4.

PRIVATE-SECTOR DEVELOPMENT AND CREATION OF DECENT JOBS: THE WAY FORWARD

4 KEY FINDINGS

A four-pillar policy response should be implemented to address the COVID-19 challenges	Support actions for the most vulnerable groups, including informal economy workers and enterprises, are needed	It is indispensable to develop national employment policies, rethink macroeconomic policies and promote private-sector development
Labour and social policies supporting the private sector should respond to the dual challenge of creating jobs and reducing deficits in decent work	Education and training should be reformed, and effective active labour market policies developed, particularly for youth	Gender equality and women empowerment need to be promoted

4. Private-sector Development and Creation of Decent Jobs: The Way Forward

A. Overview

This report advocates that the public and private sectors complement one another rather than compete against each other. It argues that active policies to assist small businesses and provide time-bound wage subsidies to entice the private sector would do more to employ young people than simply transferring financial and other resources from the public to the private sector. Hence, as argued in this report, the appropriate short-term policy lesson is to develop inclusive employment and labour market policies that reduce the current degree of rigidity and segmentation in Arab labour markets, including the attenuation of gender disparities and informal employment. This will continue to pave the way forward for future long-term policy assessment. Yet, for now, the primary concern of policymakers is to overcome the immediate challenges brought by the pandemic. To this end, ILO proposes a four-pillar policy framework to respond to the COVID-19 crisis (see section B below). The long-term reforms of inducing a structural transformation process that enhances the private sector's ability to generate formal and decent employment are discussed in section C.

B. Policy measures to respond to the COVID-19 crisis

ILO has structured its policy response to the COVID-19 crisis around four pillars, which are the following:

- Stimulating the economy and employment:
  - Active fiscal policy;
  - Accommodative monetary policy;
  - Lending and financial support to specific sectors (for instance, health sector);
- Supporting enterprises, jobs and incomes:
  - Extending social protection for all;
  - Implementing employment retention measures;
  - Applying financial and tax relief for micro, small and medium-sized enterprises (MSMEs)
- Protecting workers in the workplace:
  - Strengthening OSH measures;
  - Providing health access for all;
  - Adapting work arrangements (for instance, teleworking);
  - Expanding access to paid leave;

- Preventing discrimination and exclusion;

- Relying on structured social dialogue for developing, assessing and reviewing evidence-based solutions:
  - Strengthening the capacity and resilience of employers' and workers' organizations;
  - Strengthening the capacity of Governments;
  - Strengthening social dialogue, collective bargaining and labour relations institutions.

With the devastating impact of the crisis on individuals and businesses, policy responses should focus on supporting and protecting workers, employers and their families. This requires large-scale public support and investment, provision of paid sick leave, teleworking, and improved OSH.

Timely, large-scale and coordinated policies are needed to protect employment, help businesses and support incomes. All these measures, however, will not work in isolation and unless accompanied by effective implementation and enforcement mechanisms, as well as accessible complaint channels.

More particularly, countries in the region should consider a range of social protection measures, including wage subsidies, in-kind and cash social assistance to support the poor and vulnerable, and temporary income support to those not registered in social insurance, amongst others.

The most vulnerable groups, including informal economy workers and enterprises, should be prioritized, noting that they ordinarily tend to operate outside the reach of Government authorities and are at a greater risk of plunging deeper into poverty. Support actions include identifying their needs and priorities and determining accordingly the nature and level of interventions needed; reducing their exposure to the virus; ensuring their access to health care; ensuring their participation in social dialogue; providing income and food support to individuals and their families to compensate for the loss of, or reduction in, economic activity; and supporting SMEs both in the formal and informal sectors.[1] Migrants, refugees and internally displaced persons should also be included in governmental response strategies as these are among the most vulnerable and should be supported.

Vulnerable firms, whether SMEs or firms operating in the informal sector or in the most impacted sectors, need not only swift, continuous and expedited governmental support (such as tax holidays, reductions or rescheduling; interest-free loans; wage and employment subsidies) but also help from banks, other financial institutions (such as flexibility with debt; and increased lending, possibly conditional on retaining workers) and other parts of the private sector, with simplified administrative processes to facilitate and expedite access of those in need to the different services and funds provided.

Furthermore, female participation in the workplace is and will continue to be negatively impacted as many women grow more concerned for their and their families' safety. Therefore, governmental responses need to pay particular attention to women, including migrant domestic workers and those in self-employment, informal jobs and other precarious forms of work. Investments in infrastructure and public care services can also support women's employment and help redistribute unpaid care work while freeing women's time.

Youth need to participate in the design and implementation of the response strategy to ensure that their needs and concerns are properly addressed. Targeted measures to support youth employment are key while online training and education should be prioritized to mitigate the risks associated with skills development and education disruption.

In addition to online education, promoting online vocational and skills training is crucial, as workers

[1] ILO, 2020b.

become in dire need to reskill in order to be able to take up new jobs as economies ease their lockdown measures and businesses gradually reopen. These training programmes should also target vulnerable groups, including migrants and refugees, who are at a greater risk of losing their jobs and incomes. Recently, ESCWA, in collaboration with respective ministries, was successful in initiating an online training free of charge for 25,000 Lebanese citizens from all Lebanese governorates. Online courses were held by faculties from an international university in multiple areas of expertise.

As the Arab region has witnessed an increase in informality, poverty and inequality levels over the past decade, driven by multiple factors, including recessions, conflicts and wars, the provision of targeted support becomes even more critical. As noted in a recent paper by ESCWA, the regional poverty level is estimated to have increased significantly since 2019, with an addition of 16 million expected to fall into poverty using national definitions.[2] The outlook is even more grim in conflict-torn countries such as Iraq, Libya, the Syrian Arab Republic, and Yemen, in which poverty levels are projected to have exceeded 75 per cent. Consequently, Government policies to create additional employment in the short term to fight poverty and inequality become pivotal. Two policy options that showed success in various countries suffering from high poverty rates are employment guarantee schemes and employment intensive investment programmes.

Employment guarantee schemes are public work programmes that have been used to provide households with additional income during drought and other natural disasters especially in rural areas. If designed well, public works can allow productivity, work quality, working standards, and the quality of the works to be maintained and low-waged workers to continue to earn a livelihood. Investments in infrastructure can help promote social and economic development, increase agricultural productivity, provide care work, support education and health, and address environmental and climate-related challenges, offering a multifaceted solution, including, but not limited to, decent employment creation. Public investments can contribute to the development of needed public infrastructure while supporting the livelihoods of individuals, especially the working poor, through wage employment, thereby boosting consumption and investment.

Further to the above suggested response measures and policies, the United Nations Policy Brief on the World of Work and COVID-19[3] suggests focusing responses around the following three priority areas, namely:

a. Prioritizing immediate support for at-risk workers, enterprises, jobs and incomes;
b. Ensuring a comprehensive approach to returning to work;
c. Creating decent (formal) and productive jobs for a green, inclusive and resilient recovery.

Priority (a) includes: (i) the extension of social protection coverage and outreach; (ii) employment retention measures; (iii) sustaining business operations, especially MSMEs; (iv) avoiding increasing vulnerabilities through gender-responsive, inclusive, accessible, and targeted measures, based on social dialogue; and (v) immediate rewarding to essential workers who hold the system together, namely, health, sanitation and/or agricultural workers.

Priority (b) consists of policies to address the following: (i) safe and accessible workplaces; (ii) respect for the needs and rights of workers and employers; (iii) taking a holistic approach and sequencing with childcare and schools; (iv) effective testing and tracing; (v) well-designed active labour market policies (ALMPs), including public employment programmes; (vi) capability-building measures for those facing uncertain transitions;

[2] Abu-Ismail, K., 2020. Impact of COVID-19 on Money Metric Poverty in Arab Countries (E/ESCWA/CL2.GPID/2020/TP.10).

[3] United Nations, 2020. Policy Brief: The World of Work and COVID-19.

(vii) flexibility for continuing alternative work modalities for populations at risk; and (viii) looking beyond the short term.

Priority (c) focuses on the following: (i) social protection; (ii) accelerating transition to formality; (iii) job creation through greening economies and investments in nature; (iv) investments in the care economy, or health-care systems; (v) prioritizing skills and jobs for young people; (vi) private-sector policies with a specific focus on MSMEs and public-private partnerships; (vii) leveraging new technologies; (viii) sectoral policies for hard-hit sectors and structural transformation; and (ix) targeting policies for hard-hit groups.

Building on the above three priority areas and ILO's four-pillar policy framework, Arab countries can respond to the crisis without leaving anyone behind. It remains to acknowledge, however, that critical to all of these recommendations is the availability of resources and adequate fiscal space. Countries in the region must review and assess their revenues and expenditures and change the composition of public expenditure to give strategic priority to the much-needed response measures. Coordinated global and regional support for national stimulus packages is also urgently needed.

C. Medium-to long-term measures to address structural issues

The coherent policy recommendations, issued by the United Nations and ILO, to ease economic stress for citizens, businesses and countries are certainly a challenge to implement in the Arab region given current circumstances. However, employment challenges are complex in the region and need to be urgently and properly addressed. The pandemic has only brought pre-existing regional issues to the forefront on a magnified scale.

In response, Arab States need to review their overall policy frameworks in order to not only respond to the current COVID-19-related challenges but also address pre-existing structural labour market challenges. Comprehensive national employment policies (NEPs) need to be developed to address both the demand and supply sides of the labour market and serve as a vehicle for greater policy coherence. Labour market institutions need to be built/enhanced as appropriate along with stronger and more inclusive social protection systems and improved regulatory and legislative frameworks. Arab States need to rethink their current macroeconomic models and support economic diversification. Formalization should also be a priority in the medium-to-longer term given that informal economy workers and enterprises have fewer means to address the repercussions of this pandemic and will thus dive into deeper poverty if no support is provided. Finally, these medium- to longer-term objectives should be pursued through tripartite social dialogue, with greater participation of informal economy workers and enterprises, women and youth and should be guided by relevant international labour standards.

Building on the above, the following sections detail demand- and supply-side policy recommendations aimed at addressing the region's long-lasting structural labour market challenges with particular focus on private-sector development.

1. Developing proactive and comprehensive national employment policies

While some measures have proved to be efficient and effective in addressing a number of employment problems in the region, solving the unemployment and decent work deficits requires a broader approach that looks into various issues, from both supply- and demand-side perspectives. That said, a comprehensive approach to employment policies is urgently needed in the Arab States. Such policies, comprising macroeconomic, sectoral and structural policies as well as labour market policies and institutions, offer a practical framework for tackling the multidimensional labour market challenges faced by the Arab States, including the inefficiency of the private sector and its limited potential and capacity to create decent jobs.

An open and broad-based NEP process, built around extensive dialogue at all levels, with workers' and employers' organizations, different line ministries and agencies, and other key stakeholders, is essential to ensure increased commitment, accountability, inclusiveness, and success. NEPs should most importantly build upon evidence and an objective assessment of national contexts and should tackle several policy areas in a coherent manner. That said, labour market information and statistics are prerequisites for NEP development while, at the same time, mechanisms for coherence and coordination, such as inter-ministerial tripartite committees, should be established to ensure development of effective NEPs.

2. Rethinking macroeconomic policies and promoting private-sector development

Macroeconomic policies play a crucial role in generating decent work opportunities, which is a main challenge facing all countries in the region. However, such policies need to be carefully designed to be able to encourage decent employment creation, productivity and inclusive growth. A widely held conviction is that downsizing the public sector within a framework of fiscal consolidation should be at the core of any policy agenda that promotes private enterprises as engines of growth and employment creation. Typically, such a view is justified by comparing public-sector employment and the wage bill in Arab countries with international benchmarks. This is certainly useful, but there are analytical flaws and, in some cases, country-specific statistical anomalies that should raise doubts of uncritically embracing the notion that a reduced public sector will produce a robust private sector. A more careful analysis using the notion of an "optimal" size of government, and a more careful comparison of the so-called wage premium enjoyed by the public sector, might yield surprisingly different conclusions, as it seems to have done in the cases of Egypt and Jordan.

The specific debate on the size of the public sector has become unmoored from the findings of enterprise surveys, which do not regard a large bureaucracy in the Arab region as a major impediment to private-sector growth. Of course, concerns about inefficient bureaucracy abound in executive opinion surveys of the World Economic Forum (WEF), but whether the best way to attack bureaucratic inefficiencies is to engage in large-scale public-sector downsizing is by no means obvious. One should realize that the public sector supports the private sector through various means. Hence, it is better to reimagine the debate in terms of identifying public-private synergies. For example, well-designed transparent procurement policies can be used to contract small businesses to deliver certain public services, including cleaning and property maintenance. This is an important link to the private sector because public procurement can be as high as 13 per cent of GDP based on estimates by the Organisation for Economic Co-operation and Development (OECD).[4] Public-private partnerships are also means to promote growth and employment creation, making use of capacities and resources of both public and private sectors.

The agenda of employment creation in the formal private sector should further be linked to the broader issue of structural transformation. Of course, the very act of transferring resources from the public to the private sector is an example of structural transformation, but this report moves beyond that and reflects on the role of industrial and sectoral policies, and that of pro-employment macroeconomic policies more generally, in promoting and sustaining priority sectors and

[4] Organisation for Economic Co-operation and Development (OECD), 2016. Stocktaking Report on MENA Public Procurement Systems.

industries and supporting decent and inclusive employment creation in the private sector. These policies not only need to focus on price and macroeconomic stability but should also target strong and sustainable employment generation.

(a) Fiscal policy

A well-known approach to fiscal policy is that the primary obligation of the Government is to contain debts and deficits in the long run within predetermined targets. Theoretically, this could represent a contrast from traditional Keynesian models, in which the primary issue is to design effective counter-cyclical fiscal policies to smooth business cycles. This focus on debt and deficit management also represents a contrast from traditional models of development finance in which the primary role of the Government in low- and middle-income economies is to engage in a sustainable resource mobilization strategy to support core development goals.

Internationally recognized benchmarks that guide fiscal policy include recommendations that the fiscal deficit should not exceed 3 to 5 per cent of GDP and public debt -o-GDP ratios should not exceed 60 per cent of GDP. This debt-to-GDP ratio worked in many countries, yet some countries failed to have a sustainable debt even with a deficit at 3 per cent or a debt-to-GDP ratio at 60 per cent. These anecdotes make any debt ratios and budget-deficit thresholds questionable and subject to more scrutiny as many factors might play a key role in determining debt sustainability.

Recently, there has been an increasing tendency across different parts of the world to use fiscal rules to reinforce the debt, and deficit, limiting the role of fiscal policy. An evaluation by the International Monetary Fund (IMF), using data for the 1985-2017 period, suggests that there are 96 countries that have adopted two or more fiscal rules pertaining to limits on various budgetary aggregates. There are also several countries that have instituted independent fiscal councils to oversee and monitor the implementation of fiscal rules.

The typical rationale for using fiscal policy for long-term control of debts and deficits is that such a role enhances the credibility of the Government in terms of maintaining macroeconomic stability. This, in turn, is expected to foster market confidence and, thus, promote private-sector growth and employment creation. Hence, fiscal policy is seen as a key instrument to support private-sector development.

The key question is whether fiscal consolidation will spur private-sector growth in the long term, especially given the contractionary consequences of such fiscal action. An optimistic view is that the confidence-boosting effects of fiscal consolidation might more than offset the short-term contractionary consequences. Underlying this optimistic assessment is the implicit assumption that fiscal multipliers are low or even insignificant in many countries in the Arab world. At the very least, this optimistic view maintains that the contractionary consequences of fiscal consolidation are so mild that they can be easily offset by the growth-promoting impulses of structural reforms, such as improved business climate and enhanced labour market flexibility. Evidence from Egypt and oil-importing countries of the region shows that these fiscal multipliers are indeed low,[5,6] but following the recent economic history of Arab economies, there is much to be debated on the long-term growth impact of liberal reforms.

It must also be remembered that fiscal consolidation in the Arab world has been juxtaposed with tight monetary and financial conditions with adverse implications for aggregate demand. As a result, there is no scope within the conventional macroeconomic stabilization package to spur growth unless it is assumed that

[5] Alnashar, S.B., 2017. Egypt's Government Spending Multiplier: Its Size and Determinants. Economic Research Forum Working Paper No. 1165.

[6] Cerisola, M.D. and others, 2015. Assessing the impact of fiscal shocks on output in MENAP countries. IMF.

structural reforms alone will offer an escape route. Not surprisingly, IMF and others recommend fiscal consolidation that is growth-friendly and equitable. This means using the fiscal savings released by containing current expenditure to support investment in infrastructure, health, education, and social protection.

There is a strong case for going back to the traditional tenets of development finance to guide fiscal policy. This means identifying spending gaps and financing needs based on a clear articulation of core development goals. Financing needs for the attainment of SDGs in emerging economies amount to approximately 4 per cent of GDP, but for low-income economies, this could be as high as 15 per cent of GDP, a relevant number for poorer parts of the Arab region.[7] How these spending gaps can be met on a sustainable basis should be the core priority of fiscal policy. This would mean striking the right combination of revenue mobilization, reallocation of expenditure, prudent borrowing, and external funding. Simply undertaking fiscal consolidation to meet debt and deficit targets by compressing public expenditure will yield a lot of pain without any measurable gain.

It remains to acknowledge that fiscal tools that explicitly target employment creation, including spending on active and passive labour-market policies, are key and yield better results than those that take it for granted that employment creation will automatically follow.

(b) Monetary policy for SMEs

The role of monetary policy in supporting private-sector development derives from the general principle that macroeconomic stability is an essential element of a growth- and employment-friendly business environment. While fiscal policy is given the task of maintaining macroeconomic stability by targeting debts and deficits, monetary policy conducted by an independent central bank should focus primarily or exclusively on maintaining price stability. In operational terms, it often takes the form of maintaining low single-digit inflation. The convention is to target an inflation rate of 2 to 3 per cent for developed countries. Monetary authorities in developing and emerging economies should aim for an inflation rate below 5 per cent.

Pertinent literature has shown that, when price stability prevails, it also coincides with full employment. Hence, the private sector at this point is fully utilizing all available resources. This is the hypothesis of the so-called non-accelerating inflation rate of unemployment (NAIRU). Given that NAIRU is not readily observable, a low single-digit inflation rate can be used as a suitable proxy. Maintaining low, single-digit inflation over the medium term is, thus, the best way to maintain conditions of full employment and, hence, support the private sector.

A parallel literature has examined the so-called growth-inflation trade-off. The idea is that there is a non-linear relationship between growth and inflation, with growth rising at moderate inflation rates, but beyond a certain point, higher inflation is associated with a lower growth rate. This allows to identify the threshold inflation rate. A key finding from the literature is that the threshold rate is around the 1 to 3 per cent mark for developed countries, but it is in the 6 to 12 per cent range for developing and emerging economies according to one study, just over 5 per cent according to another, and 8 per cent in yet another.[8] The implication is that aiming for low single-digit inflation for the developing world in a way that mimics the developed country standard is not necessarily conducive to growth and employment. Setting an appropriate inflation target really needs reliable and regular estimates of a threshold rate that is rooted in country-specific circumstances.

[7] Gaspar, V. and others, 2019. Fiscal Policy and Development: Human, Social, and Physical Investments for the SDGs, IMF Staff Discussion Note 19/03.

[8] Aydin, C., Ö. Esen and M. Bayrak, 2016. Inflation and Economic Growth: A Dynamic Panel Threshold Analysis for Turkish Republics in Transition Process. *Procedia – Social and Behavioral Sciences*, vol. 229, pp. 196-205.

These academic debates have implications for monetary policy in the Arab region. One analyst raised the question which level of inflation the central banks of Arab countries should aim for. The answer should be derived from the literature on the growth inflation trade-off.[9] The long-run inflation rate (from 1980 with projections to 2024) for the region as a whole is 9 per cent, but it would be prudent to aim a little lower, given the findings of a threshold rate noted above. There is also the central issue of designing and implementing a monetary policy framework that best supports a given inflation target. Inflation targeting regimes, guided by low single-digit inflation, have turned out to be highly influential. The policy rate is used in a countercyclical manner to maintain the target inflation rate over the business cycle. But could that be possible in the Arab world, especially since many countries have a pegged exchange rate and many others are in conflict?

A more rigorous econometric investigation by ESCWA corroborates this finding. The evaluation is extended to explore the comparative performance of pegged exchange rate regimes with more flexible arrangements.[10] The evidence is mixed, with pegged exchange rate regimes in Arab countries doing better than their flexible counterparts in some respects, including lower inflation, higher investment ratios, significantly better current account performance, slightly better growth, but higher unemployment. It may well be that “small and open developing economies are better served by a fixed exchange rate”,[11] as fixed exchange rates allow more policy certainty in terms of macro variables, especially during high levels of political uncertainties. The key challenge is to ensure that a commitment to the exchange rate as a nominal anchor does not impose a burden on the private sector through sustained episodes of real appreciation. Furthermore, even if a country seeks to move towards a floating currency regime, as Egypt did in 2016, the transition should be gradual and preceded by appropriate institutional reforms. Otherwise, the adjustment costs might be too high.

The discourse on the appropriate monetary policy/exchange rate mix perhaps assigns too much weight to the role that the exchange rate can play in enabling the private sector to engage in job creation in import-competing and export-promoting activities. The exchange rate certainly matters, but there are multiple factors that matter too in boosting trade performance in the Arab region. These include greater rationalization of tariffs and non-tariff barriers, investment in trade facilitation infrastructure, improved governance, and a talent pool that can support economic diversification. The handicap imposed on Arab countries because of the insufficient presence of these enabling factors cannot be fully compensated by even a well-managed exchange rate regime.

Finally, discussion of the appropriate monetary policy/exchange rate mix needs to go beyond a focus on macro variables and explore the extent to which monetary authorities can eliminate, or at least attenuate, binding constraints on the private sector, as revealed in enterprise surveys and the opinions of key informants from the business community. As noted, lack of access to finance is holding back enterprises in reaching their full potential. Enhancing financial access, or what is now known as financial inclusion, falls within the domain and mandate of monetary authorities. A discussion of this topic ensues in the following section.

In a pro-employment macroeconomic policy framework, targeting a single digit inflation rate is not enough. On the contrary, Governments need to develop their monetary policy in a way that supports SMEs and encourages investments,

[9] Khan, M., 2013. Is Inflation Hurting Growth in the Arab Transition Countries? *Atlantic Council* (March 12).

[10] ESCWA, 2018. *Survey of Economic and Social Developments in the Arab Region 2017-2018* (ESCWA/EDID/2018/1).

[11] Browne, C. and others, 1998. Fixed or Flexible? Getting the Exchange Rate Right in the 1990s. *Economic Issues*, No. 13. International Monetary Fund.

amongst others. This could not be done without facilitating concessional financing targeted to SME's, mainly to help them enhance productivity and grow in their number of employees' overtime.

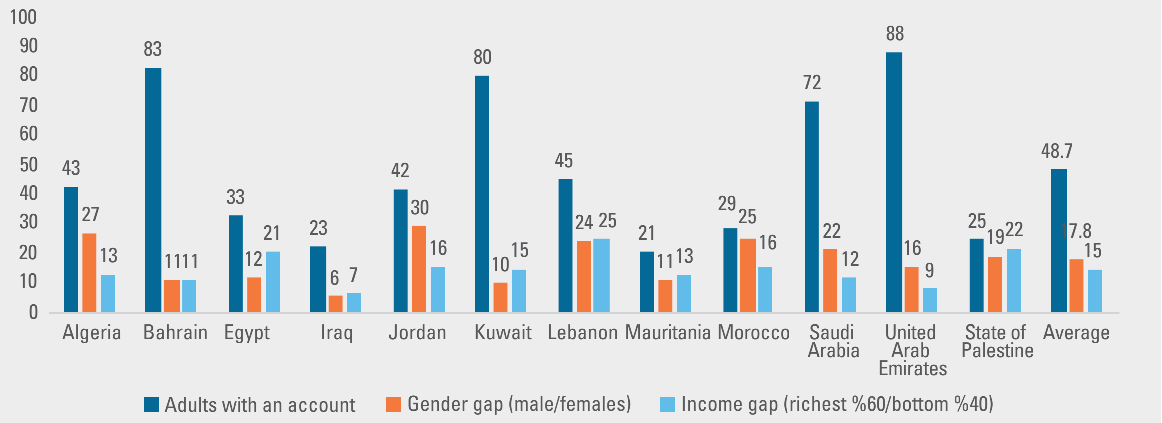
(c) Financial inclusion

Financial inclusion entails encouraging broader usage of bank accounts with formal financial institutions. Both theory and evidence suggest that financial inclusion can facilitate development.[12] One of the core indicators of financial inclusion is the level of ownership of bank accounts. This is the foundation upon which other elements of formal financial services, namely, digital payments, savings and credit instruments, and mobile phone banking, can be built. Globally, 69 per cent of adults (as of 2017) have a bank account.[13] Understandably, there is a big gap in account ownership rates between developed and developing countries, 94 per cent versus 63 per cent, respectively. There is also a significant gap within countries along income and gender dimensions.

Enhanced access for individuals, households and firms to the formal financial system contributes to poverty reduction by facilitating investments in health, education and business. It fortifies the capacity of individuals and households to cope with financial emergencies, such as job losses and crop failures. Digitalization of payments has also shown to reduce the incidence of fraudulent financial transactions.

How does the Arab region compare with the rest of the world in terms of bank account ownership? Figure 40 shows that the (unweighted) regional average is approximately 49 per cent, with a wide intraregional variation. The high-income GCC countries have account ownership rates that range from 72 per cent (Saudi Arabia) to 88 per cent (Qatar). For the non-GCC countries, ownership rates range from 21 per cent (Mauritania) to 43 per cent (Algeria). The gender and income divides in account ownership rates are quite significant in several Arab countries, such as Algeria, Jordan, Lebanon, and Morocco. Hence, the non-GCC countries lag well behind the developing country norm (63 per cent). There is considerable scope in the Arab region for increasing the degree of financial inclusion and reducing disparities along gender and income dimensions. If accomplished, this is likely to boost growth and employment, especially if SMEs become the beneficiaries of financial inclusion.

Figure 40. Bank account ownership in Arab States, 2017 (percentage)



Source: Extracted from Demirguc-Kunt, A. and others, 2018.

[12] World Bank, 2018a. Gains in Financial Inclusion, Gains for a Sustainable World.

[13] Center for Financial Inclusion, 2018. New Global Findex: 69 Percent of Global Population Is Banked.

Financial inclusion cannot only be studied from the perspective of individuals and households, but also from the perspective of firms. A firm-level analysis of financial inclusion is important given that the focus of this paper is on the drivers of private-sector development. As noted at a previous juncture, lack of access to finance is often regarded as a major constraint on business, especially SMEs.[14] Hence, if access to finance can be enhanced, it will boost the role of SMEs in creating jobs, diversifying economies and supporting growth. This is important because, in the Middle East and North African (MENA) region, SMEs account for 96 per cent of all firms in the formal sector and employ about 50 per cent of the workforce.

An econometric investigation, using pooled data for the MENA region, including Afghanistan, Pakistan and the Central Asian region, suggests that the level of economic development (using per capita income as a proxy), credit information availability for small firms (as measured by coverage of credit registries), the quality of governance (as indicated by control of corruption), the degree of economic competition (share of small firms in the private sector) and the quality of the business environment are key determinants of the financial inclusion of SMEs. The same investigation also shows that, if the financial inclusion gap in the region (as measured by the difference between the region and the best performing countries) can be eliminated, growth could, in some cases, be boosted by up to 1 per cent, potentially leading to about 16 million new jobs by 2025.[15]

What would an appropriate financial inclusion strategy look like? The central bank, in consultation with all pertinent stakeholders, cutting across Government ministries, the private sector, civil society associations and international organizations, should lead a national financial inclusion strategy (NFIS). A World Bank evaluation suggests that key success factors for an NFIS entail the following: sustained engagement with all relevant stakeholders; investment in data and diagnostics work; identification of national champions; clear articulation of objectives and targets; prioritization of actions; establishment of efficient and inclusive governance structures; mobilization of resources to support the launch of the NFIS; a clear communications strategy; flexibility to adapt the NFIS to changing economic circumstances; and a well-resourced and robust monitoring and evaluation system to track implementation progress.[16]

In the Arab region, Jordan was the first country to develop an NFIS.[17] The Central Bank of Jordan developed the NFIS in alignment with the SDGs together with the Government, the private sector, civil society, and other key stakeholders. The aim to enhance financial inclusion in Jordan, which currently is a laggard based on international comparators, includes a focus on SMEs, women, other vulnerable groups (most notably refugees), microfinance, digital financial services, financial literacy, consumer protection, and consolidation of credit bureaus, which should be able to assess the credit ratings of SME borrowers. Other countries in the Arab region will hopefully learn from the experience of Jordan that financial inclusion must be a core part of the agenda of private-sector development.

(d) Pro-employment sectoral and industrial policies for improved diversification efforts

Promoting the creation of decent employment through a strategy of private-sector growth requires a set of policies aimed at improving the quality and quantity of jobs created in this sector.

[14] SMEs are defined as those employing less than 100 workers. Small firms are defined as those employing less than 20 workers.

[15] International Monetary Fund (IMF), 2019. Financial inclusion of small and medium-sized enterprises in the Middle East and Central Asia. Middle East and Central Asia Department. Departmental Paper No.19/02.

[16] World Bank, 2018b. Developing and Operationalizing a National Financial Inclusion Strategy, Executive summary (June), p. 2.

[17] Alliance for Financial Inclusion (Afi), 2017. Jordan launches NFIS, first in the Arab region (December 4).

Further to the labour and social policies which are discussed in detail in this chapter, clear employment targeting of macroeconomic policies and the investment in priority sectors that are most capable of generating decent employment opportunities are key.

More particularly, economic diversification that promotes productive employment should be prioritized. Up to date, employment and economic growth in the Arab region continue to be concentrated in a number of low-productivity informal sectors. Structural transformation can instead be achieved through well thought-out industrial and sectoral policies that identify priority sectors with high potential for growth and decent job creation as those that have been identified in chapters 2 and 3. These policies aim to ultimately change the structures of the region's economies and move towards high-value added sectors with high-productivity and great employment growth potential.

To sum up, private-sector policy design should focus not only on country-specific factors but also on sector-specific conditions, without generalizing a policy approach as different countries have different initial conditions and resources as well as diverse levels of sectoral development and growth along with varying overall socioeconomic conditions. As shown in a recent ESCWA paper which applied a computable general equilibrium model to test the viability of a long-term structural transformation scenario of the Egyptian economy,[18] achieving long-term favourable and synergistic productivity, employment and growth outcomes is possible, provided the following:

- First, for a more effective innovative process, Governments should make appropriate interventions with rule-based policy discipline.[19] To promote diversification and advancement, developed nations use several support methods, including encouraging patent systems and large public procurements, investing in R&D and new infrastructure and boosting educational institutions and private enterprises, amongst others;
- Second, Governments should exert more efforts to encourage FDI and private investments in sectors such as manufacturing and services, which contribute the most to the economy and have high export-growth potential. Preferential credit schemes, tax exemptions and/or concessional long-term land lease agreements as well as partnership agreements with other countries (China specifically) are ways to achieve this. However, a coordinated trade and industrial policy strategy is required to guarantee that such methods are in line with the policies of trade agreements, including with the World Trade Organization. To add, non-traditional commodity exports are increasing. Even though their present contribution to the trade balance and to growth is low, they have a significant positive outlook;
- Third, Arab countries should use their public funds more effectively. Export-focused SME projects should be paired with investments in capacity-building in innovative sectors and in renewable energy and water security, particularly in green economy developments. This can raise the profitability of public investments, alleviate poverty and reduce scarcity of two major resources. The economy can be positively impacted in the long term, with an increased efficiency and crowding-in of public and private investments if the above projects are performed simultaneously with additional governance improvements and a fair taxation policy.

[18] ESCWA, 2019a. Egypt: From Stabilization to a Knowledge-based Economy: A Computable General Equilibrium Modelling Approach (E/ESCWA/EDID/2019/WP.2).

[19] According to Hausmann and Rodrik, interventions tend to create market distortions. By imposing policy disciplines, such as encouraging investment in the modern sector beforehand, and by rationalizing production afterwards, Governments can counteract possible distortions. See Hausmann, R. and D. Rodrik, 2003. Economic development as self-discovery. *Journal of Development Economics*, vol. 72, Issue 2, pp. 603-633.

In summary, Arab Governments need to rethink their current economic policies and target the employment of skilled labour along with the generation of more inclusive growth.

3. Labour and social policies to support the private sector: responding to the dual challenge of creating jobs and reducing decent work deficits

The agenda of private-sector growth and employment in the Arab countries includes both quantitative and qualitative dimensions. A previous discussion noted the scale of the employment challenge in the Arab world, namely, the need to create well over 100 million jobs by 2030. This challenge is compounded by the fact that the jobs agenda in the Arab region must cope with large-scale decent work deficits, not just in conflict-affected countries but also in more "normal" nations. This pertains to the high youth unemployment rate and the number of youth not in education, employment or training (NEET), in addition to high overall unemployment, deeply entrenched gender disparities (particularly in the sphere of employment and labour force participation), extensive presence of both income and non-income dimensions of poverty in many Arab countries (especially among the LDCs), persistence of informality, inadequate social protection coverage, heavy reliance among the oil-rich and affluent Gulf States on low-skilled and low-wage migrant labour, and unsatisfactory education and learning outcomes leading to significant skills mismatches.

(a) Formalization and expansion of social protection

Closely linked to the issue of private-sector development is the issue of formalization. The transition from the informal to the formal sector, along with broader efforts to support decent employment creation in the private sector, can complement the above-mentioned approaches of structural transformation and economic diversification, especially in countries where nationals continue to prefer working in the public sector because of the better working conditions that the latter offers. More particularly, Arab States need to develop an integrated framework that aims to address the various decent work deficits based on a proper assessment of their national contexts.

Against this backdrop, expanding social protection coverage becomes key to providing adequate protection from rising poverty and vulnerability in the region and to fulfilling the fundamental human right to social security. Up until now, most social insurance schemes in the Arab region cover only public- and private-sector workers with regular contracts, while other categories of workers, such as those operating in the informal economy, are excluded. Furthermore, most Arab States offer subsidies on goods, notably for fuel and food, without sufficiently benefiting the most vulnerable groups of the population.

That said, Arab States should first and foremost consider the implementation of national social protection floors to provide basic social security guarantees, including at least the following:

- Access to essential health care, including maternity care;
- Basic income security for children, providing access to nutrition, education, care, and any other necessary goods and services;
- Basic income security for persons in active age who are unable to earn sufficient income, in particular in cases of sickness, unemployment, maternity, and disability;
- Basic income security for older persons.[20]

Progressive achievement of higher levels of protection should also be pursued within a comprehensive social protection framework and comprehensive social security systems. Further emphasis is also placed on the need for adequate social protection coverage as non-standard forms

[20] ILO (n.d.). Social Security in the Arab States.

of employment, including in the gig and platform economy, become increasingly important in the current and future labour markets, necessitating adoption of innovative regulations and mechanisms to protect all workers and individuals.

(b) Review of labour regulations and minimum wage policies

Excessively onerous labour regulations are an obstacle to business operations, and there is a case for amending labour legislation in a nuanced and targeted manner while ensuring the implementation and enforcement of applicable legislation. Additional employment creation requires revising labour regulations to support inclusiveness and fairness in the labour market and accommodate more workers, including women. In this regard, labour regulations could be made more gender-friendly in order to reduce gender disparities. Generous redundancy packages that impose a burden on firms could be reduced and offset by a well-designed and incentive-compatible unemployment benefits scheme. Minimum wages could be applied in countries where they are either limited to the public sector or restricted to nationals.[21]

The approach adopted here is to focus on the notion of labour market inclusion and how appropriate policies that cut across labour regulations, social protection, education, and training, including active labour market policies, can attenuate decent work deficits, thus boosting the quality of employment in the Arab region. For instance, a well-established method of assessing the strictness of labour regulations is to make use of the OECD's Employment Protection Legislation (EPL) Index, which considers legislative protection pertaining to permanent workers as well as restrictions on temporary employment. The higher the value of EPL (range 0-6), the greater the restrictive nature of labour regulations. Saudi Arabia and Tunisia generally lie below global benchmarks. Hence, in these countries, labour regulations do not appear to be stricter than international norms. Nevertheless, as previous discussion has noted, labour regulations are perceived by the business community in the Arab region to be a constraint on business operations. Here, the question arises from a purely economic perspective as to whether widespread liberalizing of labour markets, including, for instance, the removal of obligations to pay minimum wages, would boost employment in the private sector.

Starting with minimum wages, they exist in many Arab countries, but often only for the public sector or only for nationals (Bahrain, the United Arab Emirates, Saudi Arabia are good examples). One could raise the question whether there a case for using minimum wages as a general labour policy instrument rather than limiting it to the public sector or nationals of a country. The standard rebuttal is that minimum wages applied across the board will create disincentives for private-sector employment. However, the employment effects of minimum wages have been intensively studied and a rigorous meta-analysis shows that minimum wages have had little detectable impact on employment. While more vulnerable groups appear to be more adversely affected by minimum wage rises, the effects tend to be small on average.[22] The evidence suggests that a well-managed minimum wage policy through statutory minimum rates or collectively bargained wage floors can be effective at improving the wages of low-paid workers without any negative effects on employment rates.

Of course, minimum wage policies need to be combined with complementary measures, such as education and skills policies and ALMPs, to tackle the problem of low-wage employment. Nevertheless, the Enterprise Survey evaluation, combined with the meta-analysis of the minimum wage-employment nexus in emerging economies, are highly relevant to the case of those Arab

[21] WEF and World Bank, 2018. *Arab World Competitiveness Report 2018*.

[22] Broecke, S., A. Forti and M. Vandeweyer, 2017. The effect of minimum wages on employment in emerging economies: A survey and meta-analysis. *Oxford Development Studies*, vol. 45, Issue 3, pp. 366-391.

countries in which there is significant incidence of low pay and working poverty. A reduction in working poverty, while desirable, can also boost aggregate demand by enlarging the size of the domestic market and becoming a new source of job creation.

An unemployment benefits scheme, which would lead to a reform of redundancy packages and shift the financial burden of unemployment benefits from enterprises to the Government, might not be well received in a region struggling with fiscal consolidation. However, it remains desirable and may be justified by the argumentation that budgetary savings engendered by general fiscal reforms should be used to support labour market policies that have a direct bearing on the welfare of workers, while reducing the burden on job-creating enterprises.

Labour regulations in the Arab countries are also not gender-friendly. This is particularly important given the large gender disparities in the labour market. Examples include bans on night work for women (except for the health sector), moderate provisions for maternity leave and a paucity of provisions for paternity leave. Amending these regulations and combining them with such initiatives as providing on-site childcare facilities might provide an incentive to boost women's employment in the private sector.

(c) Promoting gender equality and women's empowerment

Despite efforts to promote gender equality and non-discrimination in the labour market, Arab women continue to have particularly high unemployment rates coupled with low labour force participation rates. This requires more than simple supply-side interventions, as unemployment is largely due to a lack of demand for high-skilled workers and the inadequate working arrangements in the private sector, which also constitute important factors behind women's discouragement from joining the labour force. In addition, increasing the safety of public transport and improving working conditions for women, including through the provision of childcare and maternity benefits, are essential to attract skilled women into the labour force. However, with the lack of demand for such skills, the root cause of the problem is found to persist. Against this backdrop, Government interventions need to focus on generating such demand, without disregarding the importance of enhancing skills and removing supply-side bottlenecks.

Overall, and building more directly on the findings of chapter 3, improving women's labour market prospects necessitates addressing gender disparities, first by challenging prevalent sociocultural perceptions to allow women's labour mobility and access to the full range of economic sectors, including capital-intensive fields, and, second, by reforming labour laws to encourage female economic participation and employment in the private sector. Labour law reforms, as mentioned earlier, should focus on the provision of maternity benefits, while taking into consideration the financial burden imposed on private-sector employers. Private entities can encourage women's economic participation by establishing their internal maternal and paternal leave schemes. The provision of paternity leave and childcare benefits may help women maintain a work-life balance and attain shared responsibilities within the household and family, as articulated in SDG 5.4. The recent pandemic has also re-emphasized the role of teleworking and remote arrangements as viable work solutions, which would also allow women, as employers or employees, to balance between their work and family responsibilities.

Further to the above, women continue to face critical obstacles in climbing their career ladders. The private sector should enhance its internal pipelines for promotions such that women and men stand an equal chance to attain senior positions. The analysis further shows that promoting female entrepreneurship and leadership could have multiple positive ripple effects, particularly in terms of increasing female employment and career-advancement opportunities, as well as contributing to overall employment and wealth creation in the aggregate economy.

It is, therefore, necessary to create a suitable business environment and ensure women's financial inclusion to promote growth-oriented entrepreneurship and reap the overall socioeconomic benefits. Financial intermediaries could support female entrepreneurs by providing access to credit so that women-owned firms may grow to their full potential, increase their productivity and create job opportunities. It should be noted that the promotion of businesses run by women complements, but does not substitute, the need to address women's employment across the private sector in its entirety, especially given that women's entrepreneurship is still comparatively low in the Arab region.

(d) Reforming education and training and developing effective active labour-market policies, particularly for the youth

Executive opinion surveys show that a lack of an adequately educated and trained workforce represents a handicap for the private sector, especially in some Arab countries. This reinforces the evidence that students from the Arab region exhibit unsatisfactory learning outcomes, according to international benchmarks. The recently launched Human Capital Index (HCI) of the World Bank, and applied to Arab countries, corroborates this finding. This suggests the need to reform education and training so that students are endowed with the right mix of cognitive and non-cognitive skills to meet the needs of the labour market.

The 2019 Arab Youth Survey corroborates the above findings. Some 75 per cent of young Arabs are unhappy with the quality of their education and more than 50 per cent would like to pursue higher education in the West.[23] As has been noted, enterprise surveys in the Arab region usually show that the lack of adequately trained workers is constraining the capacity of the private sector to expand, although this is not always among the highest concerns of businesses. Perceived skill shortages co-exist with high unemployment among young people. This is, of course, a manifestation of skills mismatches. The standard view is that young graduates in the Arab region are keen to acquire skills that they believe will lead them to secure employment in the public sector and invest in rote learning to compete in examinations designed to screen applicants. Given these salient features of the education and training system, the core elements of a policy agenda can be sketched as follows:

To start with, key weaknesses of the education and training system, namely, low completion rates, especially at the primary level, and unsatisfactory learning outcomes, need to be addressed with a holistic policy package. This would entail overhauling the curriculum, inculcating creative and critical thinking, raising competency in STEM subjects, and investing in teacher training and facilities, together with much greater involvement of business in curricula design and delivery and greater investment in career counselling and guidance. This might require either higher levels of funding for education and training or more efficient use of existing resources, or both. At the very least, such a policy agenda should be supported by a rigorous analysis of spending needs, taking into account the need to alleviate the skills mismatches that hold back private-sector development.

For those in the workforce who are seeking to improve their employability, ALMPs focused on training and job search are pertinent. Developing economies generally spend about 0.50 per cent of GDP on ALMPs. While relevant up-to-date data are not available for Arab countries, it is suspected that these countries are unlikely to spend much more than

[23] ASDA'A BCW, 2019. Arab Youth Survey, p. 8.

the global norm.[24] International experience suggests that jobseekers benefit from in-class technical training combined with work experience acquired through internships and apprenticeships. Training programmes that combine technical skills with non-cognitive skills (reflecting interpersonal attributes) seem to help in enhancing the employability of trainees.

Governments in the region should ensure that there are adequately resourced employment services that rely on both public and private providers. The primary responsibility of these services is to support jobseekers with a full range of services, such as counselling, training, information about job opportunities, and job search assistance. Digitalization of employment services is desirable.

There is the issue of whether Governments in the region should support entrepreneurship training as part of their repertoire of ALMPs, especially given the challenge of creating wage employment through existing firms. This has turned out to be a popular option with the international community, including the ILO, which provides considerable support. Impact evaluations of ALMPs, including entrepreneurship programmes across the world, indicate how effective these proposed interventions have been in the past and are likely to be in the future, both in the Arab region and elsewhere. The appropriate lesson to be learned is that ALMPs have a role to play but must be implemented in conjunction with broader economic and social policies.

D. Conclusion

The Arab region is often prompted towards structural reforms to improve the business climate mainly by reducing the regulatory burden on the private sector within the framework of fiscal consolidation. However, there is a caveat of limitations that can be addressed by labour market inclusion, which bridges labour regulations, social protection, education, and training. Along with ALMPs, these labour market inclusions can attenuate decent work deficits, thus boosting the quality of employment in the region. Nonetheless, labour regulations aimed at enhancing or promoting inclusion and changes to social protection systems are important for reducing formal work deficits. Slow growth, cyclical unemployment, poverty, vulnerability, and informality, along with low female participation in the workplace, the proliferation of conflicts, the COVID-19 pandemic, and the digital disruption associated with the 4th Industrial Revolution have devastatingly fragmented the economic environment. With 75 per cent of young Arabs unhappy with the quality of their education and more than 50 per cent seeking to emigrate to the West,[25] a lack of resolve will only perpetuate an already unhealthy economic environment for young professionals seeking to grow (and further diminish female participation in the workforce).

In the Arab region, fiscal consolidation has been confined by limited monetary and financial conditions. These constraints, combined with adverse implications for aggregate demand, do not grant the necessary conditions for conventional macroeconomic stabilization, economic growth and decent job creation. Furthermore, structural reforms on their own cannot be counted on to solve preexisting structural issues in the region. Employment challenges are both quality- and quantity-related and should therefore be

[24] World Bank, 2019. *MENA Economic Update: Reforms and External Imbalances: The Labor-Productivity Connection in the Middle East and North Africa*, p. 36.

[25] ASDA'A BCW, 2019, p. 8.

addressed using the right mix of policies aimed at creating more and better jobs for all, including for the most vulnerable groups. Unlocking the potential of the private sector in the region to actually drive economic growth and decent employment creation is key, especially with increased pressures on Government budgets to address challenges brought by the recent pandemic and other preceding regional shocks that have impacted employment over the past decade. Only by revisiting the development model followed by Arab countries in a way that allows for enhanced productivity and increased decent work will the region be better positioned to achieve its development goals. Such efforts need to take into account the additional challenges brought by the future of work and the new emerging forms of employment, including, for example, the gig economy, which the COVID-19 pandemic has only accelerated.