THE ROAD TO HIGHER AND MORE INCLUSIVE GROWTH IN THE MIDDLE EAST AND NORTH AFRICA

Despite recent gains, regional growth remains too low and the benefits are shared by too few. Average incomes are stagnant, and poverty is rising in areas of conflict. Frustration runs high over the lack of job opportunities and access to affordable, high-quality public services. The call during the 2014 Amman Conference[1] to generate robust growth, create jobs, provide equal opportunities, and protect the vulnerable remains relevant today.

The recent growth gains in the region and upswing in the global economy offer an opportunity to implement reforms that enhance medium-term growth prospects and benefit all. Fiscal policies should support growth-enhancing activities and promote opportunity for all through more efficient and effective social spending, fair and well-targeted taxes, and support for the vulnerable. Labor market policies need to foster job creation and give all men and women equal opportunities to work. Private sector development requires well-functioning financial systems and regulations that create a level playing field for business to thrive. Good governance and transparency are essential to give all citizens greater voice. The "Opportunity for All" conference will discuss ***how*** *the region can propel and scale up reform implementation.*

This overview note provides context for that discussion, summarizing how the region performs on indicators of inclusive growth, what reforms are underway, and what measures are still needed to ensure economic opportunity is shared by all. This note is accompanied by three companion pieces that set out in greater depth key facts about job creation, excluded groups, and how fiscal policies aimed at supporting inclusive growth in the region are progressing.[2] They explore the drivers of outcomes and share country experiences in implementing reforms in these areas. They also set out policy priorities that could move the dial on inclusive growth reforms from endorsement to more effective execution.

[1] The May 2014 Amman conference "Building the Future: Jobs, Growth, & Fairness in the Arab World" was co-hosted by the Jordanian government, the Arab Fund for Economic and Social Development and the IMF. It provided an opportunity for regional policy dialogue on the core elements of an economic vision for strong and inclusive growth, including by drawing lessons from episodes of economic transformation in other parts of the world.

[2] These papers were prepared under the general guidance of Aasim Husain and Adnan Mazarei. The team was led by Catriona Purfield, Harald Finger and Karen Ongley and comprised Bénédicte Baduel, Carolina Castellanos, Alexei Kireyev, Gaëlle Pierre, Vahram Stepanyan, Erik Roos and Jorge De Leon Miranda with inputs provided by Magali Pinat and reviewed by MCD country teams. The papers also benefitted from excellent inputs from COM, FAD, ICD, SPR, and STA. The authors are grateful for the assistance provided by Esther George and Olivier Lamy.

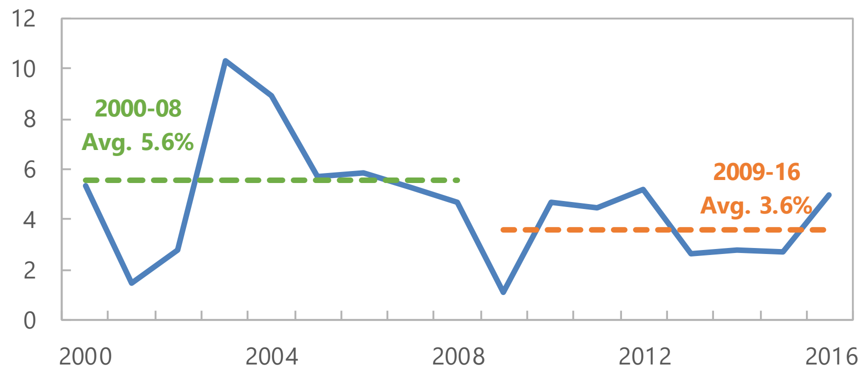
Groupings and Abbreviations: Countries are grouped into MENA Advanced Countries (MENA AD); Bahrain (BHR), Kuwait (KWT), Oman (OMN), Qatar (QAT), Saudi Arabia (SAU), and United Arab Emirates (UAE), MENA Emerging Markets (MENA EM); Algeria (DZA), Egypt (EGY), Iran (IRN), Iraq (IRQ), Jordan (JOR), Lebanon (LBN), Libya (LBY), Morocco (MAR), Tunisia (TUN) and West Bank and Gaza (WBG); and MENA Low-Income Countries (MENA LIC); Afghanistan, Djibouti (DJI), Mauritania (MRT), Pakistan (PAK), Sudan (SDN), Somalia (SOM), and Yemen (YMN). Syria has been excluded due to lack of data.

Is Growth in the Region Sufficiently High?

Persistently weak growth…

Despite a period of robust growth in the mid-2000s, the region experienced lackluster growth for much of the past decade. Growth was hard hit by the global financial crisis and has since been affected by a series of factors: the slowdown in trading partners' growth, the fall in oil prices from 2014, protracted regional conflicts, as well as a longer-term trend of stagnant or declining productivity in countries across the region. Although average regional GDP growth ticked up in 2016, the average growth rate since 2009 has been one-third slower than the average during 2000-08, and less than half its 2003 peak.

MENA Real GDP Growth
(Percent change)

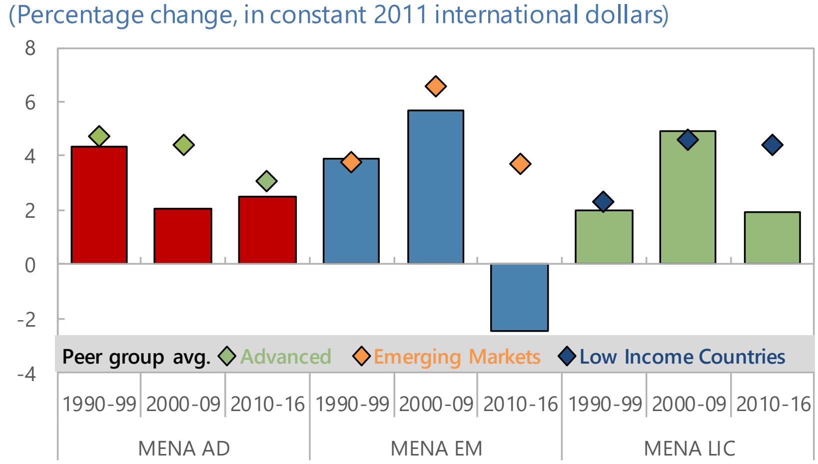


Sources: National authorities; and IMF staff calculations.
Note: The regional average is weighted by purchasing power parity adjusted GDP.

….has left incomes stagnant…

Average income per person stagnated during 2013-16, growing by only 0.8 percent per annum. This further exacerbated the gap in incomes that had emerged with peers in the previous decade.

GDP Per Capita Growth
(Percentage change, in constant 2011 international dollars)

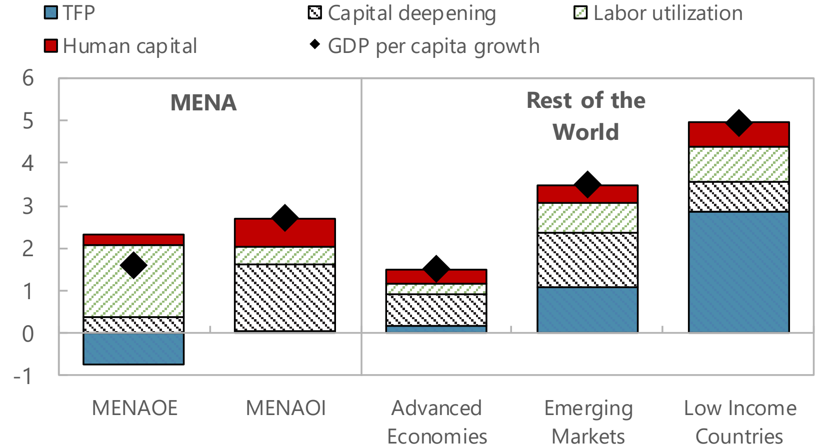


Sources: National authorities; and IMF staff calculations.

The region needs bold reforms to boost growth

To take advantage of the rebound in global growth, the region needs reforms to increase the efficiency of capital investment and improve productivity. This would reverse the drag on growth from low employment, inefficient investment, and low productivity (TFP) witnessed in the last decade.

Decomposition of Real GDP Per Capita, 2000-14
(Annual average, percent)



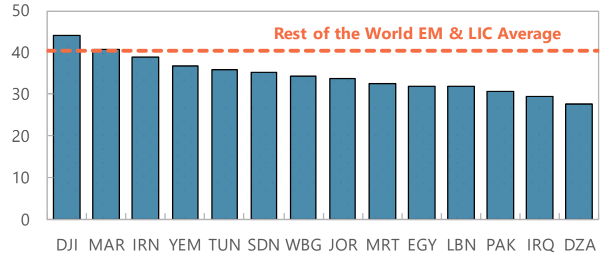
Sources: Dabla-Norris et al., 2013.
Note: MENAOE corresponds to DZA, BHR, IRN, IRQ, KWT, LBY, OMN, QAT, SAU, ARE and YEM; MENAOI corresponds to AFG, DJI, EGY, JOR, LBN, MRT, MAR, PAK, SOM, SDN, SYR and TUN.

Is Growth in the Region Inclusive Enough?

Growth has not benefitted all…

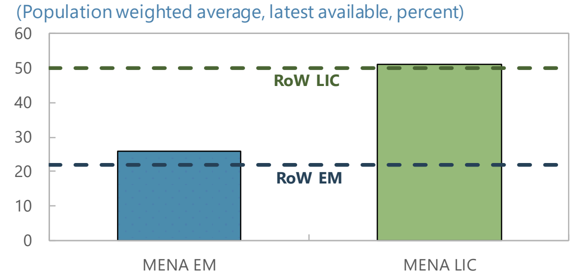
On the surface, regional indicators of poverty and inequality appear modest. Income inequality—measured by the Gini coefficient—ranges from a low of 0.28 in Algeria to a regional high of 0.44 in Djibouti, generally below peers. The middle class represents a significant share of populations, but where data is available its expansion has been slower than in other regions (IMF 2014). The reported rate of extreme poverty (living on $1.90 a day) is low. However, the United Nations Development Program shows 26 to 51 percent of MENA EM and LICs populations live in poverty when measured in multidimensional terms. Poverty also runs high in rural and disadvantaged areas. The Food and Agriculture Organization of the United Nations (2007) estimates that almost 60 percent of the poor in Algeria, Egypt, Morocco, Sudan, and West Bank and Gaza live in rural areas. Poverty is rising sharply in countries in conflict: Iraq, Libya, Syria, and Yemen.

Gini Coefficient for MENA Countries
(Percent, latest available value)



Sources: World Bank, and IMF staff calculations.

Population Living in Multidimensional Poverty
(Population weighted average, latest available, percent)



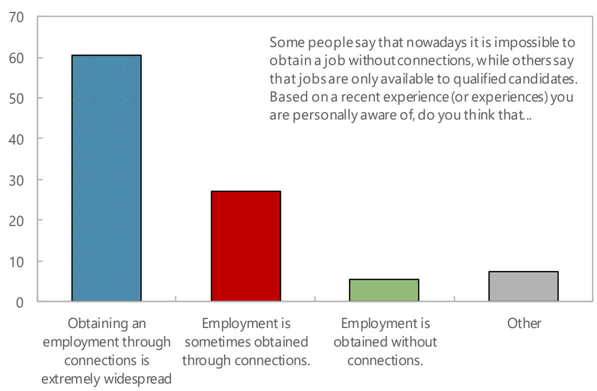
Sources: United Nations Development Programme, Multidimensional Poverty Index.
Note: MENA AD countries were excluded due to data availability. Multidimensional poverty captures poverty experienced across three dimensions of health, education, and standard of living.

...and unequal access to opportunities, public services and jobs is a concern

Citizens in the region are concerned about inequality of opportunity and access to public services. The Arab Barometer survey shows that 70 percent of citizens think that "the government is doing bad or very bad at narrowing the gap between the rich and the poor." Additionally, 60 percent think that "their government is not doing enough to improve basic health services." Three out of five also perceive that connections—or *wasta*—determine success in finding a job.

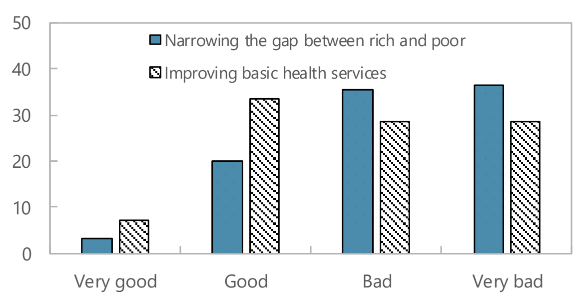
There are significant gaps in access to essential public services and finance. Access to improved sanitation is 10 percentage points lower in rural areas of the region (83 percent) than in urban areas. In Egypt, Morocco, Yemen, and Syria, children in the bottom 20 percent of the income distribution are chronically malnourished. A child in rural upper Egypt is 3.4 times less likely to go to primary school than its urban sibling. Seventy percent of the region's adults do not have a bank account.

Access to Employment: The Role of Connections
(Percent of total respondents)



Sources: Arab Barometer III.

Perception of Inclusiveness: Governments' Efforts At...
(Percent of respondents)

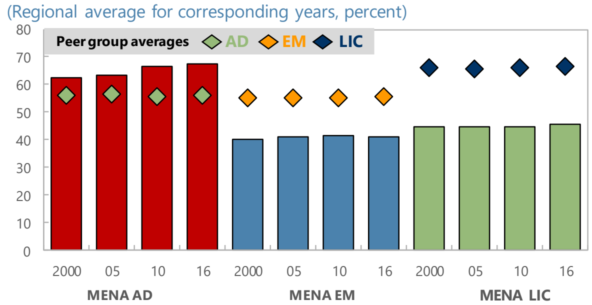


Source: Arab Barometer III.
Arab Democracy Barometer was fielded from 2012-2014 in 12 countries: DZA, EGY, IRG, JOR, KWT, LBN, LBY, MAR, SAU, SDN, TUN, and WBG.

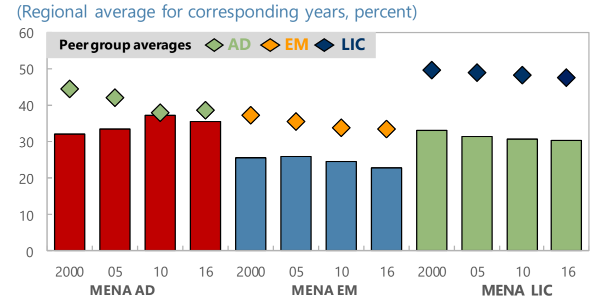
Growth has also failed to generate enough jobs

The region faces some of the lowest rates of employment globally. Less than one in every two adults work. In large part, this reflects low participation by women, who are three times less likely than men to be in the labor force and nearly twice as likely to be unemployed. Each percentage point of growth in the region has generated a rise in employment of 0.25 percentage points in the region's oil exporters and 0.39 percentage points in its oil importers, in line with other EMs and LICs but far below levels needed to employ a growing young population.

Employment to Age 15+ Population
(Regional average for corresponding years, percent)



Youth Employment to Youth Population
(Regional average for corresponding years, percent)



Over 27.6 million young people will enter the workforce over the next 5 years

The region also faces high rates of unemployment, particularly among young people. In 2016, unemployment in the region stood at 10.6 percent, and some 25 percent of the region's youth were unemployed. The 2017 Arab Youth Survey (ASDA'A Burson-Marsteller) reveals that 35 percent of Arab youth see unemployment as the biggest obstacle facing the Middle East.

With over 60 percent of its population under the age of 30, the region desperately needs higher growth and more jobs. The most recent International Labour Organization estimates show that some 5.5 million youth will enter the labor force every year in the next 5 years.

Creating job opportunities will spur growth

The region's young men and women hold huge potential to spur growth if given opportunities. If the region could generate an additional 0.5 percentage points of employment growth per year, real GDP growth would rise to 5.5 percent per annum and real per capita income would rise annually by 3.8 percent. However, if the region continues to grow and generate jobs at the current pace, unemployment would reach 14 percent by 2030 and labor force participation would not change.

Policy Priorities to Promote Opportunity for All

Promoting inclusive growth requires a broad set of reforms

Establishing the conditions for the private sector to thrive and create jobs requires macroeconomic stability. But countries must also pursue a critical mass of reforms to remove the constraints to growth and diversify economic structures. In consultation with their citizens, MENA governments will need to prioritize reforms, ensure a sound implementation of policies, and protect the most vulnerable or those adversely impacted by reforms.

The IMF has stepped up efforts to support countries' inclusive growth reforms

Over the past few years, the IMF has engaged MENA countries on the Inclusive Growth (IG) agenda through policy diagnosis and capacity building in the IMF's core areas of expertise. Article IV consultations covered issues such as women's economic empowerment and inequality in Djibouti, Iran, Jordan, Mauritania, Morocco, Pakistan, and Sudan. In programs, initiatives to address IG challenges and better protect the vulnerable from the impact of reforms included social spending floors, higher budget resources for child care services, or support of anti-corruption measures in Afghanistan, Egypt, Iraq, Jordan, Pakistan, and Tunisia. The Middle East Technical Assistance Center in Lebanon supported inclusive growth reforms in Algeria, Egypt, Jordan, Iraq, Jordan, Lebanon, Morocco, and Sudan. The IMF Middle East Center for Economics and Finance (CEF) in Kuwait offers training on inclusive growth theory and policies.

Faster progress and deeper reform is still required to improve the quality and equity of public services and taxes …

As outlined in the companion piece MENA citizens want better public services and to narrow the gap between rich and poor, fiscal policy is a key lever for governments to ensure that the benefits of growth are shared more broadly. Reforms are needed to raise the quality of, and broaden access to, public education, health, and essential infrastructure services and safety nets for the vulnerable. Creating space for higher social and investment spending will require far broader and more equitable taxation. Greater transparency and citizen participation would help tackle corruption.

…foster private sector development…

Unlocking the potential of MENA people highlights the need for a comprehensive approach to job creation grounded in reforms to diversify and develop the private sector. This requires an improved business and regulatory environment, better access to finance, and a level playing field for small firms to compete with larger firms and state-owned enterprises. Policies to attract foreign investment, promote innovation, and better integrate MENA into global trade networks would leverage the impact of reforms. A vibrant private sector requires an adaptable and skilled workforce to emerge from countries' education and training systems.

...tackle corruption and ensure equal opportunity for women, youth, rural communities, and refugees.

In Enabling inclusion in MENA, the case is made for interventions to address corruption, financial inclusion, and the obstacles facing youth, women, rural communities, and refugees. Strong institutions and greater transparency, the foundation of effective and accountable governments, can foster public trust in reforms. Fintech, microfinance, and Islamic banking would promote financial inclusion. Expanding opportunities for women requires equal legal rights and the provision of maternity protection, child care facilities, and safe transport. Public service provision to rural communities must improve. Host communities need assistance to meet the costs of integrating refugees.

MENA countries have plans to promote inclusive growth

Countries in the region have placed inclusive growth and job creation at the forefront of their national development plans and strategies, as described in Box 1. These plans promote higher growth, job creation, and inclusion through greater private sector participation, economic diversification, and better targeted fiscal policies.

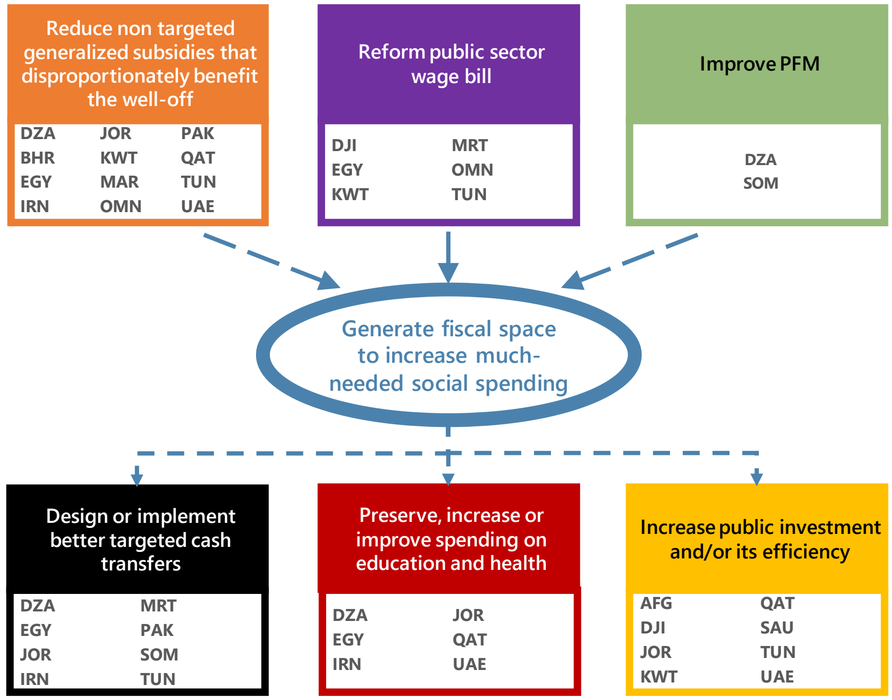
Countries are creating space for higher, more effective social and investment spending...

On the fiscal front, efforts are being made to scale up (or preserve where fiscal consolidation is needed) and improve the efficiency of social expenditures, especially in education and health so that they can better target the vulnerable and improve outcomes. Measures are also being implemented to improve the efficiency of public investment. Afghanistan and Morocco are implementing gender budgeting; Egypt has plans to implement it in 2018/19.

Still, social spending in the region (11 percent of GDP) remains low relative to peers. Only one-fifth of the region's social transfers go to the poorest 40 percent. Much more progress is needed to improve the quality of public services and broaden access.

In lower income countries or those experiencing conflict or fragility, support from the international community is urgently needed to finance humanitarian relief, social expenditures, and reconstruction costs. The World Bank estimates the damage from conflict in Libya, Syria and Yemen at about US $300 billion.

Countries creating fiscal space by reorienting spending



Source: Surveys to IMF MENA staff.

...through spending reforms...

Many are phasing out poorly targeted generalized fuel subsidies to free up resources and put in place better targeted cash transfer programs and increase other social outlays to better protect the most vulnerable. Twelve countries in the region have started or finalized fuel subsidy reforms, resulting in fuel subsidies being halved to 2.2 percent of GDP since 2010. Egypt is raising the coverage of targeted cash transfers to 2 million households in 2017/18 from 160,000 households two years ago.

... and by advancing towards collecting more revenues in an equitable manner

Countries are also taking steps to raise revenues to fund their social and investment needs. Egypt has introduced a VAT, joining some 140 countries worldwide who have one. Several GCC countries are implementing a VAT in 2018. In introducing the VAT, countries have sought to protect lower income households by excluding basic food items and setting the registration threshold to exclude smaller businesses. Countries are also broadening the capital gains tax on real estate (Djibouti) or exempting the lowest income earners from income tax (Tunisia, Djibouti).

Still, the region’s tax revenue-to-GDP ratio of under 10 percent remains low. There is scope to raise more revenues to fund inclusive growth reforms in many countries. The region needs to tackle tax evasion, close loopholes, increase progressivity, and exploit the untapped potential of property and wealth taxes. The distributional impact of tax measures and the transfers they fund needs to be fully assessed to ensure fairness and better protect the vulnerable. This will require better fiscal and household survey data.

Countries creating fiscal space by increasing revenues

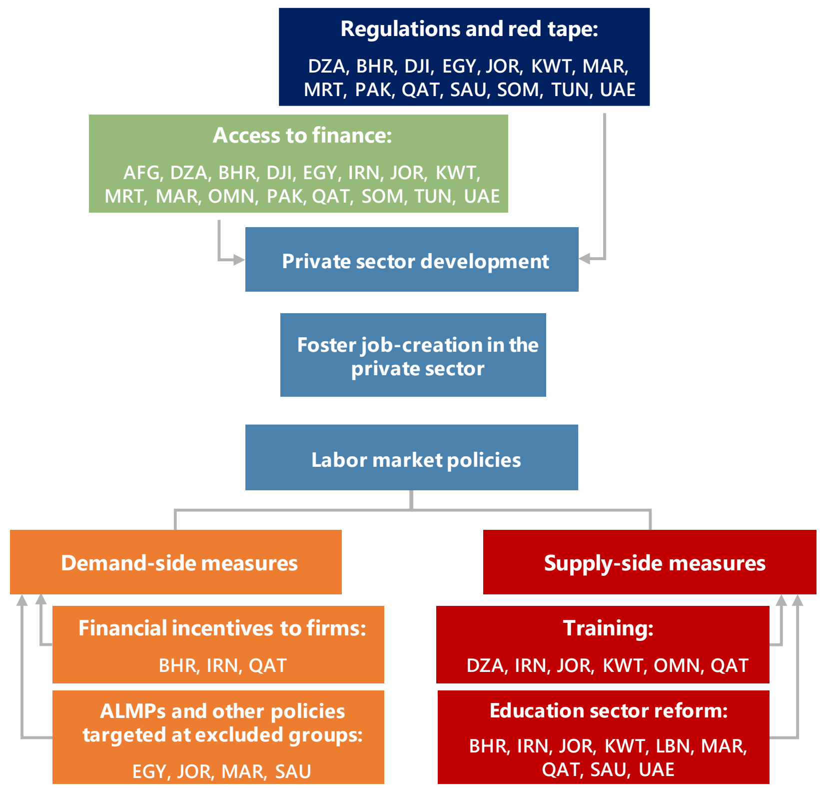
Implement or increase excise taxes	• BHR • KWT • SAU • EGY • OMN • UAE • JOR • QAT
Implement or increase VAT (including plans for future implementation)	• BHR • OMN • UAE • EGY • QAT • KWT • SAU
Reduce tax exemptions	• JOR • MAR • PAK
Broaden tax base	• JOR • WBG • PAK • TUN
Increase progressivity	• DJI • JOR • TUN
Increase non-tax revenue	• AFG

Source: Surveys to IMF MENA staff.

Countries are improving the business environment to assist private sector development

Private sector development—the engine for job creation now that fiscal space is constrained and governments can no longer be the employer of first resort—is a key priority for inclusive growth. Bahrain, Djibouti, Egypt, Jordan, Kuwait, Mauritania, Morocco, Pakistan, Qatar, Saudi Arabia, Tunisia, and the UAE are implementing policies to ease the time and cost of starting a business, introducing one-stop registration and in some cases using e-government technologies. Morocco, Tunisia, Saudi Arabia, and Sudan have streamlined customs procedures. Several countries have enacted new laws targeting small and medium-sized enterprises (Algeria); public-private partnership frameworks (Algeria, Kuwait, Qatar); or bankruptcy (UAE). Kuwait and Saudi Arabia have taken measures to facilitate foreign direct investment.

Countries fostering private sector development and labor market policies for private sector job creation and youth and women inclusion



Sources: Surveys to IMF MENA staff.

They are also taking actions to…

As a result of progress made in countries like Djibouti, Mauritania, Morocco, and the UAE, the region's score on the World Bank's Ease of Doing Business index improved to 47 percent below the level of the best global performer in 2018. There is still ample room for improvement, especially as differences in the business environment across the region are large. Further progress to improve the region's business climate requires the following steps:

…broaden access to finance for individuals and SMEs…

***** *Address access to finance*, the region's top constraint to private sector development. Seventy percent of MENA's population do not have a bank account. MENA's loans-to-SMEs ratio is the lowest in the world (2 percent of GDP), even though SMEs account for 60 percent of employment. Many countries are increasing access to finance for SMEs (Algeria, Djibouti, Egypt, GCC, Jordan, Morocco, Iran, Pakistan) and for women (Jordan, Pakistan, Somalia), expanding mobile banking (Djibouti, Jordan, Morocco, Pakistan, Somalia), and developing Islamic finance (Djibouti, Mauritania, Morocco, Pakistan).

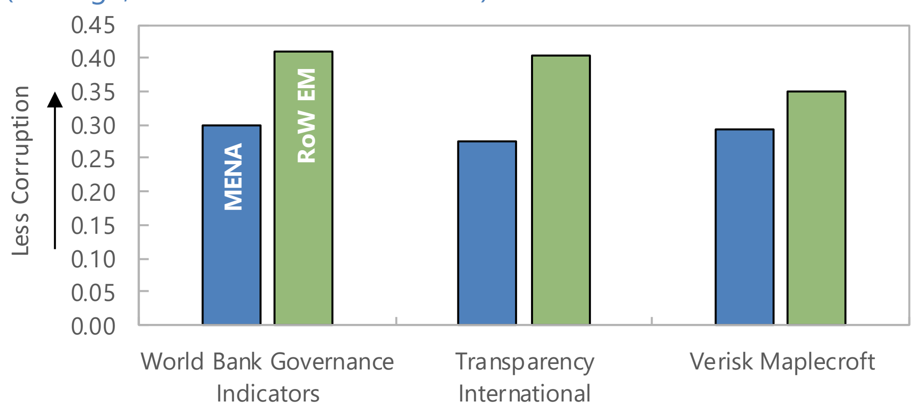
...to better equip youth for work in the private sector...

* *Improve job seekers' employment prospects.* Countries are implementing measures to improve workers' skills and boost labor demand in the private sector. Active labor market policies are being pursued to benefit women and youth in Egypt, Jordan, Morocco, and Saudi Arabia. Having ensured relatively high levels of access to schools (about 80 percent for primary education), countries are seeking to improve the quality and efficiency of education as the region performs poorly on international tests. The average TIMMS math score in the region is 20 percent below the average for other peer countries.

...and to improve governance but a more concerted effort is required to address corruption

* *Strengthen governance*. Morocco, Somalia, and Tunisia have taken measures to tackle corruption and promote transparency. Several countries also implemented policies to strengthen public financial management (Egypt, Jordan, Morocco, Tunisia, Oman, Qatar), including in some cases, the governance of state-owned enterprises. Oman, Saudi Arabia, and the UAE have introduced key performance indicators. In many cases, e-government is an important element of such reforms: Bahrain and the UAE have been ranked as top performers on the UN e-government index. Nonetheless, perceptions of corruption remain high, and more progress is needed.

Control of Corruption
(Average, normalized standard score)



Source: World Bank, Transparency International, Verisk Maplecroft, and IMF staff calculations.
Note: All three corruption indicators have been standardized between 0 and 1.

Moving the Dial on Inclusive Growth: The Marrakesh Conference

The question facing the conference is how to address the priorities identified and manage the political economy of reform, and scale-up implementation to further advance countries' inclusive growth strategies. The conference plenaries will seek to address the following questions:

a) What are the hurdles and challenges to implementing inclusive growth policies?
b) What is needed to scale up reform implementation to create more opportunities especially for youth and women?
c) How can governments engage citizens in advancing inclusive growth reforms?
d) How can the IMF, AMF, and AFESD assist reform implementation?

Box 1. Inclusive Growth Strategies in MENA countries

Afghanistan	The Afghanistan National Peace and Development Framework, issued in 2016, aims to build a broad-based and inclusive growth and to create jobs. It emphasizes policies to improve the rule of Law and address corruption.
Algeria	In 2016, the authorities adopted a broad strategy to move towards a private sector-led growth model and reduce the dependence on hydrocarbons. The action plan of the newly appointed government calls for pursuing reforms to improve economic governance and improve transparency. The government will launch wide-ranging consultations to push forward subsidy reforms and gradually adopt a social transfer policy.
Bahrain	The Bahrain Labor Fund and Development Bank supported SMEs through business management support and subsidized loans. Bahrain's Vision 2030 promotes the role of the private sector and further diversify the economy.
Djibouti	Vision 2035 is an ambitious plan to make the country a middle-income economy within the next 20 years by raising medium-term growth, making it more inclusive and reducing unemployment.
Egypt	Vision 2030 has inclusive growth objectives including reducing poverty, increasing women labor force participation, reducing the gender gap and improving the business environment.
Iran	The Sixth National Development Plan aims to develop private sector and reduce oil dependency. As part of this plan, the authorities have also set specific goals in terms of better integrating women in the labor force.
Jordan	Vision 2025, a ten-year framework for economic and social policies, which aims at advancing fiscal consolidation and broad structural reforms to enhance the conditions for more inclusive growth.
Kuwait	The government's 6-pillar reform strategy aims at underpinning gradual fiscal consolidation and at boosting private sector growth and fostering economic diversification, including through PPPs, privatizations and labor market and business climate reforms. The authorities also established an SME financing fund to tackle the SME financing problem.
Mauritania	The first pillar of the "Strategy for Accelerated Growth and Shared Prosperity 2016-30" is to promote higher, sustainable and more inclusive growth and higher job creation.
Morocco	The authorities have different plans to address IG issues including the National Strategy for Employment 2015-25, the Vision for Education 2015-30, and the National Anti-Corruption Strategy.
Oman	The 9th five-year development plan (2016-20) targets to create productive job opportunities for Omani nationals and improve their capabilities and skills through economic diversification including by investing in infrastructure, enhancing the role of the private sector and encouraging entrepreneurship and SMEs.
Pakistan	Pakistan Vision 2025, the National Financial Inclusion Strategy 2015, and the National Doing Business Reform Strategy 2016 are targeting different aspects of inclusive growth challenges.
Qatar	The Ministry of Development Planning and Statistics is currently developing its Second National Development Strategy 2017-22, with a focus on improving the quality of education, fiscal management, and the institutional framework for the conduct of fiscal policy to create room for private sector's participation in the economy. This complements Qatar's National Vision 2030, launched in 2008, to "transform Qatar into an advanced economy capable of achieving sustainable development by 2030."
Saudi Arabia	The Vision 2030 strategy and National Transformation Program (NTP) envisages an ambitious economic diversification, and job creation for its young population. It also aims to enable a greater role for the private sector, increase female labor force participation, home ownership, and transform Saudi Arabia into a trade and financial hub.
Somalia	The authorities' National Development Plan outlines their medium and long-term development strategy including reforms to social safety nets, youth and women's participation, private sector development, and access to finance.
Tunisia	The authorities' five-year economic vision 2016-2020 aims to promote stronger and more inclusive growth.
UAE	Vision 2021 aims to achieve a more diversified and a knowledge-driven economy.
West Bank and Gaza	The 2017-22 National Policy Agenda fosters social justice, education and health care, and building resilient communities.

Source: IMF country teams

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