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MENA Knowledge and Learning

Quick Notes Series

DISRUPTIVE TECHNOLOGY:

NEW GROWTH ENGINE FOR MENA?

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Unable to find a job as a hardware engineer, I now drive for Snapp making about $900 a month, higher than the average income in Iran, says Hossein, a Snapp (Iranian Uber) driver. With more than 5 million users and 120,000 drivers, Snapp has created thriving start-ups including goods and foods ordering and online delivery services in Iran.

Introduction. The economic outlook for the Middle East and North Africa (MENA) region is positive, and growth is expected to exceed 3% over the next two years after a sharp fall in 2017. While the growth increase offers hope, the current growth trajectory is well below potential and insufficient to absorb the hundred million young and educated people who will enter the labor market in the coming decades. In fact, of all the economic challenges facing MENA countries, the most pressing may be the continuing rise in unemployment rates for the youth and, especially, women. Recent World Bank data show that youth unemployment in MENA is above 30% and is much higher for women.

Jobless Growth. MENA economies have been experiencing moderate to high growth in GDP with stagnant growth in employment, a phenomenon of "jobless growth" since the 1970s. This dire situation in MENA is a result of the existing social contract, in which the state is the main provider of public sector jobs and social and economic benefits to citizens in exchange for limited public participation and accountability. Governments are no longer able to afford their end of the bargain, and youth frustration continues to rise. Challenges abound. While the public sector is still perceived as the major provider of job opportunities, it is failing to create enough jobs due to government fiscal constraints. The private sector remains weak and undeveloped, unable to create decent jobs for the youth. The growing number of young and educated people coming to the labor market each year means that millions of additional jobs will be needed. Data from the World Bank show that unemployment rate in MENA stands at 11% (recent available year), but the jobless rate is higher across MENA countries.

The official unemployment rate in Djibouti was 39% (in 2015), with women at 49% and rural areas

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at 59%. In Morocco, unemployment remains high among the youth (26.5%), and in Tunisia unemployment rate among university graduates increased to 31% in 2017 from 23% in 2010. Without a renewed social contract that can foster high and inclusive growth in the private sector together with governments' commitment to better transparency and accountability, many youths will still be trapped in a persistent "jobless growth" situation.

MENA's Economic Prospects. A favorable global economic environment, stability in the oil market at slightly higher prices, and resumption of construction activities in conflict-affected countries (Iraq) have helped economic growth return to the MENA region in 2018. Economic and social reforms are happening, albeit at a slow pace. Almost all countries are reducing or eliminating energy subsidies, considering increasing non-oil revenues, and taking on comprehensive social programs to shield the poor from the adverse effects of some reforms. Economic growth in MENA—which fell to 2% in 2017 from 4.3% in 2016 because of a sharp decline in economic activity among oil exporters—is expected to increase to 3.1% in 2018. The increase is broad-based; almost all countries will experience an uptick in growth this year. Stabilization policies, austerity measures, and a surge in foreign receipts are expected to lower MENA's fiscal and external imbalances in 2018 and beyond. In the short term, the outlook for MENA remains positive, and the growth rebound is expected to continue over the next two years, reaching 3.3% in 2019 and 3.2% in 2020. However, increasing geopolitical tensions, the challenges posed by the forcibly displaced people, including refugees, and the rising level of youth unemployment and public debt in the region could cloud the positive outlook.

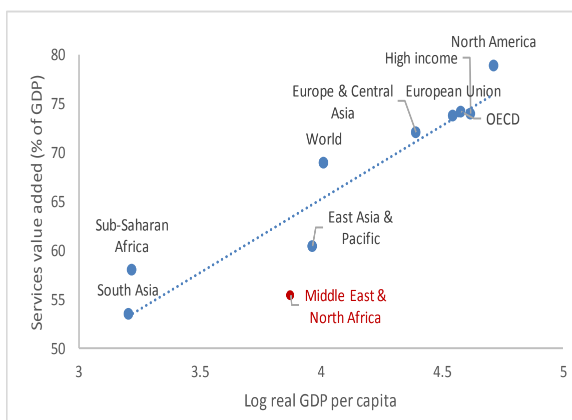
Transforming MENA's Jobless Growth Trajectory. Traditional engines of growth which were dominated by public sector and oil have proved incapable of creating sufficient jobs for the cohort of MENA's youth bulge. In fact, evidence shows that investment and growth in manufacturing that is the traditional path to diversification in developing countries has not happened in MENA.

Conversely, decades of efforts to diversify their economies away from oil have resulted in lack of diversification in the manufacturing sector, shrinking of the services sector and overdominance of oil and gas sector in the MENA region.

At about 14 percent, MENA has the world's lowest share of nonoil manufactured exports and the highest share of fuel exports—between 60 and 80 percent. Compared to the rest of the world, the region's total nonoil exports are lower than, for example, Finland's even though the region's population of above 300 million dwarfs Finland's 5 million people. MENA countries are the least integrated into the world economy and in particular among themselves. The region's 6% ratio of FDI to GDP is the world's lowest.

The growing numbers of young people—compounded by a possible increase in labor force participation, particularly among women—means that millions of additional jobs will be needed over the coming decade. With reforms started to bear fruit and economic growth expected to improve in the region, the time is ripe for MENA economies to look into the sectors (other than the public sector and oil) that can grow fast and create a massive number of jobs for the unemployed youth, at a faster rate. Studies have shown that the gap between MENA economies and fast-growing ones is the poor performance of the services sector (Figure 1).

Figure 1 Services Led Growth



Source: World Bank.

Technological advancements and rapid increases in digital technologies offer new opportunities and have the potential to boost (non-oil) private-sector-led growth. Promoting high tech jobs are crucial for creating a thriving private sector that can create decent jobs at a faster rate at least for three important reasons. Firstly, high tech jobs in developed and developing countries are more resilient to economic downturns than any other private-sector industries. A recent study finds that employment growth in tech jobs outpaced gains in other professions by a ratio of 27 to 1 between 2001 and 2011 - during the 2008 Great Recession. Secondly, estimates by McKinsey show that demand for high tech jobs will be higher than demand for other professions at least through 2020. Finally, demand from a larger digital sector could create jobs in other local goods and services sectors. This jobs multiplier effect is four times higher in the high-tech sector than the manufacturing sector. The industries that take advantage of the digital experience will have the highest productivity increases and small and medium enterprises that make better use of digital activities will grow faster (McKinsey 2016).

For each job created in the high-tech sector, approximately 4.3 jobs are created across all income groups and occupations—including teachers, lawyers, physicians, among others (McKinsey 2016). And a digital economy creates positive interlinked spillovers among economic and social sectors. E-health enables new forms of healthcare management and provision, increasing patient coverage and improving quality. E-education and online learning reach many people, even in rural areas, at low cost and good quality. Poverty reduction experiences, particularly in Bolivia and India, confirm that digital delivery can enhance inclusion and increase income among the disadvantaged.

With advances in technology, it is the right time for MENA governments to look into the "new normal" of promoting private sector-led growth through boosting high-tech jobs, particularly in the services sector. The MENA region has a fast-growing pool of university graduates and significant penetration of internet and social media, and access to smartphones. A new World Bank report, Economic Transformation argues that combining these two critical elements could serve as the foundation for a digital economy that could create much-needed private sector jobs for the young and especially for the educated over the next decade.

The State of MENA's Digital Economy: Several MENA countries have developed strategies to transform their economies and take advantage of disruptive technologies to create private sector growth and more jobs at a faster rate. But effective and better policies are needed to capture the opportunity. In Iran, E-commerce is growing fast giving rise to the emergence of local start-ups. Smartphone activity has recently risen rapidly boosting online shopping and ride sharing, thanks to Digikala (Iranian Amazon) and Snapp (Iranian Uber). According to recent estimates, Iran's ICT (Information and Communications Technology) market would reach $30 billion in 2020, up from $21 billion in 2018. Egypt's Vision 2030 foresees a competitive, balanced, and diversified economy, dependent on innovation and knowledge.

New sources of growth are emerging in fintech and innovative financing instruments in Algeria and Bahrain. Saudi Arabia's Vision 2030 seeks to raise the country's ranking in E-government, prioritizing digital transformation as one of the top four Common National Goals. The program identified five digital platforms, 29 essential digital initiatives for key sectors, and several national digital assets to receive further investment to support the government's digital transformation.

As part of the United Arab Emirates' Vision 2021, the National Innovation Strategy pinpointed digital technology as one of the top seven primary national sectors. The strategy focuses on the development of smart cities, software, and applications including advanced technology in areas of global interest such as artificial intelligence, semiconductors, nanotechnology, and 3D printing. Qatar's Vision 2030 prioritizes the creation of a knowledge-based economy characterized by innovation, entrepreneurship, excellence in education; a high-quality infrastructure; efficient delivery of public services; and transparent and accountable government.

Promoting digitalization particularly in the services sector could transform the growth path in MENA from a "jobless growth" to a "job creating" private sector-led growth that has the potential to generate massive numbers of jobs for the youth, for example through emerging start-ups. If MENA countries address the constraints to the growth in the services sector and improve digital adoption, they will not only create opportunities to move away from oil, increase new products, and boost labor productivity through skill development; they will also increase potential growth in the medium term.

The new engine of growth in MENA has important implication for the future of education, skills, and work, and on how economic policy including improving business climate and investment should be designed and implemented.

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