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Gulf Affairs: What is the role of the IMF and how does it work with and support governments in the GCC?

Masood Ahmed: the IMF is actively engaged with the GCC countries. This engagement takes place in a number of ways. First, as with all our member countries, we travel to each of the GCC countries at least once a year to discuss the economic situation and the government's policies. This is the so-called Article IV consultation. Second, we engage with the GCC as a group. Last year, the IMF's Managing Director Christine Lagarde attended the annual meeting of the GCC Finance Ministers and Central Bank Governors in Kuwait City. IMF staff prepared a number of papers for this meeting which were published on the IMF's website. Third, we provide technical assistance to the GCC countries on topics that are at the top of the policy agenda in the region. Recent technical assistance has focused on economic statistics, macroprudential policies and financial stability, and fiscal reforms. Fourth, we provide training on economic and financial issues to government officials from the region. This mainly takes place through the IMF's regional training center for member countries of the Arab League, the Middle East Center for Economics and Finance, based in Kuwait. Finally, we organize conferences on important policy issues in collaboration with GCC

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countries. Recent conferences have been on developing domestic debt markets in the GCC, private sector growth, and the challenges of economic diversification.

Gulf Affairs: What are the three main challenges facing labor markets in the GCC states?

Ahmed: To me, there is one overarching challenge in the GCC labor markets. This challenge is to create enough well-paying and productive jobs for the young and growing population. The current favorable demographic profile of the GCC countries means there is an opportunity to boost growth and living standards if these jobs are created, but there is also the risk that unemployment will increase if they are not. The GCC countries have traditionally employed most of their nationals in the public sector, but with employment in the government already at a high level, going forward the jobs will need to be created in the private sector. Creating jobs in the private sector has not been a problem in the past, but most of these jobs have been filled by expatriates rather than nationals.

This leads me to three issues that will need to be addressed if the challenge of increasing the employment of nationals in the private sector is to be met. First, nationals will need to acquire the education and skills that are in demand in the private sector. Substantial investments are being made in education and skills development, but further efforts are needed to raise the quality of education outcomes. Second, incentives will need to change so that people opt for entrepreneurship and private sector employment over jobs in the public sector. This could be facilitated by a clear message from governments that future public sector employment opportunities will be extremely limited. Third, the wage gap between national and expatriate workers with similar skills and experience will need to be bridged to make it attractive for employers to hire nationals.

Gulf Affairs: All the Gulf states have implemented labor nationalization initiatives: Emiratization, Saudization, Kuwaitization, etc. How successful have they been in your opinion?

Ahmed: Let me focus on Saudi Arabia. The *Nitaqat* program is part of a broad labor market reform program that the government is implementing. Under the program, firms are required to employ a certain quota of Saudi nationals depending on the size of the company and the sector it is working in. In addition, wage subsidies and payroll rebates are available to companies who hire Saudis, steps have been taken to support job search activities through the *Hafiz* program and the expansion of job placement companies, efforts are underway to reduce the length of the private sector work week, and an unemployment insurance system has been introduced. These programs are all designed to encourage companies to hire more Saudis and to increase the attractiveness of private sector employment for Saudi nationals.

The employment of nationals in the private sector has certainly increased in recent years. During 2012-2014, an additional 315,000 nationals took jobs in the private sector, representing a 7.3 percent annual increase. However, over this period, the employment of nationals in the public sector has also increased by 467,000 or about 5.2 percent annually.

Gulf Affairs: How critical is economic diversification for non-oil growth and job creation for GCC nationals in the private sector? Can the growth of public sector employment for 'nationals' be contained?

Ahmed: Economic diversification is very important for the GCC countries to achieve sustainable non-oil growth and create high-paying private sector jobs for nationals.

A number of policies have been adopted to diversify the GCC economies and reduce their reliance on oil. A stable, low inflation economic environment has been achieved, the business climate has been strengthened, education has been expanded, trade and FDI liberalized, and the financial sector deepened. National development plans are being implemented with a view to boosting the human capital of nationals, and developing new industries and services that can employ high-skilled labor. GCC countries are also developing the small and medium-enterprises segment to promote entrepreneurship.

Nevertheless, to date these diversification strategies have yielded mixed results. International experience shows that, in addition to creating a stable economic environment and a favorable climate for doing business, countries that have diversified successfully focused on putting in place the incentives to encourage firms to develop export markets and to support workers in acquiring the skills and education to get jobs in these new expanding areas. Drawing on their experience suggests that GCC countries need to do much more to realign incentives for firms and workers. These steps would require a shift in the growth model, away from government expenditure as the main driver, and towards rising private sector investment and productivity.

To be sure, accomplishing this shift in the growth model and containing the growth of public sector employment will require strong political will. But, it is a key change that is needed if nationals are to be encouraged to work in the private sector and if needed fiscal adjustment is to take place.

Gulf Affairs: Labor market skills-mismatches are often highlighted as a barrier to private sector employment for nationals. Can you comment on the role of GCC education systems in preparing nationals for the job market?

Ahmed: GCC governments have appropriately increased their investment in education and skills development in recent years. Empirical research clearly shows the importance of education and skills in improving growth and productivity outcomes. Nevertheless, while the payoffs from these investments are clear in terms of the number of years of schooling children in the GCC receive, the results from internationally standardized tests in mathematics and science suggest that the quality of education is lagging behind that in many other countries. Improving educational outcomes now needs to be the focus of reforms.

Gulf Affairs: What are the implications of a protracted period of 'lower' oil prices on GCC labor markets?

Ahmed: I expect that lower oil prices will result in somewhat slower growth in the non-oil sector in the GCC as governments act to slow their spending growth. This may slow overall growth of employment in the private sector. Public employment has also reached its limits and the wage bills are already high by international standards. The task is to ensure that an increasing share of the jobs created in the private sector are filled by nationals in order to prevent an increase in unemployment among nationals.

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Gulf Affairs: According to an IMF study, “a gradual reduction in the reliance on foreign labor will also require enhancements to the macroeconomic policy toolkit.” What do you mean by this?

Ahmed: What we mean is that over many years the ready availability of expatriate labor has acted as a safety valve for the economy.

When growth is strong and the demand for labor is high, companies have been able to bring in more labor from overseas to help them increase production. This has meant that wage pressures have been contained. Our analysis shows that the availability of expatriate labor has been one factor along with the credible monetary policy that comes from the pegged exchange rates in the region that has helped the GCC countries achieve relatively low inflation. Going forward, if policies are successful in reducing the reliance of the economies on foreign labor, wages and prices may respond more to conditions in the domestic economy than they have done in the past. In turn, this may mean that monetary and exchange rate policy may also need to evolve in the future to manage demand and inflation pressures.

Gulf Affairs: How do you view current female labor force participation in the Gulf states, and how can it improve?

Ahmed: In most GCC countries, female participation rates are still too low despite some increase in recent years. Women in the GCC are well-educated and will make a significant contribution to growth and productivity in the region if they enter the workforce. Therefore, while local customs and norms need to be respected, policies that open up more sectors of the economy to female employment and support women through the provision of childcare facilities and flexible work arrangements can have high payoffs for both them and for the economies as a whole.