The IMF's Call for Inclusive Growth & How it May Affect Growth in Lebanon

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Abstract

In July 2018, the IMF presented a report promoting "inclusive growth" in the Middle East and North Africa (MENA) region and it emphasizes that inclusive growth is a modern responsibility shared by the government, private sector, as well as the society. The study divides the MENA economies into Emerging Markets (MENA EMs), MENA advanced (MENA AD), and MENA LICs (Low Income Countries), with Lebanon pertaining to the first category.

The regional findings are noteworthy because they reveal the importance of having a dual barometer to measure overall growth: an "economic growth" barometer and another measuring the improvement in "social welfare". The combination of both barometers seems to spur an inclusive, sustainable growth for the region. Similarly, this study infers and highlights key takeaways on the growth of Lebanon's economy in light of the modern findings. This allowed this report to compare national parameters on fiscal policy, refugee-influx & integration, and women participation in the labour market among others, to neighboring country-indicators and/or to the MENA EMs' averages.

Policies that promote higher "inclusive growth" can help MENA governments offset engrained inequality and stagnating incomes. The IMF report published in July 2018 and titled, "Opportunity for All: Promoting Growth and Inclusiveness in the Middle East and North Africa" attributes the region's economic weakness to the absence of "*pro-inclusive growth policies*", which basically entail "*equal opportunities to all*" - that is, irrespective of people's gender, social status, location, age. Average income per person in the MENA stagnated at a 0.8% uptick per annum from 2013-2016, which triggered income inequality. In their turn, regional conflicts, like in the Yemen, Libya, and Iraq also magnified poverty to around 26 to 51% of the population in non-advanced MENA economies. Therefore, the IMF calls the afflicted nations to set country-specific policies that integrate all stakeholders in the respective economies to create jobs and lift growth. As for the Syrian conflict, it has

hugely weighed down on Lebanon's people wellbeing, economy, and infrastructure, which may be challenging to overcome as the report will further explore.

The IMF identifies three key policy priorities for the MENA in 2018. National governments are recommended to utilize the region's untapped potential, mainly the skilled youth and side-lined women; to enhance trade activity thereby creating an internal regional market ready to compete internationally; and lastly, to empower small-to-medium enterprises or SMEs (ultimately revitalizing the private sector) which can assist the government in generating job opportunities. In fact, Lebanon's policy priorities seem to partly diverge from the above-listed as will be reflected in parameters analyzed hereafter.

The IMF's new evidence finds that higher social spending and infrastructure investments benefitting "all" can improve *uneven growth* in the MENA region. The IMF explains that the MENA region can secure citizens a better future if it capitalizes on the robust global economic recovery and scales-up reform implementation. After the 2008 global financial crisis (GFC), the global economy slowed down and countries adjusted their policies to kick-start business cycles. By 2017, global growth stood at 3.7%, the highest level recorded since 2011, and it is expected to climb up to 3.9% in 2018 and 2019 as per the IMF. Meanwhile, the MENA region's growth projected at 3.5% in 2018 and 2019 remains well below the average 5.6% recorded for the region between 2000 and 2008. The IMF however, sees the stronger global economy to be an opportunity to catalyze reform implementation to improve people's welfare and spur growth.

By the same token, Lebanon's 2018 Cedre financing seems to be a virtuous infrastructure spending that promises to nurture equitable growth. The real GDP growth rate in Lebanon averaged 9.2% between 2007 and 2010 and 1.7% between 2011 and 2017. The forecasted growth for 2018 stands at 1 to 1.5%, but it is projected to climb to 3% over the medium term, and to 5% within the next decade, owing it largely to the 2018 Cedre conference and pledge. In fact, since April 2018, it seems Lebanon has been the recipient of a notable international goodwill. The country secured a total of $11B in grants and soft loans conditional upon the implementation of reforms and dedicated largely to infrastructure projects. Such a steady and virtuous spending on infrastructure may be the primary support of economic growth in the coming period.

However, spending on social safety nets in Lebanon remains subdued which may prove resistant to pro-inclusive growth policies. It is worthy to note that social security in Lebanon remains frail and limited in scope and coverage, due to administrative inefficiencies but also due to the elevated informality rate in the labour market, given around 50% of the working age population works in informal jobs (WB, 2013) while more than 43% of Syrian refuges in Lebanon also work in the informal sector as per the ILO (2015).This leaves a substantial portion of Lebanese workers without access to formal social protection. The ILO (2015) estimates that 38% of the Lebanese population does not benefit from health insurance and more than 80% of Lebanon's elderly population aged 65+ have no pension or health coverage. As for the National Social Security Fund's (NSSF) end-of-service indemnity program for the formal private sector employees, it only covers 30% of the labour force. These

inadequacies in the social protection plans translate into rigid marginalization and exclusion of a significant share of the working and retired population in Lebanon which may require stricter growth policies.

Economic growth "shared by all" can ease social frustration and poverty among citizens, especially Arabs, while the notion remains vague in the case of Lebanon. Surveys conducted with MENA citizens revealed that 70% of citizens in the Arab World believe their governments are not putting enough effort to narrow the gap between the rich and poor. In addition, 60% admitted they are dissatisfied with the limited access to public services, including: health services, education, water, sanitation, hygiene, energy. Against this backdrop, the latest IMF study explains how economic underperformance hampers access to these basic services, which if efficiently provided, can sustainably improve livelihoods, fulfill youth aspirations, and re-boost confidence in national governments. Broadening access to public services will entail improving governance, expanding financial safety nets, and implementing policies targeting the poor and vulnerable (including women and refugees).

Nevertheless, it seems citizens' dissatisfaction in Lebanon (and Egypt alike) soar beyond 80%. This may be partly explained by the fact that Lebanon scores badly on government effectiveness and corruption indices, usually at the bottom 20% of countries. Meanwhile, people's dissatisfaction in Kuwait, Jordan, and Algeria for instance stood at the lower end of around 30%. The contrasting findings can be linked to the conflict in Syria, which largely afflicted the wellbeing of Lebanese citizens, namely those residing in the North, the Bekaa, and Baalbek – all regions that have witnessed soaring poverty rates having received the highest concentrations of refugees. As a result, 90% of the local workforce in these towns reported their incomes were slashed by 30 to 50% as per the ILO (2015).

Policies must be "*tailored to country-specific circumstances since 'one size' cannot fit all*". The MENA's countries and economies are very diverse, and Lebanon seems to also have its unique set of characteristics and dynamics. As a result, policy-actions and reform priorities diverge. However, the common trait shared among the MENA region's nations was the tight fiscal space since the aftermath of the GFC. Therefore, the IMF brings forth a suggestion to focus policy-making in the region on developing and empowering the private sector, which becomes the "*engine of job-creation*" vis-à-vis governments possessing little authority over efficient public spending. In fact, the IMF highlights that the region's key challenges are: the inadequate creation of jobs, the low contribution of the private sector, and side-lined women and youth within the labour market. In Lebanon, the private sector performance is in fact measured via an eminent indicator, the Purchasing Manager's Index (PMI), which can serve as a proper substitute to economic growth estimates when GDP data is unavailable or outdated.

Pro-inclusive growth policies can improve the region's approach to job creation. IMF evidence suggests that, "*an extra 1.7 p.p of economic growth per year (from a historical 3.8% to 5.5%) would lead to a 0.5p.p of employment growth, on average, every year, and a decrease in the unemployment rate of 6 p.p by 2030.*" Fostering job creation in the region rotates around 3 pillars: improving the business climate via SME's improved access to finance and labour laws with country-specific

considerations, reforming education of the workforce to match the needs of the private sector, and attract foreign private sector investment to foster innovation.

Less than 1 in every 2 adults works in the MENA region, given growth failed to generate jobs. "*27.5M youth from the MENA region will join the workforce over the next five years, yet they have little certainty of finding a job* [..]" even though 60% of the population is under the age of 30 and the working age population is tech-savvy and highly educated. According to the report, the MENA fails to create "*high quality, skilled jobs*" to match the educational attainment of the young labour force as informality in the labour market is dominant, jobs have a low pay, and 22% of the MENA workers make less than $3.1 PPP-adjusted per day. Hence, the IMF calls for the inclusion of youth in the labour force mainly by: reforming education to prepare them for the private sector needs in the country and recreating adequate labour regulations to prevent the price-out of any stakeholder in the economy, albeit supporting trade openness & technology-use.

However, the recommended policy-actions to include all youth in Lebanon's workforce may be particularly challenging given the elevated national unemployment rate and the Arab World's. In Lebanon, unemployment stood at an average rate of 9% from 1990 to 2010 as per the International Labour Organization (ILO). However, the rate doubled to around 18% to 20% post-2011, with the increase particularly afflicting Lebanese youth aged 15-24 years, according to the World Bank (2013) and European Commission (2016). In fact, youth unemployment (UE) in the MENA EMs is very high when compared to the UE levels in the world's emerging markets. For instance, the Arab region and Lebanon embrace the highest youth unemployment rates in the world. Youth UE in the former averages 25% and large numbers of youth are excluded from formal jobs owing it to low governance, corruption, and connections ("wasta"). In Lebanon however, youth UE touched around 22% in 2016 as per the recent IMF study v/s 24% in the world's emerging markets. Nevertheless, data from the World Bank (2013) begs to differ, stating the rate of unemployed youth in Lebanon is at 34%, i.e. 1 out of 3 is unemployed.

The MENA possesses the largest labour force participation gap in the world, yet Lebanon's female participation ranks well among MENA EMs. Women in the region's labour force are twice as likely to be unemployed (compared to men) on the back of discriminatory, institutional, cultural and religious barriers. The MENA female unemployment reaches 30% in some countries (GCCs largely). Every 1 percentage point (p.p) of growth in the region generated a rise as low as 0.25p.p. in the oil-exporting MENA nations and 0.39p.p in the oil-importing MENA states. However, in Lebanon, the participation of women in the labour force (in percent of the population above 15 years old) stood at around 24% as per the IMF study, exceeding the rates in its MENA EM peers, like Morocco, Tunisia, Jordan, Egypt, Iraq, and Iran where the rate stood at 22%, 17%, 20%, 18%, 18%, and 16%, respectively. Yet overall, the gap between female and male participation remains high in MENA EMs including Lebanon, while it narrows in MENA ADs and MENA LICs.

Reducing the gender gap in employment can double GDP growth in the region, says the IMF. The MENA unemployment rate averaged 10.6% in 2016, higher than unemployment in the emerging and

advanced economies which stood at 9.8% and 7.2%, respectively, in the same period. The rate of labour force participation increased marginally from 51.8% in 2000, to 53.6% in 2016. Nevertheless, the IMF identifies the MENA's youth as skilled and tech savvy - traits which make them eminent contributors to the labour market boosting creativity and thus competitiveness. Moreover, women's participation in the labour market remains an untapped potential. As such, reducing the gender gap in labour force participation can double growth within a decade and achieve a gain of $1 trillion in cumulative output because a more dynamic private sector can step-up the provision of economic and financial access for youth and women.

In fact, Lebanon was among the leading countries taking initiatives to reduce gender disparities and reduce female unemployment. For starters, Lebanon's female unemployment rate among the population aged 15+ stands at approx. 12%, much lower than that in its emerging peers like Algeria (around 17%), Tunisia (22%), Iran (18%), Iraq (24%), Jordan (26%), Libya (26%) & Egypt (23%). Lebanon also increased the paid maternity leave and criminalized domestic violence. Moreover, Lebanon was among four other Arab MENA states to develop national gender equality strategies, namely enhancing gender diversity.

The IMF study advocates the integration of SMEs by enhancing access to finance, while Lebanon's firms have a good credit relationship with the financial sector. Even though SMEs account for 60% of total employment in the MENA, loans-to-SMEs ratio is the lowest worldwide, constituting only 2% of GDP. Post-GFC (2010 to 2015), the inflows of FDI to the MENA contracted by 53%, in contrast to those to Latin America's and sub-Saharan Africa. Moreover, the IMF explains how more than $40B or 1.25% of GDP is needed, to meet the average of foreign direct investment (FDI) inflows to GDP in the region. Financial inclusion of SMEs can nurture growth by improving resource allocation and increasing investment in skilled human capital, thereby boosting productivity. Meanwhile, data from the IMF findings reveals that Lebanon's SMEs are more connected to the national financial sector. On that parameter, the country actually ranks better than Egypt, the West bank & Gaza, Morocco, Jordan, and Yemen. Only in Tunisia, the relation between SMEs and their creditors seems to surpass Lebanon's.

The IMF calls for greater inclusion of refugees hosted in the MENA region via comprehensive strategies. The MENA region hosts 44% or 23.7M of the world's displaced population and refugees as per the report. They usually end up residing in poor living conditions and being "*disproportionately excluded*" from opportunities in education, access to healthcare, finance, and employment. The majority of the MENA's refugees (6M) are from Syria, and these mainly resided in Lebanon and Jordan. The inclusion of these groups requires providing basic services to refugees, enhancing their integration into the educational systems, and creating employment opportunities for them which can support the economy. The IMF believes that by putting citizens and refugees on the same level playing field, national growth can be nurtured.

Nonetheless, we find this "inclusive policy of refugees" to be particularly challenging and non-applicable to Lebanon. The country currently hosts the highest per capita population of refugees in the

world. By 2015, 1 in every 4 individuals in Lebanon is a Syrian refugee as per the ILO and UNHCR (2015). The World Bank and officials estimate the total number of refugees hit 1.5M by 2017, including non-registered Syrians and more than 40,000 Palestinians from Syria. These alarming figures have already weighed down on the country's public services, education, healthcare, water, sanitation, and hygiene, and inflicted distress on the Lebanese population across the regions, especially as the competition on job opportunities is magnified. The size of Lebanon's education system alone grew by almost 50% since 2011 owing it to the refugee students who constituted 1/3 of total enrollment in education.

Lastly, fiscal policy is the governments' principal tool to push for equitable growth, says the IMF. Governments play a key role in the lives of the people as they decide on the taxation and public spending policies, both of which impact growth, incomes, and thus people's access to "opportunities". In the MENA, government spending on education, healthcare, and social safety nets constituted just 11% of GDP in 2017, compared to 14% of GDP in Latin America and 19% in Emerging Europe. As for governments' revenues, they stood at 9% of GDP in 2016, which is low compared to the 11% in LICs and 18% in EMs. Room for improvement is large in adopting an inclusive growth policy approach by re-orienting public spending towards more efficient channels. For more promising outcomes.

In Lebanon, inclusive growth and distributional objectives may be achieved through fiscal policy especially given the conditional reforms tied to the Cedre pledge of $11B. According to the IMF, if 1% of GDP spending on energy subsidies is spent on infrastructure investments, real GDP would grow by 2% and 0.5M jobs will be created within the next 6 years in the MENA. This notion may apply to Lebanon which has committed to tight reform plans following its increased public spending on infrastructure this year via the Cedre grants and soft loans. The projects expand across Lebanon's regions and they are also prioritized based on the regional and people needs. Thus, they promise to improve wellbeing when coupled with reforms to help fight corruption, boost governance, and reduce fiscal deficits.

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