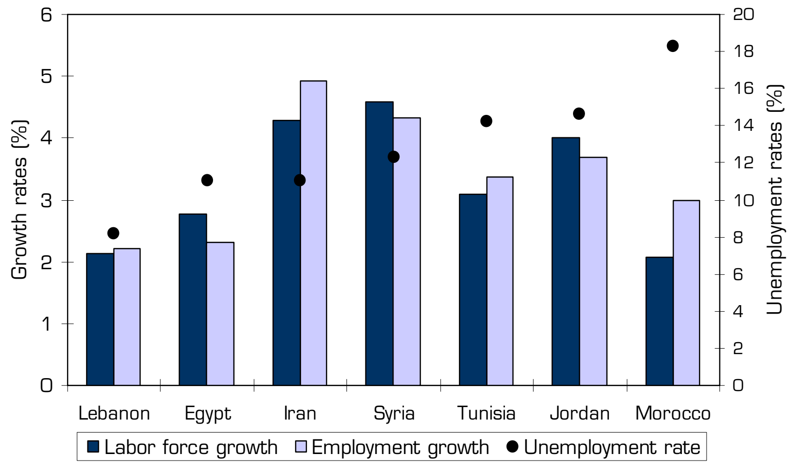
Employment and unemployment data from the Gulf Cooperation Council (GCC) countries are limited, a factor that renders an accurate assessment of recent trends problematic. Available data suggest that among nationals, unemployment remains a serious and growing problem despite high economic growth rates. In Saudi Arabia, official unemployment in 2002 was estimated at 4.6 percent, while unemployment among nationals was nearly 8.3 percent. Unemployment among nationals has been estimated at 12.4 percent in Bahrain, 11.6 percent in Qatar and 10 percent in Oman. Recent data from the United Arab Emirates (UAE) suggests that unemployment among nationals is nearly 15 percent. The skewed nature of employment outcomes in these countries is driven largely by wage differentials, the result of the public-private and national-expatriate segmentation of the labor force. Bolstered efforts to enforce stricter nationalization of employment in recent years seem to be creating incentives for manipulation of the labor force rolls as much as for job creation among nationals.

Labor outcomes for regional non-oil producers and net oil importers have been quite different from those of the oil economies. Rising costs associated with fuel, both in terms of input costs for businesses and budget constraints for governments still holding on to costly fuel subsidies, have imposed increased burdens on these economies and limited growth outcomes. Furthermore, in contrast with the last oil boom in the region, transfers between oil economies and non-oil economies in the region are comparatively weak. In the past, non-oil economies benefited from high labor remittances and direct aid from the GCC countries. While intraregional tourism and portfolio equity flows have grown in recent years, workers' remittances and aid have been limited. As a result, many of these countries have seen a slight worsening of labor outcomes in recent years.

Unemployment in Egypt rose steadily from 9.0 percent in 2000 to nearly 11.0 percent in 2005. Economic growth, at 4.9 percent a year, has not triggered enough job creation to counter Egypt's labor force growth of nearly 2.7 percent a year. Employment creation averaged only 2.3 percent a year between 2000 and 2005. Similarly, Jordan has seen unemployment rates rise from 13.2 percent in 2000 to 14.6 percent in 2005. Employment growth in Jordan has averaged nearly 3.7 percent a year, while its relatively young labor force continues to grow at nearly 4.0 percent annually.

Syria, which maintains a sizeable oil production capacity but is quickly becoming a net oil importer, saw unemployment rates rise from 11.2 percent in 2000 to 12.3 percent in 2005. Actually, the implied employment growth in Syria has been quite high, at 4.3 percent a year, but Syria's late entry into the demographic transition means that labor force growth rates in the country have averaged nearly 4.6 percent a year since 2000. Likewise, Yemen is currently experiencing labor force growth rates of nearly 4.2 percent a year. While comparable

Labor Market Outcomes in Individual MENA Countries, 2000-2005



Source: ILO 2005 and country sources

unemployment rates for Yemen are not available, labor force data suggest that labor force pressures in Yemen will be high in the long term, while oil-driven growth will decline as reserves are depleted.

The non-oil economies of Tunisia and Morocco have seen positive employment outcomes in recent years. Unemployment rates fell from 15.4 percent to 14.2 percent in Tunisia and from 22.0 percent to 18.3 percent in Morocco.[5] Such declines occurred in Morocco despite weak economic growth resulting from the expiration of the Multi-Fiber Agreement. It should be noted that labor force growth in both countries is relatively low, as Tunisia and Morocco were among the first countries in the region to bring down fertility rates and experienced peak labor force growth rates in the early 1980s. Between 2000 and 2005, annual rates of labor force growth averaged 3.0 percent in Tunisia (driven largely by increases in participation rates rather than demographic trends) and 2.1 percent in Morocco. Annual employment growth rates during the same period averaged nearly 3.4 percent in Tunisia and 3.0 percent in Morocco.

A Difficult Labor Market for Women and Youth

One common factor among countries in the MENA region is that women bear a disproportionate share of poor labor market outcomes. Rising participation rates for women mean that the female labor force is growing more rapidly that the male labor force. Growth rates for the female labor force between 2000 and 2005 averaged nearly 5.1 percent a year. This is up from the 1990s average of 4.6 percent a year, and while expected rates of female labor force growth are expected to fall to 3.9 percent a year by 2010, this is still 1.5 percentage points higher than male labor force growth.

Still, regional economies continue to face problems with finding productive employment for many of these women. Unemployment rates for women in MENA are nearly twice those of men, averaging nearly 21 percent while unemployment rates for men average only 11 percent. This figure suggests that nearly 6.6 million women are seeking but not able to find gainful employment. They make up nearly half of the unemployed while accounting for less than 27 percent of the total labor force.

Prospects for young, new entrants in the region are also weak, and even in higher growth countries young workers face difficulties in securing jobs. Unemployment rates among young people (ages 15-24) in MENA are more than double those of the total labor force. In recent years, the regional youth unemployment rate has remained above 30 percent. Rates range from 23.2 percent in Iran to 47.4 percent in Algeria. Recent estimates put youth unemployment in the UAE, among nationals, at nearly 60 percent.

Young workers face difficulties in securing jobs around the world, given a general lack of experience and, often, high reservation wages. However, the situation in MENA is particularly acute given the scale of the problem. Currently, those ages 15-24 make up nearly 26 percent of the labor force and 35 percent of the working-age population. They amount to more than 26 million potential workers, with nearly 8 million of them unable to find formal employment. There are long-term problems associated with this as well; negative experiences in securing a job at a young age may trigger long-term disillusionment with employment prospects, a factor that may lead to higher rates of discouraged workers in the future.

FUTURE PROSPECTS FOR LABOR IN MENA

While labor force growth in MENA is declining, both in terms of rates and flows, labor market pressures will remain high. Given expected growth of the regional labor force, the region's economies will have to create over 54 million jobs within the next 15 years, or 3.6 million jobs a year, to meet the demands of new entrants alone. Within the next 20 years, some 70 million jobs will have to be created to meet these needs. In addition, resolving the current unemployment situation requires the creation of an additional 15 million jobs.

As noted above, available data for 2000 and 2005 suggest that the region created 19.6 million jobs in that time period, averaging some 3.9 million new jobs a year. This suggests that MENA countries have made progress in addressing the employment challenge facing the region. However, continuing job creation at current rates for the long term depends on many factors, including continued high rates of economic growth, the maintenance of high oil prices and the translation of oil returns into sustainable job creation.

If the regional economy as a whole is able to maintain current rates of growth over the next decade, as well as maintaining its current employment elasticity, unemployment rates as a whole could drop to nearly 7.0 percent by 2010. A more sustainable elasticity rate (The average for MENA over the past 15 years has been nearly 0.7.) suggests that unemployment would decline to 11.0 percent by 2010 and less than 6.0 percent by 2015. Such estimates, however, are highly dependent on many assumptions, the most important of which is the sustainability of labor absorption in economies that have such high labor market rigidities and depend so highly on public employment.

Furthermore, such positive forecasts do not apply uniformly across countries. Projected economic growth and recent labor market outcomes suggest that oil-producing governments may be able to manage the job creation challenge with public expenditures and targeted job creation programs. Although these jobs might not be productive jobs, they would reduce many of the pressures associated with labor supply growth and unemployment. While oil economies in the region may be able to solve the bulk of the employment problem on the back of high oil prices, evidence shows that the non-oil economies of the region will continue to face long-term difficulties in securing needed job creation, difficulties that require them to take more substantive steps toward reforming their labor markets and enhancing the dynamism of their economies.

CONCLUSIONS

The oil boom in MENA has altered prospects for resolving much of the region's employment situation. Overall unemployment rates have declined, with job creation increasing at a rate that sees employment growth surpassing the growth of the labor force. Coupled with prospects of high future oil prices and economic growth, labor market trends suggest that regional unemployment will continue to decline and that regional economies as a whole will be able to absorb new entrants and decrease unemployment to minimal levels by the end of the next decade.

However, positive labor outcomes have not been shared by all countries in the region, and non-oil producers in particular still face grave challenges. Furthermore, job creation is more than a numbers challenge: enhancing worker productivity remains a primary challenge for all states in the region. Moving toward optimal outcomes, wherein labor is a functional driver of productivity, will require efforts to build the skills of regional workers and freeing the entrepreneurial spirit of private sector investors, as well as increased cooperation between educators, policy makers and business leaders in regard to resolving skill mismatches.

Thus, by and large, the messages of the World Bank's flagship report still hold. In the long term, non-oil economies in the region have little choice but to move forward on comprehensive reforms that will improve the competitiveness of their economies and strengthen the role of the private sector. Oil economies, on the other hand, do face a choice: either to muddle through a process of managed job creation or to use renewed oil wealth to speed up and ease the transition to more dynamic, productive labor markets. In many cases, the current growth environment provides a cushion that eases the processes of reform in the region, but it should not be viewed as a solution to the regional labor challenge in and of itself.

Endnotes

1. World Bank. 2004. *Unlocking the Employment Potential in the Middle East and North Africa: Towards a New Social Contract*. Washington, DC: World Bank.

2. Referenced economic data, including recent trends and prospects, are taken from the World Bank's *MENA 2006 Economic Developments and Prospects: Financial Markets in a New Age of Oil*. Washington, DC: World Bank.

3. Referenced labor force data are from International Labor Organization's Economically Active Population Estimates and Projections, 2005. Available online at http://laborsta.ilo.org. Unemployment data are taken from the ILO and various country sources.

4. A recent study by ECOtechnics suggests that unemployment in Algeria is closer to 25 percent. (ECOTechnics. 2005. *Activité et emploi en Algérie en 2004.* Algiers: ECOtechnics.)

5. Reported rates of unemployment for Morocco reflect urban unemployment. Total unemployment in Morocco in 2005 has been estimated at 11.0 percent.

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