Implications for policy

This report shows that the factors holding back formal sector job growth in MENA, such as weak firm entry and exit and low productivity growth, are rooted in a policy environment that favors a few dominant market players and insulates them from competition. The various privileges that such firms capture come at a heavy cost to job creation. Few new firms enter these markets and when they do, they are excluded from these privileges and do not grow. Aggregate job creation is therefore weak, many people stay out of the labor market, or are obliged to find employment in small-scale and low productivity activities.

The roadmap to more jobs in MENA countries cannot therefore stop at a destination that includes only improved supply-side policies – education, wages, job training, and so forth. It must also encompass significant reforms to stimulate labor demand. The findings in this report point to certain critical elements of this roadmap including: (i) removing the costly policies identified in this report; (ii) promoting competition, open markets, and equal opportunities for all entrepreneurs; and (iii) most critically, ensuring that going forward, policies and the policy administration are aimed at leveling, rather than tilting the playing field. In the rest of this section we discuss these components of the roadmap; however, the specific details will depend on each country case and should include additional policy areas not covered in this report.

First, governments in MENA should reform policies that unduly constrain competition and the ability of entrepreneurs to pursue opportunities on an equal footing. A number of policies were identified in Chapter 2 that lower competition, tilt the playing field and reduce firm entry, productivity growth, and ultimately, job creation. These policies include energy subsidies to industry; exclusive license requirements to operate in specific sectors; legal barriers to FDI; trade barriers, including non-tariff measures; administrative barriers to entry and firm growth; and barriers in access to the judiciary, land, and industrial zones. Moreover, several other policies not analyzed in this report but potentially as important in maintaining a level playing field, should also be considered when dealing with specific country cases, such as barriers to firm entry and exit resulting from restrictive hiring and firing laws, cumbersome bankruptcy laws, and so forth.

Second, policymakers should ensure that state interventions that affect competition and equality of business opportunity for all entrepreneurs are enforced uniformly across firms. The implementation of laws is not consistent for all firms, even when they operate in the same sector. The predominance of not only arbitrary, but predatory decision making in the exercise of administrative discretion discourages entrepreneurship and reduces competition. The even-handed enforcement of laws and regulations demands that public officials have incentives to exercise discretion fairly and transparently, in pursuit of the legitimate aims of public policy. Such incentives are more likely to exist when laws and regulations are clear; policy implementation is simple and predictable; entry and promotions into the administration are based on merit instead of political connections; and when merit is judged on the basis of potential or actual contributions to the legitimate goals of public policy.

Third, if MENA governments want to pursue state-led development policies, they would be wise to avoid past mistakes and ensure that these new industrial policies – and the administrative structure that implements them – minimize the scope for capture, promote competition, and tightly link support to performance. Chapter 3 lists elements of industrial policy design and complementary institutional changes that appear crucial to making industrial policy work. These
include far-reaching organizational reforms in the public sector; a focus on correcting market failures and on new economic activities where market failures are more likely to have a binding influence; an evaluation system in which the performance of both policies and officials is judged by their effects on economic growth and job creation; and ensuring that all firms and potential entrants in the targeted sector have access to these specific interventions based on their performance.

**One critical aspect of this reform agenda is to create the institutions necessary to prevent future capture, thus safeguarding competition and equal opportunities to all entrepreneurs.** While several distorting policies could be removed relatively quickly given the political will, the likelihood that other existing or new policies could be captured or serve privileged firms and undermine competition and open markets is high. Faced with external pressure to reform the economy, Egypt substantially reduced import tariffs in the early 2000s. However, when one source of privilege disappeared, another emerged: tariffs declined, but non-tariff barriers dramatically increased. Chapter 4 showed that these non-tariff barriers disproportionately benefitted politically connected firms. To prevent this, policymakers need to build institutions that promote competition and prevent future capture of policies; such institutions include, but are not limited to, a strong, well-organized and highly competent public administration. A strong public administration is necessary to implement the policy changes necessary to build open markets that are resilient to the risk for capture. These policy changes include a strong competition law and an independent competition authority; appropriate procurement laws and implementation; an independent judiciary, and so forth.

**Another component, just as important, is to ensure policy making is transparent and open, with processes that allow citizens to participate.** Transparency is not a panacea, but it is hard to conceive how institutions that safeguard open markets and competition can emerge without citizen access to information on proposed and ratified laws and regulations; citizen input into policy design and evaluation; citizen knowledge of politicians’ stakes in firms that benefit from government policies; and citizen awareness of the beneficiaries of subsidies, procurement tenders, public land transactions, privatizations, and so forth.

**Last, this report points to a decision-making guide that summarizes the foregoing, which governments can use as a framework when designing and implementing policies.** It is also important when using this framework to recognize that policymaking faces risk and uncertainty as to which policies will work and achieve its objectives. The decision-making guide is aimed to maximize the likelihood of success given inherent uncertainties and maximize the positive impact of policies on growth and jobs by ensuring that they respond to real obstacles to job growth while minimizing the risk for capture.
Policy designed to produce goods and services currently not produced domestically?

Absent market failures, does country have a comparative advantage in production?

Will the policy address a clear market failure that prevents production?

Identify market failures that prevent country from exploiting its comparative advantage

Policy is likely to be inefficient and inequitable

Will all or nearly all benefits of the interventions flow to those currently excluded from the market?

Will benefits be conditioned on rigorous measures of performance?

Will the bureaucracy and courts implement policy accurately, fairly, transparently?

Policy designed to encourage those excluded from the market to participate?

Will all entrepreneurs be eligible for the policy benefits?

Policy is likely to create jobs

Yes

Yes

Yes

Yes

Yes

Yes

Yes