



MNA Knowledge and Learning

...Fast Brief



KEY CHARACTERISTICS OF EMPLOYMENT REGULATIONS IN THE MIDDLE EAST AND NORTH AFRICA

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Introduction: This Fast Brief provides a general background on the main features of labor regulations in the Middle East and North Africa (MENA) Region. This is part of an effort to understand employability constraints in MENA and to this end a World Bank team gathered information on labor legislation and other legal acts concerning labor regulations in the region. All this rendered more urgent with the ongoing social and political turmoil in the region. Within the broader scope of labor regulations, and in order to assure regional comparability, the information that was collected focused on key issues associated with commencing or terminating employment and during the period of employment (including maternity benefits). The main sources of the data are the World Bank's Doing Business 2010² and the International Labor Organization (ILO) databank³. This Brief is to provide policymakers and international organizations with a regional analysis of how labor regulation affects labor market outcomes in the region and to inform governments on strategic approaches to employment creation through labor policy and associated reforms. This activity comes as a response to regional priorities in the context of the Arab World Initiative (AWI): one of the six strategic themes of the AWI focuses explicitly on employment creation as a top priority.

Labor Market Indicators in MENA: *Labor market indicators in the Middle East and North*

Africa (MENA) region are lagging according to international benchmarks. Labor market outcomes are a primary concern for policymakers in the region. Employment rates in MENA are low by international benchmarks - 46 percent vs. a world average of 60.3 percent in 2008. This is mainly due to very low employment and labor force participation rates among women. Unemployment rates are also high, at 10 percent vs. a world average of 6 percent in 2008, largely due to high rates of unemployment among youth (new and often educated entrants to the labor market) and women. Arab Mediterranean Countries (AMCs) display a very large youth with a consequent need to create more than 1,500,000 additional jobs per year over the next 10 years in order to provide employment opportunities for new labor market entrants and to keep the (already very high) number of unemployed unchanged (Angel-Urdinola and Kuddo, 2010). Doing so will require rates of economic growth surpassing those achieved in recent years - a rather challenging task given the current global and regional economic context. Gulf Corporation Council (GCC) countries, remain highly dependent on oil-related revenues and face challenges due to migration inflows, a public sector that cannot create jobs at the pace of labor supply, and low quality job creation that is not attractive for their nationals.

Labor Regulations and Restrictions on Employment: *Labor regulation, among other factors, introduces restrictions to employability in MENA.* Data from enterprise surveys⁴ indicate that in some MENA countries labor regulation is perceived as an important constraint to business environments and therefore to

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² www.doingbusiness.com

³ www.ilo.org/travaildatabase

⁴ www.enterprisesurveys.org

employment creation. In Egypt, Lebanon, Oman, and Syria, labor regulations are perceived by firms as a major constraint. This is true to a lesser extent in Algeria, Jordan, Morocco, and West Bank and Gaza. In Egypt, according to the 2008 Investment Climate Assessment (ICA) survey, labor regulations and mandatory contributions continue to constrain many enterprises from expanding formal employment. Manufacturing firms, service firms, and hotels in Egypt report they would hire a net of 21 percent, 9 percent, and 15 percent more workers respectively if there were no restrictions to hiring and firing workers (Angel-Urdinola et al 2010). In the Lebanon 2009 ICA, almost all firms indicated that they would hire an average of more than one third of their current workforce in the absence of existing regulations and restrictions. On the other side of the spectrum, labor regulations in GCC countries are very flexible and thus not seen as an important constraint to business climate or employment creation.

Labor regulations not only protect workers' rights, but also determine, to some extent, the flexibility of the labor market. Labor legislation – broadly speaking – regulates interactions between employers, employees, and between their representative organizations: unions and employers' associations. Besides regulating employment relationships between employers and employees, labor law serves as a mechanism to establish a more conducive environment for the creation of productive employment opportunities and for the enhancement of social dialogue. International experience confirms that, among many other factors, labor regulations constitute an important cornerstone for a favorable investment climate, which in turn, is a key determinant of foreign direct investment flows and employment creation in the labor market (particularly affecting youth and women). Despite a considerable stock of literature on labor regulation and its effect on labor market outcomes, there is little systematic analysis of these topics in the MENA region.

Evolution of Labor Legislation in the MENA Region: *In many MENA countries, labor legislation is shaped by specific features of the social contract established in the post*

independence era. Each MENA country has its own history of labor law development, with differing labor market conditions and contrasting legal and social security systems. Specific core attributes of the social contract in MENA traditionally include a preference for redistribution and equity in economic and social policy; a preference for the public sector over markets in managing national economies; reliance on state planning in determining economic priorities; and an encompassing vision on the role of the state in the provision of welfare and social services. In many MENA countries, labor laws are quite dated – Bahrain 1976, Kuwait 1964, and Lebanon 1964. Increased exposure to the global market has had an impact on labor relations in the MENA region and countries such as Egypt, Syria, Morocco, Jordan, Oman, South Arabia, and West Bank Gaza have recently revised their labor codes to better adapt to international trade, enhance labor mobility, and better attract foreign direct investment.

Workers' Rights and Labor Legislation: *In most MENA countries, labor regulation constitutes a principal mechanism to protect workers' rights as collective bargaining is not widespread.* Depending on the country, trade unions in MENA whether state-controlled or independent, rarely represent workers effectively. There are exceptions, like Tunisia where unions are influential social partners. Unionized MENA countries generally have a single, often compulsory, trade-union structure. In many countries, strikes remain illegal and workers have few ways of challenging the power of the state or private employers. In this context, the role of the main labor law as safeguard for workers is much more essential than, for example, in OECD countries where the majority of workers are covered by collective arrangements. Countries with higher levels of collective bargaining generally rely on flexible employment protection legislation (EPL), thus providing a greater role for trade unions and employers associations in determining employment relations. Most MENA countries, however, are far from this concept, which partly explains why labor codes tend to include over-protective regulation, especially on the firing of workers.

Hiring and Firing: *Hiring regulations in MENA are generally aligned to international standards.* MENA countries in general do not display strict hiring regulations as compared to international standards, although some do. Most MENA countries have quite flexible arrangements in their labor laws as far as fixed term labor contracts are concerned. Many workers in MENA work overtime to earn extra income, but overtime arrangements are often abused by employers as provisions such as wage premiums for night work and overtime are often bypassed to the benefit of the employer. In terms of annual leave, regulations in most MENA countries are rather generous by international benchmarks - partly explained by the benefit packages offered to public servants. Most MENA countries offer some form of maternity protection; but benefits are not generous by international standards. An important aspect of maternity leave provisions is who bears the costs. In most MENA countries, it is the employer who has to cover direct and indirect costs. Therefore an extensive usage of such entitlements may lead to restrictions in the hiring of potential mothers. In Algeria, Iraq, and Morocco, the cost of maternity benefits are covered by the social security system. Although in such situations the employer does not bear direct costs for maternity leave, it does cause inconveniences associated with the need to find a replacement for the female worker, or to secure a workplace upon the worker's return.

Firing Regulations in MENA: *Compared to international benchmarks, firing regulations in MENA are rather strict.* Firing regulations in MENA (and especially in non-GCC countries) remain quite strict and firing costs remain high. While the termination of workers due to redundancy is legally authorized in all MENA countries, most countries have complex regulations that require notification, justification, and approval for dismissals. In some countries, employers are even required to comply with stipulated obligations to reassign and/or retrain workers after termination. Furthermore, firing costs involving notice requirements, severance payments, and penalties due when terminating a redundant

worker, are high in most countries in the region. Protective firing regulation is partially explained by the lack of unemployment insurance schemes in most MENA countries.

Compliance: *Despite protective regulation, most workers in MENA remain largely unprotected against unemployment risks.* Even though labor legislation in MENA is rigid de jure, de facto, it is widely evaded. Employment protection in many MENA countries only applies to elite workers in the public and private sectors. As such, despite the existence of rigid/protective labor laws, labor markets in MENA remain largely unregulated and thus quite flexible in practice. There are two important factors contributing to this:

(a) *Labor legislation primarily affects hired employment in the formal sector:* The typical country in MENA produces about 27 percent of its GDP and employs 67 percent of its labor force informally (Loayza and Wada, 2009). As such, the application of the labor law in many cases is limited to the civil service, public employment and a small number of private formal sector firms, many of which are multinationals. Especially in oil rich countries, the share of foreign labor - often informal and thus less protected - is particularly high.

(b) *Law enforcement remains weak in most countries:* While laws may be applied and enforced differently in different countries, in many MENA countries, legal provisions are often not complied with. Regulations designed to protect workers, such as the establishment of minimum wages and regulations for overnight work are often bypassed for the benefit of the employer. Compliance with firing regulations (such as severance payments) is limited outside the public sector as employers use various practices to avoid payments, including forcing workers to sign undated "voluntary" resignations when starting a job.

Achieving greater labor market flexibility through the non-enforcement of laws is not an optimal choice because it undermines the rule of law, exposes firms to costly uncertainty, impedes formal employment growth and leaves workers without adequate protection (Rutkowski and Scarpetta, 2005). Many MENA

countries need to develop modern Labor Inspectorates to effectively enforce core worker rights, to supervise the implementation of labor regulations and to provide technical assistance and advisory services to enterprises. Furthermore, lack of public awareness of legal rights associated with employment may also impair the enforcement of the law in a number of MENA countries. Workers need to be aware of their legal rights and should know how to enforce them.

Labor Legislation and Private Sector Employment: *At the same time, protective labor regulation in MENA (especially concerning worker's dismissal) is hindering employment creation in the private sector.* International evidence suggests that stricter employment protection legislation (EPL) (i.e. requirements/cost of hiring and firing) is associated with higher levels of informality and youth/female unemployment, as well as lower productivity and slow labor market adjustment after economic shocks. Also, strict EPL for workers in the “formal” sector has generally been shown to restrict employment growth. Many economists argue that stricter EPL leads to segmentation in the labor market between the so-called insiders (i.e. the workers with a protected job) and the outsiders (i.e. people who are either unemployed or employed with fixed-term, part-time or temporary contracts) (Angel-Urdinola and Kuddo, 2010). In the case of MENA, in addition to high firing costs and strict dismissal requirements, regulation in many countries (mainly non-GCC) include provisions in the regulation that may make it more expensive for employers to hire women, such as generous maternity protection benefits and annual leave, especially if paid directly by the employer.

Policy Implications: *Economic efficiency and worker protection could be achieved if governments set an overarching goal of “protecting the income of workers as opposed to protecting particular jobs” through, for instance, the expansion of unemployment insurance schemes. An appropriately designed unemployment insurance scheme can provide adequate protection to workers in the context of a more flexible labor market. At the same time, only a few countries in the region have*

unemployment insurance (UI) systems, namely, Algeria, Egypt, Iran, and Kuwait. Even in countries with UI systems in place – like Egypt – the system hardly exists. The factors contributing to the low utilization are a lack of public awareness about UI benefits among plan members, restrictive eligibility conditions, the difficulty of and the stigma attached to documenting a “just-cause” firing decision, and low overall lay-off risks among covered open-ended contract employees.

Reforming Labor Regulations: *Reforms in labor regulation in MENA must go hand in hand with reforms in the social protection system. Adopting a lifecycle approach to work may require shifting from a focus on protecting particular jobs to a framework of support for employment security including social support, unemployment insurance, and active measures to assist workers during periods of transition. As such, any reforms to EPL should be adopted in parallel with reforms of other social protection policies that support laid-off workers and workers in transition between jobs and other vulnerable groups to preserve social cohesion and stability. Finally, any reform in EPL should also consider the specificities of the political economy in each country, institutional capacity, fiscal constraints, and policy preferences as set in the social contract. Unions in MENA – some of which still have strong political leverage – continue to favor the status-quo as defined by the post-independence social contract, making labor reform a rather complex and far-reaching political process.*

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