
Arab World Competitiveness Report 2011-2012



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Preface

This fourth edition of *The Arab World Competitiveness Report* is published at a critical time. The important changes taking place in North Africa and the Middle East have brought to light a number of socio-economic challenges—such as youth unemployment, regional inequalities, corruption, weak institutions, limited entrepreneurship, and the need to advance the role of women in the economy — that must be addressed if the aspirations of the region's citizens are to be met.

For many years, the World Economic Forum and the Organisation for Economic Co-operation and Development (OECD) have been supporting the region's efforts to boost competitiveness and growth. Since 2002, the Forum has been providing detailed assessments of the productive potential of Arab nations through *The Arab World Competitiveness Report* series and continues to stimulate dialogue on competitiveness between the public and private sectors in the region. Through its MENA-OECD Initiative launched in 2005, the OECD supports countries' efforts to improve governance and investment frameworks through policy reviews, sharing good practices, and national reform strategies. Based on an active network of experts and proven policy experience, the OECD works with Middle East and North Africa (MENA) governments to foster job creation, promote better governance, advance inclusive growth, and encourage international economic integration.

The *Report* analyzes the competitiveness of the Arab world with a special focus on generating employment, which, without any doubt, constitutes the region's most pressing priority. It also discusses the economic outlook of the region and analyzes current and future opportunities and challenges.

This joint *Report*, which continues the successful collaboration of our two organizations, is a contribution to understanding the key factors determining future prosperity and economic growth in the Arab world at this critical juncture. It offers policymakers and business leaders an important tool in formulating improved economic policies and institutional reforms.

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Executive Summary

The Arab world has seen many important shifts over the past decade. Almost ten years of relatively high economic growth slowed significantly with the global economic and financial crisis of 2008-2009. More recently, a wave of protests driven by longstanding socio-political and economic issues spread across several countries, leading to instability and the fall of the regimes in Tunisia, Egypt, and (after months of a violent revolution) Libya. These events – commonly known as the “Arab Spring” – have spurred major political changes, notably in Tunisia and Egypt, where new constitutions are being drafted and entirely new governments elected. Yet, political changes will have to be accompanied by structural economic reform if the root causes of the current events in the region are to be addressed.

The recent developments have heightened awareness of key socio-economic challenges, the most important of them being creating more and better employment opportunities for the 2.8 million young people entering the labor markets every year. Reducing unemployment will have to focus on three groups that are disproportionately affected – the young, the educated, and women.

Enhancing overall competitiveness should be part of the reform agenda to address the challenges and exploit the opportunities present in the Middle East and North Africa (MENA) region. Particularly needed are measures to support a vibrant, competitive, and entrepreneurial private sector. The private sector currently remains stifled by a business environment that is not conducive to the development of enterprises. Corruption, lack of transparency in government decision making, market distortion, and weak global and regional integration hinder competition and reduce efficiency.

The development of a dynamic private sector would not only involve the promotion of domestic enterprise but also the opening up of the economy to trade and investment. Although the region has made progress in these areas, the significant increase of foreign direct investment (FDI) registered during the last decade has not been sufficient to reduce the high levels of unemployment. The recent decrease in FDI flows due to the global economic crisis and the impact of the Arab Spring on investors’ confidence brings additional challenges.

Against this background, *The Arab World Competitiveness Report 2011-2012* analyzes the region’s competitive strengths and areas requiring improvement in chapter 1; examines the challenges and opportunities for reform in chapter 2; and provides an overview of the impact of FDI on employment and outlines some policy measures which could enhance that impact in chapter 3.

Chapter 1, entitled “A Time of Opportunities: The Competitiveness Performance of the Arab World” by Margareta Drzeniek Hanouz and Miroslav Dusek (World Economic Forum), analyzes the competitiveness of 14 Arab countries using the framework of the Global Competitiveness Index (GCI). Competitive economies are those that are likely to grow over the medium to longer term and have in place the policies, factors, and institutions that support productivity. Productivity is a determining factor for economic growth, which in turn is needed to generate employment.

The analysis shows that the countries are highly diverse in terms of national competitiveness, yet some common features can be identified among the three geographical sub-regions: the Gulf economies, North Africa, and the Levant. Most Gulf economies benefit from vast natural resources and rising energy prices, and have used the resulting revenues for improvements in their competitiveness in recent years. While North African and Levantine economies face numerous impediments, the current socio-political momentum does offer a unique opportunity for a robust response. These challenges include institutional concerns such as high levels of undue influence and corruption, weak domestic and foreign competition, underdeveloped financial markets, and rates of technological adoption that trail other economies at similar levels of development.

Despite the considerable differences among nations, the common denominator across the region is the imperative to provide sustainable and gainful employment. Competitiveness-enhancing reforms can be instrumental in this context, as they contribute to employment creation in the long run. The two key reforms that would address obstacles to job creation in almost all countries in the region are overhauling education systems to better respond to the needs of the rapidly evolving economy; and raising the efficiency of markets by moving towards healthier competition, fostering entrepreneurship, and supporting a more dynamic environment for enterprises.

The Arab Spring has led to significant turbulence in the region, which has had negative effects on the economic performance of countries in the short term. This is likely to persist in the medium term, as well, depending on the success and direction of political reform. However, while uncertainty about the future social, political, and economic environment and a heightened awareness of institutional weaknesses may have adverse effects in the near future, the political changes underway and the recognition of the key role of the private sector in generating jobs and growth may drive the needed political momentum to enhance competitiveness over the medium to long term.

The successful implementation of an agenda for fostering competitiveness will pave the way for more private-sector activity and lead to the creation of gainful and sustainable employment across the region. The chapter closes with an analysis of competitive strengths and weaknesses of each country in the region covered by the GCI.

Chapter 2, which outlines the main “Opportunities and Challenges in the Middle East and North Africa Region” was prepared by Anthony O’Sullivan, Marie-Estelle Rey, and Jorge Gálvez Méndez (OECD). The chapter also underlines the mostly positive macroeconomic performance in the region during the last 10 years and considers some of the—already materialized or expected—negative impacts of the recent events in MENA economies.

The most daunting and urgent challenge is the creation of more and better jobs, especially for youth, women, and the most educated. Youth unemployment (15-24 years) averages 25 percent across the region (compared with 17 percent in the OECD) and reaches 30 percent in countries such as Saudi Arabia and Tunisia. Moreover, the most educated segments of the population are not finding enough jobs: over 40 percent in Saudi Arabia and above 20 percent in Morocco and the United Arab Emirates are unemployed. Another striking feature in the region is the high level of unemployment among women (up to 40 percent) and their very low labor force participation rates (33 percent, compared with 61 percent in OECD countries).

One factor behind these high unemployment levels is a mismatch between the skills provided by current education systems and programs and those needed by firms, which calls for greater involvement of the private sector in contributing to skills development. Sustainable job creation is further hampered by the disproportionate weight of the public sector in the region’s economies—70 percent of non-agricultural employment in Egypt, for example, is in the public sector—and low levels of entrepreneurship, with economies in the region registering only 0.6 new firms per 1,000 working-age people, compared with approximately four firms in high-income countries.

While the region registered a solid economic performance over most of the last decade, registering a GDP growth of 5.2 percent between 2000 and 2008 (compared with only 2.4 percent for OECD countries), the global economic crisis and recent events have negatively impacted most economies, excepting a few oil-rich states that benefited from rising energy prices. Particularly affected are the economies of Egypt and Tunisia, which are expected to grow by 1 percent at most in 2011. Those economies are struggling to minimize instability and uncertainty for investors. Other countries, such as Morocco and, to a lesser degree, Jordan, have been indirectly affected and are also engaged in political changes. But, overall, the extent to which countries in the region are able to recover will depend on the speed, design, and execution of political transition and economic reforms, as well as on the recovery of the global economy.

Chapter 3, by Anthony O’Sullivan, Marie-Estelle Rey and Jorge Gálvez Méndez, focuses on “Foreign Investment Policies and Job Creation in the MENA Region”, with a particular emphasis on policies to maximize the role of FDI in employment. The chapter outlines theoretical and empirical evidence for how different types of investment (green field vs. mergers and acquisitions), strategies (market expansion, acquisition of resources, operational efficiency), and economic sectors targeted by FDI can have varying levels of impact on job creation.

The chapter also emphasizes that, although the MENA region registered increasing levels of FDI through almost all of the past decade, those investments failed to reduce the high levels of structural unemployment significantly. To tackle this paradox, the chapter outlines different general policies that would enhance the contribution of FDI to jobs, and includes examples of successful case studies from OECD and MENA economies. Priority policies would include implementing specific education and labor initiatives (internships, vocational training, continuing education) to align the supply and demand of skills; enhancing the flexibility of labor policies to adapt to changing markets; integrating women in the labor force; and fostering linkages between foreign enterprises and local suppliers, particularly through the use of economic zones. The analysis also puts forward two specific economic sectors that could have a potentially high impact on employment creation and increased competitiveness: green energies and tradable services.

A key message from this chapter is that, although FDI is usually identified as a driving factor of employment, the link is far from automatic and direct. Relevant policies can have an important role in making that link happen and increasing its impact on the volume and quality of jobs. Finally, the chapter underlines the pressing need for improving the availability of reliable and complete data to measure the impact of FDI on employment, both direct and indirect, in terms of both the number and the quality of jobs created. In the end, sound policies are built on the basis of sound evidence.

It is certain that the Arab Spring provides a unique window of opportunity for the MENA region to leverage its “youth bulge” and introduce the transparent and accountable policies and institutions that will support increased competitiveness and higher living standards. Achieving higher growth and employment will require that the various challenges be tackled through a coordinated and comprehensive strategy that involves governments, the private sector, civil society, and the international community. The region's governments and the international community need to work hand in hand to promote inclusive and sustainable economic growth and employment if they are to fulfil the aspirations of the Arab world's citizens.

∞ Approaches to achieving higher economic growth and employment analyzed in this report were the topic of the World Economic Forum Special Meeting on Economic Growth and Job Creation in the Arab World at the Dead Sea in Jordan on October 21-23, 2011, and will be further discussed at the World Economic Forum's Annual Meeting in Davos-Klosters on January 25-29, 2012.

1. A Time of Opportunities: The Competitiveness Performance of the Arab World

*By Margareta Drzeniek Hanouz and Miroslav Dusek,
World Economic Forum*

The year 2011 has seen important developments in the Middle East and North Africa (MENA) region. A wave of popular protest demanding more social equity and stronger economic development has led to political change at an unprecedented and unexpected scale. Social unrest affected many countries, but the degree of resulting political change varied across the region. Protests triggered economic, social, and political reforms in a number of countries, and culminated in the resignation of ruling presidents in Tunisia and Egypt and in forceful regime change in Libya. While these events have contributed to uncertainty in the short term, and many countries are set to experience a drop in economic output in 2011, they present great promise for the future development of the countries in question and the region as a whole. A political transition is under way in a number of countries, and reforms aimed at enhancing competitiveness are high on the agenda of many governments and supported by the international community. If such reforms are carried out, the region has the potential to rebound and provide better employment opportunities and improved standards of living for its population.

The recent events have placed a spotlight on the importance of job creation for the region, which *The Arab World Competitiveness Report 2005* identified as the key challenge for the coming years. In light of the region's growing population, according to the OECD MENA-Investment programme (see Chapter 2) Arab economies will need to create 25 million jobs over the next decade just to keep employment at existing levels, let alone to reduce the burgeoning unemployment rate. This will require gross domestic product (GDP) growth to reach 5.5 percent on average, one percentage point above the growth of the past decade. Boosting gainful and sustainable private sector employment is therefore arguably one of the most important development challenges for countries in the region. Competitiveness-enhancing reforms can be instrumental in this respect,

as reforms that enhance competitiveness also support higher levels of formal private sector employment in the long run. At the same time, competitive economies are more productive and are able to maintain higher wages for their populations, thereby raising the standard of living in a sustainable manner. The employment agenda for the region therefore overlaps to a large extent with the competitiveness agenda, although certainly some aspects, such as education or labor markets policies matter more than others for employment creation.

Against this background, an analysis of the competitive strengths and weaknesses of the MENA region appears particularly timely. The following chapter analyses the region's competitiveness based on the findings of the World Economic Forum's Global Competitiveness Index (GCI). At a time when economic policy in a number of countries is being reshaped, this analysis will provide a reminder of each country's competitive strengths and identify challenges that will need to be addressed by policy-makers to enhance their economies' competitiveness going forward, thereby putting them on a higher growth path.

Box 1: Overcoming the Employment Challenge by Raising Competitiveness

Over the past several decades, most countries in the Arab world have relied on the government and on state enterprises for employment creation. While this was an expedient way to create jobs in the shorter term, over the longer term, rapid population growth has made it impossible for the public sector to provide a sufficient number of jobs, in particular for the young people entering the labor market.* At the same time, the business sector has not been able to fill the gap, as it remained stifled by a business environment that did not encourage private sector growth. As a result, unemployment has risen in many countries over recent decades. Currently, regional unemployment rates are the highest worldwide, with women and youth most severely affected (see chapter 2 for a more detailed account of unemployment levels).†

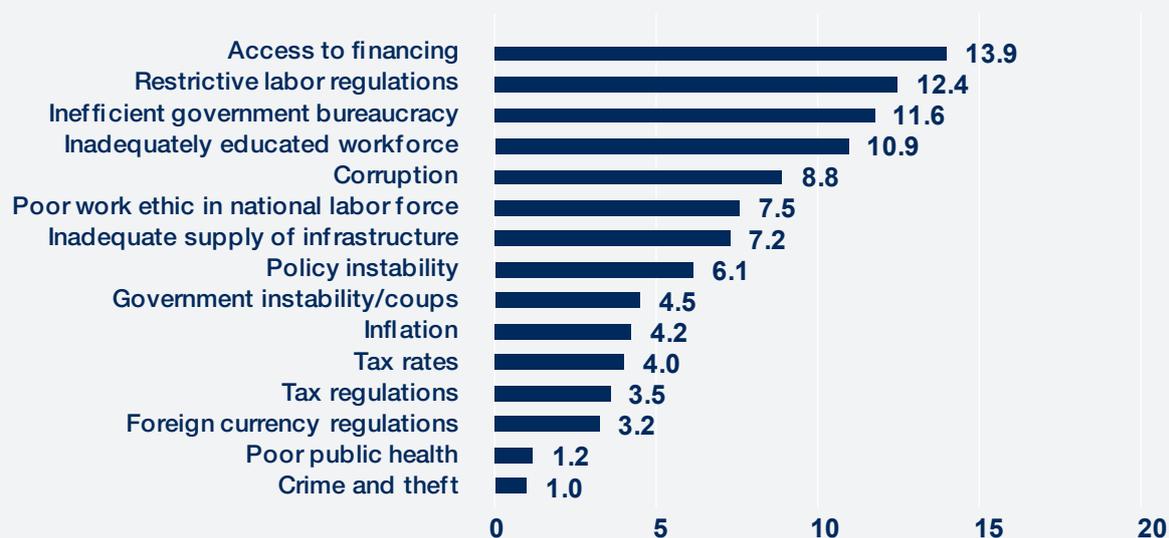
Population growth had already begun to slow prior to the economic boom that ended in 2008, reducing unemployment. However, the subsequent slowdown pushed regional unemployment back up to 10.3 percent in 2010, and is expected to remain high, at 10.0 percent in 2011.‡

In this context, the Arab region is in need of economic growth that is based on a vibrant and growing private sector if it is to attain durably higher levels of gainful employment: only the private sector can create a sufficient number of jobs in a sustainable manner. Figure 1 shows that, according to business leaders, restrictive labor regulations, inefficient bureaucracy, and a lack of access to finance are the top three hindrances to doing business in the region.

The Global Competitiveness Index (GCI) sheds light on some of the major stumbling blocks to achieving higher levels of employment over the longer term. More competitive economies are those that have in place factors, policies, and institutions that enable higher productivity. Higher productivity, in turn, tends to translate into higher employment in the context of rising demand. In the MENA region, given the untapped potential of domestic and export markets,§ higher productivity should translate into increased employment, in addition to wage increases and rising standards of living.

Despite the significant differences among Arab countries, some common trends emerge when comparing the results from national competitiveness indicators. Figure 2 shows the disparities between the best- and worst-performing countries in the region. The performances of the sub-regions are also shown, as is the European Union (EU) average, for comparison.

Figure 1: The most problematic factors for doing business in the Arab world



Source: World Economic Forum, Executive Opinion Survey 2011

* See World Bank 2003 for a detailed historical analysis of employment in the region.

† See ILO 2011.

‡ ILO 2011.

§ See World Economic Forum 2010 for more details on the export potential of the region.

When benchmarked against the EU, most countries from the region underperform in terms of health and primary education, as well as higher education and training, two areas of particular importance to competitiveness as well as for ensuring better labor market outcomes and more equitable growth. The potential for education to translate into economic growth is particularly constrained by the poor quality of the formal educational system, which is insufficiently oriented to the needs of business. As a result, just after the top three most problematic factors mentioned above, inadequate levels of education are identified as the fourth most constraining issue (see Figure 1). In the Gulf countries, this is actually the third most important constraint.

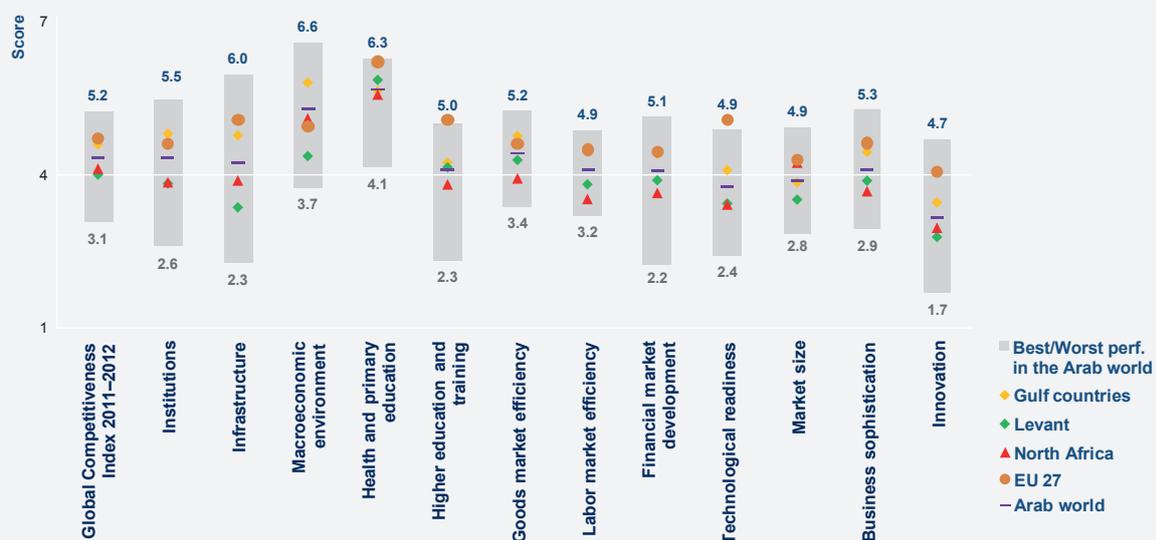
In many Arab countries, in particular in North Africa and the Levant, labor market efficiency considerably trails international best practice. Two key characteristics of labor markets in the region are worth noting in this context. First, regulations, such as those related to hiring and firing, as well as wage setting tend to be more restrictive than in other developing and emerging country groupings (e.g., the BRICS). Second, the available talent is not put to its most efficient use. The low participation of women in the labor force (see Chapter 2) limits the region's growth potential, because a significant share of talent is not put to economic use. Further, the low level of meritocracy in the workplace creates disincentives to raising individual productivity and to pursuing education. In the GCI, meritocracy is captured through two variables—the degree to which businesses rely on

professional managers when filling positions, as opposed to friends and relatives, and the relationship between pay and productivity. On both indicators, at least half of the 14 countries assessed in this chapter rank in the bottom half of the GCI (i.e., 71st or below).

Another area of significant unrealized potential is technological readiness. While innovation entails developing new products and processes, significant productivity gains can also be achieved simply by making good use of technologies that have been developed elsewhere. Further, besides increasing productivity, improved technological readiness offers direct opportunities for job creation through related sectors, such as IT-related outsourcing services, provided that education and training outcomes adjust accordingly.²² Yet, in much of the Arab world, the rates of technological adoption remain relatively low.

To sum up, higher levels of gainful employment in the region will necessitate more private sector jobs, and enhancing various aspects of competitiveness will likely support this process by boosting private sector growth in the region. Improving competitiveness and raising employment levels will clearly be a complex process necessitating simultaneous progress across a number of the interrelated challenges identified in this chapter. Yet, given the present reform momentum and policy reform coordination at the national level, much can be achieved to help Arab economies can meet these employment challenges going into the future.

Figure 2: Performance of the Arab world and the sub-regions on the Global Competitiveness Index 2011-2012



Source: World Economic Forum 2011

²² Overall, the relationship between technological change and job creation remains unclear and depends on the balance between jobs lost through rationalization in the short term and the jobs created through new opportunities. Provided that a holistic strategy is put in place (which includes reducing barriers to entrepreneurship, upgrading education and training, etc.), the effects are likely to be positive in the long term.

Methodology

For purposes of this analysis, competitiveness is defined as the set of institutions, policies, and factors that determine the level of productivity of a country. The level of productivity, in turn, determines the rates of return obtained by investments in an economy. Because the rates of return are also drivers of growth rates, a more competitive economy is likely to grow more and be more prosperous in the medium to long term.

Since its introduction in 2005, the GCI has been the key methodology used by the World Economic Forum in its assessments of competitiveness. The model, which was developed by Xavier Sala-i-Martin and the World Economic Forum, rests on the belief that the determinants of competitiveness are numerous and interact with each other in a complex manner. The GCI captures these interactions through a weighted average of many different components, each of which reflects a particular aspect of competitiveness. These components are grouped into 12 categories,¹ as follows:

1. **Institutions** are crucial for competitiveness, as they determine the legal and administrative framework within which individuals, firms, and government interact. Examples of well-functioning institutions include clearly defined and enforced property rights, an efficient and transparent public administration, a fair and independent judiciary, provision of physical security, and high corporate governance standards.
2. **Infrastructure** is key for economic activity for a number of reasons. Transport infrastructure is crucial for getting goods to markets rapidly and at low cost, electricity for smooth and interruption-free production, and telecommunications for efficient communication.
3. Stability in the **Macroeconomic environment** is important, as its absence makes it difficult for businesses to operate. Inflation limits companies' ability to plan and invest, and continued fiscal lassitude, high government debt, or inefficiencies in the financial system can result in high interest rates, restraining both public and private investment.
4. **Health and primary education** are crucial, as a healthy workforce that has received at least a basic education is much better positioned to perform to its full potential.
5. Countries cannot move up the development ladder without investing in **Higher education and training**, as more complex products and production processes require a skilled workforce.
6. Healthy competition is an important driver of efficiency and innovation, as it forces inefficient businesses out of the market and enables new ventures to enter the market. This concept is captured under the **Goods markets efficiency** pillar.
7. **Labor market efficiency** is important to ensure that talent is put to its best use in an economy. A flexible labor market, accompanied by meritocratic incentive structures absent of discrimination against societal groups, is best placed to contribute to competitiveness.
8. Much attention has recently been paid to the functioning of financial markets. The **Financial market development** pillar captures two major factors that contribute to competitiveness: the financial system's efficiency as a source of finance for businesses, and its stability and trustworthiness.
9. **Technological readiness** reflects a country's ability to adopt the latest technologies and use them to increase domestic productivity. We distinguish between adoption of technology (the 9th pillar) and technological innovation (the 12th pillar), as these two factors affect competitiveness in different ways. Technological adoption raises the productivity of existing processes, whereas innovation expands the technology frontier. Much of the productivity-enhancing effect, in particular in emerging markets that do not operate at the technology frontier, can therefore be harnessed through adoption of foreign technologies.
10. **Market size**, viewed as domestic markets expanded by international markets, is taken into account because large markets enable companies to realize economies of scale.
11. **Business sophistication** plays an important role for productivity. Clusters of economic activity raise the efficiency of many processes within businesses, while activities such as marketing and distribution raise productivity by increasing the value of products and services.
12. As noted above, **Innovation** is essential, as it can expand the technology frontier. Businesses in advanced economies can sustain the high wage levels in the country only through moving the technology frontier outwards; they must therefore develop cutting-edge products or services and/or unique processes.

Although taken into account separately in the Index, the categories are highly interrelated. In fact, they tend to reinforce each other. For example, innovation (pillar 12) is not possible in a country where weak competition among companies (pillar 6) or poor protection of intellectual property (pillar 1) reduce incentives to innovate. Likewise, a well-educated population (pillar 5) best contributes to raising productivity when the labor market is flexible and meritocratic incentives are common in the workplace (pillar 7).

The Index also takes into account the fact that the different dimensions of competitiveness are not of equal importance to all countries. As a country becomes increasingly advanced in economic terms, its products and services must become increasingly sophisticated in order to sustain the rising productivity levels necessary to maintain a growing wage level. The Index therefore applies different weighting schemes depending on a country's level of development. Economies are grouped in three stages of development: the factor-driven stage, the efficiency-driven stage, and the innovation-driven stage, based on GDP per capita and the importance of natural resources in their economies. ²



Source: World Economic Forum, 2011

A total of 14 Arab countries have been added to the sample of economies covered by the GCI over the past decade. Presently, the Index captures Algeria, Bahrain, Egypt, Jordan, Lebanon, Morocco, Kuwait, Oman, Qatar, Saudi Arabia, Syria, Tunisia, United Arab Emirates, and Yemen. Libya, which has been included in past editions of the GCI, was excluded this year because it was not possible to carry out the survey during the civil unrest in the country. Table 1 shows how countries in the Arab World are allocated into the three stages and provides details about the weighting scheme.

It is important to note that the GCI is calculated using two distinct types of data. Data for approximately one-third of the indicators are obtained mainly from major international organizations, such as the World Bank, International Monetary Fund, UNESCO, and so on. For the remaining indicators, data are derived from the World Economic Forum's annual Executive Opinion Survey. By surveying business executives, it provides an assessment of the more qualitative aspects of competitiveness, as well as of dimensions for which statistical sources are not available for all countries covered by the GCI. The Survey is conducted in collaboration with partner institutions in each country, which administer the survey process. In 2011, over 14,000 business executives were surveyed in 142 countries between January and May.³

Since 2007, the Survey data have been calculated as a moving average of the present and the previous year, in line with a Bayesian updating approach. There are several reasons for doing so. First, it renders the results less sensitive to the specific point in time when the survey is administered. Second, it increases the amount of available information by providing a larger sample size and by retaining some previous information that continues to be deemed valuable. Additionally, because the Survey is carried out during the first quarter of the year, averaging the responses from the first quarter of 2010 and the first quarter of 2011 better aligns the survey data with many of the data indicators from sources other than the Forum, which are often year-average data.

Table 1: Arab world economies by stage of development

	Arab world	Other countries in this stage	Important areas for competitiveness
Stage 1 (factor-driven) GDP per capita (US\$) < 2,000;	Yemen	Bangladesh, Bolivia, Kenya, Pakistan, Vietnam	Basic requirements (60%) and efficiency enhancers (35%)
Transition from 1 to 2 2,000 < GDP per capita (US\$) < 3,000;	Algeria, Egypt, Kuwait, Morocco, Qatar, Saudi Arabia, Syria	Brunei Darussalam, Indonesia, Iran, Islamic Rep., Ukraine, Venezuela, Argentina, Brazil, China, Malaysia,	Basic requirements (between 40% and 60%) and efficiency enhancers (between 35% and 50%)*
Stage 2 (efficiency-driven) 3,000 < GDP per capita (US\$) < 9,000;	Jordan, Lebanon, Tunisia	Mexico, Russian Federation, South, Africa, Turkey	Basic requirements (40%) and efficiency enhancers (50%)
Transition from 2 to 3 9,000 < GDP per capita (US\$) < 17,000;	Oman	Chile, Croatia, Poland, Trinidad and Tobago	Basic requirements (between 20% and 40%) and efficiency enhancers (50%) Innovation factors (10% to 30%)*
Stage 3 (innovation-driven) GDP per capita (US\$) > 17,000;	Bahrain, United Arab Emirates	Germany, Korea, Rep, Norway, Spain, United Kingdom, United States	Basic requirements (20%) and efficiency enhancers (50%) Innovation factors (30%)*

Note: For countries with a share of mineral export in total exports higher than 70% are moved towards a lower stage of development. Source: Global Competitiveness Report 2011-2012

Box 2: The Impact of the Arab Spring on the Region's Competitiveness Assessment

The events that have become known as the Arab Spring started sweeping across the region in early 2011, bringing about political change and creating expectations of increased future prosperity. *The Global Competitiveness Report* covers a number of countries that were affected by these events. It is still too early to gauge the full extent of the changes on longer-term structural factors that affect competitiveness. However, given the short-term drop in economic activity expected for 2011 in some of these countries, the question arises about the extent to which the Index captures the effects of Arab Spring events on the countries' economic potential.

The most important element is certainly the time period reflected by the data. Although the Index captures some shifts in the competitiveness performance of selected economies, the full extent could not be captured this year due to traditional lags in data collection and presentation. Most of the quantitative data used in the Index, which account for about one-third of the variables, reflect 2010 values and therefore do not reflect the evolving situation. The Executive Opinion Survey (Survey), which accounts for the remaining data, was carried out most recently between February and May 2011, and is combined with similar data from the same period in 2010. The Survey data therefore capture the regional turbulence and political change to varying degrees. In the particular case of Libya, social unrest was so disruptive that the Survey data could not be collected, making the country's inclusion impossible this year. Tunisia and Egypt, where the events peaked in mid-January and mid-February with the resignation of the respective presidents, are the only countries where this year's Survey data capture the situation in the wake of political change. For both countries, GCI ranking dropped considerably – by 13 places for Egypt and eight for Tunisia. Our interpretation is that the drop reflects higher uncertainty in both countries during the early transition process, as well as heightened public awareness of persisting structural weaknesses, resulting mainly in poorer assessments of various aspects of public and private institutions and, to a lesser degree, also of goods and labor markets efficiency. To varying extents, similar effects can be observed in some other countries from North Africa and the Levant, notably Jordan, Lebanon, and Algeria.

In sum, the extent to which current events affect competitiveness in this year's assessment varies across countries and is impossible to quantify at this early stage. Nevertheless, we observe some shifts in the rankings. The full impact of political change on national competitiveness will thus be captured only in future iterations of the GCI.

Results of the Global Competitiveness Index 2011-2012 for the Arab World

In economic terms, the Arab world is a highly diverse region, which is reflected in the levels of economic performance across the countries. Per capita GDP for 2010 ranges from a high of US\$ 76,167 in Qatar, one of the wealthiest economies in the world, down to US\$ 1,281 in Yemen.⁴ Economic structures also differ – while some countries are highly dependent on their abundant energy resources, other economies are more diversified, with relatively better-educated labor forces and benefitting from geographical proximity and facilitated access to the large European market.

A basic comparison of the competitiveness rankings of Arab world economies to other countries is presented for informational purposes in Table 2. However, while it is useful for countries to benchmark themselves internationally, a deeper analysis requires an approach that reflects the region's diversity of economic structures. For this reason, the next section discusses the results by three sub-regions: the Gulf, North Africa, and the Levant. Tables 3, 4, and 5 present the GCI rankings by these groupings.

Table 2: Global Competitiveness Index 2011-2012 ranking

Rank	Country/Economy	Score	Rank	Country/Economy	Score	Rank	Country/Economy	Score	Rank	Country/Economy	Score
1	Switzerland	5.74	37	Bahrain	4.54	73	Morocco	4.16	109	Guyana	3.73
2	Singapore	5.63	38	Czech Republic	4.52	74	Bulgaria	4.16	110	Dominican Republic	3.73
3	Sweden	5.61	39	Thailand	4.52	75	Philippines	4.08	111	Senegal	3.70
4	Finland	5.47	40	Tunisia	4.47	76	Croatia	4.08	112	Suriname	3.67
5	United States	5.43	41	Poland	4.46	77	Romania	4.08	113	Zambia	3.67
6	Germany	5.41	42	Barbados	4.44	78	Albania	4.06	114	Ghana	3.65
7	Netherlands	5.41	43	Italy	4.43	79	Macedonia, FYR	4.05	115	Nicaragua	3.61
8	Denmark	5.40	44	Lithuania	4.41	80	Botswana	4.05	116	Cameroon	3.61
9	Japan	5.40	45	Portugal	4.40	81	Trinidad and Tobago	4.00	117	Malawi	3.58
10	United Kingdom	5.39	46	Indonesia	4.38	82	Ukraine	4.00	118	Pakistan	3.58
11	Hong Kong SAR	5.36	47	Cyprus	4.36	83	Namibia	4.00	119	Cape Verde	3.58
12	Canada	5.33	48	Hungary	4.36	84	Guatemala	4.00	120	Tanzania	3.56
13	Taiwan, China	5.26	49	Panama	4.35	85	Argentina	3.99	121	Uganda	3.56
14	Qatar	5.24	50	South Africa	4.34	86	Honduras	3.98	122	Paraguay	3.53
15	Belgium	5.20	51	Malta	4.33	87	Algeria	3.96	123	Belize	3.52
16	Norway	5.18	52	Sri Lanka	4.33	88	Georgia	3.95	124	Venezuela	3.51
17	Saudi Arabia	5.17	53	Brazil	4.32	89	Lebanon	3.95	125	Nepal	3.47
18	France	5.14	54	Mauritius	4.31	90	Greece	3.92	126	Kyrgyz Republic	3.45
19	Austria	5.14	55	Azerbaijan	4.31	91	El Salvador	3.89	127	Nigeria	3.45
20	Australia	5.11	56	India	4.30	92	Armenia	3.89	128	Mali	3.39
21	Malaysia	5.08	57	Slovenia	4.30	93	Moldova	3.89	129	Côte d'Ivoire	3.37
22	Israel	5.07	58	Mexico	4.29	94	Egypt	3.88	130	Madagascar	3.36
23	Luxembourg	5.03	59	Turkey	4.28	95	Serbia	3.88	131	Timor-Leste	3.35
24	Korea, Rep.	5.02	60	Montenegro	4.27	96	Mongolia	3.86	132	Zimbabwe	3.33
25	New Zealand	4.93	61	Costa Rica	4.27	97	Cambodia	3.85	133	Mozambique	3.31
26	China	4.90	62	Iran, Islamic Rep.	4.26	98	Syria	3.85	134	Swaziland	3.30
27	United Arab Emirates	4.89	63	Uruguay	4.25	99	Gambia, The	3.84	135	Lesotho	3.26
28	Brunei Darussalam	4.78	64	Latvia	4.24	100	Bosnia and Herzegovina	3.83	136	Burkina Faso	3.25
29	Ireland	4.77	65	Vietnam	4.24	101	Ecuador	3.82	137	Mauritania	3.20
30	Iceland	4.75	66	Russian Federation	4.21	102	Kenya	3.82	138	Yemen	3.06
31	Chile	4.70	67	Peru	4.21	103	Bolivia	3.82	139	Angola	2.96
32	Oman	4.64	68	Colombia	4.20	104	Benin	3.78	140	Burundi	2.95
33	Estonia	4.62	69	Slovak Republic	4.19	105	Tajikistan	3.77	141	Haiti	2.90
34	Kuwait	4.62	70	Rwanda	4.19	106	Ethiopia	3.76	142	Chad	2.87
35	Puerto Rico	4.58	71	Jordan	4.19	107	Jamaica	3.76			
36	Spain	4.54	72	Kazakhstan	4.18	108	Bangladesh	3.73			

Table 3: Gulf economies in the GCI ranking

Economy	GCI 2011-2012		GCI 2010-2011	
	Rank	Score	Rank	Score
Qatar	14	5.24	17	5.10
Saudi Arabia	17	5.17	21	4.95
United Arab Emirates	27	4.89	25	4.89
Oman	32	4.64	34	4.61
Kuwait	34	4.62	35	4.59
Bahrain	37	4.54	37	4.54
Yemen	138	3.06	n/a	n/a

Table 4: Levantine economies in the GCI ranking

Economy	GCI 2011-2012		GCI 2010-2011	
	Rank	Score	Rank	Score
Jordan	71	4.19	65	4.21
Lebanon	89	3.95	92	3.89
Syria	98	3.85	97	3.79

Table 5: North African economies in the GCI ranking

Economy	GCI 2011-2012		GCI 2010-2011	
	Rank	Score	Rank	Score
Tunisia	40	4.47	32	4.65
Morocco	73	4.16	75	4.08
Algeria	87	3.96	86	3.96
Egypt	94	3.88	81	4.00

The Competitiveness of Gulf Economies

In recent years, competitiveness has been high on the agenda of economies in the Gulf region, resulting in numerous investments and reforms aimed at improving specific dimensions of national competitiveness. High energy prices have provided the financial means for investment. Unlike in previous periods of high energy prices, many countries of the region have taken advantage of this window of opportunity. It is important to note that, although almost all Gulf countries have attained very high GDP levels, only Bahrain and the United Arab Emirates are sufficiently diversified to be categorized in the innovation-driven stage of development. The remaining economies are classified into lower stages of development, as shown in Table 1, due to their dependence on natural resources. Classification into significantly less advanced stages of development has implications for the Index results, as it changes the weighting of the pillars of competitiveness, placing more weight on the basic factors – institutions, infrastructure, macroeconomic environment, and health

and primary education. In most of these pillars, Gulf economies traditionally perform well and, in many ways, improvements are easier to achieve, particularly given the availability of abundant financial resources for investment.

As shown in Table 3, all Gulf economies except for Yemen rank in the upper half of the rankings. Qatar leads the region at 14th, while Saudi Arabia occupies second place at 17th out of 142 countries, followed by the United Arab Emirates (27th), Oman (32nd), Kuwait (34th) and Bahrain (37th).

Qatar, one of the fastest-growing and most prosperous economies in the world, reaffirms its position as the most competitive economy in the Gulf region at 14th overall. Its strong performance rests on solid foundations made up of a high-quality institutional framework (14th), a stable macroeconomic environment (5th), and an efficient goods market (17th). Low levels of corruption and undue influence on government decisions, highly efficient government institutions, and high levels of security are the cornerstones of the country's very solid institutional framework. These institutional attributes provide good foundations for efficiency.

As noted in previous years, reducing the country's vulnerability to commodity price fluctuations will require diversification into other sectors, as well as reinforcing some areas of competitiveness. Despite efforts to strengthen the financial sector, its trustworthiness and confidence and the soundness of banks are assessed as low by the business community (80th), and the legal rights of borrowers and lenders are insufficiently protected (105th). Given high wage levels in the country, diversification into other sectors will require Qatar to raise productivity by continuing to promote greater use of the latest technologies (33rd). In addition, Qatar currently ranks 53rd in openness to foreign competition, reflecting barriers to international trade and investment. To become more competitive, it will have to foster greater openness to foreign competition.

Saudi Arabia occupies the second-highest place among the Gulf economies, ranking 17th overall. The country has seen a number of improvements to its competitiveness in recent years, including a more solid institutional framework, more efficient markets, and increasingly sophisticated businesses. As is the case for other countries from the region, Saudi Arabia is classified as transitioning from the factor-driven to the efficiency-driven stage of development, so that most emphasis is placed on the basic factors and the efficiency drivers included in the GCI.

As commendable as these recent developments are, Saudi Arabia faces important challenges going forward. Health and education are not up to the standards of other countries at similar income levels. While some progress is visible in health outcomes and the quality of education is improving quickly, the country's starting point was low. As a result, the country continues to occupy a low rank in the health and primary education pillar (61st), and room for improvement remains on the higher education and training pillar (36th). Boosting these areas, in addition to fostering a more efficient labor market (50th), is of particular importance to Saudi Arabia given the high level of unemployment in the country and the growing numbers of young people who will enter the labor market in the coming years. A more efficient use of talent, in particular higher female labor participation, will increase in importance as global talent shortages loom on the horizon and the country attempts to diversify its economy, which will require a more skilled and educated workforce. Last but not least, a greater use of the latest technologies should be encouraged (43rd); this is an area where Saudi Arabia continues to trail other Gulf economies and where significant productivity gains are at stake.

The **United Arab Emirates** ranks 27th, a very good showing given the country's advanced stage of development. The UAE's overall competitiveness reflects the high quality of its infrastructure, where it ranks a very good 8th, as well as its highly efficient goods markets (10th). Strong macroeconomic stability (11th) and some positive aspects of the country's institutions – such as high public trust in politicians (8th) and high government efficiency (5th) – round up the list of competitive advantages. However, over recent years, we have observed a poorer assessment of institutions overall – an assessment that was probably affected by the particular severity of the country's economic crisis. The resulting reorientation of the country's development model will demand an investment in solid foundations and ongoing competitiveness-enhancing structural reforms to reduce the risk of asset bubbles and to put economic development on a more stable footing. Priorities in this context should include further investment to boost health and educational outcomes. Raising the bar with respect to education will require not only measures to improve the quality of teaching and the relevance of curricula, but also incentivizing the population to attend schools at the primary and secondary levels.

Ranked 32nd, **Oman** reaps the benefits of its economic development strategy of the past years. A stable macroeconomic environment, with healthy budgetary surpluses (9th), low government debt (4th), and high savings rates (8th), bodes well for the future. Moreover, the country benefits from highly competitive markets for goods and services (23rd), complemented by an institutional set-up that ensures low levels of corruption (13th), high efficiency of the government (13th), and a secure environment (7th). These factors are the cornerstones of the country's competitiveness.

Despite these clear strengths, Oman will need to address a number of challenges that are longer term in nature. Education levels are below those of countries at similar levels of development, and, despite efforts to reform the education system, enrolment rates remain very low. About 13 percent of children at primary schooling age do not attend school (127th). The quality of education, in particular in math and science and in management, needs to be upgraded. Related to this are weaknesses in labor market efficiency. Although markets are flexible on average, human capital, in particular female talent, is not used efficiently for raising productivity in the economy (95th). Fostering technological change and more intense adaptation and use of technologies by the business sector as well as the public would allow the country to reach higher productivity levels fairly quickly. Use of information and communication technologies (ICT) is presently constrained by low Internet bandwidth (73rd) and few broadband Internet subscriptions (89th).

Kuwait occupies the 34th rank in the Index. This good assessment rests primarily on the country's strong macroeconomic environment (2nd), which compensates for a number of weaknesses in other areas. The country's energy resources contribute to a healthy fiscal situation with the second-highest budgetary surpluses in the sample and low government debt (10.5 percent of GDP). These factors, combined with high levels of physical security in the country (32nd) and healthy levels of domestic competition (39th), contribute to a stable and predictable business environment.

Despite these important advantages, a number of challenges must be tackled for Kuwait to become more competitive. Most important, the education system is in need of upgrading. Enrolment rates are low, in particular for primary and tertiary institutions, and the quality of education is assessed as poor and not attuned to the needs of the business sector (108th) when it comes to primary (90th), math and science (94th), and management (99th) education. Other challenges are related to the efficiency of goods (53rd), labor (62nd), and financial (59th) markets. Intensifying foreign competition to raise the efficiency of domestic producers would be a step in the right direction. Although tariff rates are rather low, domestic rules on Foreign Direct Investment (FDI) (133rd) keep foreign investment from coming into the country (135th), thereby depriving the economy of beneficial spill-over effects in management practice, technology, and innovation. Labor markets would benefit from making the use of talent more efficient (87th), and particularly from greater reliance on professional management skills as opposed to the employment of relatives and friends (93rd). Last but not least, financial markets are in need of stabilization to raise confidence in the system (95th).

Bahrain ranks 37th, and has remained relatively stable over the past years. One of the two economies from the region that have reached the innovation-driven stage of development, the country's competitiveness is characterized by a solid institutional framework, with well-defined property rights (18th), fairly little corruption (18th), and a relatively efficient government (9th). The country benefits from highly efficient goods markets (6th). Domestic competition appears fairly intense (25th), in particular when considering the small size of the country, and anti-monopoly laws effectively prevent abuse of market power (8th). Other notable competitive advantages include a highly developed financial market and solid performance in education and training. The high level of efficiency of financial services (4th), which is reflected in easy access to different types of finance for business and the stability of the banking sector (18th), results from the government's targeted efforts to develop the country into a regional financial centre.

In light of its small market size (104th), Bahrain could benefit from more openness to trade, as it would even further increase efficiency of the domestic business sector. Nevertheless, it remains difficult to enter markets due to administrative barriers – it takes nine days and seven procedures to start a business – and tariffs are still above levels found in other countries of similar size (57th).

In order to increase competitiveness, three areas merit additional attention: the macroeconomic environment, technological readiness, and innovation. With energy prices moving up again, consolidating fiscal accounts remains crucial for the country's competitiveness. Although debt remains at manageable levels (32 percent of GDP), the budget has recorded a high deficit of 7.8 percent of GCP in 2010, which will have to be reduced in the coming years. Upgrading technological readiness, currently ranked 39th, would allow the country to reap rapid productivity gains resulting from the adoption of the latest technologies available abroad. Particular emphasis should be placed on fostering domestic innovation, given the country's innovation-driven stage of development, its high wage level, the fairly diversified structure of its economy, and the limited availability of energy resources.

The Gulf economies ranking closes with **Yemen** at a low 138th. This low ranking reflects the numerous challenges the country faces in working to improve competitiveness and enhance economic growth. Among the limitations to be addressed on a priority basis, given the country's factor-driven stage of development, are its weak institutional framework (140th) as it relates to both public sector and private sector governance, its poor educational and health outcomes (127th), and its underdeveloped infrastructure (132nd). Tackling these challenges would enable the country to experience some productivity improvements, building on strengths such as its market size, the economy's openness to trade, and its flexible labor markets.

North Africa's National Competitiveness Assessment

In early 2011, most North African countries experienced a wave of social protests that impacted countries in different ways. While political transitions are now under way in Egypt, Tunisia, and Libya, Morocco and, to a lesser extent, Algeria have also embarked on political and economic reform programs. The uncertainty associated with these events inevitably has led to a short-term decline in economic and competitiveness performance for 2011 in the most affected countries. However, the political changes bring with them the opportunity to put into place competitiveness-enhancing measures that will enable countries to move towards a higher growth path quickly and to generate employment opportunities for their populations.

While competitiveness has been high on the agenda of most economies over the past several years, progress across North Africa has been mixed. The economies of Egypt and Algeria have declined in the rankings, while Morocco and Tunisia have remained stable.

Tunisia, the country where the Arab Spring began, maintains the lead as the by far most competitive economy in North Africa at 40th place overall. The popular uprising in the spring of 2011 was accompanied by a rise in uncertainty, and has brought to light a number of challenges related to the institutional environment, among others. These two developments resulted in a less favorable assessment of the quality of public and private institutions, which drops from 23rd last year to 41st. There seems to be a greater recognition within the institutional framework of the prevalence of corruption and government favoritism, as well as concerns about the independence of the judiciary. Not surprisingly, the security situation – one of the country's main competitive advantages in the past – is seen as more costly for business than in previous years (47th).

However, the country's core competitive strengths bode well for the future. First, Tunisia continues to display solid educational outcomes, which remain significantly above the North African average in terms of not only quality (33rd), but also participation at the primary and secondary levels (91.8 and 33.7 percent of the respective age groups) Second, the macroeconomic environment was traditionally maintained at a healthy state (38th in 2010), so the country's new government will benefit from manageable levels of public debt that will not significantly constrain investment in the future. Despite these strengths, the economic agenda is challenging. Political leaders must not lose sight of the long-term picture. Providing the country's youth with employment opportunities in the future will require not only stronger and more transparent institutions and a

more meritocratic business culture, but also a business environment that is more conducive to vibrant and healthy competition. Such an environment requires reducing domestic barriers to market entry – presently constrained by red tape and high taxes (107th and 122nd, respectively) – and lowering import tariffs. Some of the measures enacted by the interim government aim at fighting corruption and undue influence and will raise the country's competitiveness in the future.

Placing 73rd in the GCI, **Morocco** is consolidating its position. The country's strong macroeconomic fundamentals balance out some pronounced competitive weaknesses in other areas. A low fiscal deficit (1.8 percent of GDP in 2010), a favorable interest rate spread (18th), and low inflation (1 percent) contribute to a stable and predictable business environment. Likewise, some aspects of the institutional framework are assessed rather positively, such as public trust in politicians (48th) and the degree of government favoritism (46th). Morocco has made important progress in terms of reducing red tape when creating enterprises (34th for number of procedures to start a business) and reducing the burden of customs procedures (49th). Additional reforms were implemented in 2010 and 2011 to facilitate administrative procedures related to the functioning of enterprises.

According to the GCI, challenges persist in two areas that are important not only for competitiveness, but also for social cohesion in the country – education and the efficiency of labor markets. Education systems across all levels need improvement. Access to education is less prevalent than in other countries from the region, with enrolment rates for secondary and tertiary education remaining low (112th and 101st, respectively). At the same time, curricula and teaching methods are not aligned sufficiently with the needs of business (93rd). One positive aspect is the prevalence of on-the-job training (58th), which certainly has the potential to compensate for some shortcomings in the educational system. Yet, for education to translate into higher productivity, labor market structure must allow for an efficient use of talent and sufficient flexibility. This is currently not the case in Morocco, where labor market efficiency is assessed at 132nd overall. Labor market regulations are rigid with respect to the hiring process and wage setting, and meritocracy is not prevalent among management. Last but not least, the potential of the female labor force for productivity improvement is underused (134th).

Despite its undeniable potential, **Algeria** lags behind many other economies of the region, and ranks 87th overall. Although the country performs poorly on most of the categories of the GCI, the results point to a number of important advantages that support Algeria's potential going forward. First of all, the country has a fairly stable macroeconomic environment (19th), with a low budget deficit in 2010, almost no government debt, and a healthy national savings rate that could potentially provide funds for domestic investment. Together with Algeria's considerable domestic market size (47th), this advantage provides a good base for future development. The country also stands out positively in some aspects of the business environment, such as the relatively good participation in education (79th for secondary and 73rd for tertiary enrolment), as reflected in enrolment rates of 83.2 percent for the secondary level and 93.8 percent for the primary level.

However, a number of challenges remain to be tackled for Algeria to become more productive. First, the institutional set-up must be overhauled. Public institutions remain ridden with corruption (114th) and are subjected to undue influence (118th) and excessive red tape (136th).

The efficiency of markets for goods and services could be heightened by fostering more intense competition domestically and further opening the country to foreign trade and investment. Like some other countries in the region, Algeria is not a member of the World Trade Organization (WTO). As a result, tariff rates remain high (13.8 percent on average) and domestic rules discriminate against foreign investment (131st). With respect to labor market efficiency, a somewhat more mixed picture emerges. While hiring and firing practices are considered not too burdensome (79th), companies are not in a position to fully determine wages (125th) and talent is not used efficiently (141st).

Reforming financial markets is perhaps the most important task that Algeria's policy-makers need to tackle in order to enhance competitiveness. As it stands currently, the market is not fulfilling its function as provider of finance to the business community. Financial services are unavailable (139th) and expensive (142nd), and regulation and prudential supervision do not ensure that the financial system is sound and trustworthy: the country ranks 138th on the indicator measuring the soundness of banks.

Finally, the security situation imposes significant costs on doing business in the country (114th) due to terrorism as well as common crime and violence.

Moving Algeria to a higher growth trajectory will require that competitiveness-enhancing policy measures are put in place and that targeted investments are made. Overall, Algeria is well-positioned to move forward, given the country's endowments in natural resources and its geographical proximity to Europe. However, some recent policy measures, such as restrictions on FDI in key sectors, do not point in the right direction.

Egypt occupies the 94th position. Recent events brought to light the country's numerous challenges, in particular those related to the institutional environment.

The country's new political leadership will need to address several competitive challenges, starting with a reform of the labor market, which suffers from an inefficient use of available talent and rigid labor regulations. Unleashing job creation will also necessitate a continuation of private-led growth, as well as support for small and medium enterprises to mobilize additional demand for labor. All this must be combined with support for vibrant domestic competition and greater openness to trade and FDI. Combined with the country's large market size and its proximity to the large European market, competitiveness-enhancing reforms could efficiently enhance business activity in the short to medium term. A longer-term issue that remains to be tackled is the overhaul of the educational system. Reforms must ensure high enrolment and must gear educational outcomes more strongly towards the needs of the business community, thus addressing a pronounced skill mismatch that hinders additional employment creation.

The macroeconomic situation in Egypt is worrisome. Although public debt has been reduced in the past, the widening fiscal deficit and resulting inflationary pressures are expected to continue to burden the economy. In fact, such pressures are likely to increase in the coming years, as additional spending becomes necessary to address concerns about social injustice.

Going forward, providing Egypt's population with opportunities and prosperity will require putting the country on a more sustainable and inclusive growth path. If the upcoming political reforms are to boost economic growth, they must be accompanied by measures to raise the economy's productivity levels. Along with job creation, the most immediate focus should be on addressing security problems and lingering political uncertainty, which have recently limited economic growth.

Box 3: Competitiveness and Socio-Economic Development in Egypt: Priorities for the Future

By Magda Kandil and Iman Al-Ayouty, Egyptian Centre for Economic Studies

Out of 142 countries, Egypt occupies the 94th position in a year that has so far proven particularly challenging for the country. The weakening institutional environment contributed to a drop of 13 places in the ranking as compared to the Global Competitiveness Index (GCI) 2010-2011. Economic conditions are further burdened by a deterioration in the macroeconomic situation, a high level of unemployment, and a worsening standard of living coupled with widening inequality. Indeed, the fruits of high growth over the past few years were highly concentrated, with little wealth trickling down, owing to rampant corruption, inadequate human development, and lack of political reforms – all culminating in the outbreak of the January 25 revolution.

Despite reduced public debt (according to data included in the GCI), the widening fiscal deficit and resulting inflationary pressures are expected to continue to burden the economy going forward. The Egyptian government has been compelled to accommodate growing social demands in the form of higher wages and salaries to civil servants, new commitments to subsidies, and additional employment in the public sector – all resulting in higher consumption-based support after the revolution. If such measures are maintained without the necessary back-up of additional fiscal revenues, Egypt's competitiveness ranking may drop even further in the coming years.

The short- to medium-term social agenda should include concrete measures to ration government spending. Such rationing calls for a reform of the subsidy system towards a more targeted scheme that would help contain leakages and establish greater equity. In parallel, to mobilize additional revenues, reform of public finances should aim to widen the tax base, increase efficiency in tax collection, and encourage better compliance.

To improve social justice in the context of inclusive growth, economic priorities should be focused on providing more jobs in parallel with supporting productive activity. This should help vulnerable groups graduate from continued dependence on subsidies, and to capitalize on their skills so as to grow income in line with productivity. Yet unleashing job creation will also necessitate a continuation of private-led growth and the support of small and medium enterprises to mobilize additional demand for labor while enhancing domestic competition and promoting greater openness to trade and FDI.

Competitiveness-enhancing reforms call for overhauling the educational system and curricula, in order to increase the return on education. Specifically, Egypt needs to ensure high enrolment, gear educational outcomes more strongly towards the needs of the business community, and address a pronounced skill mismatch that has hindered additional employment creation to date. Enhancing competitiveness also calls for attention to the quality of scientific and research institutions, their twinning with business needs, the intensity of research and development, and its implications for product and process innovations.

The labor market in Egypt suffers from an inefficient use of available talent, rigid labor regulations, and an inadequate system of collective bargaining, coupled with the relative absence of trade unions as legitimate venues for voicing employees' concerns. To mobilize additional demand for labor, the government needs to continue its support to private sector activity via increasing tax incentives for job creation, providing concessionary credit to small and medium enterprises, investing in education and training, and increasing efficiency to close the gap between demand and supply. A reformed pay system should consider variations across sectors, based on economic indicators of growth and value added, to align wages with productivity indicators. Further, rules and regulations constraining hiring activity in the private formal sector should be revisited to ease structural bottlenecks and increase incentives for formality. On the supply side, there is a pressing need to change the current mindset from one that views vocational and technical education as a mere valve for easing pressure on universities, to one where such forms of education are sound means for aligning labor supply with business needs for highly skilled workers. As graduates of vocational schools constitute a large and growing group among new entrants into the labor market, such alignment becomes essential for reducing unemployment and increasing growth potential.

To conclude, the current political reform agenda should go hand-in-hand with a well-defined and forward-looking economic strategy. Investment in quality institutions, good governance, transparency, rule of law, improved domestic security, a much-streamlined bureaucracy, and drastically reduced corruption will boost investors' confidence and secure sustainable and equitable growth to increase the welfare of Egypt's growing population.

Competitiveness of Levantine Countries

Despite their geographical proximity, the three economies of the Levant region show a great degree of diversity in terms of national competitiveness. The range of GCI rankings, from Jordan at 71st to Lebanon at 89th and Syria at 98th, reflects the gap that exists between these economies, but also conceals significant differences in their respective competitive strengths and weaknesses.

Jordan (71st) experienced decreasing competitiveness over the past few years. Indeed, in the 2009 edition of the GCI, the country was ranked 50th. The drop reflects a weakening assessment of the institutional environment, as well as declining efficiency and stability of financial markets.

Jordan is well positioned to regain its competitiveness levels of a few years ago. Despite the more critical assessment, it still enjoys a fairly solid institutional set-up, with appropriately defined and enforced property rights for intellectual (40th) and physical and financial (34th) property, and levels of security that do not impose a particularly high cost on business (30th). Some transport infrastructure facilities are also assessed as satisfactory, in particular roads (47th) and air transport (34th). Labor markets (39th) are less rigid than in other countries in the region.

On a less positive note, Jordan will need to continue efforts to stabilize its macroeconomic environment (97th). The budget deficit remains at over 5 percent of GDP (in 2010) and government debt has surpassed 60 percent of GDP. If not addressed, these imbalances could have consequences for the future competitiveness of the Jordanian economy. Moreover, labor markets do not make talent available for the most productive use there is a weak culture of meritocracy in the country. Jordanian business leaders rate as very low the degree to which companies rely on professional qualifications as opposed to personal networks when deciding on management positions (100th). And while the efficiency of the goods market and the development of the financial sector are satisfactory (54th and 65th, respectively), tariffs remain high in international comparison (9.9 percent on average), and taxation is assessed as burdensome by the business community (99th). Further developing exports would help overcome the country's relatively small market size (88th).

Lebanon (89th) displays a number of competitive strengths and weaknesses. The country has one of the better educational systems in the region, with both the quality of teaching and enrolment rates being assessed as good (57th). While the overall quality of education is ranked 12th, math and science teaching (6th) is considered excellent by the business community, and Lebanon is also home to high-quality management schools (18th). To improve educational outcomes even further, Lebanese businesses should provide more opportunities for on-the-job training (98th) in order to ensure continuous learning and upgrading of skills. Another important competitive advantage is the presence of intense domestic competition on local markets (28th), which is one of the factors ensuring high efficiency in the goods market (35th). Low administrative barriers to entering markets (23rd for the number of procedures necessary to start a business) and a taxation system that limits distortions (21st) also contribute to a healthy, competitive environment. In this context, some room for further improvement remains with respect to streamlining customs procedures to facilitate the flow of goods over the border and continuing efforts to attract FDI.

Going forward, the key challenges for Lebanon remain the weak institutional set-up, underdeveloped infrastructure, and the country's difficult macroeconomic environment. Institutions suffer from corruption (132nd), inefficient government agencies (117th), and a judiciary that does not meet the needs of business (105th) and is subject to influence by others (127th). At the same time, the security situation imposes significant costs on the business community (105th), mainly due to the prevalence of terrorism (137th). Upgrading infrastructure in the country will necessitate stabilizing electricity supply (141st) and investing in roads and railroads (115th and 122nd, respectively). Such investment may necessitate private-sector participation, in view of the need for fiscal consolidation resulting from repeatedly high fiscal deficits (7.2 percent of GDP in 2010) and the unsustainable level of government debt (139.7 percent of GDP in 2010). However, given its solid base in terms of education and its entrepreneurial and dynamic environment, the country is well positioned to become more competitive and to reap the benefits in terms of higher growth – provided these key challenges are addressed.

Syria (98th) faces a number of important challenges related to competitiveness, some of which have led to ongoing social unrest since early 2011. Labor markets are among the most inefficient worldwide (134th), due to factors such as lack of meritocracy (139th) and low female participation (141st). Entrepreneurs also face significant rigidities when employing workers or adjusting the workforce to their needs. In fact, Syria ranks 93rd for labor market flexibility. Other markets suffer equally from inefficiencies. Financial markets are underdeveloped (117th), and access to finance remains constrained for the business sector (108th) across different types of products and services. However, in developing its financial markets, the country can build on a relatively sound banking system (59th). Progress in goods market efficiency will be crucial for Syria to raise its competitiveness. Markets remain to a large degree dominated by few firms (118th), anti-monopoly policy is inefficient (90th), and foreign competition remains constrained by high tariffs (122nd), other trade barriers (127th), cumbersome customs procedures (133rd), and rules governing FDI that discourage foreign investors (112th).

A longer-term challenge is to upgrade the educational system. Although the quality of primary education is satisfactory (67th), higher education and training lag behind those of other economies, and are among the key weaknesses in the country's competitiveness framework. Educational outcomes are poor both in terms of enrolment rates in secondary and tertiary education (98th and 78th, respectively) and in terms of quality of teaching, which is particularly poor in management schools (108th) and requires better alignment to business needs (96th). Competitiveness-enhancing reforms would lift the country onto a higher growth path, which in turn would enable it to pursue greater social cohesion.

Conclusions

This chapter has analyzed the performance of 14 Arab countries in terms of national competitiveness using the framework of the Global Competitiveness Index. The countries analyzed include Algeria, Bahrain, Egypt, Jordan, Lebanon, Morocco, Kuwait, Oman, Qatar, Saudi Arabia, Syria, Tunisia, United Arab Emirates, and Yemen.

The analysis shows that the countries are highly diverse in terms of national competitiveness. While most Gulf economies benefit from vast natural resources and rising energy prices, and have used the ensuing revenues in recent years for improvements in their competitiveness, the challenges are more profound in North Africa and the Levant. Economies in these two sub-regions – with the notable exception of Tunisia, which ranks a strong 40th out of 142 countries – display numerous competitive weaknesses that will have to be addressed going forward, especially in light of the employment challenges these countries face. Most important, education systems must be upgraded to better respond to the needs of business, and markets must be made more efficient by moving towards healthier competition, fostering entrepreneurship, and supporting a more dynamic environment for enterprises. Education and market efficiency are the two key aspects that would address crucial supply- and demand-side challenges to job creation.

The Arab Spring has led to significant turbulence in the region, which will likely influence the economic and competitive performance of countries in the shorter and longer term. Uncertainty about the future business environment, as well as a heightened awareness of some institutional weaknesses, may have adverse effects in the short term. However, the political changes and the recognition of the need to create private-sector employment have significant potential to drive the political momentum needed for enhanced competitiveness in the medium term.

Creating gainful employment for their populations is currently the key challenge for most of the countries from the region. Competitiveness-enhancing reforms will pave the way to more private-sector activity that will lead to the creation of gainful and sustainable employment across the region for the benefit of both present and future generations.

Notes

¹ For a more detailed discussion of the 12 pillars and their contributions to competitiveness, see Sala-i-Martin et al. 2010. Appendix A shows the detailed structure of the GCI.

² This is proxied by the share of exports of mineral products as a share of total exports.

³ For a detailed breakdown of survey respondents and more details about the Executive Opinion Survey and the processing of the data, see Browne and Geiger 2011.

⁴ Taking into account the countries covered by this chapter.

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Appendix A: Computation and Structure of the Global Competitiveness Index 2011-2012

This appendix presents the structure of the Global Competitiveness Index 2011-2012 (GCI). The number preceding the period indicates to which pillar the variable belongs (e.g. variable **1.01** belongs to the 1st pillar and variable **12.04** belongs to the 12th pillar).

The computation of the GCI is based on successive aggregations of scores from the indicator level (i.e., the most disaggregated level) all the way up to the overall GCI score. Unless otherwise mentioned, we use an arithmetic mean to aggregate individual variables within a category.^a For higher aggregation levels, we use the percentage shown next to each category. This percentage represents the category's weight within its immediate parent category. Reported percentages are rounded to the nearest integer, but exact figures are used in the calculation of the GCI. For example, the score a country achieves in Pillar 9 accounts for 17 percent of the country's score in the efficiency enhancers sub-index, irrespective of the country's stage of development. Similarly, the score achieved on the sub-pillar *transport infrastructure* accounts for 50 percent of the score of the infrastructure pillar.

Unlike the case for lower levels of aggregation, the weight put on each of the three sub-indexes (*basic requirements, efficiency enhancers, and innovation and sophistication factors*) is not fixed. Instead, it depends on each country's stage of development, as discussed in the article.^b For instance, in the case of Yemen – a country in the first stage of development – the score in the basic requirements sub-index accounts for 60 percent of its overall GCI score, while it represents just 20 percent of the overall GCI score of Bahrain, a country in the third stage of development.

Variables that are not derived from the Executive Opinion Survey (Survey) are identified by an asterisk (*) in the following pages. The Technical Notes and Sources section in Appendix B provides detailed information about these indicators. To make the aggregation possible, these variables are transformed onto a 1-to-7 scale to align them with the survey results. We apply a *min-max* transformation, which preserves the order of, and the relative distance between, country scores.

Variables that are followed by the designation "1/2" enter the GCI in two different pillars; to avoid double counting, we assign a half-weight to each instance.^d

Basic Requirements	Weight (%) within immediate parent category	
Pillar 1: Institutions	25%	Pillar 2: Infrastructure
A. Public institutions	75%	A. Transport infrastructure
1. Property rights	20%	2.01 Quality of overall infrastructure
1.01 Property rights		2.02 Quality of roads
1.02 Intellectual property protection ^{1/2}		2.03 Quality of railroad infrastructure
2. Ethics and corruption	20%	2.04 Quality of port infrastructure
1.03 Diversion of public funds		2.05 Quality of air transport infrastructure
1.04 Public trust of politicians		2.06 Available seat kilometers*
1.05 Irregular payments and bribes		B. Energy and telephony infrastructure
3. Undue influence	20%	2.07 Quality of electricity supply
1.06 Judicial independence		2.08 Fixed telephone lines* ^{1/2}
1.07 Favoritism in decisions of government officials		2.09 Mobile telephone subscriptions* ^{1/2}
4. Government inefficiency	20%	Pillar 3: Macroeconomic environment
1.08 Wastefulness of government spending		3.01 Government budget balance*
1.09 Burden of government regulation		3.02 National savings rate*
1.10 Efficiency of legal framework in settling disputes		3.03 Inflation* e
1.11 Efficiency of legal framework in challenging regulations		3.04 Interest rate spread*
1.12 Transparency of government policy-making		3.05 Government debt*
5. Security	20%	3.06 Country credit rating*
1.13 Business costs of terrorism		Pillar 4: Health and primary education
1.14 Business costs of crime and violence		A. Health
1.15 Organized crime		4.01 Business impact of malaria ^f
1.16 Reliability of police services		4.02 Malaria incidence* ^f
B. Private institutions	25%	4.03 Business impact of tuberculosis ^f
1. Corporate ethics	50%	4.04 Tuberculosis incidence* ^f
1.17 Ethical behavior of firms		4.05 Business impact of HIV/AIDS ^f
2. Accountability	50%	4.06 HIV prevalence* ^f
1.18 Strength of auditing and reporting standards		4.07 Infant mortality*
1.19 Efficacy of corporate boards		4.08 Life expectancy*
1.20 Protection of minority shareholders' interests		B. Primary education
1.21 Strength of investor protection*		4.09 Quality of primary education
		4.10 Primary education enrolment rate* ^g

Efficiency Enhancers

Pillar 5: Higher education and training 17%

- A. Quantity of education 33%
 - 5.01 Secondary education enrolment rate*
 - 5.02 Tertiary education enrolment rate*
- B. Quality of education 33%
 - 5.03 Quality of the educational system
 - 5.04 Quality of math and science education
 - 5.05 Quality of management schools
 - 5.06 Internet access in schools
- C. On-the-job training 33%
 - 5.07 Local availability of specialized research and training services
 - 5.08 Extent of staff training

Pillar 6: Goods market efficiency 17%

- A. Competition 67%
 - 1. Domestic competition variable h
 - 6.01 Intensity of local competition
 - 6.02 Extent of market dominance
 - 6.03 Effectiveness of anti-monopoly policy
 - 6.04 Extent and effect of taxation ^{1/2}
 - 6.05 Total tax rate*
 - 6.06 Number of procedures required to start a business*ⁱ
 - 6.07 Time required to start a business*ⁱ
 - 6.08 Agricultural policy costs
 - 2. Foreign competition variable h
 - 6.09 Prevalence of trade barriers
 - 6.10 Trade tariffs*
 - 6.11 Prevalence of foreign ownership
 - 6.12 Business impact of rules on FDI
 - 6.13 Burden of customs procedures
 - 10.04 Imports as a percentage of GDP*^g
- B. Quality of demand conditions 33%
 - 6.14 Degree of customer orientation
 - 6.15 Buyer sophistication

Pillar 7: Labor market efficiency 17%

- A. Flexibility 50%
 - 7.01 Cooperation in labor-employer relations
 - 7.02 Flexibility of wage determination
 - 7.03 Rigidity of employment*
 - 7.04 Hiring and firing practices
 - 7.05 Redundancy costs*
 - 6.04 Extent and effect of taxation ^{1/2}
- B. Efficient use of talent 50%
 - 7.06 Pay and productivity
 - 7.07 Reliance on professional management ^{1/2}
 - 7.08 Brain drain
 - 7.09 Female participation in labor force*

Pillar 8: Financial market development 17%

- A. Efficiency 50%
 - 8.01 Availability of financial services
 - 8.02 Affordability of financial services
 - 8.03 Financing through local equity market
 - 8.04 Ease of access to loans
 - 8.05 Venture capital availability
- B. Trustworthiness and confidence 50%
 - 8.07 Soundness of banks
 - 8.08 Regulation of securities exchanges
 - 8.09 Legal rights index*

Pillar 9: Technological readiness 17%

- A. Technological adoption 50%
 - 9.01 Availability of latest technologies
 - 9.02 Firm-level technology absorption
 - 9.03 FDI and technology transfer
- B. ICT use 50%
 - 9.04 Internet users*
 - 9.05 Broadband Internet subscriptions*
 - 9.06 Internet bandwidth*
 - 2.08 Fixed telephone lines* ^{1/2}
 - 2.09 Mobile telephone subscriptions* ^{1/2}

Pillar 10: Market size 17%

- A. Domestic market size 75%
 - 10.01 Domestic market size index*^j
- B. Foreign market size 25%
 - 10.02 Foreign market size index*^k

Innovation and Sophistication Factors

Pillar 11: Business sophistication 50%

- 11.01 Local supplier quantity
- 11.02 Local supplier quality
- 11.03 State of cluster development
- 11.04 Nature of competitive advantage
- 11.05 Value chain breadth
- 11.06 Control of international distribution
- 11.07 Production process sophistication
- 11.08 Extent of marketing
- 11.09 Willingness to delegate authority
- 7.07 Reliance on professional management ^{1/2}

Pillar 12: Innovation..... 50%

- 12.01 Capacity for innovation
- 12.02 Quality of scientific research institutions
- 12.03 Company spending on R&D
- 12.04 University-industry collaboration in R&D
- 12.05 Government procurement of advanced technology products
- 12.06 Availability of scientists and engineers
- 12.07 Utility patents*
- 1.02 Intellectual property protection ^{1/2}

Notes

- a. Formally, for a category i composed of K indicators, we have:

$$\text{category}_i = \frac{\sum_{k=1}^K \text{indicator}_k}{K}$$

- b. As described in the article, the weights are the following:

Weights	Factor-driven stage (%)	Efficiency-driven stage (%)	Innovation-driven stage (%)
Basic requirements	60	40	20
Efficiency enhancers	35	50	50
Innovation & sophistication factors	5	10	30

- c. Formally, we have:

$$6 \times \frac{(\text{country score} - \text{sample minimum})}{(\text{sample maximum} - \text{sample minimum})} + 1$$

The sample minimum and sample maximum are, respectively, the lowest and highest country scores in the sample of economies covered by the GCI. In some instances, adjustments were made to account for extreme outliers. For those indicators for which a higher value indicates a worse outcome (e.g. disease incidence, government debt), the transformation formula takes the following form, thus ensuring that 1 and 7 still correspond to the worst and best possible outcomes, respectively:

- d. For those categories that contain one or several half-weight variables, country scores for those groups are computed as follows:

$$\frac{(\text{sum of scores on full-weight variables}) + \frac{1}{2} \times (\text{sum of scores on half-weight variables})}{(\text{count of full-weight variables}) + \frac{1}{2} \times (\text{count of half-weight variables})}$$

- e. To capture the idea that both high inflation and deflation are detrimental, inflation enters the model in a U-shaped manner as follows: for values of inflation between 0.5 and 2.9 percent, a country receives the highest possible score of 7. Outside this range, scores decrease linearly as they move away from these values.
- f. The impact of malaria, tuberculosis, and HIV/AIDS on competitiveness depends not only on their respective incidence rates but also on how costly they are for business. Therefore, to estimate the impact of each of the three diseases, we combine its incidence rate with the survey question on its perceived cost to businesses. To combine these data, we first take the ratio of each country's disease incidence rate relative to the highest incidence rate in the whole sample. The inverse of this ratio is then multiplied by each country's score on the related survey question. This product is then normalized to a 1-to-7 scale. Note that countries with zero reported incidences receive a 7, regardless of their scores on the related survey question.

- g. For this variable, we first apply a log-transformation and then a min-max transformation.
- h. The competition sub-pillar is the weighted average of two components: domestic competition and foreign competition. In both components, the included variables provide an indication of the extent to which competition is distorted. The relative importance of these distortions depends on the relative size of domestic versus foreign competition. This interaction between the domestic market and the foreign market is captured by the way we determine the weights of the two components. Domestic competition is the sum of consumption (C), investment (I), government spending (G), and exports (X), while foreign competition is equal to imports (M). Thus we assign a weight of $(C + I + G + X)/(C + I + G + X + M)$ to domestic competition and a weight of $M/(C + I + G + X + M)$ to foreign competition.
- i. Variables 6.06 and 6.07 combine to form one single variable.
- j. The size of the domestic market is constructed by taking the natural log of the sum of the gross domestic product valued at purchasing power parity (PPP) plus the total value (PPP estimates) of imports of goods and services, minus the total value (PPP estimates) of exports of goods and services. Data are then normalized on a 1-to-7 scale. PPP estimates of imports and exports are obtained by taking the product of exports as a percentage of GDP and GDP valued at PPP. The underlying data are reported in the data tables section (see Tables 10.03, 10.04, and 10.05).
- k. The size of the foreign market is estimated as the natural log of the total value (PPP estimates) of exports of goods and services, normalized on a 1-to-7 scale. PPP estimates of exports are obtained by taking the product of exports as a percentage of GDP and GDP valued at PPP. The underlying data are reported in the data tables.

Appendix B: Technical Notes and Sources for the Global Competitiveness Index

Institutions

1.01 Property rights

How would you rate the protection of property rights, including financial assets, in your country? [1 = very weak; 7 = very strong] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.02 Intellectual property protection

How would you rate intellectual property protection, including anti-counterfeiting measures, in your country? [1 = very weak; 7 = very strong] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.03 Diversion of public funds

In your country, how common is diversion of public funds to companies, individuals, or groups due to corruption? [1 = very common; 7 = never occurs] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.04 Public trust of politicians

How would you rate the level of public trust in the ethical standards of politicians in your country? [1 = very low; 7 = very high] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.05 Irregular payments and bribes

Average score across the five components of the following Survey questions: In your country, how common is it for firms to make undocumented extra payments or bribes connected with (a) imports and exports; (b) public utilities; (c) annual tax payments; (d) awarding of public contracts and licenses; (e) obtaining favorable judicial decisions? In each case, the answer ranges from 1 (very common) to 7 (never occurs). | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.06 Judicial independence

To what extent is the judiciary in your country independent from influences of members of government, citizens, or firms? [1 = heavily influenced; 7 = entirely independent] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.07 Favoritism in decisions of government officials

To what extent do government officials in your country show favoritism to well-connected firms and individuals when deciding upon policies and contracts? [1 = always show favoritism; 7 = never show favoritism] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.08 Wastefulness of government spending

How would you rate the composition of public spending in your country? [1 = extremely wasteful; 7 = highly efficient in providing necessary goods and services] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.09 Burden of government regulation

How burdensome is it for businesses in your country to comply with governmental administrative requirements (e.g. permits, regulations, reporting)? [1 = extremely burdensome; 7 = not burdensome at all] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.1 Efficiency of legal framework in settling disputes

How efficient is the legal framework in your country for private businesses in settling disputes? [1 = extremely inefficient; 7 = highly efficient] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.11 Efficiency of legal framework in challenging regulations

How efficient is the legal framework in your country for private businesses in challenging the legality of government actions and/or regulations? [1 = extremely inefficient; 7 = highly efficient] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.12 Transparency of government policy-making

How easy is it for businesses in your country to obtain information about changes in government policies and regulations affecting their activities? [1 = impossible; 7 = extremely easy] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

1.13 Business costs of terrorism

To what extent does the threat of terrorism impose costs on businesses in your country? [1 = to a great extent; 7 = not at all] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

1.14 Business costs of crime and violence

To what extent does the incidence of crime and violence impose costs on businesses in your country? [1 = to a great extent; 7 = not at all] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

1.15 Organized crime

To what extent does organized crime (mafia-oriented racketeering, extortion) impose costs on businesses in your country? [1 = to a great extent; 7 = not at all] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

1.16 Reliability of police services

To what extent can police services be relied upon to enforce law and order in your country? [1 = cannot be relied upon at all; 7 = can be completely relied upon] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

1.17 Ethical behavior of firms

How would you compare the corporate ethics (ethical behavior in interactions with public officials, politicians, and other enterprises) of firms in your country with those of other countries in the world? [1 = among the worst in the world; 7 = among the best in the world] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

1.18 Strength of auditing and reporting standards

In your country, how would you assess financial auditing and reporting standards regarding company financial performance? [1 = extremely weak; 7 = extremely strong] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

1.19 Efficacy of corporate boards

How would you characterize corporate governance by investors and boards of directors in your country? [1 = management has little accountability to investors and boards; 7 = investors and boards exert strong supervision of management decisions] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

1.2 Protection of minority shareholders' interests

In your country, to what extent are the interests of minority shareholders protected by the legal system? [1 = not protected at all; 7 = fully protected] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

1.21 Strength of investor protection

Strength of Investor Protection Index on a 0-10 (best) scale | 2010
This variable is a combination of the Extent of disclosure index (transparency of transactions), the Extent of director liability index (liability for self-dealing), and the Ease of shareholder suit index (shareholders' ability to sue officers and directors for misconduct).
Source: World Bank/International Finance Corporation, Doing Business 2011: Making a Difference for Entrepreneurs

Infrastructures

2.01 Quality of overall infrastructure

How would you assess general infrastructure (e.g. transport, telephony, and energy) in your country? [1 = extremely underdeveloped; 7 = extensive and efficient by international standards] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

2.02 Quality of roads

How would you assess roads in your country? [1 = extremely underdeveloped; 7 = extensive and efficient by international standards] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

2.03 Quality of railroad infrastructure

How would you assess the railroad system in your country? [1 = extremely underdeveloped; 7 = extensive and efficient by international standards] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

2.04 Quality of port infrastructure

How would you assess port facilities in your country? [1 = extremely underdeveloped; 7 = well developed and efficient by international standards] For landlocked countries, the question is as follows: How accessible are port facilities? [1 = extremely inaccessible; 7 = extremely accessible] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

2.05 Quality of air transport infrastructure

How would you assess passenger air transport infrastructure in your country? [1 = extremely underdeveloped; 7 = extensive and efficient by international standards] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

2.06 Available airline seat kilometers

Scheduled available airline seat kilometers per week originating in country (in millions) | 2011
This variable measures the total passenger-carrying capacity of all scheduled flights, including domestic flights, originating from a country. It is computed by taking the number of seats available on each flight multiplied by the flight distance in kilometers, summing the result across all scheduled flights in a week during January (winter schedule) and July (summer schedule) 2011, and taking the average capacity of the two weeks.

Source: International Air Transport Association, SRS Analyser

2.07 Quality of electricity supply

How would you assess the quality of the electricity supply in your country (lack of interruptions and lack of voltage fluctuations)? [1 = insufficient and suffers frequent interruptions; 7 = sufficient and reliable] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

2.08 Fixed telephone lines

Number of active fixed telephone lines per 100 population | 2010

A *fixed telephone line* is an active line connecting the subscriber's terminal equipment to the public switched telephone network and having a dedicated port in the telephone exchange equipment. Active lines are those that have registered an activity in the past three months.
Source: *International Telecommunication Union, World Telecommunication/ICT Indicators 2011 (June 2011 edition)*

2.09 Mobile telephone subscriptions

Number of mobile cellular telephone subscriptions per 100 population | 2010

This measure refers to subscriptions to a public mobile telephone service that provides access to public switched telephone network using cellular technology, including the number of pre-paid SIM cards active during the past three months. This includes both analogue and digital cellular systems and 4G subscriptions, but excludes mobile broadband subscriptions via data cards or USB modems.

Source: *International Telecommunication Union, World Telecommunication/ICT Indicators 2011 (June 2011 edition)*

Macroeconomic environment

3.01 Government budget balance

General government budget balance as a percentage of GDP | 2010

Net lending (+)/ borrowing (-) is calculated as general government revenue minus total expenditure. This is a core Government Finance Statistics balance that measures the extent to which general government is either putting financial resources at the disposal of other sectors in the economy and non-residents (net lending), or utilizing the financial resources generated by other sectors and non-residents (net borrowing). This balance may be viewed as an indicator of the financial impact of general government activity on the rest of the economy and non-residents. Revenue consists of taxes, social contributions, grants receivable, and other revenue. Revenue increases government's net worth, which is the difference between its assets and liabilities. General government total expenditure consists of total expense and the net acquisition of nonfinancial assets.

Source: *International Monetary Fund, World Economic Outlook Database (April 2011 edition); African Development Bank, African Statistical Yearbook 2011; AfricanEconomicOutlook.org (accessed July 1, 2011); national sources*

3.02 Gross national savings

Gross national savings as a percentage of GDP | 2010

Aggregate national savings is defined as public and private sector savings as a percentage of nominal GDP. National savings equals gross domestic investment plus the current-account balance.

Source: *International Monetary Fund, World Economic Outlook Database (April 2011 edition) and Public Information Notices (various issues); national sources*

3.03 Inflation

Annual percent change in consumer price index (year average) | 2010

Annual percent change in year average consumer price index

Source: *International Monetary Fund, World Economic Outlook Database (April 2011 edition); national sources [D6]. NOTE: See Appendix A of Chapter 1.1 for details about the treatment of inflation in the Global Competitiveness Index.*

3.04 Interest rate spread

Average interest rate spread between typical lending and deposit rates | 2010

This measures the difference between the typical short-term lending and deposit rates.

Source: *International Monetary Fund, International Financial Statistics' database (accessed 17 July 2011) and country tables (July 2011); Economist Intelligence Unit, CountryData Database (accessed 17 July 2011)*

3.05 Government debt

Gross general government debt as a percentage of GDP | 2010

Gross debt consists of all liabilities that require payment or payments of interest and/or principal by the debtor to the creditor at a date or dates in the future. This includes debt liabilities in the form of special drawing rights, currency and deposits, debt securities, loans, insurance, pensions and standardized guarantee schemes, and other accounts payable. Thus, all liabilities in the *Government Finance Statistics Manual 2001* system are debt, except for equity and investment fund shares and financial derivatives and employee stock options.

Source: *International Monetary Fund, World Economic Outlook Database (April 2011 edition) and Public Information Notices (various issues); Asian Development Bank, Asian Development Outlook 2011; Economist Intelligence Unit, CountryData Database (accessed 17 July 2011); national sources*

3.06 Country credit rating

Expert assessment of the probability of sovereign debt default on a 0-100 (lowest probability) scale | March 2011

Institutional Investor's Country Credit ratings, developed by Institutional Investor, are based on information provided by senior economists and sovereign-debt analysts at leading global banks and money management and security firms. Twice a year, the respondents grade each country on a scale of 0 to 100, with 100 representing the least chance of default.

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Health and primary education

4.01 Business impact of malaria

How serious an impact do you consider malaria will have on your company in the next five years (e.g. death, disability, medical and funeral expenses, productivity and absenteeism, recruitment and training expenses, revenues)? [1 = a serious impact; 7 = no impact at all] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

4.02 Malaria incidence

Number of malaria cases per 100,000 population | 2006

Source: *World Health Organization, World Malaria Report 2008; national sources [D6]*

4.03 Business impact of tuberculosis

How serious an impact do you consider tuberculosis will have on your company in the next five years (e.g. death, disability, medical and funeral expenses, productivity and absenteeism, recruitment and training expenses, revenues)? [1 = a serious impact; 7 = no impact at all] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

4.04 Tuberculosis incidence

Number of tuberculosis cases per 100,000 population | 2009

Source: *The World Bank, World Development Indicators & Global Development Finance Catalog (April 2011 edition); national sources*

4.05 Business impact of HIV/AIDS

How serious an impact do you consider HIV/AIDS will have on your company in the next five years (e.g. death, disability, medical and funeral expenses, productivity and absenteeism, recruitment and training expenses, revenues)? [1 = a serious impact; 7 = no impact at all] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

4.06 HIV prevalence

HIV prevalence as a percentage of adults aged 15-49 years | 2009

Source: *UNAIDS, Global Report on the Global AIDS Epidemic (2008 and 2010 editions); United Nations Development Programme, Human Development Report 2007/2008; national sources*

4.07 Infant mortality

Infant (children aged 0-12 months) mortality per 1,000 live births | 2009

Source: *The World Bank, World Development Indicators & Global Development Finance Catalog (April 2011 edition); national sources*

4.08 Life expectancy

Life expectancy at birth (years) | 2009

Source: *The World Bank, World Development Indicators & Global Development Finance Catalog (April 2011 edition); national sources*

4.09 Quality of primary education

How would you assess the quality of primary schools in your country? [1 = poor; 7 = excellent – among the best in the world] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

4.1 Primary education enrolment rate

Net primary education enrolment rate | 2008

The reported value corresponds to the ratio of children of official school age (as defined by the national education system) who are enrolled in school to the total population of the corresponding official school age. Primary education (ISCED level 1) provides children with basic reading, writing, and mathematics skills, along with an elementary understanding of such subjects as history, geography, natural science, social science, art, and music.

Source: *UNESCO Institute for Statistics (accessed May 4, 2011); UNICEF ChildInfo.org Country Profiles; UN Millennium Development Indicators; The World Bank, EdStats Database (accessed July 8, 2011); national sources*

Higher education and training

5.01 Secondary education enrolment rate

Gross secondary education enrolment rate | 2008

The reported value corresponds to the ratio of total secondary enrolment, regardless of age, to the population of the age group that officially corresponds to the secondary education level. Secondary education (ISCED levels 2 and 3) completes the provision of basic education that began at the primary level, and aims to lay the foundations for lifelong learning and human development, by offering more subject- or skills-oriented instruction using more specialized teachers.

Source: UNESCO Institute for Statistics (accessed May 4, 2011); UNICEF ChildInfo.org Country Profiles; The World Bank, EdStats Database (accessed July 8, 2011); national sources and The World Development Indicators 2009 (CD-Rom edition)

5.02 Tertiary education enrolment rate

Gross tertiary education enrolment rate | 2008

The reported value corresponds to the ratio of total tertiary enrolment, regardless of age, to the population of the age group that officially corresponds to the tertiary education level. Tertiary education (ISCED levels 5 and 6), whether or not leading to an advanced research qualification, normally requires, as a minimum condition of admission, the successful completion of education at the secondary level.

Source: UNESCO Institute for Statistics (accessed May 4, 2011); UNICEF ChildInfo.org Country Profiles; The World Bank, EdStats Database (accessed July 8, 2011); national sources and The World Development Indicators 2009 (CD-Rom edition)

5.03 Quality of the educational system

How well does the educational system in your country meet the needs of a competitive economy? [1 = not well at all; 7 = very well] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

5.04 Quality of math and science education

How would you assess the quality of math and science education in your country's schools? [1 = poor; 7 = excellent – among the best in the world] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

5.05 Quality of management schools

How would you assess the quality of management or business schools in your country? [1 = poor; 7 = excellent – among the best in the world] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

5.06 Internet access in schools

How would you rate the level of access to the Internet in schools in your country? [1 = very limited; 7 = extensive] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

5.07 Local availability of specialized research and training services

In your country, to what extent are high-quality, specialized training services available? [1 = not available; 7 = widely available] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

5.08 Extent of staff training

To what extent do companies in your country invest in training and employee development? [1 = hardly at all; 7 = to a great extent] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

Goods market efficiency

6.01 Intensity of local competition

How would you assess the intensity of competition in the local markets in your country? [1 = limited in most industries; 7 = intense in most industries] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

6.02 Extent of market dominance

How would you characterize corporate activity in your country? [1 = dominated by a few business groups; 7 = spread among many firms] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

6.03 Effectiveness of anti-monopoly policy

To what extent does anti-monopoly policy promote competition in your country? [1 = does not promote competition; 7 = effectively promotes competition] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

6.04 Extent and effect of taxation

What impact does the level of taxes in your country have on incentives to work or invest? [1 = significantly limits incentives to work or invest; 7 = has no impact on incentives to work or invest] | 2010-11 weighted average
 Source: *World Economic Forum, Executive Opinion Survey*

6.05 Total tax rate

This variable is a combination of profit tax (% of profits), labor tax and contribution (% of profits), and other taxes (% of profits) | 2010
 The total tax rate measures the amount of taxes and mandatory contributions payable by a business in the second year of operation, expressed as a share of commercial profits. The total amount of taxes is the sum of five different types of taxes and contributions payable after accounting for deductions and exemptions: profit or corporate income taxes, social contributions and labor taxes paid by the employer, property taxes, turnover taxes, and other small taxes. For more details about the methodology employed and the assumptions made to compute this indicator, please visit <http://www.doingbusiness.org/methodologysurveys/>.
 Source: *World Bank/International Finance Corporation, Doing Business 2011: Making a Difference for Entrepreneurs*

6.06 Number of procedures required to start a business

Number of procedures required to start a business | 2010
 For details about the methodology employed and the assumptions made to compute this indicator, please visit <http://www.doingbusiness.org/methodologysurveys/>.
 Source: *World Bank/International Finance Corporation, Doing Business 2011: Making a Difference for Entrepreneurs*

6.07 Time required to start a business

Number of days required to start a business | 2010
 For details about the methodology employed and the assumptions made to compute this indicator, please visit <http://www.doingbusiness.org/methodologysurveys/>.
 Source: *World Bank/International Finance Corporation, Doing Business 2011: Making a Difference for Entrepreneurs*

6.08 Agricultural policy costs

How would you assess the agricultural policy in your country? [1 = excessively burdensome for the economy; 7 = balances the interests of taxpayers, consumers, and producers] | 2010-11 weighted average
 Source: *World Economic Forum, Executive Opinion Survey*

6.09 Prevalence of trade barriers

In your country, to what extent do tariff and non-tariff barriers limit the ability of imported goods to compete in the domestic market? [1 = strongly limit; 7 = do not limit] | 2010-11 weighted average
 Source: *World Economic Forum, Executive Opinion Survey*

6.1 Trade tariffs

Trade-weighted average tariff rate | 2010
 This indicator is calculated as the average of the applied tariff rates, including preferential rates that a country applies to the rest of the world. The trade pattern of the importing country's reference group (2007 data) is used as a weighting.
 Source: *International Trade Centre*

6.11 Prevalence of foreign ownership

How prevalent is foreign ownership of companies in your country? [1 = very rare; 7 = highly prevalent] | 2010-11 weighted average
 Source: *World Economic Forum, Executive Opinion Survey*

6.12 Business impact of rules on FDI

To what extent do rules governing foreign direct investment (FDI) encourage or discourage it? [1 = strongly discourage FDI; 7 = strongly encourage FDI] | 2010-11 weighted average
 Source: *World Economic Forum, Executive Opinion Survey*

6.13 Burden of customs procedures

How would you rate the level of efficiency of customs procedures (related to the entry and exit of merchandise) in your country? [1 = extremely inefficient; 7 = extremely efficient] | 2010-11 weighted average
 Source: *World Economic Forum, Executive Opinion Survey*

6.14 Imports as a percentage of GDP

Imports of goods and services as a percentage of gross domestic product | 2010
 Source: *World Trade Organization, Statistics Database: Time Series on International Trade (accessed July 4, 2011); Economist Intelligence Unit, CountryData Database (accessed July 4, 2011)*

6.15 Degree of customer orientation
How well do companies in your country treat customers? [1 = generally treat their customers badly; 7 = are highly responsive to customers and customer retention] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

6.16 Buyer sophistication
In your country, how do buyers make purchasing decisions? [1 = based solely on the lowest price; 7 = based on a sophisticated analysis of performance attributes] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

Labor market efficiency

7.01 Cooperation in labor-employer relations
How would you characterize labor-employer relations in your country? [1 = generally confrontational; 7 = generally cooperative] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

7.02 Flexibility of wage determination
How are wages generally set in your country? [1 = by a centralized bargaining process; 7 = up to each individual company] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

7.03 Rigidity of employment
Rigidity of Employment Index on a 0-100 (worst) scale | 2009
This index is the average of three sub-indexes: Difficulty of hiring, Rigidity of hours, and Difficulty of firing. The three sub-indexes have several components and all take values between 0 and 100, with higher values indicating more rigid regulation.

Source: World Bank/International Finance Corporation, Doing Business 2010: Reforming Through Difficult Times

7.04 Hiring and firing practices
How would you characterize the hiring and firing of workers in your country? [1 = impeded by regulations; 7 = flexibly determined by employers] | 2010-11 weighted average
Source: World Economic Forum, Executive Opinion Survey

7.05 Redundancy costs
Redundancy costs in weeks of salary | 2009
This variable estimates the cost of advance notice requirements, severance payments, and penalties due when terminating a redundant worker, expressed in weekly wages.

Source: World Bank/International Finance Corporation, Doing Business 2010: Reforming Through Difficult Times

7.06 Pay and productivity
To what extent is pay in your country related to productivity? [1 = not related to worker productivity; 7 = strongly related to worker productivity] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

7.07 Reliance on professional management
In your country, who holds senior management positions? [1 = usually relatives or friends without regard to merit; 7 = mostly professional managers chosen for merit and qualifications] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

7.08 Brain drain
Does your country retain and attract talented people? [1 = no, the best and brightest normally leave to pursue opportunities in other countries; 7 = yes, there are many opportunities for talented people within the country] | 2010-11 weighted average

Source: World Economic Forum, Executive Opinion Survey

7.09 Female participation in labor force
Ratio of female participation in the labor force (%) to male participation in the labor force (%) | 2009
This measure is the percentage of women aged 15-64 participating in the labor force divided by the percentage of men aged 15-64 participating in the labor force.

Source: International Labour Organization, Key Indicators of the Labor Markets Net (accessed 4 May 2011); national sources

Financial market development

8.01 Availability of financial services

Does the financial sector in your country provide a wide variety of financial products and services to businesses? [1 = not at all; 7 = provides a wide variety] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

8.02 Affordability of financial services

To what extent does competition among providers of financial services in your country ensure the provision of financial services at affordable prices? [1 = not at all; 7 = extremely well] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

8.03 Financing through local equity market

How easy is it to raise money by issuing shares on the stock market in your country? [1 = very difficult; 7 = very easy] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

8.04 Ease of access to loans

How easy is it to obtain a bank loan in your country with only a good business plan and no collateral? [1 = very difficult; 7 = very easy] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

8.05 Venture capital availability

In your country, how easy is it for entrepreneurs with innovative but risky projects to find venture capital? [1 = very difficult; 7 = very easy] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

8.06 Soundness of banks

How would you assess the soundness of banks in your country? [1 = insolvent and may require a government bailout; 7 = generally healthy with sound balance sheets] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

8.07 Regulation of securities exchanges

How would you assess the regulation and supervision of securities exchanges in your country? [1 = ineffective; 7 = effective] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

8.08 Legal rights index

Degree of legal protection of borrowers and lenders' rights on a 0-10 (best) scale | 2010
This index measures the degree to which collateral and bankruptcy laws protect borrowers and lenders' rights and thus facilitate lending.
Source: *World Bank/International Finance Corporation, Doing Business 2011: Making a Difference for Entrepreneurs*

Technological readiness

9.01 Availability of latest technologies

To what extent are the latest technologies available in your country? [1 = not available; 7 = widely available] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

9.02 Firm-level technology absorption

To what extent do businesses in your country absorb new technology? [1 = not at all; 7 = aggressively absorb] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

9.03 FDI and technology transfer

To what extent does foreign direct investment (FDI) bring new technology into your country? [1 = not at all; 7 = FDI is a key source of new technology] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

9.04 Internet users

Percentage of individuals using the Internet | 2010
Internet users refers to people using the Internet from any device (including mobile phones) in the last 12 months.
Source: *International Telecommunication Union, World Telecommunication/ICT Indicators 2011 (June 2011 edition)*

9.05 Broadband Internet subscriptions

Number of fixed broadband Internet subscriptions per 100 population | 2010
Total fixed (wired) broadband Internet subscriptions refers to subscriptions to high-speed access to the public Internet (a TCP/IP connection), at downstream speeds equal to, or greater than, 256 kb/s. This can include, for example, cable modem, DSL, fiber-to-the-home/building, and other fixed (wired) broadband subscriptions. This total is measured irrespective of the method of payment. It excludes subscriptions that have access to data communications (including the Internet) via mobile cellular networks.

Source: International Telecommunication Union, World Telecommunication/ICT Indicators 2011 (June 2011 edition)

9.06 Internet bandwidth

International Internet bandwidth (kb/s)/capita | 2010

Internet bandwidth is measured as the sum of capacity of all Internet exchanges offering international bandwidth. The data were rescaled for the sake of readability. The capacity is measured in kilobits per second (kb/s) per capita.

Source: International Telecommunication Union, World Telecommunication/ICT Indicators 2011 (June 2011 edition)

Market size

10.01 Domestic market size index

Sum of gross domestic product plus value of imports of goods and services, minus value of exports of goods and services, normalized on a 1-7 (best) scale | 2010

The size of the domestic market is calculated as the natural log of the sum of the gross domestic product valued at PPP plus the total value (PPP estimates) of imports of goods and services, minus the total value (PPP estimates) of exports of goods and services. Data are then normalized on a 1-7 scale. PPP estimates of imports and exports are obtained by taking the product of exports as a percentage of GDP and GDP valued at PPP.

Source: Authors' calculation. For more details refer to Appendix A in Chapter 1.1 of this Report.

10.02 Foreign market size index

Value of exports of goods and services, normalized on a 1-7 (best) scale | 2010

The size of the foreign market is estimated as the natural log of the total value (PPP estimates) of exports of goods and services, normalized on a 1-7 scale. PPP estimates of exports are obtained by taking the product of exports as a percentage of GDP and GDP valued at PPP.

Source: Authors' calculation. For more details refer to Appendix A in Chapter 1.1 of this Report.

10.03 GDP (PPP)

Gross domestic product valued at purchasing power parity in billions of international dollars | 2010

Source: International Monetary Fund, World Economic Outlook Database (April 2011 edition); national sources

10.04 Exports as a percentage of GDP

Exports of goods and services as a percentage of gross domestic product | 2010

Source: World Trade Organization, Statistics Database: Time Series on International Trade (accessed July 4, 2011); Economist Intelligence Unit, CountryData Database (accessed July 4, 2011)

Business sophistication

11.01 Local supplier quantity

How numerous are local suppliers in your country? [1 = largely nonexistent; 7 = very numerous] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

11.02 Local supplier quality

How would you assess the quality of local suppliers in your country? [1 = very poor; 7 = very good] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

11.03 State of cluster development

In your country's economy, how prevalent are well-developed and deep clusters? [1 = nonexistent; 7 = widespread in many fields] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

11.04 Nature of competitive advantage

What is the nature of competitive advantage of your country's companies in international markets based upon? [1 = low-cost or natural resources; 7 = unique products and processes] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

11.05 Value chain breadth

In your country, do exporting companies have a narrow or broad presence in the value chain? [1 = narrow, primarily involved in individual steps of the value chain (e.g. resource extraction or production); 7 = broad, present across the entire value chain (i.e., do not only produce but also perform product design, marketing sales, logistics, and after-sales services)] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

11.06 Control of international distribution

To what extent are international distribution and marketing from your country owned and controlled by domestic companies? [1 = not at all, they take place through foreign companies; 7 = extensively, they are primarily owned and controlled by domestic companies] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

11.07 Production process sophistication

In your country, how sophisticated are production processes? [1 = not at all – labor-intensive methods or previous generations of process technology prevail; 7 = highly – the world's best and most efficient process technology prevails] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

11.08 Extent of marketing

In your country, to what extent do companies use sophisticated marketing tools and techniques? [1 = very little; 7 = extensively] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

11.09 Willingness to delegate authority

In your country, how do you assess the willingness to delegate authority to subordinates? [1 = low – top management controls all important decisions; 7 = high – authority is mostly delegated to business unit heads and other lower-level managers] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

Innovation

12.01 Capacity for innovation

In your country, how do companies obtain technology? [1 = exclusively from licensing or imitating foreign companies; 7 = by conducting formal research and pioneering their own new products and processes] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

12.02 Quality of scientific research institutions

How would you assess the quality of scientific research institutions in your country? [1 = very poor; 7 = the best in their field internationally] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

12.03 Company spending on R&D

To what extent do companies in your country spend on R&D? [1 = do not spend on R&D; 7 = spend heavily on R&D] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

12.04 University-industry collaboration in R&D

To what extent do business and universities collaborate on research and development (R&D) in your country? [1 = do not collaborate at all; 7 = collaborate extensively] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

12.05 Government procurement of advanced technology products

Do government procurement decisions foster technological innovation in your country? [1 = no, not at all; 7 = yes, extremely effectively] | 2010-11 weighted average

Source: *World Economic Forum, Executive Opinion Survey*

12.06 Availability of scientists and engineers

To what extent are scientists and engineers available in your country? [1 = not at all; 7 = widely available] | 2010-11 weighted average
Source: *World Economic Forum, Executive Opinion Survey*

12.07 USPTO patents grants

Number of utility patents (i.e., patents for invention) granted in 2010, per million population | 2010
Utility patents are recorded such that the origin of the patent is determined by the first-named inventor at the time of the grant.

Source: *United States Patent and Trademark Office; United Nations Fund for Population*

2. Opportunities and Challenges in the MENA Region

By Anthony O'Sullivan, Marie-Estelle Rey, and Jorge Galvez Mendez*

Introduction

Since the start of the Arab Spring in January 2011, the political and economic outlook for much of the Middle East and North Africa (MENA) region remains uncertain. The popular and mostly secular call for greater political and economic freedom and representation and the end of corrupt and authoritarian regimes in Tunisia and Egypt rapidly spread to other countries in the region. The protests and demands for reforms have led to varying degrees of political change and, notably, the toppling of three long-ruling presidents: Tunisia's Zine El Abidine Ben Ali, Egypt's Hosni Mubarak, and Libya's Muammar Qaddafi. Tunisia and Egypt are now preparing for elections while some other governments – particularly the monarchies of Morocco and Jordan – have also undertaken a gradual process of political reform.

The opportunity for political reform in the MENA region is unprecedented. However, structural political change cannot be dissociated from further economic reforms. The interdependent structural challenges faced by many countries – such as high unemployment, low female labor force participation rates, low levels of private sector development, weak public and corporate governance, bloated public sectors, limited competition, and pervasive corruption – will need to be addressed. Indeed, political reform cannot fully respond to citizens' demands if it is not accompanied by better living standards. The current events provide an opportunity to develop a more transparent and effective economic governance to unleash the region's economic potential.

This chapter provides an overview of the economic challenges facing the MENA region, some of which have been brought to light even further by the Arab Spring. The chapter also reviews the region's economic performance over past years and the short-term economic impact of recent events. Finally, it highlights the economic potential of the MENA region and the way to maximize the great opportunities that lie ahead. The central argument throughout this chapter is that

the current wave of political change provides a unique window of opportunity to introduce the transparent and accountable policies and institutions that will lead to increased competitiveness and better living standards.

An assessment of the economic challenges facing MENA should take into account the region's diversity. Throughout this chapter, the analysis considers three groups of countries, taking into account the level of hydrocarbon resources and population size: resource-rich, labor-abundant countries, resource-rich, labor-importing countries, and resource-poor countries (Box 1).

Box 1. Groups of Countries According to Population and Hydrocarbon Resources

The diversity of the MENA region is such that it could be segmented in many different ways. Two of the most notable defining characteristics among MENA countries are the availability of oil resources and the size of their native populations. Based on these two factors, MENA countries can be classified in three main groups:

Resource-rich, labor-abundant countries are producers and exporters of oil and gas and have large native populations, which represent almost the totality of their residents. This group of countries includes Algeria, Iraq, Syria,¹ and Yemen.

Resource-rich, labor-importing countries are producers and exporters of oil and gas and have large shares of foreign or expatriate residents, who represent a significant percentage of the total population, even the majority in some cases. This group of countries comprises the Gulf Cooperation Council (GCC) members (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates) and Libya.

Resource-poor countries are small producers or importers of oil and gas. These countries include Djibouti, Egypt, Jordan, Lebanon, Mauritania, Morocco, Tunisia, and the Palestinian Authority.

Source: Adapted from World Bank (2007).

*The authors would like to thank the MENA-OECD Investment Programme and the World Economic Forum Middle East team for their valuable contributions.

Key Challenges for the MENA Region

The Arab Spring has brought to light key challenges in the MENA region that had already existed for some time. These challenges include high unemployment levels (in particular among youth); pervasive corruption and lack of accountability and transparency; bloated public sectors with state-owned enterprises that crowd out the development of private enterprise and investment; low levels of enterprise creation; and, for a number of countries, a high dependence on fuel and food imports generating extensive exposure to commodity price volatility. Given that these challenges are both structural and interconnected, they can be addressed only through a coordinated and comprehensive strategy that involves governments, the private sector, civil society, and the international community.

Job creation is the top priority

Job creation is the first priority in the MENA region. The available evidence indicates that the region suffers from long-term unemployment, ranging between 10 and 25 percent, and that the employment situation is likely to worsen in the context of recent events.² It should be noted that high unemployment rates are also prevalent in some OECD countries, especially following the global economic crisis of 2008-09.³

In Tunisia, Morocco, and Egypt, official unemployment rates have remained close to 10 percent over the last ten years. Furthermore, the Palestinian Authority and Yemen have witnessed significant increases in unemployment since 2000. The lowest levels of unemployment can be found in Kuwait, the United Arab Emirates, and Saudi Arabia (Figure 1). Although total unemployment rates for Gulf Cooperation Council (GCC) countries are low, and native participation in the labor force is very limited, unofficial estimates suggest that unemployment among GCC young nationals (16-24 years), and especially among university graduates, is more than twice that of the total labor force (more than 35 percent across the GCC region).⁴ It is also important to note that unemployment figures provide only a partial picture of the employment situation in the region, where important shares of the population are underemployed in the informal economy (Figure 2). While the informal sector can act as a buffer for employment, wages are much lower and less secure, and there are serious deficits in employee work conditions.⁵

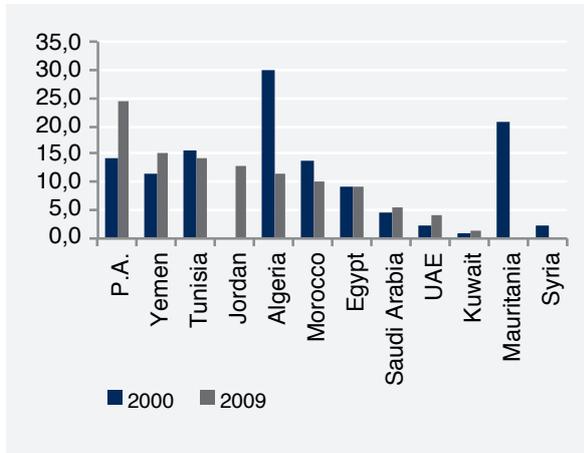
Labor market rigidities, which discourage firms from expanding employment even in expansionary economic periods, play a role in the high

unemployment levels. According to the Index 2011, summarized in the previous chapter, hiring and firing regulations in resource-poor countries are more restrictive than the average in other emerging and developing countries. Evidence from the World Bank Enterprise surveys also indicates that the share of firms identifying labor regulation as a major constraint to business is on average higher in MENA resource-poor countries.⁶

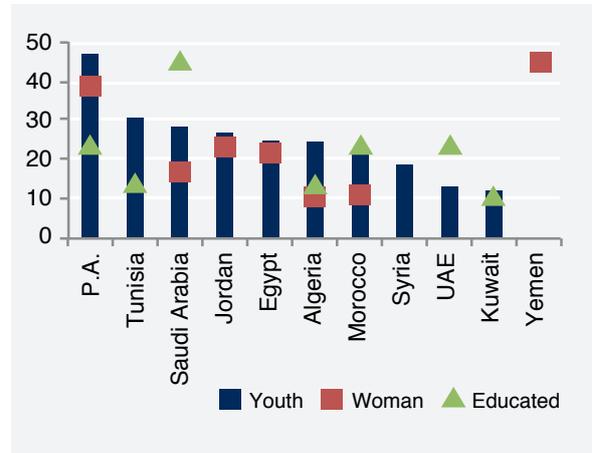
Long-term structural unemployment represents a daunting challenge for the MENA region. The MENA-OECD Investment Programme estimates that, in order to remain at current unemployment levels, 25 million jobs will need to be created over the next decade, requiring an average annual growth rate of 5.5 percent,⁷ one point above the average growth of the last decade. Much more dire estimates from the World Bank suggest that the region will need to create twice as many jobs – at least 50 million – over the next decade in order to ensure social and political stability.⁸ Reaching this higher target would require annual growth rates of at least 6.5 percent for the MENA region, two points higher than the average growth in the last decade.⁹ In this more pessimistic scenario, the growth rate required for resource-poor countries is estimated to be even higher, at 7.5 percent.¹⁰

Figure 1. MENA registers high unemployment levels, mostly among youth, women, and the educated

A. Unemployment rates in percent in 2000 and 2009 or closest years for which data are available



B. Unemployment in percent among youth, women, and the educated in 2009 or most recent year for which data are available

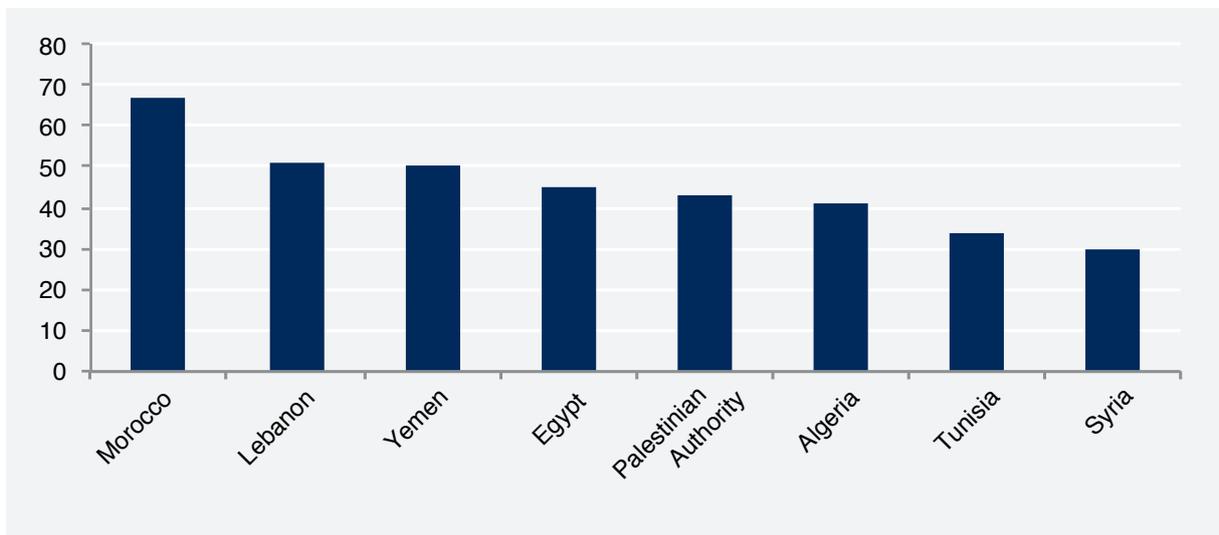


Source: World Bank 2011a.

Notes: Recent unemployment data are not available for Mauritania and Syria. Youth unemployment refers to the unemployed aged 15-24 as a percent of total labor force aged 15-24. Women's unemployment refers to the female unemployed as a percent of the female labor force. Unemployment among the educated refers to the unemployed with tertiary education as a percent of total unemployment. P.A. stands for Palestinian Authority.

Figure 2. Employment in the informal economy is high in some MENA countries

Informal employment as percent of total non-agricultural employment, 2000-07



Source: Heintz and Chang 2007.

Unemployment is particularly acute among youth (15-24 years), averaging approximately 25 percent in the MENA region, which is significantly higher than the 17.3 percent of the OECD area.¹¹ Youth unemployment is about 25 percent in Jordan and Egypt, closer to 30 percent in Saudi Arabia and Tunisia, and nearly 50 percent in the Palestinian Authority (Figure 1, chart B). Furthermore, the 2.8 million young workers who enter the labor market every year¹² are finding it increasingly difficult to find formal employment. Youth unemployment is exacerbated by weak economic growth, restricted government budgets (limiting further expansion of employment in the public sector), and a private sector – the main vehicle for sustainable job creation – that is stifled by red tape, corruption, and unfair competitive practices, especially in resource-poor countries.¹³ Again, it should be highlighted that some OECD countries also have specific problems with youth unemployment, which reaches over 20 percent in Belgium, France, Finland, and Poland, and around 30 percent in Greece, Ireland, Italy, and Spain.

A striking feature of unemployment in MENA is that it is also high among the most educated: over 43 percent of those with tertiary education are unemployed in Saudi Arabia; 24 percent in the Palestinian Authority; 22 percent in Morocco and the United Arab Emirates; 14 percent in Tunisia; and over 11 percent in Algeria (Figure 1, chart B).

One of the reasons for high levels of unemployment for youth and the educated is a persistent gap between the skills acquired at schools and universities and the requirements of business. Enterprises often cite lack of suitable skills as an important constraint to hiring: according to the World Bank's Enterprise Surveys, firms identify labor skill levels as a major constraint in Lebanon (38 percent of surveyed firms), Syria (36 percent), Jordan (33 percent), Mauritania and Egypt (31 percent in both countries).¹⁴ The World Economic Forum (2011) has also identified an inadequately educated labor force as one of the most problematic factors for doing business in the Arab World.¹⁵

Skills mismatches are not exclusive to the MENA region. In 2005, an average 25.3 percent of workers in OECD countries for which data are available were over-qualified for their jobs, and 22.2 percent were under-qualified.¹⁶

Unemployment is also disproportionately high among women. According to the World Economic Forum's Global Gender Gap Report 2010, significant progress has been made in the region to increase women's educational attainment rates, and over the past decade, almost all MENA countries have closed 90 percent or more of the gender gap in education. However, these improvements in education have not been matched with comparable increases in female labor force participation rates: approximately 33 percent of working-age women join the labor force,¹⁷ compared with 56 percent in low- and middle-income countries and 61 percent in OECD member countries.¹⁸ The very low participation of women in the labor force and low employment levels are widely considered a missed opportunity for economic growth and development.¹⁹

Furthermore, in all countries of the MENA region (with the exception of the Palestinian Authority), women who join the labor force have consistently higher unemployment rates than their male counterparts. The gender gap in unemployment is the largest in the United Arab Emirates, Saudi Arabia, Kuwait, Yemen, and Egypt, where the female unemployment rate is nearly four times the male unemployment rate. The labor market outcomes for women in the MENA region could be attributed to prevailing cultural attitudes, gendered laws, and weak support services.²⁰ The OECD-MENA Women's Business Forum, an inter-regional network bringing together civil society, government, and private sector representatives, works to overcome these obstacles by supporting the development of targeted policies and business support services for women entrepreneurs.²¹

The advent of the Arab Spring is adding pressure to unemployment rates, which are expected to increase, given the slowdown in economic activity in the most affected countries and the slowdown in the economic growth of major OECD and non-OECD economies.²² For example, the Ministry of Finance of Egypt estimates that, because of the contraction in consumption (the main economic driver in the country) and economic activity, unemployment has increased to 12 percent, compared with less than 8.9 percent in December 2010, and will be unlikely to decrease before 2013-14. Similarly, unemployment in Tunisia is estimated by the Ministry of Finance to have increased from 13 percent in 2010 to close to 17 percent, mostly because of the economic slowdown and the repatriation of Tunisians working in Libya. These higher unemployment rates add to social pressures in the short term.

Emigration is expected to rise as a result of the Arab Spring

Emigration is expected to increase in those countries most affected by the Arab Spring. Emigration to GCC countries, which already host significant shares of Arab immigrants, is expected to rise. Numerous accounts have been reported of emigrants fleeing from Northern Africa to Europe. Furthermore, a survey of Egyptian young people by the International Organisation for Migration found that the onset of protests and instability may have acted as a primary push factor for youth who reported prior intentions to migrate. The survey's results indicate that two-thirds of respondents with migration intentions who were working prior to the start of the protests were negatively affected by the events: 26 percent lost their jobs, 20 percent were asked to take unpaid leave, and 19 percent witnessed a reduction in their working hours.²³

The security situation in Libya – which hosted around 1.5 million migrant workers in 2010, mostly from Egypt and Tunisia – is also expected to have negative effects: it is estimated that, around 100,000 Tunisians have returned to their country following the conflict in Libya. However, the Libyan National Transition Council's territorial and political successes and its recognition by many countries and the UN are seen as signs of hope for the reconstruction of Libya and the stabilization of emigration from the country.

Fighting corruption and strengthening the rule of law are essential for economic growth and development

Along with high unemployment levels and limited economic opportunities, the main drivers of the Arab Spring have included pervasive corruption, cronyism, and lack of democratic representation. And, although these concerns can be generally identified as the “political” demands of protestors, it is undeniable that they can also have significant effects on economic activity and investment decisions. Widespread corruption, for instance, hinders a level playing field for businesses and obstructs transparency and clarity in business environments. Similarly, cronyism, or the granting of special privileges based on relationships, distorts markets and competition, (e.g. by granting business contracts to a privileged few) and prevents government efficiency (e.g. by appointing government officials based on relationships and not on merit). The World Economic Forum (2011) has confirmed that corruption is a problematic factor for doing business in the Arab World, especially in the Levant and in North Africa.

High levels of corruption and the misuse of political power have existed for some time in the MENA region. According to Transparency International's Corruption Perceptions Index (2010), the MENA region is widely perceived as very corrupt, with an average score of 3.1.²⁴ The only two MENA countries to perform well in the index are Qatar (7.7) and the United Arab Emirates (6.3).

The Arab Spring and the reform process that it has unleashed in some countries constitute an invaluable opportunity to fight corruption and to promote the rule of law. The Egyptian and Tunisian transitional governments have pledged to investigate corruption and abuses by former regimes, and expect to introduce measures to improve governance and transparency, including addressing conflicts of interests, abuse of power, and the realization of private gains from a public position. The MENA-OECD Working Group on Corporate Governance is placing a particular emphasis on good practices related to state-owned enterprises (SOEs), such as transparency and disclosure, the organization of the ownership function, and regulatory functions. Positive results, however, cannot be expected quickly, given the entrenched character of corruption.

A bloated public sector has distorted labor markets and crowded out the private sector

Another key challenge facing the region is bloated public sectors, including both government agencies and SOEs, that employ significant shares of the labor force. Employment in the public sector ranges from 22 percent in Tunisia to around 33-35 percent in Syria, Jordan, and Egypt. Worse, if only non-agricultural employment is considered, the share of the public sector reaches 42 percent in Jordan and 70 percent in Egypt.²⁵ The public sector in the MENA region acts as a magnet for young graduates attracted by high salaries, employment protection, and a special social status, in particular with SOEs. The position of the public sector as a prime target for employment may create incentives for individuals to acquire knowledge and skills in areas demanded by that sector, thus reducing the pool of qualified candidates for the private sector.

In crisis situations such as the Arab Spring, the first reaction of governments is to increase salaries and jobs in the public sector as a short-term response to social discontent. The government of Egypt, for instance, has announced a 15 percent increase to the base wage of all civil servants (5.8 million employees) and “incentives schemes” for the lowest-paid government employees (around 1.9 million people, working mostly in municipalities). Tunisia’s transitional government has also announced an employment plan, which includes the creation of 20,000 jobs in the public sector. Similar measures have been undertaken by many other MENA governments. Although such measures are helpful in mitigating unemployment in the short term, appeasing social discontent, and contributing temporarily to revitalizing the economy through increased consumption, they also add pressure to already strained public budgets in resource-poor countries. In a context of diminishing public budgets, these policies are not sustainable. Furthermore, such measures do not help to advance the sustainable development of the private sector. Addressing the issue of public sector dominance will require not only government policy but also a change in deeply embedded cultural norms – which could take at least a generation.

Entrepreneurship is very limited in most MENA countries

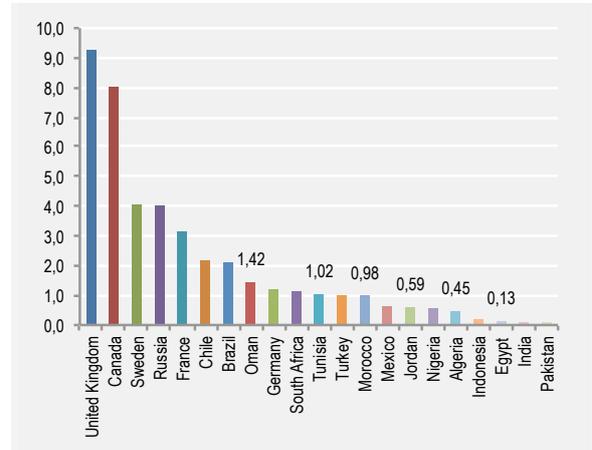
Yet another important challenge facing the region is the low level of enterprise creation. World Bank Group Entrepreneurship Survey (WBGES) data show that there is a wide variation in firm entry density across regions and income groups. High-income countries register, on average, four new firms per 1000 working-age people (15-65 years), whereas MENA countries register only 0.63 new firms (ahead of only sub-Saharan Africa). Data vary significantly from country to country; Tunisia and Oman register the highest entry rates in the MENA region, with over one entry per 1000 people of working age. However, the entrepreneurial performance of individual MENA economies for which data are available is lower than that of large developed and emerging economies (Figure 3).²⁶

Figure 3. Entrepreneurship is lagging at the regional and at the individual country level

A. Firm entry density by region
2004-2009 averages



B. Firm entry density in selected economies
2004-2009 averages



Source: World Bank 2010a, and Klapper and Love 2010.

Note: Entry density is calculated as the number of newly registered limited liability firms in the corresponding year as a percent of the country's working age population.

Findings from the MENA-OECD Investment Programme Working Group on SMEs and Entrepreneurship (2011a) confirm that the limited development of entrepreneurship in MENA can be explained by at least three factors: (1) high barriers to doing business, particularly for smaller firms (e.g. corruption, complex licenses, rigid labor laws, high taxes, and unfair competition); (2) cultural norms in which entrepreneurial activity is seen by young graduates as second-best compared with employment in the public sector, which offers more job security; (3) the very low participation of women in the labor force and in entrepreneurial activity.²⁷ MENA economies need to step up their efforts to provide a more enabling business environment and to promote entrepreneurship and the development of small and medium enterprises (SMEs) – with a particular focus on gender-specific barriers to entrepreneurship.

Food and fuel price volatility have contributed to protests in resource-poor countries

Apart from the structural weaknesses outlined above, the Arab Spring has also been triggered by exceptional spikes in food and fuel prices, which have most powerfully affected the low- and middle-income sectors of society.²⁸

High inflation, the product of a high dependence on fuel and food imports, also represents a major challenge for resource-poor countries. Consumer price inflation has remained high since the oil and fuel price spikes of 2007-08. As shown in Table 1, most countries registered higher inflation rates in the period 2006-10 than in 1996-2005. This is particularly the case in Egypt, which registered an inflation rate of 5 percent during 1996-2005 and a significantly higher rate of 11 percent during 2006-10. A notable exception to high inflation has been Morocco, which has kept consumer price increases below 3 percent.

Inflation rates have remained comparatively higher in resource-poor countries, which import significant amounts of food and fuel and which do not have the financial resources of resource-rich countries to implement compensatory measures, such as subsidies and lowered food import tariffs, without hurting their government finances (Figure 4). The most affected have been low- and middle-income population segments, which devote large shares of their revenues to food and energy items, as compared with wealthier segments of society.

Given the rising incomes and expanding middle class in major emerging countries and the continuing instability in the MENA region, it is likely that recent fuel and food price peaks signal longer-term price increases. Moreover, the implementation of compensatory measures as a result of the Arab Spring, particularly the increase in food and fuel subsidies, will add further pressure to the already negative fiscal balances of those countries (see the following section on economic performance and the impact of the Arab Spring).

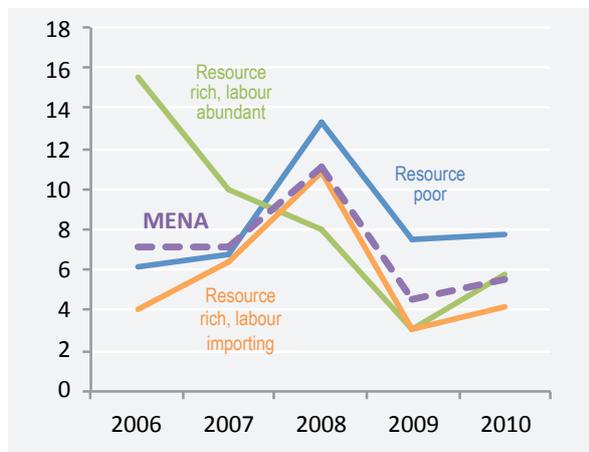
Table 1. Inflation, average consumer prices, percentage change

Economy	1996-2005	2006-2010	Difference
Algeria	4.6	4.1	-0.5
Bahrain	0.7	2.7	2.0
Djibouti	2.0	5.2	3.2
Egypt	5.0	11.0	6.0
Iraq	n/a	17.4	n/a
Jordan	2.6	5.8	3.2
Kuwait	1.8	5.4	3.7
Lebanon	2.5	5.2	2.7
Libya	-0.6	4.7	5.3
Mauritania	6.1	5.9	-0.2
Morocco	1.6	2.2	0.6
Oman	0.1	5.7	5.6
Qatar	3.6	6.7	3.1
Saudi Arabia	-0.1	5.3	5.5
Syria	2.3	7.5	5.2
Tunisia	2.9	4.1	1.2
UAE	3.1	7.0	3.9
Yemen	13.2	10.5	-2.7
MENA	3.0	6.5	3.4

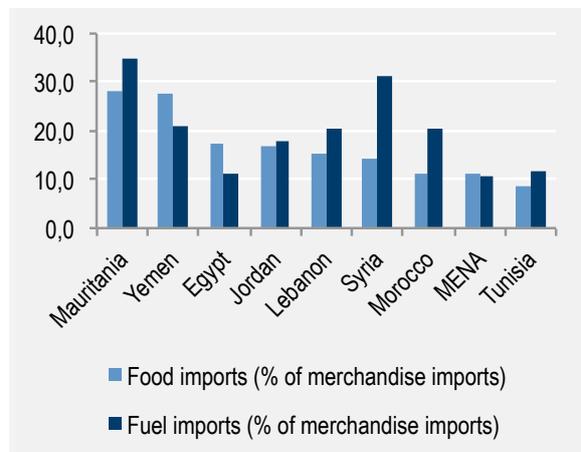
Source: IMF 2011d.

Figure 4. High dependence on food and fuel imports has led to high inflation rates in resource-poor countries

A. Consumer price inflation



B. Food and fuel imports, 2009 or latest



Source: OECD staff calculations based on IMF 2011d and World Bank 2011a. Note: Chart A is based on weighted averages based on GDP

Economic Performance over the Past Decade and the Effects of the Arab Spring

Although the MENA region has registered relatively high economic growth during the last decade, the absence of a vibrant private sector, able to create more and better jobs, has meant that economic performance has not been reflected in improved living standards for the majority. As has already been noted, some factors causing this deficiency are rigid labour markets, skills mismatches, the crowding out of private enterprise by SOEs, high corruption levels, and cronyism, among others. But there are also other economic and structural factors, such as low levels of competitiveness in manufacturing sectors, lack of export-market diversification, and low intraregional integration. Furthermore, although the Arab Spring provides an important opportunity for economic reform, its immediate effects will be negative for those countries most affected by social and political instability.

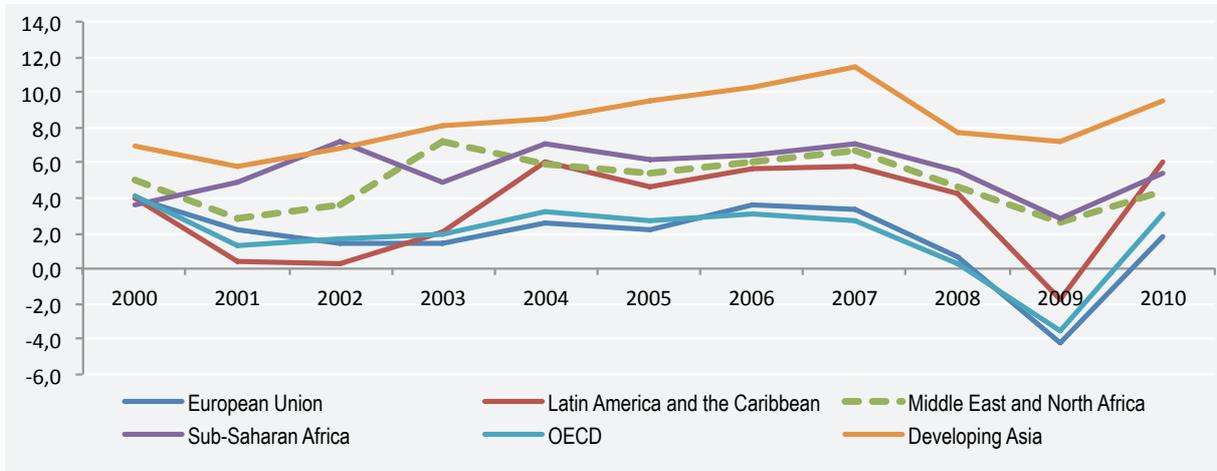
Despite economic growth over the past decade, GDP is likely to be dramatically affected by the events of the Arab Spring

Economic performance in terms of GDP growth in the MENA region has been mostly positive, although volatile, during the last decade. As a group, MENA countries (including Iran) grew 5.2 percent from 2000 to 2008, compared with only 2.4 percent in OECD economies. Furthermore, although economic growth decreased in 2009 as a result of the global economic and financial crisis, the MENA region, together with developing Asia and sub-Saharan Africa, were the only regions registering positive growth in that year (Figure 5).

Comparatively high levels of economic diversification in resource-poor countries have resulted in relatively high and stable economic growth.²⁹ During 2000-10, all resource-poor countries, except Djibouti and Mauritania, grew at an average yearly rate of 4.5 percent to 6 percent, a level on par with resource-rich, labor-importing countries and above that of resource-rich, labor-abundant countries.³⁰ These rates were also less volatile than in the oil-rich, labor-importing countries (Figure 6).

Figure 5. GDP growth in the region has been comparatively high during the last decade

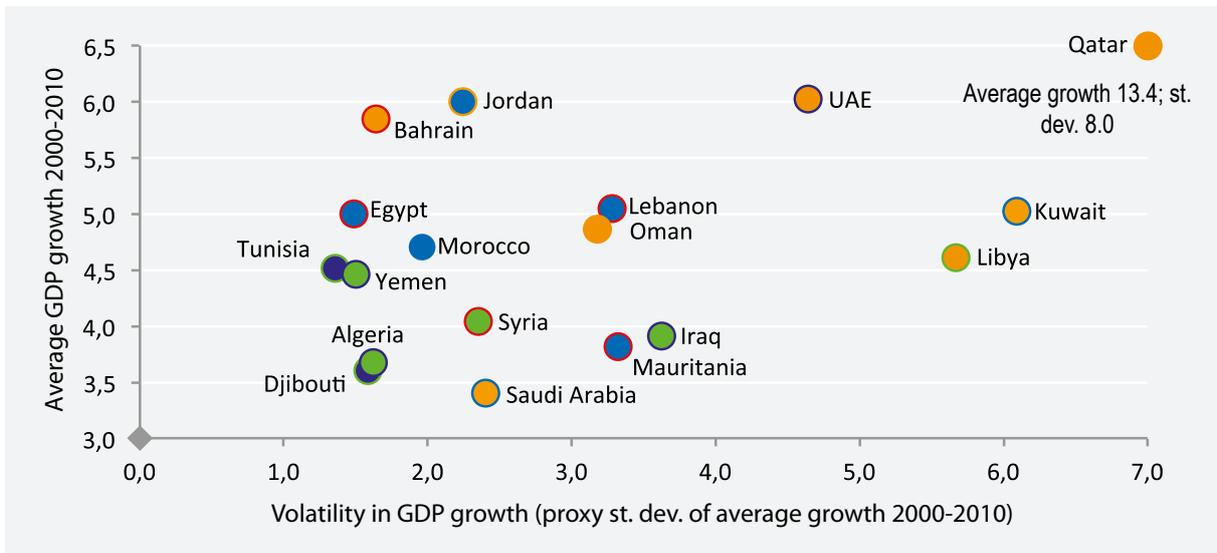
GDP growth by region, percent change, constant prices



Sources: IMF 2011d and OECD 2011c

Figure 6. Average economic growth has been relatively higher and less volatile in resource poor countries

Average GDP growth and volatility in GDP growth (proxied by standard deviation of average growth) in MENA countries, 2000-2010

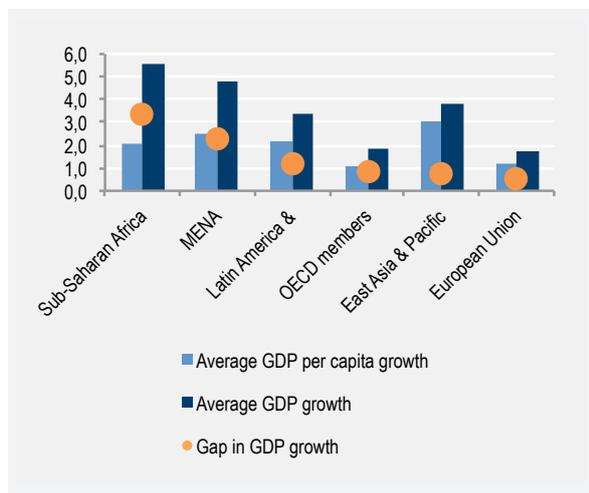


Source: OECD staff calculations based on data from IMF 2011d.

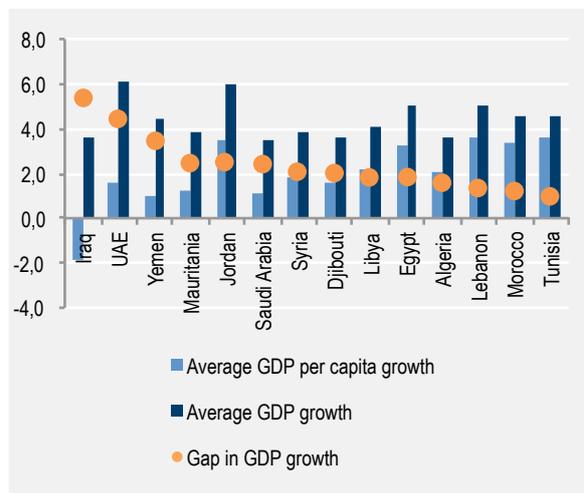
However, high GDP growth rates have not been reflected in GDP per capita growth, which indicates that economic growth has not kept pace with population growth.³¹ Economic growth during 2000-10 in the MENA region has averaged 4.8 percent, whereas average GDP per capita growth for 2000-09 (the latest year for which data are available) has been only 2.5 percent. This gap between GDP and GDP per capita growth is one of the highest in the world, below only sub-Saharan Africa. But performance among countries differs, with Tunisia, Morocco, and Lebanon registering the lowest gaps between GDP and GDP per capita growth, and Iraq, the United Arab Emirates, and Yemen registering the widest gaps (Figure 7).

Figure 7. Income per capita growth is not keeping up with overall economic growth

A. GDP and GDP per capita growth 2000-09/10 by region



B. GDP and GDP per capita growth 2000-09/10 in selected countries



Source: World Bank 2011a.

The widespread political and social instability arising from the Arab Spring and associated uncertainty in several MENA countries has had direct negative economic effects in those countries most affected by turmoil. It has also indirectly benefitted the more stable resource-rich, labor-importing countries, notably Saudi Arabia and, to a lesser extent, Kuwait, where rising energy prices and increasing oil production fuelled GDP growth. However, the degree of economic loss for the most affected countries and the likely length of the transition-induced recession will depend on the degree and duration of uncertainty caused by the events, as well as on the impact on economic fundamentals.

Egypt and Tunisia are expected to register low economic growth during 2011 given the substantial levels of political and social uncertainty, the cancelation or postponement of investment and consumption decisions, and the temporary shutting down of banks, stock markets, factories, shops, and ports (Box 2). However, the economic fundamentals of these two countries are not expected to be significantly affected, and economic growth can be expected to resume if a successful political transition is achieved and if economic reforms continue to be implemented. While Morocco and Jordan have experienced more limited social tensions than other MENA countries, their economies have also suffered from negative spillover effects from instability in other countries in their respective regions.

Other countries registering higher levels of violence and instability, such as Libya, Syria, and Yemen, can be expected to suffer more in the short and medium terms, given the likely dents on their infrastructure and economic fundamentals, which have already begun to materialize.

As a result of the Arab Spring, forecasters have already revised their economic growth projections for 2011. Egypt and Tunisia, which are currently in a wide and far-reaching process of political transition, have seen their forecasts for 2011 sharply reduced. When the IMF published its economic outlook in October 2010, it was expecting the Egyptian economy to grow at a rate of 5.5 percent, in line with previous years. In contrast, the projections of September 2011 have been cut by more than 4 percentage points, to 1.2 percent (Table 2). Similarly, back in October 2010, Tunisia was expected to grow by almost 5 percent in 2011. These projections have now been revised to 0 percent.

Saudi Arabia, and Kuwait, on the other hand, are expected to benefit from the significant increases in oil prices to which the unrest contributed and from increased oil production to compensate for lost Libyan oil output.³² The IMF has thus revised its growth forecasts for 2011 for Saudi Arabia to 6.5 percent (+2 percentage points). Furthermore, recent reports also point to increased economic activity in the United Arab Emirates during the first half of 2011 as a result of its stability in comparison to other countries in the region.³³

The weaker-than-expected economic activity in major OECD economies during the first half of 2011, and the fall in consumer and business confidence (mostly caused by weak economic growth, fiscal gridlock in the United States, and the euro area sovereign debt crisis)³⁴ are likely to have negative repercussions in MENA countries, especially those with meaningful links to OECD economies (notably Tunisia, Morocco, and Egypt).

Table 2. IMF economic growth forecasts

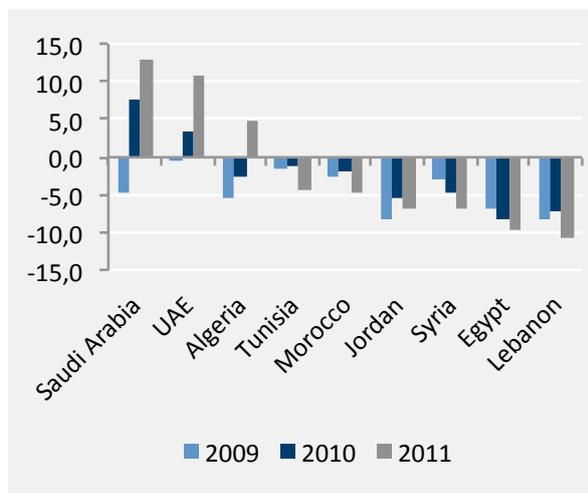
	Forecast in October 2010		Forecast in September 2011		
	2011	2012	2011	2012	
Economy					
Algeria	4.0	4.1	2.9	3.3	↓
Bahrain	4.5	4.8	1.5	3.6	↓
Djibouti	5.4	6.1	4.8	5.1	↓
Egypt	5.5	5.7	1.2	1.8	↓
Iraq	11.5	11.0	9.6	12.6	↓
Jordan	4.2	5.0	2.5	2.9	↓
Kuwait	4.4	5.1	5.7	4.5	↑
Lebanon	5.0	4.0	1.5	3.5	↓
Libya	6.2	6.4	n/a	n/a	n/a
Mauritania	5.1	5.4	5.1	5.7	=
Morocco	4.3	5.0	4.6	4.6	↑
Oman	4.7	4.1	4.4	3.6	↓
Qatar	18.6	9.3	18.7	6.0	↑
Saudi Arabia	4.5	4.4	6.5	3.6	↑
Syria	5.5	5.6	-2.0	1.5	↓
Tunisia	4.8	5.0	0.0	3.9	↓
UAE	3.2	3.9	3.3	3.8	=
Yemen	4.1	4.1	-2.5	-0.5	↓

Source: IMF 2010b and IMF 2011d.

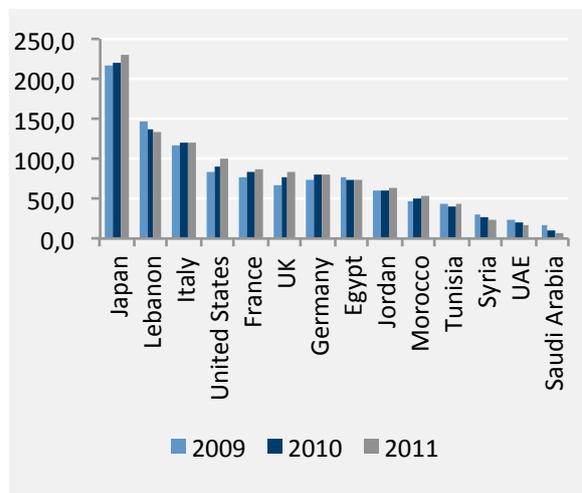
Slower economic activity and higher government spending are expected to put additional pressure on already negative fiscal balances of resource poor countries (Figure 8 and Box 2). And, although gross government debt is lower than in OECD countries (except in Lebanon), this debt is likely to increase in 2011 (Figure 8, chart B). Furthermore, downgrades in sovereign credit ratings will drive up borrowing costs.

Figure 8. Resource-poor countries are expected to register higher fiscal deficits and government debt in 2011 as a result of the Arab Spring

A. General government fiscal balance (revenue minus total expenditure) as percent of GDP



B. General government gross debt as percent of GDP



Source: IMF 2011c and national sources for fiscal balance in Egypt

Box 2. The Economic Impact of the Arab Spring on Egypt and Tunisia

The Egyptian Ministry of Finance estimates that the January 25 revolution caused a slowdown in economic growth, leading to just 1.9 percent growth in the fiscal year (July 1 to 30 June) 2010-11 (the lowest growth in a decade). The Ministry expects a figure of 3-3.2 percent growth for 2011-12, a rate well below the average GDP growth of 5 percent for the period 2000-10. This slowdown will be driven by the cancellation of investments; the decrease of consumption (which has been the engine of economic growth); and impacts on key economic sectors. The overall economy is estimated to have contracted by 4.2 percent (year on year) during the third quarter of fiscal 2011-12 (January-March) because of sharp declines in investment expenditures (-25.9 percent), tourism (-33 percent), construction (-9.1 percent), and manufacturing (-11.4 percent). The Ministry of Finance notes early signs of a slow recovery, especially in the tourism, construction, and communications sectors. However, it also notes a still weak performance in investment and consumption.

The response of the Egyptian government to these events has been the execution of exceptional spending programs, which are estimated at 2.9 percent of GDP and which have consisted of increased spending on food and fuel subsidies, healthcare, housing, and education, as well as the rise of public sector salaries and employment. This, however, has pushed the fiscal deficit target for 2011-12 to 9.5 percent of GDP, against a previous target of 7.5 percent.

The Finance Ministry of Tunisia has also estimated the negative effects of the revolution and expects an economic growth of only 0.2 percent in 2011 (in line with the IMF forecast) if the emergency economic measures announced in March and June help reduce the negative economic impacts; if they do not, the government reckons that economic growth could even be negative. As in Egypt, the tourism sector has been one of the most affected, with a revenue decrease of 51 percent and a drop in visitors of 39 percent. On the other hand, the manufacturing sector is estimated to have suffered much less, with an actual increase on exports of 15 percent during the first semester of 2011.

In terms of public finance, the Ministry of Finance has estimated that the Tunisian fiscal deficit will be four times higher in 2011 than in 2010, given the loss of economic activity and the significant increase (20 percent) of government expenditure attributable to rises in salaries and subsidies.

Box 2 in chapter 1 includes an overview of how the Arab Spring has affected some Arab countries in terms of competitiveness.

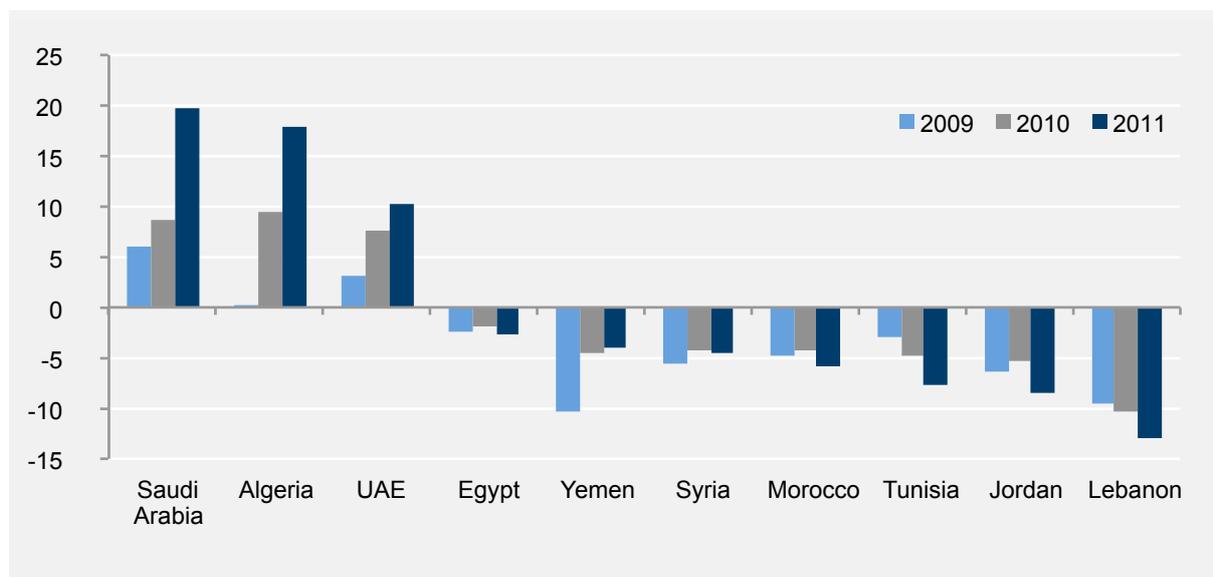
Trade diversification and intra-regional trade are low

Exports from the overall MENA region have increased considerably over the past two decades, partly as a result of growing economic openness and the signature of trade agreements, but mostly because of higher oil production and exports. The region's volume of total exports as a share of GDP grew from around 35 percent in 1990 to 39.2 percent in 2000 and to around 53 percent by 2009. At first glance, this represents higher exporting levels than in other regions. However, a closer look reveals the weight of resource-rich countries, which account for almost 85 percent of all MENA exports, and whose exports are mostly hydrocarbons. Furthermore, without the export engine of hydrocarbon resources, and in the absence of a competitive exporting industry, many resource-poor countries register persistent deficits in their current account balances (Figure 9).

Given lower levels of economic activity in the context of the Arab Spring, exports are expected to decrease in 2011, and the deficit in the current account balance is expected to worsen (Figure 9). However, recent estimates by the governments of Egypt and Tunisia seem to point to better-than-expected results. According to the Tunisian Ministry of Finance, the manufacturing sector has had a better-than-expected performance, with exports actually increasing by 15 percent during the first half of 2011. Similarly, the Egyptian Ministry of Finance has recorded better-than-anticipated results in the balance of payments due to higher Suez Canal receipts, strong private remittances, and a nominal depreciation of the Egyptian pound vis-à-vis the US dollar and the euro. In this light, the current account deficit for fiscal 2011-12 is anticipated to be around 2 percent of GDP (in line with the forecasted deficit of 1.9 percent by the IMF in 2011).

Figure 9. Resource-poor countries register current account deficits

Current account balance as percent of GDP



Source: IMF 2011d.

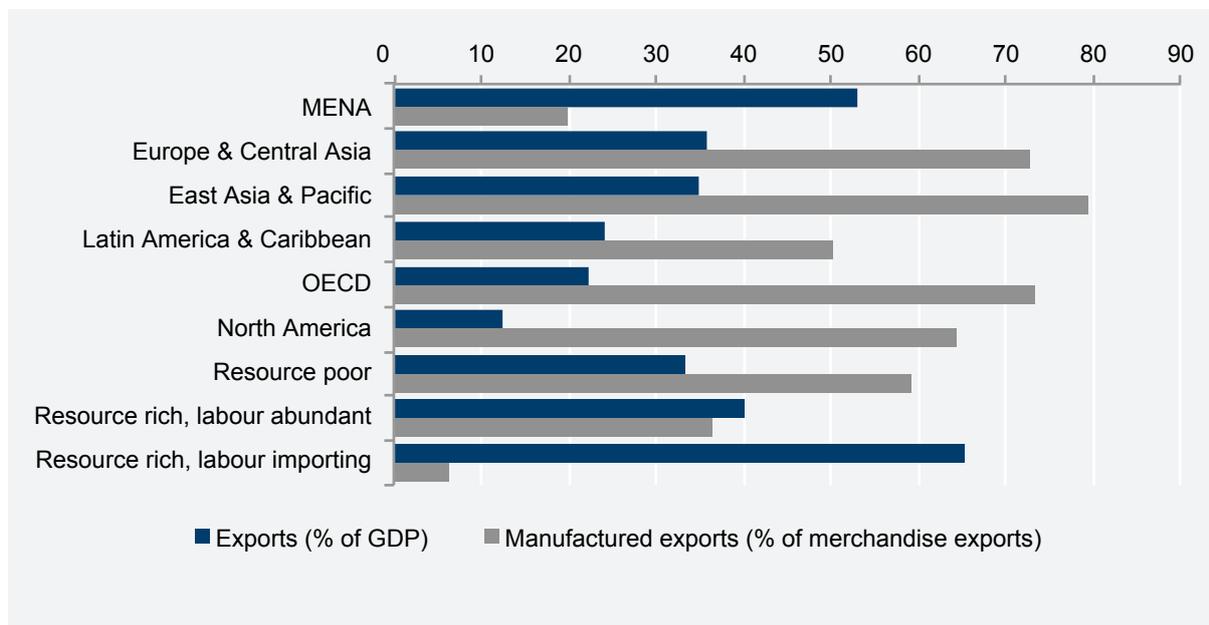
In the MENA region, manufactured exports are a smaller share of merchandise exports than in any other region. Moreover, while the share is higher in the subgroup of resource-poor countries than in that of oil-rich countries, it is still below the levels in other regions, except for Latin America (Figure 10). Indeed, growing exports in the MENA region have been driven mostly by hydrocarbons, whereas non-oil exports growth has remained low. Furthermore, MENA oil importers have fallen below the emerging market average in terms of per capita export growth since 1990.³⁵

In terms of trade diversification, resource-poor countries' exports are mostly concentrated in the European Union market. Intra-regional trade, on the other hand, has been increasing in importance since the 1990s, although it is still modest when compared with trade with other countries, particularly the European Union (EU) (Figure 11). Furthermore, despite the increasing global economic weight of BRIC countries (Brazil, Russia, India and China), they still account for a small share of resource-poor countries' exports.

Export market diversification, however, varies from country to country. Chart B in Figure 11 shows that exports from Tunisia and Morocco are greatly concentrated in the EU market, and in Mauritania most exports are destined to BRIC countries (mainly China, which accounts for over 40 percent of the country's exports, primarily consisting of iron ore). Lebanon and Djibouti, on the other hand, send their exports mostly to other MENA countries. These variations are mainly attributable to the different composition of goods exported from resource-poor countries and the demand characteristics in the importing markets (e.g. China imports mainly raw materials). Morocco and Tunisia, for instance, are mostly exporters of manufactured products, whereas Mauritania is a large producer of raw materials. Exports from Egypt are relatively well diversified in terms of geography: 35 percent of total exports are dispatched to other MENA countries, 30 percent to EU markets, 11 percent to BRIC countries, and over 6 percent to the United States.

Figure 10. Exports as a share of GDP are high in MENA, but manufactured exports are comparatively low

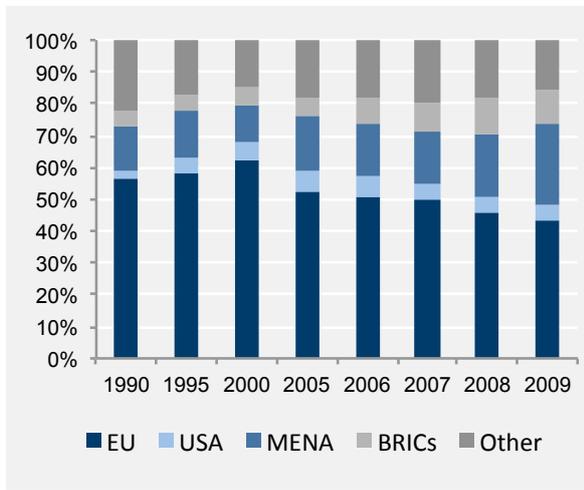
2009 or most recent year



Source: World Bank 2011a.

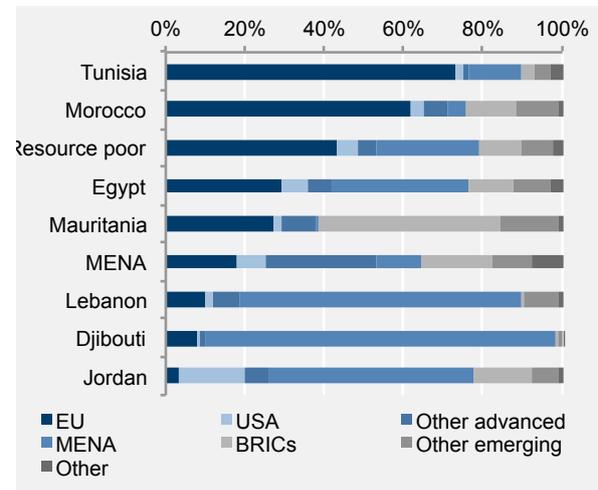
Figure 11. Resource-poor countries' main export market is the EU, but to varying degrees

A. Goods exports destinations, resource-poor countries



Source: IMF, 2011a.

B. Goods exports destinations in individual countries, 2009



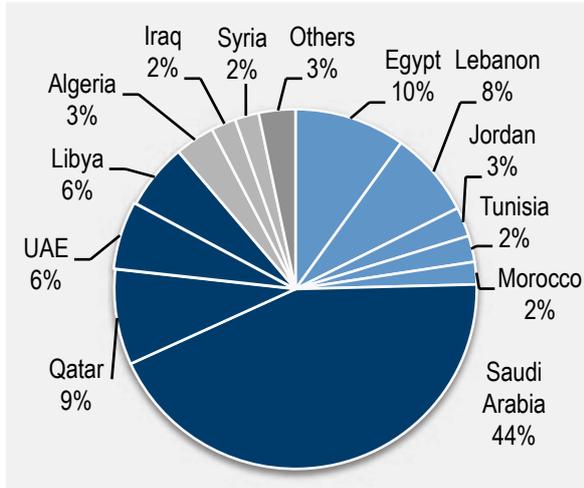
Foreign investment in the region has increased, but is still concentrated in resource-rich countries and is expected to decrease in countries suffering political instability

Of the US\$ 64.5 billion of foreign direct investment (FDI) inflows into the region in 2010, two-thirds went to resource-rich, labor-importing countries, with Saudi Arabia alone accounting for over 44 percent of the MENA total (Figure 12). The resource-poor group of countries, on the other hand, received about 25 percent of FDI flows (US\$ 16 billion), with Egypt and Lebanon as the main recipients.³⁶

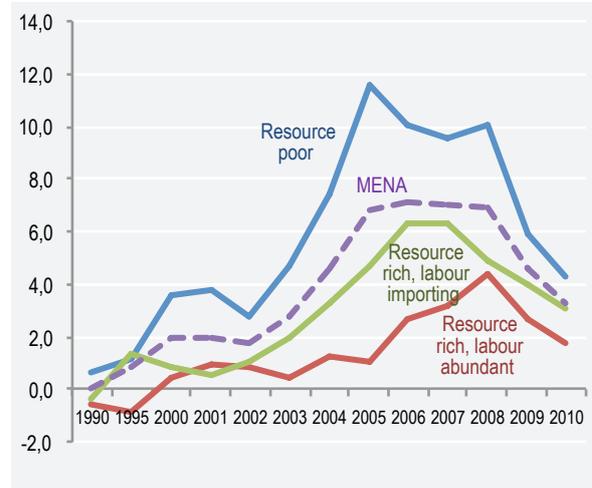
Although in absolute terms (i.e., in US\$) FDI inflows to resource-poor countries have remained below the levels of inflows to resource-rich, labor-importing countries, in relative terms their performance has been stronger. FDI as a share of GDP has increased over the past two decades, which points to the increasing attractiveness of resource-poor countries as destinations for investments. As shown in chart B (Figure 12), FDI inflows to resource-poor countries soared from around 0.6 percent of GDP in 1990 to over 12 percent in the mid-2000s, well above the levels in resource-rich countries and developed and developing economies. These levels decreased again during the 2008-09 global crisis, but they remained above the regional average.

Figure 12. Resource-rich countries are the main recipients of FDI in dollar terms; and resource-poor countries are the main destinations in terms of FDI as a percent of GDP

A. FDI inflows to the MENA region, 2010



B. FDI inflows as a share of GDP

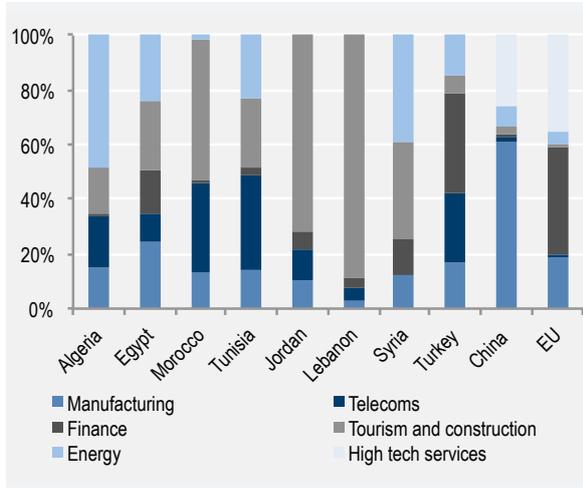


Source: UNCTAD 2011.

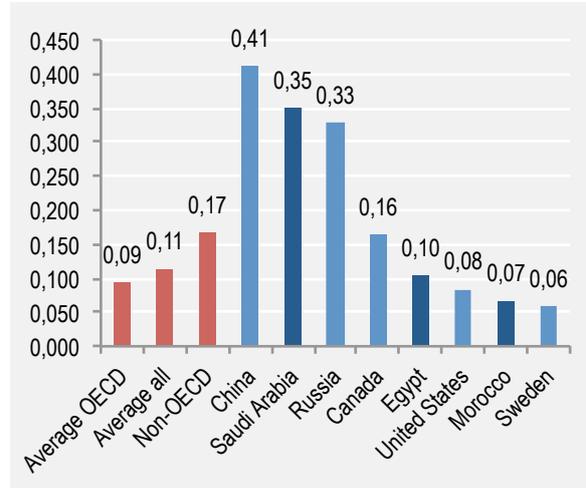
In resource-poor countries, FDI outside the energy sector has been directed mostly to non-tradable sectors.³⁷ Chart A in Figure 13 shows that FDI to MENA countries for which data are available has been mostly directed to non-tradable sectors such as telecommunications, tourism, and construction, whereas the share of FDI invested in manufacturing sectors has been comparatively low, and FDI in high-tech services has been in-existent. This suggests that export sectors in the MENA region have not been competitive and attractive for FDI and that FDI is not driving MENA exports as it drives them in Eastern Europe and Asia.³⁸ This is evident in the specific cases of Egypt and Morocco, which register low levels of regulatory restrictiveness to FDI³⁹ but which have not been able to attract significant foreign investments in the manufacturing sector (Figure 13 chart B).

Figure 13. Most FDI outside the energy sector is targeted to non-tradable sectors

A. FDI by economic sector, cumulative 2000-07, percent of GDP



B. FDI Regulatory Restrictiveness, 2010 (1=closed, 0=open)



Source: World Bank 2009 and OECD 2010.

Although FDI estimates are not yet available for 2011, it is expected that the events of 2011 will limit FDI flows in the short term, especially in the affected North African and Levantine countries. According to the ANIMA Network, the number of FDI projects in the southern Mediterranean has decreased by 13 percent since the start of the Arab Spring. In particular, both Egypt and Tunisia have registered an expected decrease of 50 percent in FDI projects during the first quarter of 2011.

Along the same lines, according to official statements and news reports, the head of the Egyptian General Authority for Investment and Free Zones (GAFI) has stated that a 40 percent decline in FDI for the fiscal year 2010-11 is expected, down to US\$ 4 billion. Similarly, the Tunisian Foreign Investment Promotion Agency (FIPA) has stated that FDI inflows decreased by 29 percent in the first quarter of 2011 (US\$ 250 million in the first quarter of 2011, compared with US\$ 350 million in same quarter the year before).

Opportunities in the MENA Region and the Way Forward

Despite huge challenges in the MENA region, the Arab Spring offers unprecedented opportunities for positive changes. Several countries have embarked on a process of political transition that needs to be accompanied by structural economic reforms to address the root causes of the current events.

The young population represents a great potential as a market and as a labor force

The average median age in the MENA countries is 25 years, below the average of other emerging regions such as Asia (29 years) and Latin America and the Caribbean (27.7), and well below the average of developed countries in Europe (40.2) and North America (36.9). These young populations represent a tremendous opportunity, both as a market and as a labor force.

Currently, the ratio of people aged 0-14 to those in working age (15-64), or the child dependency ratio, is very high at 48.7. This “demographic bonus” means that, in the coming years, the labor force will grow more rapidly than the population dependent upon it, which will free up resources for investment in economic development and welfare.⁴⁰ The youth bulge represents a window of opportunity, but not a guarantee of economic and social development. To materialize this opportunity, governments and civil society need to create well-functioning institutions and implement effective policies to promote employment, health, education, housing, etc.

Renewable energies have the potential to become an important economic activity

The MENA region also has great potential for renewable energies, particularly electricity generation from solar sources.⁴¹ Some MENA countries also have potential for developing hydropower resources (e.g. Egypt on the Nile River, Iran on its north-western plains, and Iraq and Syria in the Tigris-Euphrates basin) and wind resources (e.g. along the Red Sea and on Morocco’s Atlantic coast). Furthermore, renewable sources of energy are almost unexploited: in 2008, less than 3 percent of the region’s electricity came from renewables. Some countries did exceed this average, such as Egypt with 12 percent of its energy coming from renewable sources, Syria with 7 percent, and Morocco with 6 percent.⁴²

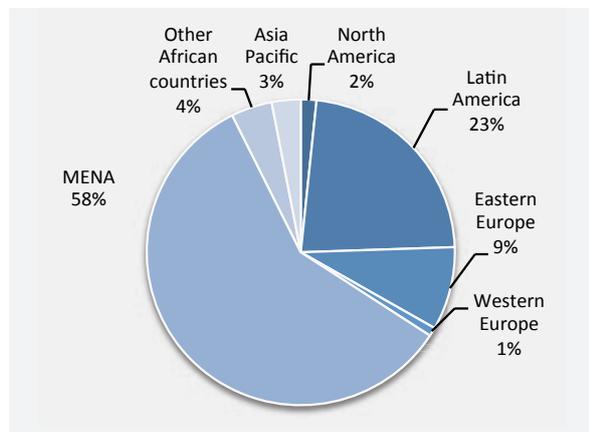
Renewable energies in MENA represent a great opportunity for investment and development. The International Energy Agency forecasts that the use of renewables for electricity generation could grow up to 33 percent by 2035, with investments possibly reaching over US\$ 400 billion by that year if policies conducive to renewables are implemented as planned. Furthermore, several MENA countries have already launched strategies and plans to promote the renewable energy sector. The Chapter 3 in this report includes a more detailed analysis of the potential of the renewable energies sector in employment creation, particularly through FDI.

Hydrocarbons still represent a great asset for many countries

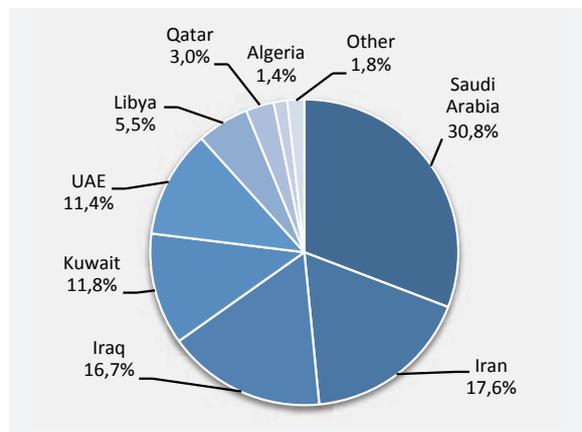
The resource-rich countries in the region are home to nearly 60 percent of the estimated 1.4 trillion barrels of proven global crude oil reserves,⁴³ with six countries (including Iran) accounting for 94 percent of the proven oil reserves in the region, and Saudi Arabia taking the lion’s share (at 31 percent or 265 billion barrels) (Figure 14). This same group of countries also accounts for over 45 percent of the world’s proven natural gas reserves of over 192 trillion standard cubic meters.

Figure 14. MENA holds nearly 60 percent of the world’s proven oil reserves, with only six countries accounting for 55 percent of those reserves

A. World proven crude oil reserves by region, 2010



B. MENA proven crude oil reserves by country, 2010



Source: OPEC 2010.

There are significant development opportunities for manufacturing and services, including agribusiness and tourism

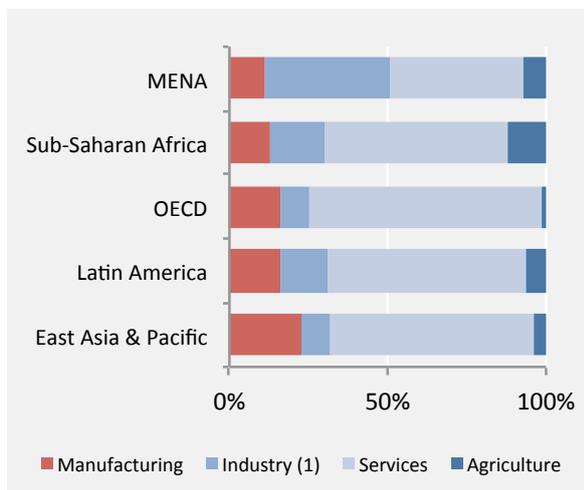
The MENA region also offers great development potential in terms of manufacturing and services industries, which already represent an important share of GDP in some resource-poor countries (Figure 15). The manufacturing sector in Jordan accounts for 20 percent of total value added, while those of Tunisia, Egypt, and Morocco account for 16 percent. This represents a higher share than the average manufacturing value added in other regions except for East Asia and the Pacific. Similarly, the value added in the services sector in Lebanon, Jordan, Tunisia, and Morocco is either above or equal to the average in the OECD, East Asia and Pacific, and Latin America and Caribbean regions.

The geographical proximity of resource-poor countries to large European markets is a potential source of economic growth and diversification and an opportunity to develop further the manufacturing and services industries. Furthermore, the growing population and labor force in MENA countries should help develop domestic markets in the region.

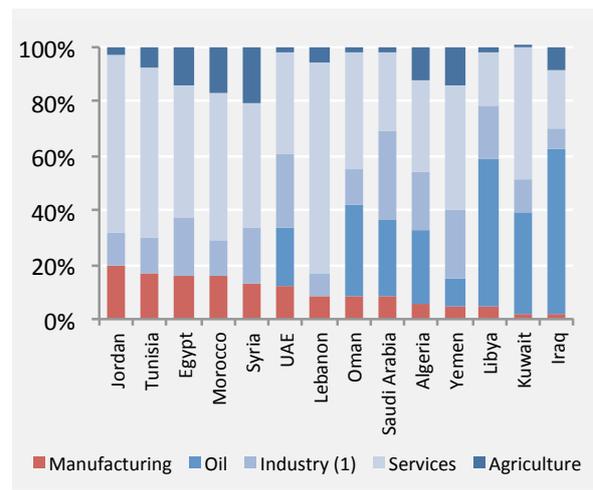
Tourism is a relatively well-developed industry in some MENA countries and provides important sources of employment and revenues. According to data from the World Bank, international tourism receipts⁴⁴ in 2009 represented 9.1 percent of total exports in MENA countries, well above the world average of 6.4 percent and the OECD average of 6.6 percent.⁴⁵ MENA countries that have benefited most from tourism are Lebanon, Jordan, Morocco, Egypt, Tunisia, and Bahrain (Figure 16). These countries have great potential to develop their international tourism industry further, given their touristic assets and geographical proximity to the European and GCC markets. High economic growth rates and rising incomes in emerging economies will also represent an opportunity for these MENA countries to attract visitors beyond the traditional European and Gulf markets.

Figure 15. The manufacturing sector is relatively well developed in some MENA countries

A. Value added in selected regions
2009 or most recent year



B. Value added in the MENA region
2009 or most recent year



Source: World Bank 2011a.

Note: (1) Excluding manufacturing. Industrial activities comprise Mining and quarrying (ISIC 10-14), which include oil and gas extraction; Manufacturing (ISIC 15-37), Electricity, gas and water supply (ISIC 40-41) and Construction (ISIC 45). In this case, "industry" refers to industrial activities excluding manufacturing, which is shown separately; and oil. ISIC is the UN International Standard Industrial Classification of All Economic Activities.

Box 3. The Impact of the Arab Spring on Tourism

The tourism sector is particularly sensitive to political instability. The Arab Spring is reported to have caused damage to the tourism industry in affected countries already, both in terms of visitors and investment. Some initial evidence indicates that:

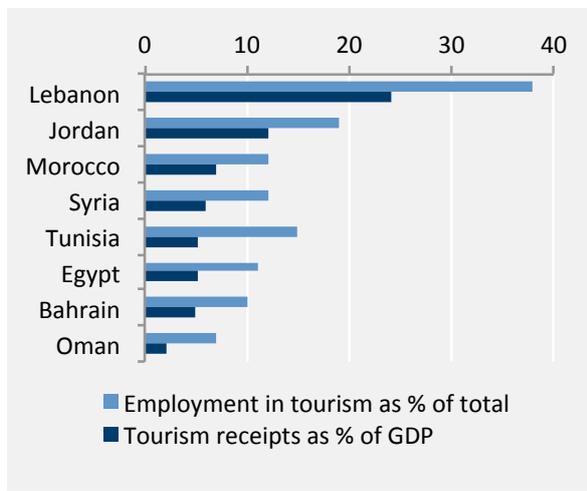
- During 2011, receipts from tourism are expected to decline in Egypt and Tunisia by up to 1 percent of GDP.
- According to Egypt's Tourism Minister, revenues from tourism last February were 80 percent below 2010 levels. In March, this number fell by 60 percent and in April by 35 percent. The latest available data point to an overall fall of 33 percent during January-March 2011. Tourism revenues are expected to fall by 25 percent for the whole of 2011, although recent estimates by the Egyptian government indicate a gradual recovery in this sector.
- According to Tunisian officials, tourism receipts to the end of April 2011 dropped by 48 percent in comparison to 2010. Recent estimates point to a fall of 51 percent in income from tourism and 39 percent in the number of tourists during the first half of 2011.
- The UN World Tourism Organisation estimates that, during the first two months of 2011, international tourist arrivals to Tunisia decreased by 44 percent and receipts by 43 percent.
- In Bahrain, hotel occupancy rates plummeted to only 10 percent. In addition, the Formula One Grand Prix, which contributed US\$ 600 million or 2.9 percent of GDP to Bahrain's economy in 2008, was cancelled in 2011.
- Although estimates are not yet available for Syria, the tourism industry, which accounts for 12 percent of employment and GDP, is being greatly damaged by the current levels of instability.

Given the scarcity of water resources in the MENA region, agriculture is not a dominant economic activity in most countries. Figure 17 shows water availability, agricultural land, and agriculture value added in countries for which data are available (latest data for 2007 and 2008). A glance reveals that, of the 14 MENA countries displayed, only Iraq, Lebanon, and Morocco have water resources above or near 1000 cubic meters per capita.⁴⁶ It is in these countries and others with important freshwater sources, albeit at lower per capita levels, such as Egypt and Syria, that the agribusiness sector has the greatest development potential.

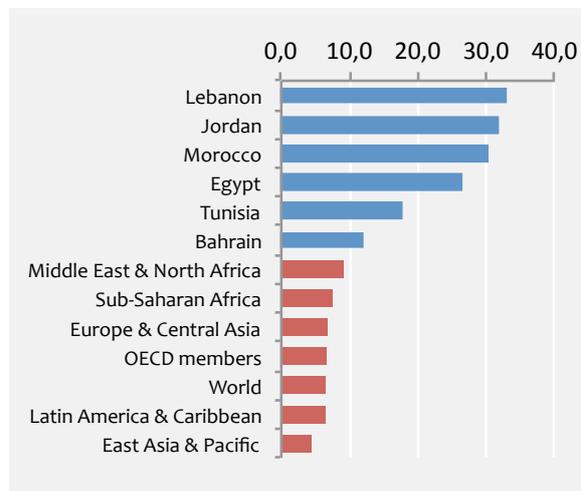
Agro-industrial activities are related to the processing, preservation, and preparation of agricultural production (including fisheries and forestry) for intermediate and final consumption. They are a component of the manufacturing sector, where value is added to agricultural raw materials and are recognized as important drivers of economic growth and development.⁴⁷ Agro-industries associate the industrial and agricultural sectors and create downstream and upstream linkages, which can have multiplier effects in terms of job creation and value addition in connected sectors such as agriculture, manufacturing, commerce, and services. They also have the potential to provide employment for the rural population, not only in farming but also in off-farm activities such as handling, packaging, processing, transporting, and marketing of food and agricultural products.⁴⁸ These activities could be particularly relevant for MENA countries.

Figure 16. Tourism is a key economic sector for several countries in the region

A. Employment and receipts in the tourism sector, 2010

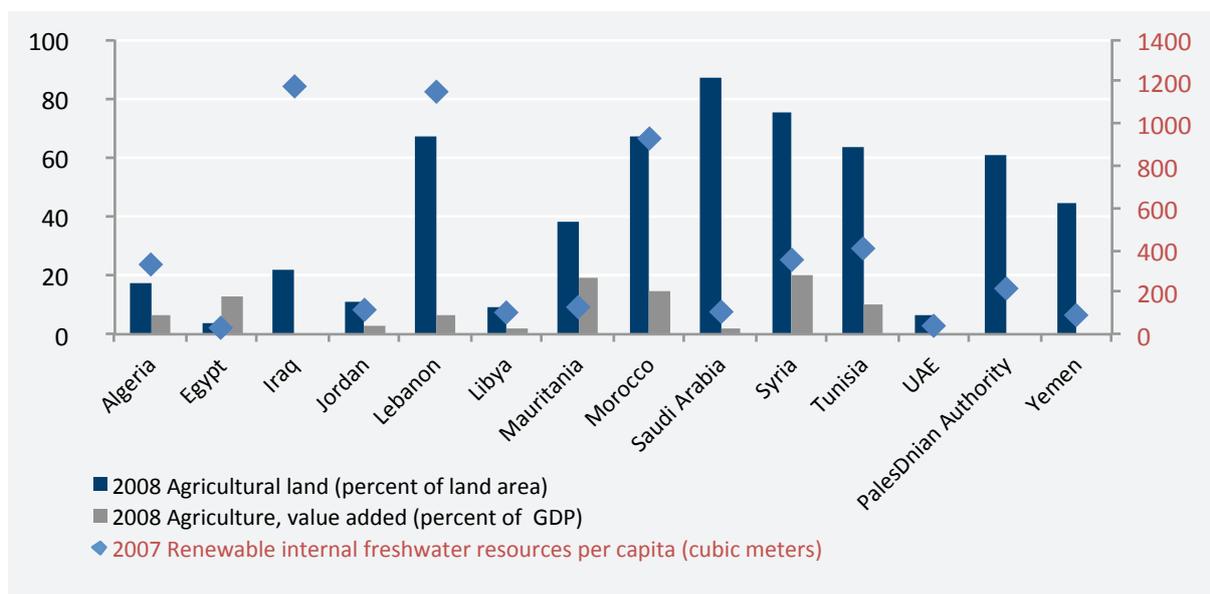


B. International tourism receipts as percent of total exports, 2009



Sources: IMF 2011d and World Bank 2011a.

Figure 17. MENA countries could exploit opportunities in agribusiness development



Source: World Bank 2011a.

Note: Data on agriculture value added as percent of GDP are not available for Iraq, the UAE, the Palestinian Authority and Yemen.

The Way Forward

The Arab Spring may prove to be a turning point for some countries in the MENA region. After the fall of their previous regimes, Egypt and Tunisia are now engaged in far-reaching political reform and defined milestones. Both countries have lifted bans on political parties and groups, have eased restrictions on political competition, and are preparing the formation of constituent assemblies to elaborate new constitutions. Following the winds of change, Morocco and Jordan are also introducing significant political reforms.

"In Libya, after months of violent confrontations, the regime of Muammar Qaddafi was ousted and the National Transition Council (NTC), which has been recognized by numerous countries and the United Nations, has announced the formation of a transition government, the drafting of a new constitution and the election of a new government. This may lay the foundations of a political transition process. On the other hand, Syria and Yemen continue to suffer from political and social tensions and high instability."

To respond genuinely to citizens' demands for improved living standards, MENA governments, with the support of the international community and in cooperation with the civil society, including the business community, also need to develop strategies to promote inclusive economic growth and employment, building on improved governance, transparency, and the rule of law. Those strategies need to break with a past of public sector-led economies and cronyism and to center on the development of a competitive private sector, which can provide economic opportunities that correspond to peoples' aspirations.

In this context, Egypt, Jordan, Morocco, and Tunisia, in collaboration with the international community, particularly the G8 nations (under the "Deauville Partnership"), are developing wide-ranging agendas to address four closely interconnected areas:

- Improving governance, transparency, accountability, and citizen participation in economic life;
- Increasing social and economic inclusion by expanding opportunities to all and improving the effectiveness of support for the vulnerable;
- Modernizing their economies, supporting the private sector, particularly SMEs, aiding job creation, and developing human capital and skills;
- Fostering regional and global integration to reap the benefits of globalization.

The strategies to address these areas need to be not only comprehensive but also adapted to the particular circumstances, needs, and potential of each country. For all MENA countries, raising international competitiveness and attracting more and better foreign direct investment (FDI) will be fundamental components to securing sustainable growth, employment, and better living standard.

¹ Syria is classified by the World Bank as a resource-rich, labor-abundant country and by the IMF as an oil-importing country. This report follows the World Bank's classification, even though Syria's oil production (at 250,000 barrels per day) and proven oil reserves (2.5 billion barrels) are low compared with other resource-rich countries.

² It should be noted that MENA data on employment are often incomplete and outdated. They also do not take into account a large informal sector that acts as a buffer for employment, especially for the poorer segments of the population. This point is further highlighted in Figure 2.

³ Unemployment rates vary among OECD countries. For instance, Ireland registered less than 5 percent unemployment prior to the crisis (2007) whereas in 2010 the figure was 13.7 percent; Spain, which had already a high unemployment rate of 8.3 percent in 2007, registered over 20 percent in 2010. And the United States, which had an unemployment rate of 4.6 percent in 2007, registered a high of 9.6 percent during 2010. Korea, on the other hand, has registered an average rate of 3.6 percent over the past ten years, with 3.7 percent in 2010. The overall OECD average unemployment rate (for the 28 OECD countries with data available for 2010) increased from 6.9 percent in 2000 to 8.8 percent in 2010.

⁴ de Boer and Turner 2007, as cited by Shochat 2008.

⁵ International Labor Office 2009.

⁶ as cited in IMF 2010a.

⁷ The MENA-OECD Investment Programme estimates the number of jobs to be created based on historical annual new entrants into the labor market, taking into account demographic evolutions. Growth projection based on IMF data.

⁸ World Bank 2011b. In 2009, the World Bank estimated that 40 million new jobs would need to be created over ten years to meet the fast-growing labor force. World Bank, 2010b.

⁹ Assuming that the ratio of jobs created to economic growth remains constant. IMF, 2010a.

¹⁰ This figure refers to Egypt, Jordan, Lebanon, Morocco, Syria, and Tunisia. IMF, 2011b.

¹¹ This number refers to the first quarter of 2011, compared with 7 percent of unemployment among adults (aged 25 and over). Youth unemployment rates have increased in the OECD since this sector of the population was hard hit by the 2008-09 economic crisis, OECD, 2011b.

¹² OECD estimates based on ILO data of Economically Active Population for 2005-10.

¹³ It should be noted that some resource-rich countries, such as Saudi Arabia, have made impressive progress in reducing red tape in recent years.

¹⁴ as cited in IMF 2010a.

¹⁵ Inadequately educated force is the fourth most problematic factor in the Arab World, after access to financing, restrictive labor regulations and inefficient government bureaucracy.

¹⁶ Over-qualified workers are those whose highest qualification exceeds the one required by their jobs. Conversely, under-qualified workers' highest qualification is lower than the one required by their jobs. OECD, 2011b.

¹⁷ World Economic Forum 2010. Labor-force participation rate refers to the proportion of the working-age population (15-64) that is either employed or seeking employment.

¹⁸ Based on data from the World Bank, Genderstats.

¹⁹ See, for instance, Chamlou 2008.

²⁰ UNDP and AFESD 2006.

²¹ See www.oecd.org/mena/investment/wbn

²² OECD 2011d.

²³ IOM 2011.

²⁴ Transparency International measures perceptions of corruption on a scale of 0 to 10 with 0 indicating the highest level of corruption and 10 indicating the lowest.

²⁵ IMF 2010.

²⁶ The Global Entrepreneurship Monitor (GEM) MENA Regional Report 2009 reinforces this point: "although pursuing entrepreneurial activity is a way of life for millions of citizens" in MENA countries, "their rates of involvement, based on comparisons with other countries participating in the GEM surveys, are generally lower than might be expected for countries at their level of development" (Global Entrepreneurship Monitor, 2010). The MENA countries covered by the GEM's regional report are Algeria, Jordan, Lebanon, Morocco, Syria, Yemen, and the Palestinian Authority. According to the report, only Lebanon, Yemen, and Algeria register higher than expected total entrepreneurial activity, an indicator of entrepreneurial activity during the firm pre-establishment and newly established phase. Along these lines, a recently launched Global Entrepreneurship and Development Index (Acs & Autio, 2010), which ranks 71 countries in terms of their performance in the creation of high-growth enterprises and high-impact entrepreneurship, revealed that MENA economies lag behind most developed and emerging economies.

²⁷ When using data on self-employment as a proxy for entrepreneurial activity, findings from the OECD-MENA Women's Business Forum reveal that although female self-employment varies across MENA countries [with the highest female self-employment rates in Algeria (30.6 percent) and Djibouti (27.5 percent)], female self-employment rates are consistently lower than male rates (which is the case in most countries around the world), Stevenson, forthcoming.

²⁸ Another important triggering factor not analyzed in this report is the contagion or inspirational effect of protests occurring in other MENA countries, prominently those in Tunisia and Egypt.

²⁹ Other factors also explaining this comparatively high economic growth are expansionary monetary policies, the importance of remittances, urbanisation, etc.

³⁰ It is worth mentioning that for the resource-rich countries, gross national income (including terms of trade) is perhaps more relevant than GDP.

³¹ Total population in the MENA region has increased significantly during the last decades, growing from around 109 million (3 percent of the world total) in 1970 to nearly 200 million (3.75 percent) in 1990 and almost 300 million (4.4 percent of the world's population) in 2009. And, although the pace of growth has been decelerating from over 3 percent in 1970-1989 to 2.4 percent in the 1990s and 2.1 percent during the last decade, the population growth rate is still one of the highest in the world.

³² There are reports, however, that Saudi Arabia actually has not increased its oil production as compared with 2010.

³³ Arab Financial Forum 2011.

³⁴ OECD 2011d.

³⁵ IMF 2010. The IMF analysis and figures refer to countries in the Middle East and North Africa (including Iran and Sudan) plus Afghanistan and Pakistan.

³⁶ It is worth noting that resource-poor countries are home to nearly 50 percent of MENA population, whereas resource-rich, labor-importing ones account for less than 15 percent.

³⁷ Tradable goods or services can be sold in locations distant from their place of production, for instance, manufactured goods, as opposed to non-tradable goods and services.

³⁸ World Bank 2009.

³⁹ In terms of restrictions to foreign-owned equity in firms, land ownership, closed sectors, etc.

⁴⁰ Lee and Mason 2006.

⁴¹ IEA 2010a.

⁴² Ibid.

⁴³ OPEC 2010.

⁴⁴ International tourism receipts are expenditures by international inbound visitors, including payments to national carriers for international transport. Their share in exports is calculated as a ratio to exports of goods and services. World Bank 2011a.

⁴⁵ When comparing the MENA region with other regions, it must be considered that, in absolute terms, international tourism arrivals are significantly lower in MENA (77.4 million) than in the OECD (492 million) and Europe and Central Asia (468 million). Similarly, international tourism receipts in current US\$ are 75.4 billion, compared with 479 billion in Europe and Central Asia and 673 billion in the OECD.

⁴⁶ But even in these countries, water availability is below the levels of other regions such as Latin America (over 23,000 cubic metres per capita), the OECD (8,600 metres per capita), and East Asia and the Pacific (4,765 cubic metres per capita).

⁴⁷ Henson and Cranfield 2009.

⁴⁸ Ibid.

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3. Foreign Investment Policies and Job Creation in the MENA Region

*By Anthony O'Sullivan, Marie-Estelle Rey, and Jorge Gálvez Méndez, OECD**

Introduction

It is generally recognized that foreign direct investment (FDI)¹ can play an important role in the economic development of a country. In addition to providing fresh sources of capital in a context of scarce resources, it improves the development and internationalization of domestic firms through linkages, and generates business and market opportunities for domestic investors. FDI can also create spillover effects and productivity gains through technology and know-how transfers, imitation, skills development, and mobility of human resources.

In theory, the direct effects and the positive externalities of FDI should contribute to economic growth and employment creation.² In reality, the employment impact of FDI depends on a number of factors related to the type of investment, its purpose, and the economic sector targeted. Furthermore, other factors in the recipient economy are also important, such as the level of economic development, the business environment, the efficiency of the local labor market, and the quality of human capital.

Governments can play an important role in introducing policies that enhance the effects of FDI on employment, including labor policy, skills development, and investment incentives, with a view to strengthening the links between foreign investors and the local economy.

The aim of this chapter is to provide an overview of the impact of FDI on employment in the Middle East and North Africa (MENA) region and to outline some policy measures which could enhance that impact.³ The chapter starts by analyzing the trends and characteristics of FDI and employment creation in the region, with a particular focus on the conceptual and actual impact of the different types of FDI (green field vs. mergers and acquisitions), its objectives or strategies (resource seeking, operational efficiency, or market expansion), and economic sectors targeted (labor or capital intensive). Next, the chapter analyzes proactive investment policies that could enhance the impact of FDI on employment (education and labor policies, fostering the integration of women in the labor force, and promoting and strengthening linkages between foreign investment and the local economy). The arguments in this section are supported with specific policy examples from MENA and OECD economies. Finally, the chapter puts forward two sectors in which FDI in the MENA region could have particularly positive effects on employment.

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I. The Link between FDI and Job Creation

1. Overview of Trends in FDI and Job Creation

After a decade of FDI growth, inflows decreased as a result of the global crisis and the impact of the Arab Spring.

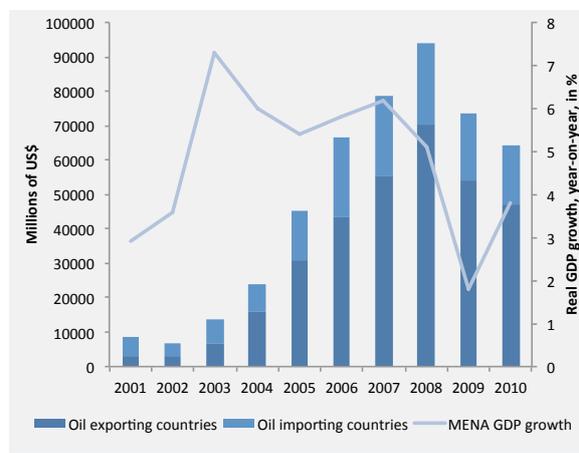
In recent years, the MENA region has experienced a steep increase in FDI inflows, which grew tenfold from US\$8.7 billion in 2001 to US\$94 billion in 2008 (Figure 1). This surge was due in some countries to a wave of economic liberalization and increased integration with the world economy. But the FDI boom was also driven by rising oil prices, which attracted higher levels of investment in the hydrocarbons sector. Other sectors—such as real estate, construction, financial services, and telecommunications—have also been major recipients of foreign investments. This rise in FDI was accompanied by sustained economic growth in the region, with average real GDP growth of 5.2 percent annually between 2000 and 2008.

While economic growth in the MENA region was relatively resilient in the early stages of the global financial and economic crisis (mainly owing to a lower degree of integration with the world economy), FDI eventually fell by 22 percent, from US\$94 billion in 2008, to US\$73 billion in 2009, and has been slow to recover, with a further drop of 12 percent in 2010 to US\$64 billion (Figure 2).

The wave of protests that has spread throughout several MENA countries since early 2011—and the resulting political instability they sparked—have prompted an additional drop in FDI. In Egypt, the General Authority for Investment and Free Zones announced a 40 percent decline of FDI inflows for fiscal year 2010-11 (July to June), and an outright contraction in FDI in the first quarter of 2011. In Tunisia, FDI inflows declined by almost 30 percent in the first quarter of 2011, compared to the same period in 2010 according to the country's Foreign Investment Promotion Agency. Other MENA countries also experienced more limited FDI inflows caused by a weakening of investor confidence throughout the region.⁴

Figure 1. MENA countries experienced a tenfold increase in FDI inflows from 2001 to 2010

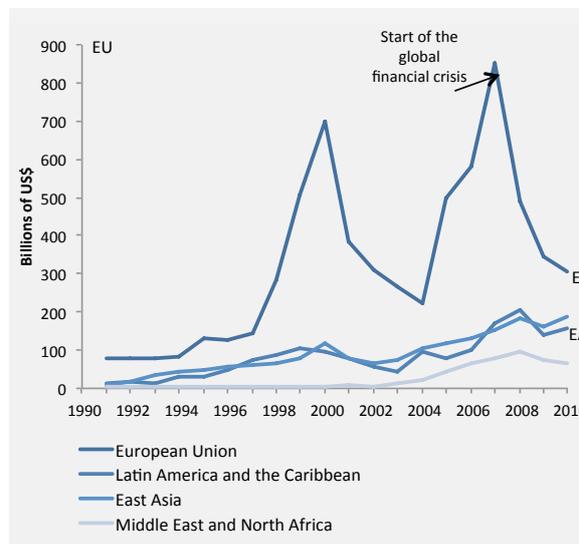
FDI inflows and GDP growth in the MENA region (2001-2010)



Source: UNCTAD 2011b; IMF 2011.

Figure 2. FDI inflows to MENA countries had not recovered from the global economic crisis by the end of 2010

FDI inflows to selected regions (1991-2010)



Source: UNCTAD 2011b.

High economic growth and the surge in FDI during the last decade were not sufficient to reduce the persistently high levels of unemployment.

The Arab Spring has brought into sharp focus one of the most daunting challenges facing the region today: unemployment, in particular among youth, women, and the educated. Indeed, despite the decade-long surge in FDI inflows and robust economic growth, MENA countries continue to suffer from long-term structural unemployment. This apparent paradox of rising growth and investment on the one hand and persistent structural unemployment on the other hand can be explained by a number of factors, including an underdeveloped private sector which has not been able to absorb a rapidly expanding labor force and a workforce that lacks the necessary skills to respond to business needs (Section II.1 below). This situation is likely to worsen in the short term as a result of the global economic downturn⁵ and the economic slowdown in a number of MENA countries in the first half of 2011.

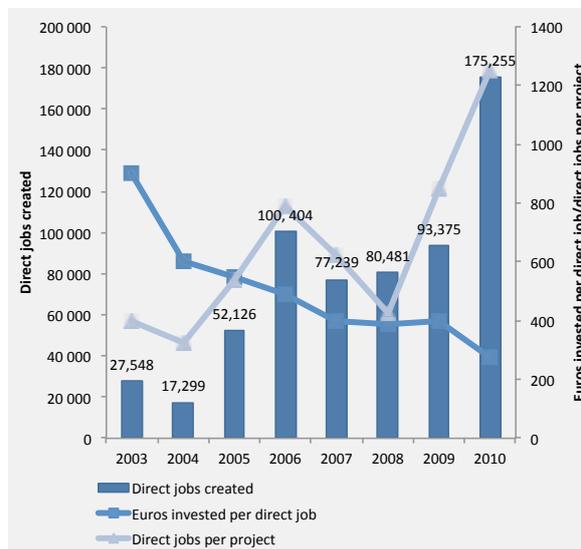
However, available evidence indicates that FDI has had some impact on job creation.

It is difficult to assess the impact of FDI inflows on jobs—in terms of both numbers and quality—especially in developing countries where data availability is limited.⁶ A survey of MENA governments conducted by the MENA-OECD Investment Programme for this edition of the Arab World Competitiveness Report⁷ revealed that governments themselves struggle to access reliable data. However, the available information suggests that FDI inflows to the region have created some direct and indirect jobs, although there are differences among countries and sectors.

According to the ANIMA Investment Network, in 2010, FDI created 175,000 direct jobs and approximately 585,000 indirect jobs in 11 surveyed Mediterranean countries (including Turkey and Israel and excluding the Gulf countries, among others) (Figure 3).⁸ It should be highlighted, however, that ANIMA bases its forecasts (and the associated job creation measured) on announced projects, rather than on projects that have actually been carried out.

Figure 3. The number of direct jobs created by FDI has increased over the last few years

Direct jobs created by FDI in the Mediterranean region (2003-2010)⁹



Source: ANIMA 2011b.

The Moroccan Investment Agency, in response to the survey of the MENA-OECD Investment Programme, indicated that about 15,000 direct jobs were created by foreign businesses in 2009, but only 7,500 in 2010.¹⁰ Assuming a ratio of 1.6 indirect jobs created for every direct job,¹¹ the impact of FDI on employment in Morocco would represent about 21 percent of new labor market entrants in 2009 but only 9 percent in 2010.¹²

While these estimates are not conclusive, they do suggest a link between FDI and job creation in the MENA region.

2. Characteristics of FDI and Job Creation

The impact of FDI on job creation depends on a number of factors.

The impact of FDI on employment is influenced by the type of investment (green field vs. mergers and acquisitions), the objectives of foreign investors (acquisition of resources, operational efficiency, or market expansion), and the economic sectors targeted by FDI (labor or capital intensive). A country's level of economic development—as measured by the level of productivity and costs of labor—also influences the employment impact of FDI.¹³

Green field FDI is more conducive to employment creation than mergers and acquisitions.

FDI¹⁴ is typically divided into mergers and acquisitions (M&As) and green field investments. M&As refer to the purchase of existing assets, either through a cross-border merger resulting in two companies becoming a single entity, or through a cross-border acquisition in which foreign investors buy some or all of the shares or assets of a domestic company. Green field investment refers to the creation and development of new assets, such as factories, equipment, and offices.

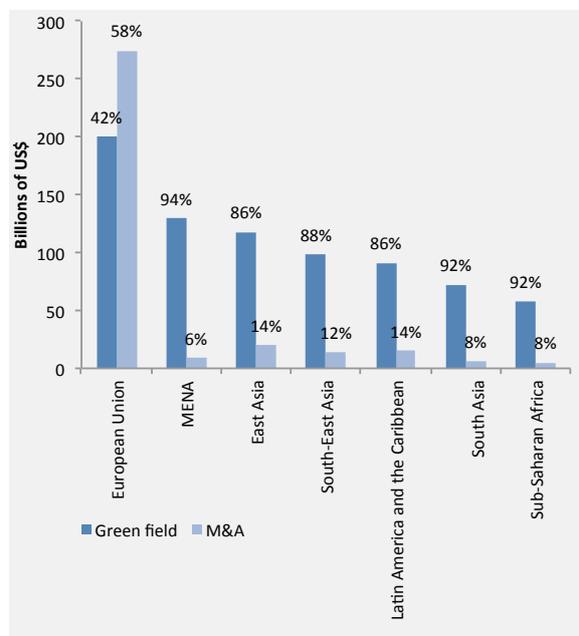
M&As, by nature, do not necessarily create jobs, and they can even lead to job losses, especially in the short term. For example, privatization, rationalization, or modernization measures can reduce the number of employees if they involve layoffs. However, M&As can also increase efficiency and productivity, which may translate into renewed job creation over the longer term.

Conversely, green field projects should have a positive impact on job creation from the outset, since the newly created assets require new employees for their use. The positive impact of green field investment is even more noticeable when it is directed to labor-intensive sectors. Green field investment can also have positive spillover effects that lead to indirect job creation through linkages with the wider economy, but this is true of M&As, as well.

The share of green field investment in the MENA region is estimated at over 90 percent of FDI over the last five years (Figure 4). However a large part of those green field investments have been oriented to the hydrocarbons sector, which is more capital than labor intensive. Occasionally, FDI is boosted by “high-profile” (i.e., very large) M&As, especially in small, resource-rich countries or in resource-poor countries (Figure 5). For example, the partial privatization of Tunisian state-owned telecommunications operator Tunisie Télécom accounted for 67.5 percent of total FDI in 2006.¹⁵

Figure 4. The MENA region registers the highest levels of green field investments as a share of total FDI compared with other regions

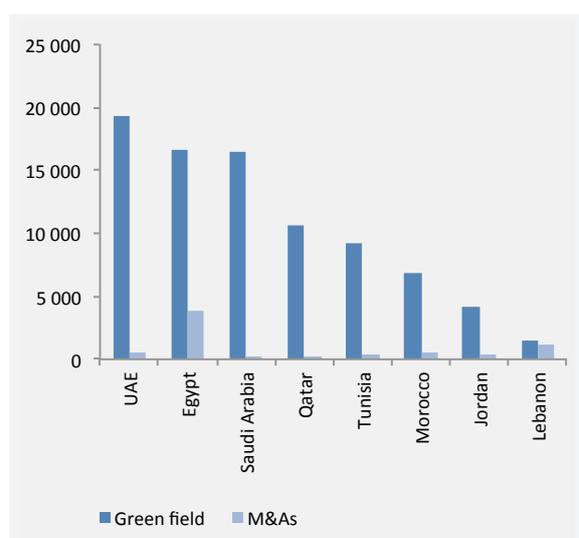
Average annual value of green field investments and M&As in selected regions (2005-2010)



Source: UNCTAD 2011b.

Figure 5. Conversely, the share of M&As in total FDI is low in most countries

Average annual value of green field investments and M&As in selected countries (2005-2010)



Source: UNCTAD 2011b.

The impact of FDI on jobs also depends on the recipient economic sector.

In addition to the mode of entry, the impact of FDI on employment also depends on the recipient economic sector, which can be either capital or labor intensive. Labor-intensive sectors include agriculture, manufacturing, construction, real estate, tourism, and wholesale and retail trade. In contrast, sectors that are mostly capital intensive comprise hydrocarbons, telecommunications, power generation, water supply, mining, and energy-intensive manufacturing industries such as fertilisers or high-grade metals.

In the MENA region, the lion's share of FDI is invested in the hydrocarbons sector. Despite geopolitical risks and high levels of price volatility, the returns in this strategic sector are high and have further increased with the oil boom of the past decade. More than a quarter of FDI inflows in the Mediterranean Arab countries are directed to the energy sector.¹⁶ FDI in hydrocarbons is unsurprisingly higher among net exporters of oil and gas, with Saudi Arabia accounting for almost 45 percent of the total FDI inflows to the MENA region (including all economic sectors, not only hydrocarbons). Similarly, in Algeria, FDI in the energy sector represented close to 50 percent of GDP on average between 2000 and 2007.

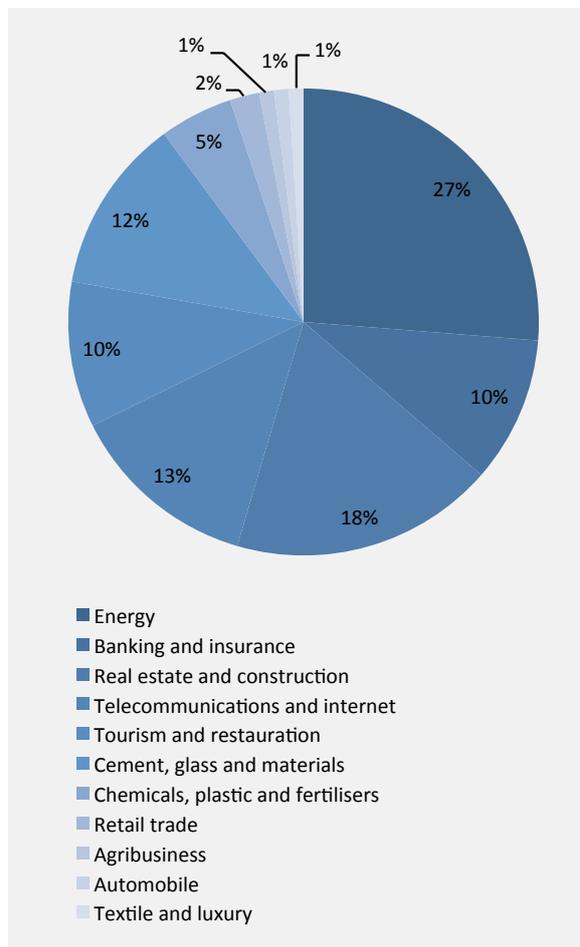
Given the increasing profitability of hydrocarbons extraction (due to high prices), hydrocarbon FDI flows have also been directed to countries with smaller oil and gas reserves. For example, in Tunisia, 61 percent of all FDI inflows in 2010 went to the energy sector.¹⁷ Similarly, in Egypt in fiscal year 2009-10 (July-June), petroleum accounted for 45 percent of total FDI inflows.¹⁸

The hydrocarbons sector is highly capital intensive and generates few jobs in proportion to its levels of investment. Moreover, the specialized skills required in this sector—such as petroleum engineering skills—are in limited supply in MENA countries and must often be imported from abroad. In other words, although FDI figures may be quite high, they can also be misleading with regards to the anticipated impact on employment in the recipient country.

Beyond hydrocarbons, a significant share of FDI inflows in the MENA region have been directed to sectors such as financial services and telecommunications, following partial privatizations on the back of a wave of economic liberalization efforts. FDI in the telecommunications sectors in Morocco and Tunisia accounted for 33 percent and 35 percent, respectively, of total FDI inflows between 2000 and 2007, while the banking and telecommunications sectors together accounted for 36 percent of announced FDI projects in the Arab Mediterranean countries between 2003 and 2010 (Figure 6).

Figure 6. Energy is the most important recipient sector of FDI in most MENA countries

Composition of cumulative announced FDI inflows to the Arab countries of the Mediterranean (2003-2010)



Source: UNCTAD 2011b.
 Note: The Arab countries of the Mediterranean are Algeria, Egypt, Jordan, Lebanon, Libya, Morocco, Palestinian Authority, Syria, and Tunisia.

There is considerable variation in the proportion of FDI among countries and sectors, even within more labor-intensive sectors such as real estate and construction, tourism, and traditional manufacturing. What is clear, however, is that these sectors have the greatest impact on the volume of FDI-related employment. For instance, in Morocco, FDI in the real estate and construction sector accounts for almost 30 percent of total FDI-related employment, followed by the automotive industry (almost 17 percent), and tourism (14 percent).¹⁹

The objectives of the investor also have an impact on employment outcomes.

In terms of the investor objectives, FDI can be categorized as resource seeking (investing in natural resources), efficiency seeking (outsourcing activities based on the availability of certain skills or lower costs), or market seeking (targeting a large or specific market).

As has been noted, resource-seeking FDI has a limited impact on employment, given the capital intensity of the economic sectors in which those investments are made. Efficiency-seeking FDI, conversely, would be expected to yield higher benefits in terms of job creation. In developing countries, efficiency-seeking FDI often takes the form of outsourcing parts of the value chain in order to reduce production costs. It flows into both manufacturing industries (e.g., textiles) and services (e.g., software development), and is often export oriented, a characteristic that generally has a positive effect on economic development.

Efficiency-seeking FDI is particularly present in North Africa, where some sectors have been developed into an outsourcing hub for the European market. For instance, Morocco has attracted investments from Renault, a large French auto manufacturer, which have contributed to the development of a vast network of automotive suppliers. The newly launched Tangier Med project (an ambitious port and industrial project) represents EUR1 billion of investment and involves plans to produce 400,000 vehicles per year and create 36,000 direct and indirect jobs by 2014.²⁰ Another example from Morocco is the case of Sumitomo, a large Japanese industrial conglomerate. Its activities started in 2001 and expanded in 2005 with the implementation of a production site for automotive cable harnesses, creating 1,100 jobs. Since then, the group has increased its presence in Morocco, with six additional production sites across the country. Today, the Sumitomo Group is ranked the largest employer in the industrial sector in Morocco. It employs 15,712 people across its three subsidiaries.²¹

Egypt has also attracted several information technology multinational enterprises to the “Smart Village” outside Cairo, including world heavyweights such as Microsoft, Oracle, and IBM. At the end of 2010, 35,000 people worked in over 150 foreign and domestic enterprises there. The Egyptian government intends to make the “Smart Village” home to 500 companies and 100,000 employees by 2014.

Market-seeking FDI can also have an impact on jobs. Egypt’s Ministry of Trade and Industry highlights the development of international retail hypermarkets (such as Makro, Lulu, Carrefour, Metro, and Marks & Spencer), which have generated over 5,000 local jobs, though the indirect impact on small shop keepers is not estimated.²² Market-seeking FDI is generally directed towards markets with large populations or potential for high growth, such as telecommunications, utilities, or banking. These are not always labor intensive. In the MENA region, market-seeking FDI is still rather limited but is becoming increasingly important, mainly in the Gulf Cooperation Council (GCC) countries and in Lebanon, but also in Egypt, which represents a market of around 80 million people. Further liberalization of regional trade and investment (including in services) could transform the MENA region and its 300 million inhabitants into a prime target for market-seeking investment.

In sum, while it is clear that FDI in the MENA region has contributed to employment, the overall impact on the number and quality of jobs is difficult to assess. Further work is needed to collect employment data related to FDI in a more systematic manner, involving several ministries and national investment agencies. Across the region, even though the most frequent type of investment (green field) tends to be conducive to employment creation, the sectors targeted (mainly hydrocarbons) have been more capital than labor intensive. In order to increase the impact of FDI on employment, efforts should be made by investment promotion agencies to diversify FDI away from hydrocarbons and to encourage more efficiency- and market-seeking FDI.

To help attract FDI conducive to promoting job creation, the MENA-OECD Investment Programme has been working closely with policy makers to enhance and harmonize national investment laws and progress towards a regional investment framework which would facilitate cross-border investment. Governments can implement additional proactive measures to further stimulate job creation through FDI. Some of these measures are outlined in the next section.

II. Proactive Investment Policy Measures to Stimulate Job Creation

1. Education and Labor Policies

The MENA region suffers from significant skills mismatches, underperforming tertiary education systems, and rigid labor markets. Despite important progress made in education, foreign investors often have difficulty finding the right skills among the local workforce to meet their business needs, especially technical and management skills. In addition, foreign investors often face rigid labor market regulations. Difficulties in hiring and dismissing employees represent a major disincentive to employing local workers and investing in labor-intensive sectors. This section addresses some of the challenges that the region is facing in the education and labor areas and suggests policies to help close the gap. It also highlights the economic potential of a larger share of women participating in the labor force and how this can be reinforced.²³

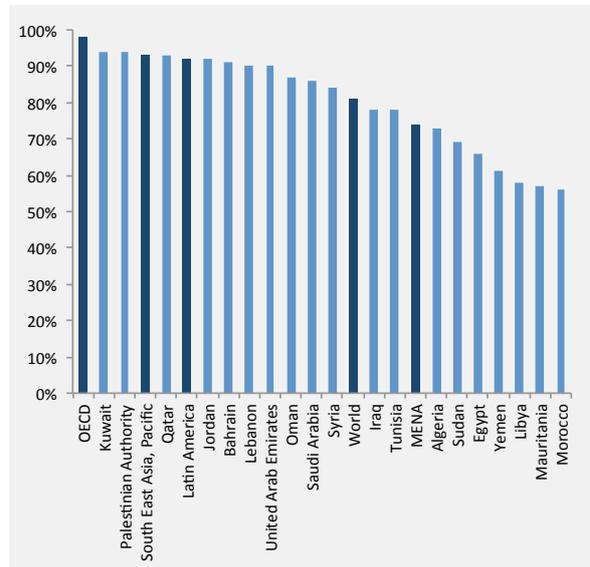
The level and quality of education of the labor force in MENA countries continue to lag behind other emerging regions.

The level and quality of education of the workforce are important factors for attracting FDI and raising the level of employment in a country. By one estimate, each additional year of average educational attainment increases the FDI stock by approximately 2 percent.²⁴ Recent OECD work suggests that improvements in the quality of learning outcomes by even a little—as measured by the OECD Programme for International Student Assessment (PISA)—can lead to significant gains in economic growth and personal income.²⁵ For certain sectors, such as information and communication technologies (ICT), the quality of education is even more critical in attracting investment and determining the level of job creation.²⁶

Research conducted in OECD countries concludes that countries able to achieve literacy levels 1 percent above the international average will gain 2.5 percent labor productivity compared to other countries.²⁷ While literacy rates have improved dramatically in the MENA region over the past decade, they are still low when compared to other parts of the world, such as Latin America and Southeast Asia and the Pacific (Figure 7). Moreover, students' performance at the pre-university level (for MENA countries for which the OECD has data) has been mixed (Figure 8), despite the fact that a relatively high share of available resources is devoted to education—around 5 percent of GDP, in line with the OECD average (Figure 9).²⁸

Figure 7. Average literacy levels in the MENA region are below the world average

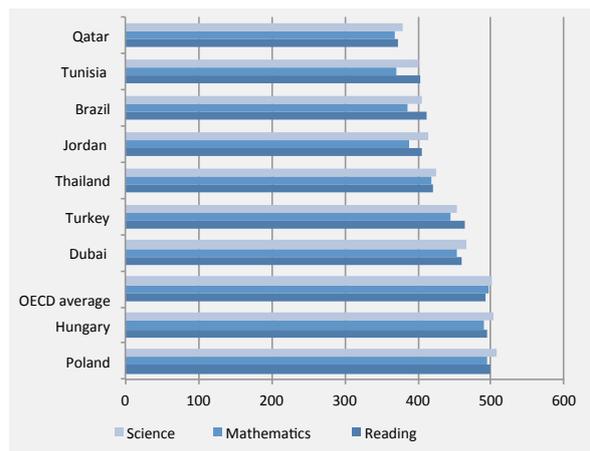
Comparison of literacy rates (2009)



Source: UNESCO Statistical Institute 2009.

Figure 8. Students' performance in selected MENA countries is below the OECD average

Comparison of PISA results on educational attainment of 15-year-old pupils (2009)

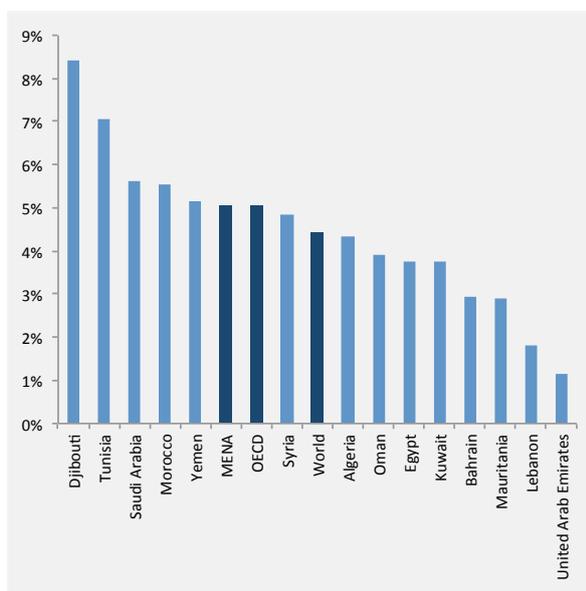


Source: OECD 2010f.

Note: PISA 2009 results included data on only four MENA countries (Qatar, Dubai, Tunisia, and Jordan).

Figure 9. Expenditure on education is comparable to OECD countries

Annual public expenditure on education as percent of GDP



Source: UNESCO Statistical Institute 2006.

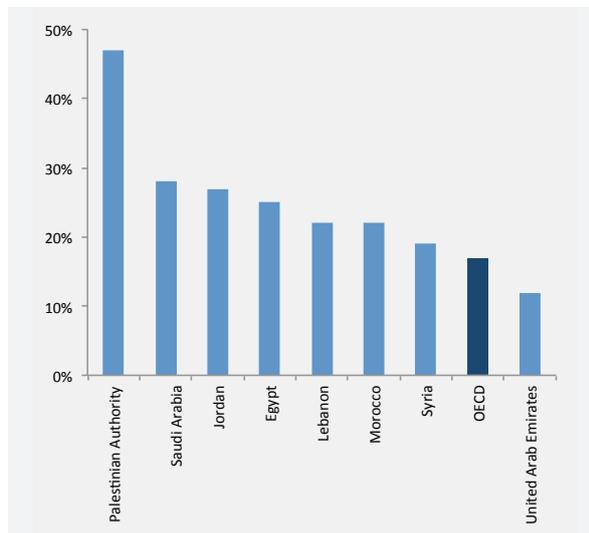
A mismatch between available skills and the job market's needs hinders employment growth.

To enhance the employability of the young, educated people in the MENA region, one of the fundamental issues to address is the mismatch between the skills of young people, especially university graduates, and the skills sought by the private sector. The skills mismatch occurs in various areas, such as entrepreneurial and managerial skills, language acquisition, analytical capabilities, and other technical skills. A recent OECD publication, *Off to a good start? Jobs for the youth*, offers suggestions from a large number of countries on how to overcome the skills mismatch and ease the transition to the workforce.²⁹

Youth unemployment rates in the MENA region are high, exceeding 20 percent in some countries, according to available data (Figure 10). Such high unemployment rates are related to the difficult transition from school to work and to limited links between schools and businesses to ensure that education curricula are aligned with job market needs. It is striking that the unemployment rate for university graduates in some of the MENA countries is higher than for non-graduates—the reverse of the situation in most OECD countries. An OECD index drawing on questions from the PISA study³⁰ suggests that countries such as Qatar and Jordan could strengthen the links between their educational systems and the business community (Figure 11), although Jordan still scores higher than the PISA average.³¹

Figure 10. Youth unemployment in MENA reaches very high levels

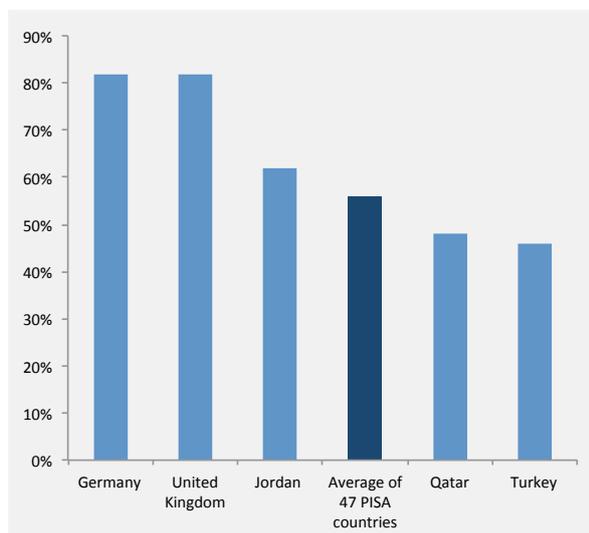
Percent of young people unemployed, 2009 or most recent year for which data are available



Source: World Bank 2011.

Figure 11. Links between school and business could be strengthened in MENA countries

Index of school and business links (2006)



Source: OECD analysis with the support of Professor Richard Sweet (University of Melbourne).

Policies to develop vocational and continuing education, and to improve cooperation with the private sector and civil society, would help reduce the skills gap.

International best practice helps identify policies to improve the skills level of the MENA workforce and bring it closer to market needs. These include:³²

- Vocational education and training (VET), which involves programs at the upper-secondary level that target specific occupations or trades;
- Continuing education and training (CET) to ensure that skills are maintained and developed on a continuous basis; and
- Initiatives that involve the private sector and civil society, such as internship programs or partnerships between the public and private sectors for skills development.

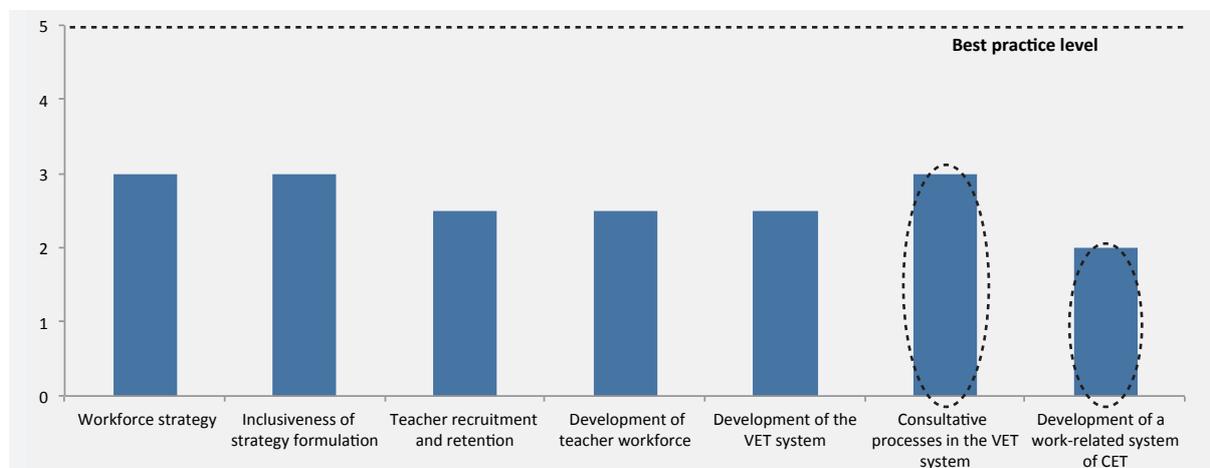
Vocational Education and Training (VET)

VET is a fundamental part of a country’s educational system and, in many countries, provides a career direction for young people from weaker socio-economic backgrounds (Box 1). VET programs can be developed in areas such as textiles, electricity, trade, agriculture, commerce, management, and services. VET systems in the MENA region still have further room for development, in particular related to their relevance to the job market’s needs.

Egypt has been a pioneer in implementing technical VET (TVET) systems in the MENA region. However, the joint OECD-World Bank Review of Higher Education in Egypt released in 2010 highlighted the poor outcomes of the TVET system, particularly reflected in the high unemployment rate of TVET graduates.³³ The study emphasized the need to better adapt TVET trainings to the labor market through systematic consultation with the private sector. The assessment of human capital development policies in Egypt conducted by the OECD in 2009-10³⁴ showed that, despite the establishment of the Supreme Council for Human Resource Development, workforce skills development strategies, including those related to VET and CET, remain fragmented and uncoordinated (Figure 12).

Figure 12. VET and CET systems are underperforming in Egypt

Level of reform in human capital development in Egypt (2010)



Source: OECD 2010b.

Note: In the framework of the Business Climate Development Strategy of Egypt, the OECD scored a series of indicators related to 12 policy dimensions, including human capital. The 5-level assessment is based on OECD and non-OECD best practice. Level 5 represents a level of reform that meets best practice, while 0 indicates absence or lack of policies or measures.

Box 1. Innovation in VET: Lessons from Hungary

Hungary has developed an innovative VET system which may offer some instructive examples for MENA countries. The Hungarian VET system has faced some of the same challenges as those encountered in the MENA region. These include the perceived irrelevance of the VET system to labor market demands (in particular complaints that it is too theoretical), falling enrollment in VET-specific secondary programs, high unemployment, a lack of skilled trainers, and a lack of new recruits. Despite these challenges, Hungary has recognized the important role of VET in offering career paths to persons with different educational aptitudes and interests, in easing school-to-work transitions, and in integrating the unemployed into the labor market.

Two programs highlighted in the OECD report *Working out Change*³⁵ exemplify how Hungary is making VET qualifications more responsive to the labor market. The first is the National Vocational Qualification Register, an updated and flexible qualifications framework designed to reflect the skill needs of the labor market accurately. This framework also organizes VET in Hungary, as programs can now be linked to definitions and qualifications in the Register. The Register directs the focus of VET onto labor-market competencies and increases the relevance of VET. It is also designed to be flexible enough to evolve and to reflect changing labor market demands.

Another innovation in VET, Step One Forward, is a program for helping low-skilled, unemployed adults acquire marketable qualifications. The program was introduced with substantial EU support and launched in November 2005. Step One Forward is designed to allow both underemployed and unemployed adults to advance their educational or professional development. It aims to integrate those populations most at risk in the Hungarian context: the long-term unemployed, early school leavers, the Roma, and those with special needs. The program has enrolled a higher number of adults than any other similar scheme.

Source: OECD 2010c.

Continuing Education and Training (CET)

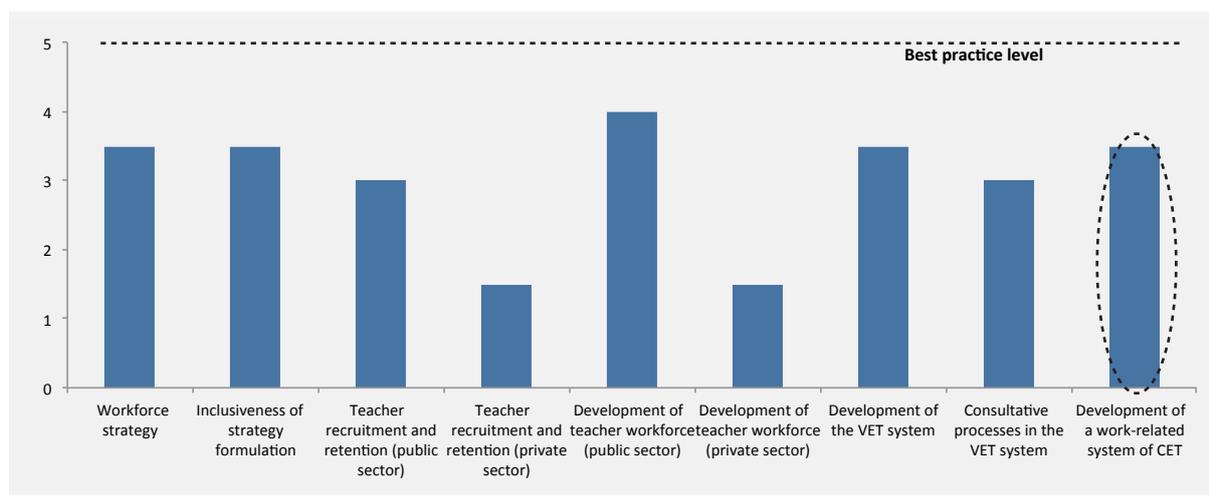
CET is essential to ensure that skills are not lost over time and that the employability of the workforce remains high. CET is particularly relevant to MENA countries in responding to market needs. Morocco is one of the countries in the MENA region that has invested heavily in CET (Figure 13). The main components of Morocco's CET policy include:

- Specialized work associations (Groupements interprofessionnels d'aide au conseil) that help companies define their specific competency needs. The work associations involve 1,400 companies (75 percent of which are small- or medium-sized enterprises), covering most sectors of the economy;
- Special training contracts (Contrats spéciaux de formation) that allow for partial reimbursement of costs incurred by companies to involve their employees in CET³⁶; and
- Public financing to support training of employees in targeted strategic sectors (Métiers mondiaux du Maroc), such as automobile, aeronautics, electronics, and offshore services. A good related example is the automotive training institute set up by the government in cooperation with Renault (Box 2).

An assessment of the CET system in Morocco conducted in 2006 concluded that user enterprises saw an increase of 14.5 percent in their turnover and a rise of 11.5 percent in their production value.³⁷ However, CET suffers from lack of institutional follow-up and evaluation to assess impact. A policy framework and process are needed to ensure the quality and generalization of the system.

Figure 13. VET and CET systems are relatively well-developed in Morocco, though results are not yet reaching expectations

Level of reform in human capital development in Morocco (2010)



Source: OECD 2011d.

Note: In the framework of the Business Climate Development Strategy of Morocco, the OECD scored a series of indicators related to 12 policy dimensions, including human capital. The 5-level assessment is based on OECD and non-OECD best practice. Level 5 represents a level of reform that meets best practice, while 0 indicates absence or lack of policies or measures.

Policies to Involve the Private Sector in Skills Development

Internships constitute an essential means for young people to acquire both the skills and the social acumen that will increase their chances of employment. Internships also help enhance the efficiency of school-to-work transition and can be an effective way for employers to evaluate potential employees to hire.³⁸ Some of the barriers to the development of internships in the MENA region are the limited tradition of student placement schemes, a labor code that does not facilitate internships, and competition from informal labor markets that discourages firms from investing in training.³⁹

Box 2. Renault Tangier: Training Institute for Future Technicians

In March 2011, Morocco opened its first training institute specializing in the automotive industry, the Institut de formation aux métiers de l'automobile, in cooperation with Renault, a French car manufacturer that has been operating in Morocco for 80 years. The institute is managed by Renault Tangier Méditerranée and will provide training for its current and future employees. It can train up to 350 people and will provide technical training along the whole value chain of car manufacturing. Furthermore, Renault Tangier will also offer training for complementary services such as procurement, logistics, management, and human resources. The institute cost EUR7.85 million, which was covered by the Moroccan state with the support of the French Development Agency. The Moroccan state will pay up to EUR6,000 towards the training of each Moroccan employee of Renault Tangier. At the end of the training, the institute will issue certificates to graduates, stating the competencies acquired using a scheme developed by Renault and approved by the Ministry of Employment.

Source: OECD interviews and press clippings.

Box 3. United Kingdom: Involving Small and Medium-Sized Enterprises in Internships

The Step program, which was originally set up and funded by Shell, is the leading student placement initiative in the United Kingdom. It provides an example of how internship programs can benefit both students and companies, and in particular small or medium-sized enterprises (SMEs).

Local officers of Step meet with SMEs at the local level, identify their needs, and then liaise with universities to select interns who could perform these tasks as part of an internship. In order to market its placement services, Step has segmented SMEs according to their typical expectation for internship programs. Feedback from participating companies is extremely positive: 79 percent state that the benefits of taking part in Step outweighed the net costs. Most say they are considering participating in the program again and hiring the students who participated.

Over more than 20 years, Step has demonstrated that internships can build links between academia and the private sector while bringing benefits to all players. Although donor and public funding was essential in the first few years, the program is now self-financed.

Source: OECD 2010a.

Public-private initiatives can also enhance the quality and relevance of education. INJAZ, for instance, is a partnership in the MENA region between ministries of education and the private sector that enables business leaders to teach marketable skills to high school and college students, including basic business skills, teamwork, leadership skills, and entrepreneurial thinking. It thus creates a valuable resource pool for local and foreign companies.

Box 4. Injaz: Partnership in the MENA Region Addressing the Skills Mismatch

INJAZ, a group of local non-governmental organizations across the MENA region, links ministries of education with international and national corporations in order to address the skills mismatches between Arab youths and available jobs. The organizations aim to equip students with practical, business-related skills as part of their regular educational curriculum. Courses offered focus on business skills, economics, financial literacy, and career development. INJAZ also organizes internship programs, career centers, and job fairs.

INJAZ organizations are currently running in Jordan, Morocco, Tunisia, Egypt, Palestine, Lebanon, Saudi Arabia, Kuwait, Bahrain, Qatar, United Arab Emirates, and Oman; and are forthcoming in Algeria, Libya, Syria, and Yemen.

Source: INJAZ, <http://www.injazalarab.org/en>.

Enhanced regional cooperation on higher education can encourage employment.

To help countries improve the educational attainment of their populations through higher education, and thus to overcome the problem of skills mismatches and concomitant youth unemployment, the authors recommend the promotion of structured regional cooperation in the field of higher education and research. Such cooperation should focus on areas such as the mutual recognition of qualifications and education systems, learning of foreign languages, and mobility of students, economic developers, and researchers, all of which would be important for foreign investors (Box 5).⁴⁰ In that regard, the EU's Mobility Partnerships are very useful tools. They are jointly managed circular migration schemes for students, businesspeople, and skilled workers between north and south Mediterranean countries.⁴¹ Such schemes could help stem the acceleration of the brain drain away from the southern Mediterranean countries and may encourage business links with northern countries.

Box 5. The Nordic Council: Enhancing Students' Mobility through Regional Cooperation

Regional cooperation can be an efficient way to pursue common goals while taking advantage of economies of scale. The Nordic Council is a good example. Founded in 1953, the Nordic Council is the common advisory council of the countries of Denmark, Finland, Iceland, Norway, and Sweden. Parliamentary delegations and appointed cabinet representatives from each member country meet annually to promote inter-Nordic cooperation in areas including research and education and to coordinate national laws and practices. Education ministers meet biannually to work on expanding cooperation at all levels of education policy, from pre-primary to higher and adult education, language learning, and ICT. Their resolutions take the form of recommendations to member governments and are usually acted upon favorably. The Council also operates schemes to promote the mobility of students and teachers among Nordic countries.

Source: OECD 2010c.

Several initiatives are currently being rolled out in the MENA region, and need to be further encouraged. For example, in the framework of the Union for the Mediterranean, the Euro-Mediterranean University, based in Slovenia, was established in June 2008 as an international network of universities (179 members from 38 countries). The mission of the university includes improving the quality of higher education through the implementation of postgraduate study and research programs.⁴² Another initiative is the launch of the Mediterranean Integration Centre (Centre de Marseille pour l'intégration en Méditerranée) in cooperation with the World Bank. Its aims are to facilitate labor mobility, alleviate skills mismatches, foster life-long learning, and improve mutually recognized certified qualifications.⁴³

There are a number of key reform measures in the area of education that MENA governments could carry out to foster employment of graduates by local and foreign enterprises. The effectiveness of these policy reforms can be increased if they are embedded in a comprehensive plan to address skills mismatches, quality of teaching, and transferability of skills.⁴⁴ Actions to consider include reinforcing VET and CET systems, enhancing cooperation with the private sector through facilitated internships, research & development programs, stronger links with universities and job centers, fostering regional cooperation among universities, and enhancing mutual recognition of qualifications. The conclusions of a joint OECD-World Bank study on higher education in Egypt could offer some useful insights for other countries in the region (Box 6).

Box 6. Higher Education in Egypt: OECD-Proposed Agenda for 12 Reform Initiatives

1. Developing a national qualifications framework, with statements of graduate attributes for each type and level of qualification, linked to the Bologna Process and the ECTS.⁴⁵ This is a foundational reform, as it sets the focus on learning outcomes that will drive subsequent reforms to educational practice.
2. Renewing technical and vocational education and training, including enhancing the status of TVET qualifications within a comprehensive national qualifications framework; indicating the pathways for learners through secondary schooling and all forms of tertiary education; upgrading facilities; and marketing the value of technical skills to the community. This is an essential reform for expanding access, raising learning productivity, and improving the fit of graduate supply to labor market needs.
3. Expanding private institutions to cater to a large increase in student enrollment. This is also essential for cost-effectively accommodating future growth in student demand without aggravating the quality problems in public institutions.
4. Investing in the material upgrading of public higher education institutions and developing their capacity for responsible self-management. This is essential in view of the inadequate condition of many public higher education institutions and their insufficient responsiveness to the changing environment.
5. Expanding the criteria for student access to higher education by developing a test of generic reasoning and thinking skills to complement the national secondary school examinations in decisions on student admissions. Encouraging students to express multiple preferences of programs and institutions in their applications for higher education admissions.
6. Encouraging students to express multiple preferences of programs and institutions in their applications for higher education admissions, including by program and institution.
7. Permitting institutions, within a total student volume cap and funding amount, to determine their own mix of enrollments across fields of study.
8. Introducing an enrollment-based funding formula to enable institutions to exercise greater flexibility and responsibility.
9. Clarifying the distinctive mission of each higher education institution as a basis for its strategic planning in the context of greater student choice, and formally involving employers and professional bodies in defining learning objectives and providing feedback on their satisfaction with graduates.
10. Establishing a professional career advising service to help students and parents make informed educational choices.
11. Mapping the research strengths of public universities as a basis for identifying areas for future investment and inter-institutional collaboration.
12. Undertaking a competitive process for concentrating investment in research and graduate education, linked with national economic development priorities.

Source: OECD and World Bank 2010.

MENA countries are characterised by rigid labor regulations.

Alongside helping young people acquire the skills needed in the labor market, it is important to promote labor market regulations and institutions that facilitate rather than discourage labor mobility—especially from declining firms, sectors, and regions into expanding ones. A number of factors characterizing labor market flexibility should be taken into consideration by foreign investors. These include procedures for hiring workers, requirements for individual and collective dismissals, regulations for temporary forms of employment, wage levels, requirements for employment protection, labor taxes, and the strength of labor unions.⁴⁶

Labor policies in the MENA countries are particularly rigid. Out of 142 countries ranked in the 2011 World Economic Forum's Global Competitiveness Index (GCI), half of the 14 MENA countries rank in the bottom half on the Labor Market pillar of the GCI. Morocco (132nd), Egypt (141st) and Syria (134th) rank amongst the countries with the least efficient labor markets. Interviews with selected companies conducted by the MENA-OECD Investment Programme suggest that one particular stumbling block to hiring young graduates—apart from skills mismatches—is the difficulty in setting up short-term contracts or internships which would help graduates to acquire valuable skills for the marketplace while allowing companies to test the employees over a fixed period before making a longer-term hiring decision.

Labor policies in MENA countries must be more flexible and adapt to changing market realities and the need to attract FDI.

The evidence suggests that foreign investors are attracted to countries that implement core labor-market standards.⁴⁷ While labor standards are respected in most MENA countries, there is nonetheless scope to make MENA labor markets more flexible.

A starting point to work towards a more flexible labor regime in MENA countries would be to encourage tripartite consultations between the main labor market actors—employers and trade unions—and the government. Such discussions would benefit from taking into account lessons learned from other countries. The Arab Spring may eventually have a positive impact on industrial relations, softening the traditional rigid relationship between management and workers in the region. At the same time, the authority of the state has been weakened, and this may undermine the government's role as the "honest broker." Furthermore, owing to the current economic slowdown and the perception among some that the market economy was to blame for the poverty and exclusion of youth, there is a risk that rigid labor market policies in the near term may become even more entrenched as the state re-enters many sectors that were previously opened up to private investors.

One way to lessen the concerns associated with a greater easing of labor market regulations would be to accompany such measures by an increase in social protection. This could include some of the policies from countries that are characterised as having a system of "flexicurity" (Box 7).

Box 7. Flexicurity: The Example of Denmark

One model that could be a source of inspiration for MENA countries is the so-called "flexicurity" model that was pioneered by Denmark in the 1990s. The Danish, or Nordic, model—varieties of which have also been used in Finland, Sweden, and the Netherlands—has attracted widespread attention from policy makers in Europe and elsewhere, as it links a low unemployment rate with a high standard of social security for the unemployed. The model offers significant labor market flexibility, along with a high level of social protection stemming from generous unemployment benefits and active labor market policies. Flexicurity can thus be considered an integrated strategy for enhancing both flexibility and security in the labor market.

The four main components of flexicurity are generally (1) flexible and reliable contractual arrangements, (2) comprehensive lifelong learning strategies, (3) effective, active labor market policies, and (4) modern social security systems. Specific incentives, such as lower labor taxes for hiring university graduates in exchange for a minimum commitment of training, can help reduce the tax wedge for companies to some degree and encourage more formal hiring. In Denmark, in particular, there are few restrictions on dismissals, and social security contributions of employers are virtually nil.

However, there are a number of features that make the model, and especially the Danish version of it, difficult to apply to other countries. As stated by Jianping Zhou,⁴⁸ the Danish flexicurity model may not in fact be a product of a carefully designed and deliberate strategy but the by-product of a long historical and institutional evolution and social compromises. It is therefore difficult to duplicate the flexicurity model in other countries.

Some of the drawbacks of the model include the fact that the generous social benefits and training courses are funded by income taxes. Social security costs to employers may be low, but income taxes in Denmark are among the highest in the OECD; Denmark ranks second, after Sweden, with regard to the overall tax burden. The state carries most of the burden of Denmark's social security schemes in return for high taxation. This is socially acceptable in Denmark, but would be difficult to implement in a country with budget difficulties or with a large informal sector, and thus a small tax base.

Part of the success of the Danish model, however, stems from a political, and to some degree also societal, willingness to continue to adjust labor market policies. While the overall flexicurity model may be difficult to implement, some of Denmark's labor market policies would help alleviate the pressures on MENA labor markets.

The key tenet of the Danish model has been ongoing labor market reform.⁴⁹ The initial emphasis was on measures to increase participation rates; the employment effect was limited. The emphasis then shifted to strengthening work incentives and enhancing employability. Although benefits have remained generous, the reforms have been associated with reductions in structural unemployment, particularly for the young and long-term unemployed. Since the late 1990s, the authorities have introduced further measures to improve the functioning of the labor market. An income-tax reform gradually lowered the marginal tax rates on labor incomes until 2010. In addition, labor market measures until 2006 included the following, among others:

- The unemployed are now obliged to accept job offers outside their occupational area after three months of receiving unemployment benefits.
- All persons under 25 must "activate" (i.e., accept a job or a placement in a training/retraining scheme) after six months of unemployment. Failure to activate entails a complete loss of benefits.
- The maximum unemployment benefit period was reduced from five to four years.
- Training for the unemployed has become more targeted, and participation in educational leave schemes has become more restrictive.
- The full- and part-time early retirement schemes were merged, creating a more flexible, more unified, and ostensibly more transparent system.
- Tax and benefit incentives were put in place to prolong full-time working life until 62 years of age.
- Income incentives were enhanced to discourage early retirement.

The Danish, or Nordic, models have been implemented in small countries with small populations. While they have proved efficient in achieving full employment, they may not be applicable in their entirety to the countries of the MENA region.

For the flexicurity model to work in MENA, industrial relations would need to be improved, in many cases from a very low starting point. Tripartite negotiations are a key element of the success of implementation and acceptance of the measures (accepting little employment protection in return for generous benefits). As argued elsewhere, the Arab Spring may indeed pave the way for such improvements in industrial relations, breaking down the traditional divide between management and workers. If so, one aspect that would be particularly attractive in the MENA region, and especially in North Africa, would be more flexible labor contracts associated with lifelong learning programs.

Source: OECD 2004, chapter 2; European Commission 2007; Zhou 2007.

Measures to encourage employing local staff include job centers and specific incentives for foreign investors.

A further policy option for MENA countries to consider is the development of employment assistance through job centers. In a MENA Roundtable on Entrepreneurship and Education in Morocco in 2010, it was acknowledged that there is a need for some type of local market clearing mechanism that is not overly reliant on educational institutions.⁵⁰ Following the example of Denmark and other OECD countries, the job centers could be specifically directed towards target populations such as university graduates or women. Services offered by such job centers include job search assistance, skill assessments, guidance, upgrading of skills and qualifications, and orientation towards the right company opportunities.

It should be noted that the first experiences in the MENA region with job centers have not been very promising. A study by the International Labour Organisation (ILO) conducted on Syria and Egypt⁵¹ concluded that institutions supporting school-to-work transition currently play only a minor role in helping young people to join the labor market. The data showed that employers who hire young persons in Syria mainly use informal methods of recruitment, through relatives and friends. Likewise, the majority of Egyptian youth use informal networking for their job search or direct applications to employers. Generally speaking, social networks (friends and family) remain the primary means of finding work for young people.

Job center models that have been successful in OECD countries would need to adapt to these local market conditions. The rapid expansion of online social networks could provide a promising avenue for connecting employers with potential young employees.

Besides building greater flexibility and relevance in the labor market and providing new channels to communicate opportunities, governments can directly support foreign investors who create employment. For example, in Morocco, investors who create at least 250 direct and sustainable jobs may benefit, as part of an investment agreement to be concluded with the government, from advantages amounting to 5 percent of the total investment via the Investment Promotion Fund. This includes a state share of up to 20 percent of the costs of vocational training.⁵² The new Investment Charter, still awaiting approval, contemplates additional special incentives for investment projects that are especially large (i.e., that create a minimum of 1,250 jobs), innovative, or targeted to specific sectors or underdeveloped regions. The charter also provides labor tax exemptions targeting graduates from higher education and VET, through the insertion program Idmaj. Egypt also offers investment incentives

in specific regions, such as the provision of up to LE15,000 (approximately US\$2,500) for every new job created in Upper Egypt.⁵³ In Jordan, the Ministry of Communication and Information Technology incentivizes the hiring of fresh graduates in the ICT field by subsidizing their wages (50 percent for their first year and 25 percent for the next 6 months).⁵⁴

Nationalization employment policies may have a negative impact on FDI.

Faced with high levels of unemployment for their citizens,⁵⁵ a number of resource-rich countries in the Gulf have turned to so-called "nationalisation of employment" policies, with mixed results. Factors explaining the high level of unemployment among nationals are, on the one hand, the unavailability of nationals with adequate qualifications and training and, on the other hand, the unlimited availability of the cheaper expatriate workforce. Despite the sponsorship system in most GCC countries, which requires every immigrant worker to have a local sponsor to obtain an entry visa or a permit of residence, governments have set up nationalization policies to increase the rate of nationals' employment. However, employers, whether national or foreign, are worried that the imposed nationalization employment measures will prevent them from meeting their staffing needs and increase labor costs.

MENA countries have a number of options to boost employment by improving the skills of their workforce and putting in place a more flexible labor market regime. To find the optimal policy mix to suit local conditions, governments can leverage best practice from other countries, develop options through active consultation with the private sector and civil society, and make skills development and improvement of labor market regulations a top priority.

2. Women's Integration in the MENA Labor Force

Women constitute only a small share of the formal labor force in the MENA region. On average, a mere 32 percent of working-age women join the labor force in the MENA region, compared to 56 percent in low- and middle-income countries and 61 percent in OECD member countries.⁵⁶ By comparison, the male participation rate in the MENA labor force is 81 percent. (Figure 14).

The MENA region is highly diverse in terms of female labor force participation rates, with Gulf countries generally faring better than North African and Levantine countries. This diversity is manifest in the composition of the female labor force, which includes decidedly distinct profiles, ranging from highly educated urban women working in the ICT sector to low-skilled women working in the agriculture sector.

Highly educated women represent an untapped potential for private investors.

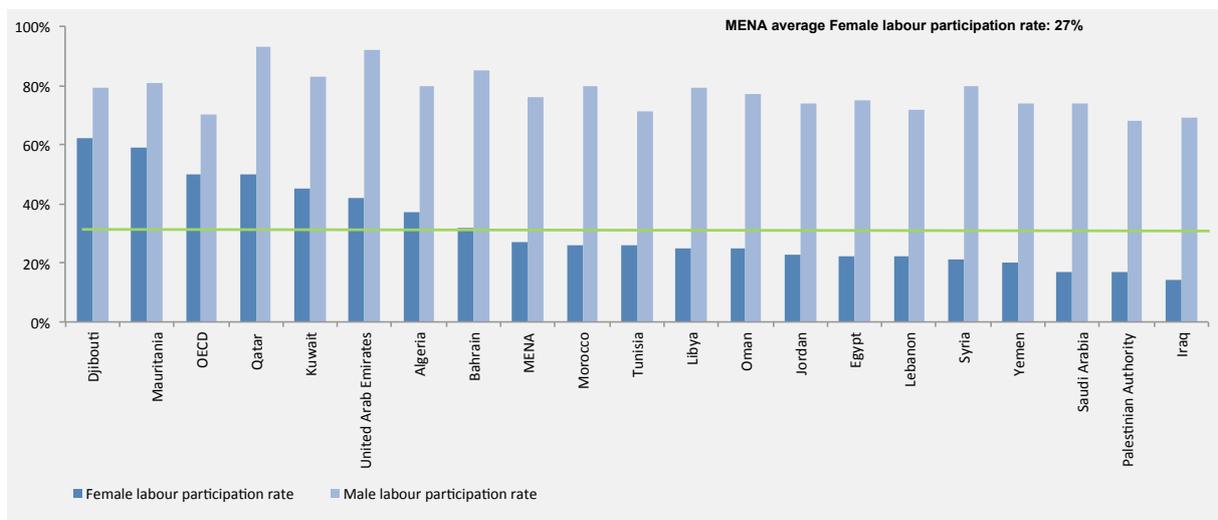
In over half of the MENA countries, particularly the GCC countries, women consistently outperform and outnumber their male counterparts in tertiary education. They are increasingly qualified for high-skills jobs in domains such as engineering, medicine, chemistry, and mathematics.

However, investors are reluctant to employ women in the MENA region, notably as a result of rigid labor legislation, financial costs, organizational and practical problems in countries that apply sharia, issues relating to working hours, and social perceptions of both employers and employees.⁵⁷

As a result of these factors, women that cannot find formal work turn to the informal sector, where they are highly active. This economic reality leads to losses of revenue and resources for governments, as a large share of the workforce and enterprise sector thus escapes registration. Governments could possibly encourage female-led firms in the informal sector to enter the formal economy by providing them with incentives such as access to formal financing and business support services.

Figure 14. Female labor force participation rate in MENA is low compared to OECD countries

Labor force participation rate in MENA countries, 2009



Source: World Bank 2011.

Proactive and innovative policies could unleash the female labor force potential.

While there have been some improvements in many MENA countries in terms of promoting gender equality and advancing women's roles in socio-economic activities, stronger efforts are needed to encourage and enable more women to participate in the labor force and to broaden the scope of occupational opportunities. The Arab Spring represents an opportunity to further these goals. Some avenues for consideration may include:

- **Enhancing contract flexibility** to allow women faced with domestic considerations to join the labor market or remain professionally active. This would be especially attractive to those who choose to leave the labor force shortly after joining it, typically to start a family. Most Arab women still get married before the age of 25. Such flexible working arrangements may include part-time employment, teleworking, support services for women in the workplace, and training programs for women reintegrating into the labor force.
- **Ensuring equal access to social benefits** such as pensions to encourage women's participation in the formal labor force.
- **Leveraging new technologies** to increase the opportunities for training and e-learning and to facilitate working arrangements in industries that do not require a physical presence in the office (such as product development, software engineering, or market research). Technology can also be tapped to allow women to identify employment opportunities.
- **Reviewing tax policies** as appropriate to limit any disincentives to greater participation of women in the formal labor force. This is especially the case for policies to encourage SMEs to enter the formal sector, as most women outside of the public sector work in SMEs.
- **Considering affirmative action** to increase equality of opportunity and treatment of women in the public sector, in terms of wages, flexibility, merit-based advantages, continuing education, and support services. This might set an example for the private sector, as well.
- **Promoting regional and international businesswomen's networks**, such as the OECD-MENA Women's Business Forum,⁵⁸ to enhance knowledge of the lack of participation of women in the formal labor market, share good practices, and raise awareness of policy options for creating a more conducive environment for women's employment.

3. Fostering Linkages between Foreign Investors and Local Suppliers

FDI can play an important role in the development of local SMEs if the right conditions are in place. A range of public policies pursued by the host country can help maximise the positive contributions of FDI, particularly its impact on direct and indirect employment creation. Encouraging local businesses to become suppliers, clients, and service providers for FDI projects is an important component of such policies. Indeed, fostering and strengthening business linkages between local SMEs and multinational enterprises (MNEs) can be an effective tool to improve SME competitiveness and generate further employment.

Business linkages maximize the employment impact of FDI through promotion of local SMEs.

Business linkages between MNEs and local SMEs have several advantages. For MNEs and their affiliates, "benefits may include lowering transaction costs, providing greater flexibility, spurring local adaptations and fostering corporate social responsibility. For local SMEs, potential gains relate to increased local market opportunities, upgraded management skills, benefiting from new technology, facilitating their access to capital and increased possibility of internationalising their business."⁵⁹ Given that SMEs account for over 95 percent of the business population,⁶⁰ business linkages can stimulate the economy of the host country and create employment. There is a direct employment effect on the SME suppliers and partners, but also an indirect spillover impact on job creation.⁶¹

Business linkages can take several forms: backward linkages with suppliers, forward linkages with customers, and linkages with technology partners through joint ventures, licensing, and strategic alliances. Backward linkages are likely to have the strongest impact on direct and indirect job creation.

Business linkages should normally result from market forces, but a number of barriers can prevent markets from creating linkages. The skills gap is the first obstacle, as local SMEs need to have the technological and managerial capabilities required by MNEs. The second main barrier relates to the lack of information regarding potential local suppliers and the needs of the client enterprises. Public policies can play an active role in overcoming these barriers and facilitating the creation and expansion of business linkages.

In the MENA region, SMEs must improve business performance to benefit from business linkages.

SMEs represent the vast majority of all businesses in the MENA region and therefore constitute a pool of potential suppliers and the best source of job creation. However, the MENA region lags behind other regions in terms of entrepreneurial performance and SME creation and expansion. This leads to underused employment capacity of the domestic private sector. SMEs face many obstacles which limit their attractiveness as suppliers for MNEs, such as undercapitalization, weak production processes, poor access to adequately priced inputs, poorly skilled workers, low value-added production, inadequate diversification, and limited access to markets and distribution channels.

To benefit from business linkages, MENA SMEs need to strengthen their capabilities and upgrade their skills to become competitive suppliers to international or multinational clients. An example of a policy solution is the National Suppliers Development Programme, launched in 2005 by Egypt, which started with a pilot project in the automotive industry (Box 8). This was a very successful program and could be replicated in the region

Box 8. Egypt's National Suppliers Development Programme

In July 2005, General Motors (GM), a large US car manufacturer, and Egypt's Ministry of Trade and Industry agreed to proceed with a program to help upgrade GM's network of local suppliers. Under the terms of the program, Egypt committed to upgrading GM's network of suppliers in Egypt to international standards at no cost to GM. In return, GM promised to place those local companies that successfully met their international requirements in its global network of suppliers. The formula was simple: GM would secure the quality of suppliers its local business needed; in return, GM would help place Egyptian suppliers on the global sourcing map, making it possible for GM's international operations in countries such as Brazil or Turkey to obtain their automobile parts from Egypt's local feeder industry.

The success of this pilot project has been replicated across many industrial sectors in Egypt. The Ministry of Trade and Industry approached 100 of Egypt's leading companies and invited them to participate in a similar arrangement. Thirty-seven so-called "mother companies" from a variety of industrial sectors have signed up for the program. Companies that have joined include consumer products firms Procter & Gamble (USA), Unilever (UK and the Netherlands), Cadbury (UK), and electronics companies Siemens (Germany) and LG (South Korea).

Source: OECD 2009a.

International best practice provides additional examples of policy measures that could further develop business linkages.

Some countries have developed policies that encourage business linkages. The Irish National Linkage Programme is frequently presented as a successful case. It began by targeting the electronics sector but was expanded to cover engineering, chemicals, pharmaceuticals, food, and consumer products. Malaysia has also implemented several specific programs, starting with the Vendor Development Programme in 1988. This program linked local SMEs with large domestic and multi-national enterprises. Through skills development, technology transfers, and quality improvements provided by MNEs and affordable loans provided by the state, local suppliers could expand and provide MNEs with better output at lower costs. In 1996, Malaysia added the Industrial Linkage Programme, which offers tax incentives for capacity-building activities in selected manufacturing activities and in the service industry. By 2007, 906 SMEs had registered for the program, and 128 of them were able to link with MNEs and other large companies. Malaysia again added the Global Supplier Programme, which has the objective of developing SMEs into competitive suppliers in the supply chain of MNEs through mentoring activities and training in vital skills via Skills Development Centers. During its first year, the program trained 813 employees from 225 SMEs. Moreover, 23 MNEs were involved, such as Intel, an electronic components manufacturer.⁶³ The case of Singapore provides another example of policies that successfully fostered linkages (Box 9).

Box 9. The Local Industry Upgrading Programme of Singapore

The Local Industry Upgrading Programme was created in 1986 by the Economic Development Board of Singapore to help local SMEs in the electronics and ICT sector to improve their efficiency and reliability and to upgrade their technologies to make them competitive on an international level and enable them to develop new products. Local SMEs willing to be part of the program and able to perform business contracts are assisted by the Economic Development Board in acquiring the necessary technologies and skills in collaboration with MNEs. The policy tools used by the program include:

- SMEs that are part of the program have priority to benefit from available investment incentives.
- MNEs are encouraged to assist local SMEs in meeting required expectations. An MNE manager is invited to work as a part- or full-time consultant in a selected SME to upgrade the process of production. The salary is paid by the Economic Development Board.
- The Economic Development Board conducts regular workshops to upgrade the capabilities of local suppliers.

The program is implemented in three phases. First, overall operational efficiency of the SMEs is improved, including, for instance, production planning, inventory control, plant layout, and financial and management control techniques. Second, new products and processes are introduced and implemented by the local SME. The last step focuses on joint product and process research with MNEs.⁶⁴

Since 2002, the program has helped local enterprises in the ICT industry to develop over 560 new or improved products and services and trained more than 1,700 employees. One of the first MNEs in the electronics industry that successfully participated in the program was Hewlett Packard with its production of technologically advanced membrane switches and circuits.

Source: Government of Singapore, <http://www.ida.gov.sg/home/index.aspx>; Perry 1999.

MENA countries could emulate successful business linkage programs.

Business linkage programs need to be strategically and efficiently planned. Implementing business linkage programs can involve substantial amounts of time and financial resources. An example of how to develop business linkages is the OECD's five-stage approach (Figure 15). The first step is a period of strategy definition, where objectives are clearly established and a self-assessment is conducted. Next, the institutional and functional set-up is created. In a third phase, firms are approached and introduced into the program. The fourth and fifth parts consist of monitoring results and implementing follow-up support for businesses involved in the program. This approach ensures that policy makers play to their strengths in high-potential sectors and that stakeholders are closely involved in the process, two important ingredients for success identified by the OECD.

Business linkage programs need to be designed and implemented at a sectoral level. Starting with a pilot program in a selected sector or industry has been a key success factor for several countries. Once results are monitored and strengths assessed, the program can be replicated in another sector or expanded to another region. The establishment of economic zones could prove useful in piloting programs in selected industries to promote linkages between FDI and local firms (Box 10).⁶⁵

The communication aspect of a business linkage program is essential. Enterprises need to connect and exchange ideas and plans before entering into business operations. Well-planned and targeted events (B2Bs, business fairs, etc.) are useful for bringing together SME owners with representatives of MNEs. Investment promotion agencies should play an important role in organizing these get-togethers, but also in developing firms' databases to help incentivize business matching. Certification and standardization are also key policy components to accompany a successful business linkage program. When linked to MNEs' operations, local enterprises need to respond to the requirements of international markets and develop export capabilities.

Box 10. Economic Zones in the MENA region

The logic of economic zones (EZs) is to offer specific conditions and services to investors—both foreign and local—in order to encourage investment and exports. In addition to tax incentives, EZs can offer services such as dedicated infrastructure, easy access to land and office space, rapid registration and licensing of companies, and fast-track customs procedures. Consequently, EZs can be particularly attractive to investors in a country with high barriers to doing business. EZs can be used to achieve specific development objectives, for instance to attract investors to poorer regions with limited employment opportunities or to test new policies before rolling them out on a national scale. Finally, EZs can be an important vehicle for a country to develop its exports by attracting foreign investors with capital and know-how.

The number of EZs in the MENA region has increased significantly, from 10 in 2005 to almost 73 in 2008.⁶⁶ According to the World Bank Group, EZs so far have created at least 1.5 million direct jobs in the MENA region,⁶⁷ corresponding on average to 1.6 percent of national employment. The share of employment generated by EZs is much higher in some countries, such as Tunisia and the United Arab Emirates, where it reaches, respectively, 8 percent and 25 percent of national employment in EZs. The OECD survey conducted for this report in selected MENA countries indicates that the Free Zone of Tangier in Morocco has

created over 50,000 direct jobs in 10 years.⁶⁸ The effect is larger if one accounts for indirect employment effects.

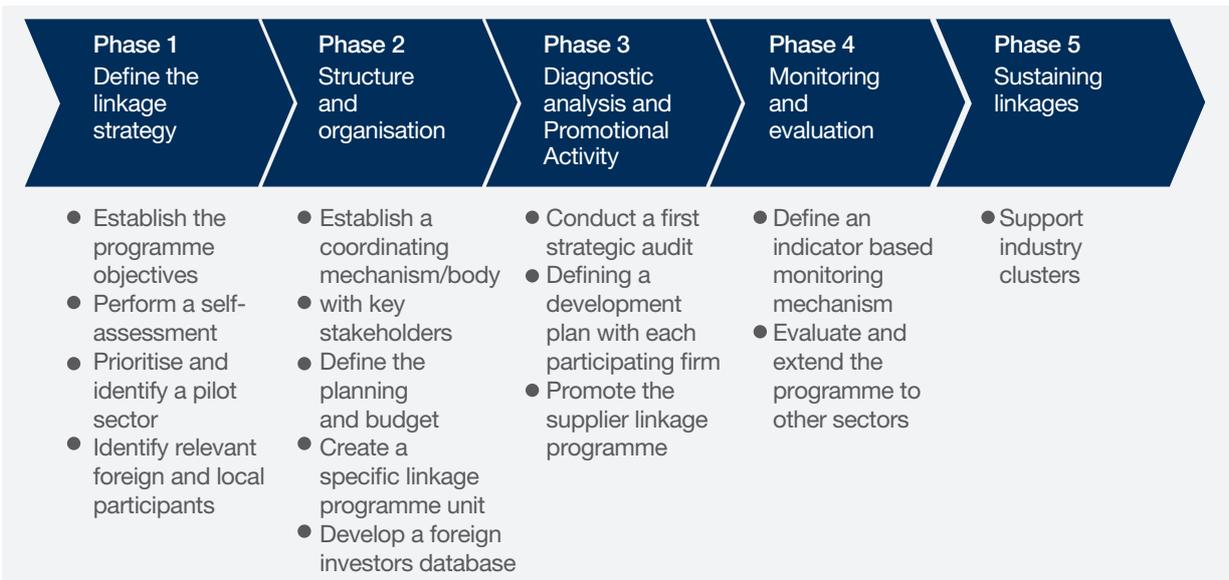
As EZs generally provide jobs for low-skilled employees, they rely particularly on a female workforce, which represents two-thirds of the EZ workforce.⁶⁹ As economic activity diversifies away from simple assembly operations, the percentage of women in the workforce decreases.

In order to have an effect on the overall level of employment, an EZ must avoid diverting existing investments to the zones and instead attract new, additional investment. Such "additionality" of investment is more likely to occur in countries with high barriers to doing business, where an EZ offers an attractive alternative.

The most successful EZs are structured around clearly defined development objectives (e.g., reducing unemployment in a specific region); are focused on export processing in labor-intensive industries; and are combined with business linkage programs to encourage the development of value chains with local suppliers (see section 3 for further information).

Experience shows that EZs are also more efficient when providing the right services and infrastructure, rather than tax incentives. When tax incentives are provided, it is important that they be clearly justified, regularly assessed, and limited in time via "sunset clauses."

Figure 15: Business linkages in five stages



Source: OECD 2009a.

Fostering forward and backward linkages with FDI businesses can help raise the indirect-to-direct job creation ratio, and would therefore improve the employment impact of FDI. If implemented successfully, such efforts could have strong multiplier effects, spreading growth and job creation from MNEs to local enterprises.

4. FDI in High-Potential Sectors for Employment Creation: the Case for Renewable Energies and Tradable Business Services

The geographical position, natural endowments, and skills potential in MENA countries constitute a comparative advantage for the development of two high-growth sectors with employment creation potential: renewable energies and tradable business services. As part of their strategies for economic growth and employment creation, MENA countries could promote the development of those sectors, namely by removing any barriers to attracting FDI.

The MENA region offers a substantial potential for the development of renewable energies.

The MENA region has one of the greatest potentials for solar energy generation in the world. It is estimated that, with current technology, Concentrated Solar Power plants could generate 100 times the combined electricity consumption of the MENA and European regions together.⁷⁰ In addition, the North African coast and the Red Sea coast have important wind resources, which could be used to develop large-scale wind farms. Yet, despite their potential, renewable energy resources remain almost unexploited in the region, accounting for only 3 percent of electricity production.⁷¹

Even so, MENA countries are progressively taking the lead in developing renewable energies as a consequence of rising domestic energy demand and climbing energy prices. Moreover, oil-importing countries could not only take advantage of this opportunity to boost economic growth but also lower their dependence on energy imports. Against this background, several MENA countries have adopted national plans with quantitative targets to expand the share of renewable energy in their national electricity generation. They have also set up state agencies in charge of promoting renewable energies. For instance, Morocco launched its National Renewable Energy and Efficiency Plan in 2008, which sets the target of 15 percent of energy produced by renewables by 2020. The Plan is expected to create more than 40,000 jobs and stimulate over DIR 4.5 billion in investment (USD 550 million)

Proximity to European markets represents a significant advantage.

The geographic proximity of the MENA region to European countries, which are setting targets for cuts in their carbon emissions, provides an opportunity for exploiting renewable sources of energy. Several regional projects have been launched to take advantage of this opportunity.

The Mediterranean Solar Plan was launched in Paris in July 2008 to reinforce Euro-Mediterranean cooperation in solar energy. It is one of six key initiatives of the Union for the Mediterranean that aim to meet the major energy and climate challenges facing the Mediterranean region and the European Union in the coming decades. The plan has two complementary targets: i) developing 20 gigawatts of new renewable energy production capacity and ii) achieving significant energy savings around the Mediterranean by 2020, thus addressing both supply and demand.

The Desertec Industrial Initiative in MENA is an initiative launched by the Desertec Foundation that includes a network of politicians, scientists, and economists from around the Mediterranean Rim.⁷² It aims to support the development of renewable energies—particularly solar energies—in MENA by stimulating and coordinating industrial initiatives and to generate energy to supply both European and MENA countries. Desertec has set a target of supplying 15 percent of the European Union's energy needs by 2050. To reach this goal, the Initiative plans to build 30 Concentrated Solar Power plants in the Sahara by 2050 to produce a 20-gigawatt renewable energy capacity with an estimated investment of EUR400 billion.

The Transgreen project is highly complementary to Desertec's project, as the latter concentrates on power plant infrastructure in North Africa, whereas the former focuses on energy transmission systems. The Transgreen project brings together a consortium of power companies, network operators, and manufacturers of high-tension equipment headed by Electricité de France, to set up a trans-Mediterranean supergrid consisting of high-voltage direct current cables and capable of exporting 5 gigawatts to Europe by 2020.

The renewable energy sector's direct impact on employment could be higher than that of traditional energy sectors.

Quantitative assessments of the impact of renewable energies on labor markets highlight that all forms of renewable energy have significantly higher labor intensity than fossil or traditional energy per unit of installed capacity, per unit of power generated, and per dollar invested.⁷³ The table below, based on findings from a range of studies published in 2001-04, shows that solar photovoltaics (PV) will use, on average, seven times more labor than coal-fired energy for the production of the same quantity of megawatt; and wind power will use, on average, 1.83 times more labor than natural gas.

Table 1. Estimated Employment per Megawatt, Renewable and Fossil Fuel Power Plants⁷⁴

Average Employment over Life of Facility (Jobs per megawatt of average capacity)

	Manufacturing, Construction, Installation	Operation & Maintenance/Fuel Processing	Total
Solar PV	5.76-6.21	1.20-4.80	6.96-11.01
Wind power	0.43-2.51	0.27	0.7-2.78
Biomass	0.40	0.38-2.44	0.78-2.84
Coal-fired	0.27	0.74	1.01
Natural gas-fired	0.25	0.7	0.95

Source: UNEP 2008.

Available evidence thus suggests that the renewable energy sector is more labor intensive than the traditional hydrocarbons sector. During the last decade, the fossil-fuel sector increased its energy production, while the number of jobs provided by the sector declined. For example, in Saudi Arabia, employment in the electricity and gas sector decreased by 13 percent between 2001 and 2009,⁷⁵ despite a strong increase in electricity consumption. In the mining and quarrying sector, which includes mining of coal and extraction of crude petroleum and gas, job losses have been even more pronounced. Employment in the sector dropped by 40 percent in Egypt between 2001 and 2008 and by 13 percent in the United Arab Emirates between 2000 and 2004. Employment in mining and quarrying accounted for only 1 percent of Saudi Arabia's workforce in 2008. These data highlight the limited employment potential of the hydrocarbon sector, suggesting that a progressive transition to renewable energy could lead to a net increase in employment in the MENA region.

Renewable energies can generate employment opportunities at various stages of the production process, ranging from design to manufacturing. These sectors require a wide range of skills, from low-skilled to highly specialized jobs. Employment opportunities would also be generated at the local level. Indeed, it may be more profitable for investors to produce the bulky components of solar panels and wind turbines locally, owing to high shipping costs. As a result, MENA countries would greatly benefit from technology transfers to enable local manufacturing, and from training and education to develop the appropriate skills in order to extend the value chain of the renewable energy sector.

The advent of renewable energy can have a beneficial effect on economic development and job creation in rural areas. Most of the MENA countries have broadly adequate access to electricity, with an average electrification rate of about 90 percent.⁷⁶ However, an estimated 24 million people still lack access to electricity, particularly in rural areas, where people often rely on biomass for their energy needs.⁷⁷

Energy poverty restrains local economic development in general and women's empowerment in particular.⁷⁸ One of the characteristics of renewable energy technology is the possibility of developing small energy plants in rural areas, even at the individual household level (solar panels in the roof). Not only does access to energy act as a spur to local economic activity, creating opportunities for local entrepreneurs, but the maintenance of power plants in itself generates employment. A well-known initiative that supports this argument is Bangladesh's Grameen Shakti Microloans Solar Photo Voltaic program. It has led to the installation of more than 100,000 home solar systems and over 1,000 women have been trained as solar PV technicians and maintenance workers in rural communities in Bangladesh.⁷⁹

Public-private partnerships are potential instruments for developing the renewable energies sector.

A well-performing energy infrastructure is vital for economic prosperity. Given the traditional characteristics of high capital intensity and high barriers to entry into a country's energy infrastructure, energy infrastructure is often under the charge of the government through state-owned enterprises or enterprises with state participation. The high cost of the investments, their long-term nature, and the energy's utility nature make energy provision a natural monopoly, so it is reasonable for governments to remain involved in this sector.

The renewable energies sector is no exception. Although more labor intensive than the traditional energy sectors, projects in this sector, such as wind farms and geothermal plants, also require high capital investments. However, given the specific requirements in terms of knowledge, technology, and skills of this emerging sector, private-sector participation alongside public-sector involvement would be desirable for the successful development and implementation of such projects.

Participation by the public and private sectors in renewable energy projects could take the form of public-private partnerships (PPPs), which would allow private-sector financing, know-how, technology, and pricing risks in these projects. However, the energy sector presents specific challenges that have to be taken into account, such as the long-term character and high complexity of energy infrastructure contracts. There is also the double imperative of ensuring financial sustainability while meeting user needs and social objectives.⁸⁰ In some cases, PPPs have failed because of deficient design and conception, and because they have been seen as means not to maximize public and private sector strengths but to overcome gaps in government capacity. In other cases, unrealistic designs have led to runaway costs and the lack of consultation and communication with stakeholders has led to strong opposition from local communities.

Hence, PPPs should be understood as a policy alternative that requires the appropriate institutional framework and rigorous ex-ante analysis to measure their feasibility and value. Also, the design, management, and evaluation of a PPP have implications for government capacity, which usually needs reinforcing.⁸¹ This is contrary to the idea that PPPs involve lower levels of responsibility and engagement by governments.

The OECD Principles for Private Sector Participation in Infrastructure were developed to support governments that seek to involve the private sector in infrastructure development, to attract investment and mobilize private-sector resources for the benefit of society, and

to achieve sustainable development (Box 11). Such principles could prove helpful for MENA countries wishing to tap the financial and technological resources and expertise of the private sector in renewable energy projects through PPPs and, at the same time, to strengthen government capacity in their design and implementation.

Box 11. The OECD Principles for Private Sector Participation in Infrastructure

The Principles help governments work with private-sector partners to finance and bring to fruition projects in areas of vital economic importance, such as transport, water and power supply, and telecommunications. They offer a checklist of policy issues to consider in ensuring that citizens get the services they need at a fair cost and with viable returns to private-sector partners.

The Principles cover five important sets of challenges for national authorities:

1. Deciding on public or private provision of infrastructure services: The benefits, costs, and risks of involving the private sector in infrastructure services have to be considered and thoroughly analyzed.
2. Enhancing the institutional environment for PPPs: The rule of law, transparency, the protection of property and contractual rights, public and corporate governance, and anti-corruption efforts are some of the key elements of an institutional environment conducive to PPPs.
3. Goals, strategies, and capacities at all levels: Consultations with stakeholders, a clear communication of strategies and objectives for PPPs at all levels of government, and mechanisms for cross-jurisdictional cooperation need to be considered.
4. Making public-private cooperation work: Clear communication between the public and private sectors, full disclosure of all project-relevant information, due diligence, transparency in the awarding process, responsibilities, risk allocation, and dispute resolution mechanisms are key in making cooperation work.
5. Encouraging responsible business conduct: Principles and standards for responsible business conduct, good faith and fairness from public- and private sector participants, the participation of the private sector in communicating and consulting with the general public, and avoiding socially unacceptable outcomes should be included in PPP design.

Source: OECD 2007d.

Tradable business services have significant potential to generate growth and employment.

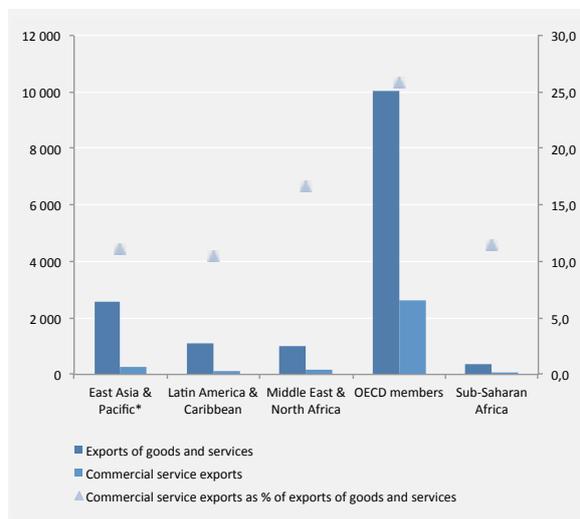
Multinational enterprises are increasingly outsourcing business services to cut costs and increase competitiveness. With its considerable advantages—proximity to European markets, comparatively low labor costs, and, in some countries, the availability of relatively well-educated populations—the MENA region is well-situated to take advantage of this trend. However, although MENA's commercial services exports represent a higher share in GDP than any other region bar OECD countries, in absolute values these exports are behind other regions such as developing East Asia and Pacific (US\$ 162 billion vs. US\$220 billion) (Figure 16). This suggests that there is scope to increase the role of services, especially business services, in the economy and employment.

The development of a dynamic and competitive services sector is a priority for the MENA region. Attracting further investment in services in MENA would not only increase economic diversification and competitiveness but also contribute to employment creation.

While exports of commercial services in MENA are more diversified than in other regions and vary from country to country (Figures 17 and 18), **travel services** remain the region's leading commercial service-exporting sector, ranging from 51 percent in Egypt to over 71 percent in Jordan. The region's second most important commercial service export is **computer, communications, and other services**. Exports of **transport services** are the third most important service export activity in the overall MENA region, however, the importance of exports of transport services varies greatly at the country level, with oil exporters registering generally higher shares than resource-poor countries. **Insurance and financial services** exports represent the smallest share of services exports in all regions, and account for 4.3 percent in the MENA region.

Figure 16. Share of commercial service exports are relatively high in MENA, but low in absolute terms

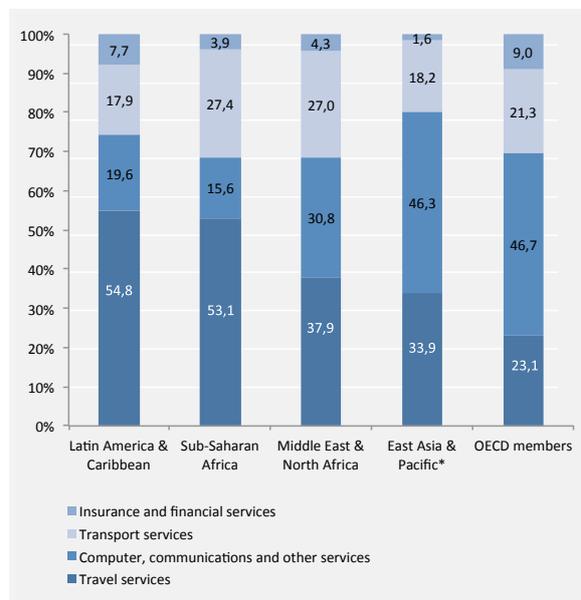
Exports of goods and services in US\$ billion, 2010 or latest



Source: World Bank 2011.
Note: * Developing countries only

Figure 17. Exports of commercial services are well diversified in the MENA region

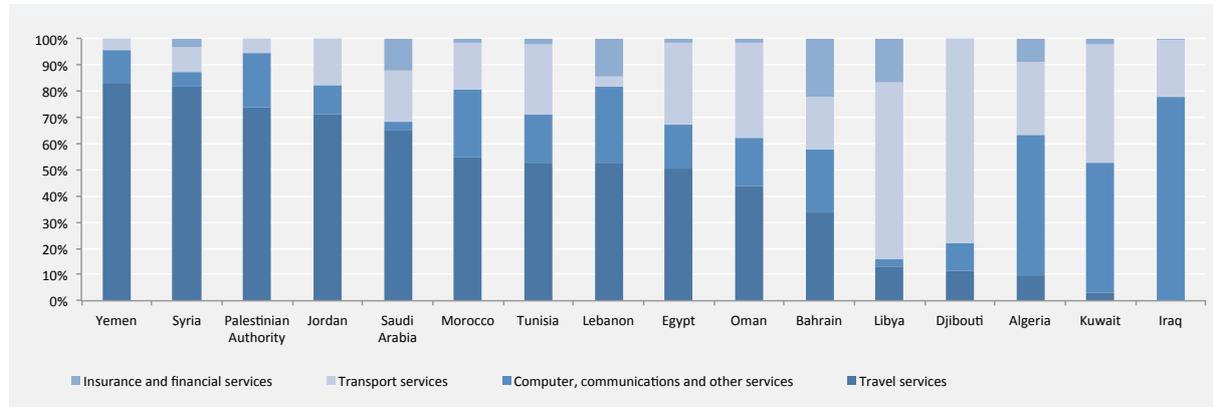
Exports of services as percent of commercial service exports, 2010 or latest available



Source: World Bank, 2011.
Note: * Developing countries only

Figure 18. The composition of exports of services greatly varies at the country level

Exports of services as percent of commercial service exports, 2010 or latest available



Source: World Bank 2011.

Note: * Developing countries only

Promoting the development of the tradable services sector, in particular tourism and business process outsourcing services, could boost job creation and competitiveness in the MENA region, given its geographical, cultural, cost-competitiveness, and human-capital advantages.

As noted in chapter 2, tourism represents an important potential for exploiting the rich cultural and natural resources of many countries in the region, but also for creating employment for ample segments of the population, given the sector's lower skills requirements. Furthermore, tourism heavily involves SMEs, which translates into job creation and opportunities for entrepreneurship. Additionally, FDI in tourism can help revitalize declining urban and rural centers.⁸²

Business services represent another potential sector for attracting FDI and employing people with higher skills levels, especially in North African countries with relatively educated populations. Tunisia and Morocco are recipients of foreign investments in business services, especially from European (mostly French) firms. However, outsourcing activities to date have mostly been directed to call centers (given the cultural and linguistic ties of those countries and France), which require relatively low levels of skills as compared to other services, such as R&D, accounting, and legal services.⁸³

In the case of Egypt, the relatively low costs of doing business, the existence of programs to support the offshoring industry, and the availability of a young, welltrained, and multilingual work force has encouraged the development of information technology outsourcing and business process outsourcing sectors.⁸⁴ However, Egypt faces significant competition from major outsourcing centers in Asia, notably India.

To tap the full potential of the services sector, governments must remove key barriers to their development.

Creating the conditions to attract FDI in higher-value business outsourcing services could result in productivity gains and innovation adoptions and developments. However, to realize the potential of those investments, governments would need to implement measures to facilitate the exchange of services by removing barriers to trade and improving infrastructure, among others.

Despite their importance to the overall domestic economy and to the international flow of ideas, knowledge, and technology, trade in services is only 30 percent of total world trade.⁸⁵ This low share is partly due to the fact that services are traditionally non-tradable economic activities, since many of them are not usually sold in locations distant from their place of production. Another obstacle is the complexity of trade in services regulation and liberalization negotiations, as evidenced by the unachieved Doha Round and the implementation of the General Agreement on Trade in Services of the World Trade Organisation. Indeed, the nature of trade in services, its mostly domestic regulatory character, and the lack of internationally comparable data on barriers to trade (in contrast to the trade in goods, for which there is more complete information on tariff and non-tariff barriers) make it difficult to assess the economic impact of trade in services. The OECD is undertaking efforts to surmount these difficulties by developing a Services Trade Restrictiveness Index (TRI) (Box 12).

A number of studies on the liberalization of trade in services using the trade restrictiveness index approach⁸⁸ have been undertaken in the MENA region, notably in Egypt, Jordan, Lebanon, Morocco, and Tunisia.⁸⁹ Those analyses have targeted services that are fundamental for the economy (“backbone services”), which are essential for the integration of the MENA region into the world economy: the banking sector, telecommunications (fixed and mobile), transportation, and insurance. (These services are also essential in creating employment opportunities for youth and the well educated, which are disproportionately affected by high unemployment rates not only in those countries but in the overall region.)

This evidence suggests that further removing barriers to services would also have positive effects in increasing competition and productivity in the business services sector and spillover effects in the overall economy, facilitating the transition to a knowledge-based and more competitive economy.

Box 12 The OECD’s Services Trade Restrictiveness Index

Through the development of a Services Trade Restrictiveness Index, the OECD is undertaking significant efforts to improve assessments of regulatory barriers to trade, to help make services markets more open and efficient. The index can help identify which policy measures restrict trade and suggest best practice to focus reform efforts on priority sectors and measures.⁸⁶

A services trade regulatory database provides internationally comparable current information on regulatory policies affecting trade in services, such as requirements for joint ventures, screening of investments, quotas on the movement of people, regulatory requirements for foreign participation in government procurement, etc. The index itself translates that qualitative information into quantitative measures using a scoring and weighting mechanism to capture the essence of restrictiveness in trade of services. The index currently covers computer services, telecommunications, construction, professional services (engineering, architecture, and legal and accounting services), transport (air, maritime, rail, road, and courier), distribution, and audiovisuals in 34 countries.⁸⁷

Barriers in the financial services sector persist.

The TRI studies analyze the regulatory framework and initiatives (de jure trade regulations) and the actual behavior of governments in liberalizing trade in services (de facto barriers to trade). A key finding in the financial sector is that, although most governments have undertaken significant initiatives to limit regulations regarding foreign equity participation in services, de facto barriers remain. For instance, in Morocco the authorities control foreign participation in the largest banks by constraining the amount of capital in their businesses. In the case of Jordan, although insurance services have been opened up to foreign participation, the high fragmentation of the sector has discouraged FDI.

MENA countries need to improve telecommunications and transport infrastructure.

Concerning the telecommunications and transport sectors, the analyses indicate that improving quality and coverage in the countries studied and reducing prices would be essential, not only for backbone services but also to increase overall economic competitiveness and for the development of tourism and tradable business services.

Other barriers must be removed.

Removing barriers to trade in services would also be instrumental in promoting FDI in these sectors, in particular regulations related to foreign equity participation (which have been already lifted or softened in the banking and telecom sectors in Egypt, Jordan, Morocco, and Lebanon) and liberalizing or relaxing limitations on the commercial presence of foreign companies.⁹¹ But broader economic reforms are also needed, notably enhancing the flexibility and performance of labor markets, improving educational and training policies and outcomes, and fostering the overall business and investment environment.

Finally, it is also essential to note that more efforts are needed in terms of data and information collection on trade and investment in services in order to generate accurate assessments and policy recommendations to maximize the contribution of FDI in services in employment and economic development.

Conclusions: Ensuring the Employment Impact of FDI in the MENA Region

This chapter has presented an overview of the impact of FDI on employment in the MENA region and policy recommendations to enhance the FDI impact on employment. Despite the significant increase in FDI inflows and robust economic growth between 2001 and 2008, MENA countries continue to suffer from long-term structural unemployment. The high unemployment rate, in particular among youth, women, and the educated, has been exacerbated by the financial crisis and the economic slowdown which followed the Arab Spring. While FDI can have a positive impact on employment, the link between FDI and employment creation is not automatic. It depends on a number of factors, including the type of investment, the objectives of foreign investors, and the sectors that are the investment target.

Limited employment creation in the MENA region can be explained in large part by an underdeveloped private sector, which was not able to absorb a rapidly expanding labor force, a workforce which lacks the necessary skills to respond to business needs, and FDI that was focused on capital-intensive sectors such as hydrocarbons. Governments can help increase the impact of FDI on jobs (in terms of volume and quality) by designing and implementing better policies in the areas of skills development, labor policy, further economic integration of women, expansion of linkage programs, and development of sectors with high employment potential.

This chapter outlined several specific policy recommendations to support governments in implementing better policies for job creation. First, proactive investment policy measures are essential, in particular the harmonization of national investment laws and progress towards a regional investment framework, which would facilitate cross-border investment, namely in services. Second, education and labor policies should address the skills mismatch between market supply and demand and introduce less rigid labor market policies. Third, proactive and innovative policies are required to unleash the female labor force potential. These include enhanced contract flexibility, equal access to social benefits, leveraging new technologies, and the promotion of international business women's networks. Additionally, fostering and strengthening business linkages between local SMEs and MNEs can help small businesses expand and generate more jobs. Finally, targeted policies to encourage investment in high growth and labor intensive sectors such as renewable energies and services can have a direct impact on employment.

In conclusion, it should also be noted that the quality of data on FDI flows and employment should be improved to develop more targeted policy recommendations maximising the impact of FDI on employment in the MENA region.

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Notes

¹ According to the definition of the World Bank, foreign direct investment is the net inflow of investment to acquire a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy other than that of the investor. It is the sum of equity capital, reinvestment of earnings, other long-term capital, and short-term capital as shown in the balance of payments. The OECD Glossary of FDI Terms and Methodology defines FDI as a category of investment that reflects the objective of establishing a lasting interest by a resident enterprise in one economy (direct investor) in an enterprise (direct investment enterprise) that is resident in an economy other than that of the direct investor. The lasting interest implies the existence of a long-term relationship between the direct investor and the direct investment enterprise and a significant degree of influence on the management of the enterprise. The direct or indirect ownership of 10 percent or more of the voting power of an enterprise resident in one economy by an investor resident in another economy is evidence of such a relationship.

² See, for example, Borensztein et al. 1998; Agosin and Mayer 2000; Driffield 2001; Görg and Strobl 2003; Colen et al. 2006; Karlsson et al. 2007. FDI can sometimes have a greater impact in developing economies as they attract important shares of green field FDI, which has a higher potential to increase productivity and produce technology transfers. However, the positive impact of FDI in developing and emerging economies could be reduced (at least in the short term) if it results in a crowding-out of local industries and increased competition.

³ This chapter focuses on government policies to strengthen the direct link between FDI and job creation. It does not cover other important specific factors related to the host economy, such as the business climate, the levels of entrepreneurship, the availability and quality of labor, etc. For an overview of policies to improve the investment environment, see OECD 2006, OECD 2010a, and OECD 2011d.

⁴ Box 2 in Chapter 2 outlines some of the reported impacts of the Arab Spring in Egypt and Tunisia, and Box 2 in Chapter 1 presents the impact on the region's competitiveness assessment.

⁵ The OECD recently announced a halt in the recovery from the global crisis, a growth deceleration in major OECD economies and weak global economic growth perspectives. OECD 2011h.

⁶ UNCTAD 1994.

⁷ OECD 2011f.

⁸ ANIMA/Invest in Med 2011a. ANIMA member countries include the Arab countries of the Mediterranean plus Turkey and Israel. They do not include Iraq, the countries of the Arab peninsula, or non-Mediterranean North African countries. ANIMA estimates are based on FDI project announcements from investors. Indirect employment is estimated based on a ratio of 3.3 indirect jobs for every direct job (average estimate of investors surveyed). In the view of the authors of this chapter, this ratio appears to be overestimated. UNCTAD has adopted a lower ratio of 1.6 based on a series of eight case studies. See UNCTAD 1994. Based on a ratio of 1.6, the number of indirect jobs created would amount to 280,000.

⁹ The large increase in 2010 is possibly due to the fact that ANIMA methodology is based on project announcements and that forecasts from investors tend to be more positive.

¹⁰ Another government source suggests that between 2008 and 2011, 61,000 direct jobs were created following the approval of 218 foreign investment projects by the National Investment Commission. Government of Morocco, "Emploi," <http://www.makassib.ma/fr/acquis-citoyens/emploi> (accessed November 2011).

¹¹ UNCTAD 1994.

¹² OECD estimates based on ILO data. The estimates indicate that 179,000 Moroccans entered the labour market in 2009 and 208,000 in 2010.

¹³ There are also a series of indirect factors that influence the impact of FDI on job creation, in particular the levels of entrepreneurship and the business environment (see endnote 3). Indeed, foreign investments can be hindered by a number of factors including red tape, corruption, unfair competitive practices, high taxes, administrative hurdles, weak institutional support, and the weight of the informal sector, among others.

¹⁴ See the definition of FDI in endnote 1.

¹⁵ Foreign Investment Promotion Agency of Tunisia, "Key Figures: Foreign Investment," http://www.investintunisia.tn/site/en/article_map.php?id_article=808 (accessed November 2011).

¹⁶ See the section on the role of hydrocarbons as an asset for some countries in the MENA region in Chapter 2 and Figure 13, Chart A, in Chapter 2.

¹⁷ Foreign Investment Promotion Agency of Tunisia, "Key Figures: Foreign Investment," http://www.investintunisia.tn/site/en/article_map.php?id_article=808 (accessed November 2011).

¹⁸ Ministry of Investment of Egypt, "Investment" www.investment.gov.eg/en/Investment (accessed November

2011).

¹⁹ OECD 2011f.

²⁰ These future job estimates are probably over-optimistic, given the current global economic downturn and the fact that the estimated total jobs created in 2009 were 24,000, only two-thirds of this estimate.

²¹ OECD 2011f.

²² OECD 2011f.

²³ This section further develops the section on employment creation presented in Chapter 2.

²⁴ Nicoletti et al. 2003.

²⁵ OECD 2010f.

²⁶ Bartelsman et al. 2004.

²⁷ Coulombe et al. 2004.

²⁸ Indeed, the share of education expenditure in GDP per capita is relatively high in MENA countries. However, given that GDP per capita is well below the OECD average (almost US\$33,000 in OECD countries, as compared with less than US\$7,000 in resource-poor MENA countries, see IMF 2011), the absolute level of effective expenditure per head in the MENA countries is low.

²⁹ OECD 2010d. For instance, Poland has strengthened financial incentives for young people to participate in training, while the Slovak Republic has adopted measures for regional schools designed to improve pupils' knowledge and skills and to bring vocational education and training closer to labor market requirements.

³⁰ The OECD's Programme for International Student Assessment (PISA) surveys have been designed to collect information about 15-year-old students in participating countries. The database includes information on student performance in three main areas of assessment—reading, mathematics and science—for nearly 400,000 students from 65 countries. To ensure representativeness, each country must provide a minimum of 5,000 students from a minimum of 150 schools is required. Each country collected its own data following international guidelines. Results of the tests in three areas are measured on a scale of 0-600. The lowest score attained among the 65 countries surveyed was 314, with one country scoring 600. The scaling is conducted so as to achieve a distribution with mean 500 and standard deviation of 100 for the 30 participating OECD countries (mathematics and reading do not average to 500 in this chart, in order to make it comparable to earlier studies). The internationally comparable information provided by PISA allows

countries to assess how well their 15-year-old students are prepared for life in a larger context and to compare their relative strengths and weaknesses.

³¹ The index is a simple average of five indices constructed using five questions from the PISA questionnaire, which are related to the degree of school exposure to business. The graph shows the existence of school and business links on a scale of 0-100 percent. While Germany and UK have very good links between schools and businesses, Qatar and Jordan score only 50 percent and 60 percent, respectively.

³² Based on OECD 2010b. The chapter on human capital is available at <http://www.oecd.org/dataoecd/63/7/46359082.pdf> (accessed on November 2011). While primary education is very important, the focus of this section is on tertiary and professional (vocational) education and policies to adapt skills to market needs.

³³ "While much of the unemployment can be attributed to economic circumstances, it seems that a major cause of the poor outcomes is the quality of the TVET system itself. The most telling criticism of the system is that TVET curricula are not sufficiently responsive to labour market needs. The reason for this can really be traced to the supply-driven nature of the system. Finance is allocated to TVET in a way that takes no account of emerging needs, or of the performance of institutions." OECD and World Bank 2010.

³⁴ OECD 2010b.

³⁵ OECD 2009d.

³⁶ The financing of the specialized work associations and special training contracts is covered by a professional training tax (taxe sur la formation professionnelle) that covers 1.6 percent of the salary mass.

³⁷ OECD 2011d. Human capital chapter available at <http://www.oecd.org/dataoecd/58/3/48218735.pdf>.

³⁸ Sweet 2009.

³⁹ Sweet 2009.

⁴⁰ UfM 2011.

⁴¹ Bauer and Hanelt 2011.

⁴² Euro-Mediterranean University (EMUNI), <http://www.emuni.si/en/>.

⁴³ Centre de Marseille pour l'Intégration en Méditerranée (CMI), <http://www.cmimarseille.org/web/base2/cmi/index.html>.

⁴⁴ OECD 2011g.

⁴⁵ The Bologna Process is an initiative by the European Union to create a European Higher Education Area

based on international cooperation and academic exchange. It is based on reforming and harmonizing educational systems and establishing comparable degrees in a three-cycle structure (bachelor-master-doctorate). The European Credit Transfer and Accumulation System (ECTS) facilitates the recognition of studies among European countries and allows for the transfer of learning experiences between institutions, greater student mobility, and more flexible routes to gain degrees. European Commission, "The Bologna Process—Towards the European Higher Education Area," http://ec.europa.eu/education/higher-education/doc1290_en.htm, and "European Credit Transfer and Accumulation Systems (ECTS)," http://ec.europa.eu/education/lifelong-learning-policy/doc48_en.htm - (accessed December 2011).

⁴⁶ The OECD has created a methodology for determining the strictness of employment protection legislation. Among a series of indicators, it analyzes the costs of hiring and firing permanent and temporary employees and the costs of collective dismissals.

⁴⁷ "It is often claimed that low labour standard countries are a location criteria for foreign investors, because they ensure a competitive advantage due to lower labour costs. This has sparked fears that there might be a "race to the bottom" on fundamental worker rights. But the empirical support for this conventional wisdom is lacking. All of the available studies find no statistically robust connection between weaker measures of workers' rights and greater inflows of foreign direct investment. Most of the variation in labour costs across countries disappears once adjusted for differences in productivity (Rodrik, 1999). In fact, more often, available research has identified that core labour standards actually help to attract FDI." OECD 2006.

⁴⁸ Zhou 2007.

⁴⁹ Zhou 2007.

⁵⁰ World Economic Forum 2010a.

⁵¹ Sufyan 2007.

⁵² See Moroccan Investment Charter of 1995, articles 17 and 18; OECD 2011f.

⁵³ OECD 2011f.

⁵⁴ OECD 2011f.

⁵⁵ For example, the United Arab Emirates, with a rate of total unemployment of 4.2 percent in 2009, experience a rate of unemployment among nationals of 14 percent. United Arab Emirates National Bureau of Statistics, November 2011. However, the UAE is a very particular example, as only 19 percent of its 5 million residents are nationals. GCC Statistics, November 2011.

⁵⁶ World Bank 2009b.

⁵⁷ A recent review of gender-related practices in the workplace in the Jordanian private sector shows that the drivers of workplace inequality include both external factors (such as the legal framework and social and cultural perceptions and pressures) and factors specific to the company (such as corporate culture and values, human resources structure, and the application of corporate social responsibility tools). Schema Tactical Thinking 2011.

⁵⁸ See OECD 2011i.

⁵⁹ UNCTAD 2011a.

⁶⁰ OECD 2006.

⁶¹ According to UNCTAD, the conservative job creation ratio of 1.6 indirect jobs per direct job, established in 1994 based on a series of case studies, is composed of 0.9 indirect jobs created through backward linkages, and 0.7 through forward linkages. See UNCTAD 1994. In other words, this ratio implies that a supplier creates about one job for every job created by a foreign investor, and that clients employ roughly two workers for every three workers hired in an FDI business.

⁶² In terms of employment, SMEs account for more than 80 percent of total jobs in the UAE and Saudi Arabia, 74 percent in Egypt, and 50 percent in Jordan. Standard Chartered Bank 2009.

⁶³ UNCTAD 2011a.

⁶⁴ UNCTAD 2011a.

⁶⁵ OECD 2009c

⁶⁶ OECD 2008.

⁶⁷ FIAS 2008.

⁶⁸ OECD 2011f.

⁶⁹ FIAS 2008.

⁷⁰ IEA 2010..

⁷¹ Egypt (12%), Syria (7%), Morocco (6%), and Lebanon (3.5%) are the most proactive countries in this regard. For the other MENA countries, the share of electricity from renewable sources is less than 2%.

⁷² Desertec Foundation 2011.

⁷³ ILO 2008c.

⁷⁴ UNEP et. al 2008

⁷⁵ Based on data from the ILO, Laborstata: <http://data.un.org/Data.aspx?d=LABORSTA&f=tableCode:2B>, accessed on November 2011.

⁷⁶ IEA 2009.

⁷⁷ IEA 2009.

⁷⁸ Energy poverty mainly affects women in the local workforce, since they are usually responsible for providing energy for the household. ILO 2009.

⁷⁹ Grameen Shakti. 2009.

⁸⁰ OECD 2007d.

⁸¹ OECD 2007d.

⁸² UNCTAD 2007

⁸³ World Bank 2010c

⁸⁴ UNCTAD Forthcoming

⁸⁵ Bottini et. al. 2011

⁸⁶ OECD 2011e.

⁸⁷ OECD 2011e.

⁸⁸ The concept of Trade Restrictiveness Index was first proposed by Anderson and Neary (1994) (as cited by Bottini et. al. 2011).

⁸⁹ Bottini et. al. 2011; Marouani and Munro 2009; Bottini and Marouani 2009; and Konan and Kim 2004.

⁹⁰ Bottini et. al. 2011

⁹¹ Bottini et. al. 2011

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The MENA-OECD Investment Programme

Established in 2005, the MENA-OECD Investment Programme supports business climate reforms in 19 economies of the Middle East and North Africa (MENA) region. The objective is to help beneficiary’s governments to design policies to modernise and strengthen the business and investment climate, using OECD tools of policy guidelines and peer reviews. The Programme also strengthens regional dialogue and partnerships of governments and businesses with a view to promoting investment, competitiveness, job creation and regional integration in the MENA region. It builds on the long-standing expertise of OECD Members and partners in a wide range of policy areas.

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