



Euro-Mediterranean Partnership

6th Meeting of Experts on Economic Transition (Brussels, 18-19 June 2002)

Chairman's Summary and Conclusions

The group of government experts on economic transition is an established feature of the Euro-Mediterranean Partnership. Its importance is further underlined by the fact that we are now on the verge of having Association Agreements between the EU and all Mediterranean partners in the Barcelona Process. The Euro-Mediterranean Free Trade Zone is becoming a reality. Transition policies will now take a central role in the policy agenda of the Mediterranean partners. This makes the sharing of views and experiences all the more important.

These expert meetings have proven to be of value in providing inputs to successive Ministerial Conferences; there is the ambition to do better still and to demonstrate the usefulness of these meetings in terms of providing inputs into the design of concrete economic strategies related to the implementation of the Association Agreements and Free Trade Zone in partner economies. This is an informal event, enabling participants to freely voice their opinion on key policy issues, in order to foster a better understanding of these issues and help decision makers.

This year, there were two main subjects on the agenda: the possible economic consequences of September 11 and growth and employment policy issues in the Mediterranean partner economies. The latter them included a look at EU and candidate member states' employment policies and approaches. At the end of the meeting, a web site with documents and useful links for the Euro-Mediterranean Economic Transition Network was launched (www.europa.eu.int/comm/external_relations/euromed/etn/).

1. The possible economic impact of the September 11 events

At the outbreak of the September 11 crisis, most of the world economy was already in recession and the Mediterranean partner economies were facing a structural growth deficit. The events compounded this un-supportive economic environment. The September 11 crisis was transmitted through various channels: tourism receipts, workers remittances and the transport sector. Financial markets were characterised by an initially strongly negative reaction and an equally strong rebound shortly thereafter. Emerging market bond spread indicators showed a rapid return to normalcy, apart from a slight impact of the Argentina crisis.



Impact differs however from partner to partner. Turkey seemed to be heavily affected because the September 11 shock came only a few months after a major financial crisis. Egypt was mostly affected through a strong reduction in tourism. Tunisia was already affected by a prolonged drought. Lebanon, Israel and the Palestinian Territories were less affected by the September 11 events, though the latter two suffer much more from the negative impact of the recent wave of violence. For the Maghreb countries, Jordan and Syria, the direct effects of September 11 seem to be pretty much absorbed. The negative impact on tourism has been rapidly reversed and some partners even experienced stronger growth as a result of switching consumer preferences.

Most Mediterranean partner economies responded in an encouraging way, tightening fiscal policy (reduced recurrent and delayed capital expenditures), sometimes opting for a nominal correction (exchange rates) and combined with some external financial support. It shows however that the partner economies are still quite vulnerable to shocks and need to strengthen their capacities to respond, including through more flexible and diversified economic structures.

In order to re-establish economic confidence in the region, a number of approaches can be recommended:

First, “second generation” reform policies need to be pursued vigorously: institutions for economic governance and effective competition in domestic markets, functioning of financial markets and access to international financial flows, strengthening the attractiveness for private sector investments, including in the housing sector.

Second, the Euro-Mediterranean Association Agreements can serve as a platform to re-launch confidence in the region. Their implementation could be accelerated and deepened (notably through application of the pan-Euro-Med cumulation of rules of origin, and increased regional integration) and even more emphasis on the economic transition agenda. The establishment of a monitoring system for the implementation of the Agreements would send a strong signal that implementation is taken seriously.

2. Growth and Employment

2.1. Employment issues in the Mediterranean partner economies

The task of defining appropriate labour market policies in the Mediterranean partner economies during economic transition towards a Free Trade Zone is made more difficult because of unfavourable demographic trends. Labour force growth has outpaced economic growth over the last decade and is projected to accelerate substantially over the next 10 to 15 years and some 25 million additional jobs will have to be created over that period in order to absorb this increased labour force. Fast labour force growth constitutes both an opportunity and a challenge. It may potentially increase participation rates and thereby boost per capita and household



incomes, with positive effects on overall welfare. The challenge is that this opportunity can only be realised if the increasing workforce is able to find productive employment in the economy. Job creation will thus be the key to meeting this challenge. To some extent, labour force growth can fuel employment and economic growth by itself through supply- and demand-side effects, for example in the labour-intensive housing sector. Lifting the many institutional and legal constraints that currently impede private housing development would enable private investment, employment and economic growth to take a ride on the demographic wave, and thereby contribute to the achievement of both social and economic policy objectives.

However, given the high level of structural unemployment, these self-fuelling effects are unlikely to be sufficiently strong to keep unemployment down and more active economic growth- and employment-promoting policies, including labour market reforms, may be required.

While the economic growth performance picture varies considerably by country, some general conclusions were drawn regarding the causes of slow growth at regional level. Human capital accumulation (in terms of educational attainment) has been remarkably strong. Physical capital accumulation (investment) was strong throughout the 1960s and 1970s but slowed down in the 1980s and 1990s. Since accumulation was largely driven by the public sector, fiscal constraints are a major cause for that slowdown. Total Factor Productivity growth was negative throughout the 1970s and 1980s and zero in the 1990s. Factor productivity growth is triggered mostly by structural reform measures: trade openness and enhanced competition in markets, lower transaction costs, enhancing the quality of property rights institutions, improving governance in public and private sector, etc.

One lesson that could be drawn from this economic growth performance evaluation is that the region needs more investment, to re-fuel physical capital accumulation that slowed down so much in the 1990s. However, the enabling environment for private investment remains rather weak. Another lesson therefore is that the region needs to become more attractive for (domestic and foreign) private sector investment, which brings the discussion back to measures that enhance total factor productivity growth.

Though unemployment rates in the region are high, hovering close to 20% of the labour force, this should not put partner governments in a policy dilemma and slow down reforms. Public sector employment is already at high levels and fiscal constraints leave no room for more recruitment. More adaptable labour markets and more active employment policies are needed to reinforce the role of the private sector in generating employment. As examples from partner economies showed, improved employment performance requires a comprehensive approach. In addition to devoting direct attention to improving the functioning of the labour market, it is useful to mainstream employment and labour market concerns to cover all aspects of economic and social policy.



Three conclusions have been drawn from this debate:

First, the Mediterranean partner economies share a number of typical characteristics: high labour force growth, an already high educational attainment, low labour force participation rates and high unemployment, and the public sector as a large provider of employment.

Second, several diagnoses of economic growth performance, presented at the meeting, highlighted the importance of variables such as investments, employment and total factor productivity. The latter is a measure of the efficiency of production factors in an economy. All these variables interact with each other; growth policies should not focus exclusively on one of them.

Third, and as a consequence of the second, we need to take a comprehensive approach to design policies that respond to all aspects of the employment and growth challenge in the region. Policies need to address a combination of continued macro-economic stabilisation, individual sectoral issues, enhance private sector financed investment (domestic and foreign investment, housing) and looking at the legal and regulatory environment. Within the domain of employment itself, various issues need to be addressed, including size, composition and efficiency of public sector employment, gender issues, wages and regulatory issues.

2.2. EU employment policies and Joint Assessments

To illustrate the use of labour market policies for employment promotion during economic transition periods, examples from inside the EU as well as from the EU's candidate member states in Central and Eastern Europe were discussed, including labour market reform policies in EU member states in the framework of the Lisbon Agenda for structural reform.

EU employment policy has changed, from reducing unemployment to creating employment opportunities. It focuses attention on improving employability, developing entrepreneurship and job creation, encouraging adaptability, and strengthening equal opportunities. Particular attention is paid to prevention of early retirement, increased participation and stimulation of life long learning. A right balance is sought between increased flexibility and increased security of employment, notably through investments in human capital and the quality of labour, which involves a shift from passive benefits towards an active and preventive approach. EU policies set specific performance indicators, for instance in terms of labour force participation rate targets, both for men and women, employability of job seekers, adaptability and the creation of an entrepreneurial culture, and policies aimed at particularly vulnerable groups. Some EU countries were able to trigger a substantial acceleration in employment growth as a result of reforms in the 1980s and 1990s. The cases of Spain and the Netherlands were discussed at the meeting.



There was also extensive debate about labour market policies in the transition economies of Central and Eastern Europe and how these countries managed to cope with the employment challenges induced by economic transition. While the experience of the transition economies in Central and Eastern Europe is not strictly comparable to that of the Mediterranean partners, a rapid rise in unemployment and the initial dominance of the public sector are two common characteristics. Strong labour market pressure during the initial years after the collapse of the centrally planned economies put labour market policies under considerable strain and created policy dilemmas as well. The requirements related to accession to the EU led to further employment policy changes and the so-called "Joint Assessments of Employment Priorities", between the European Commission and the candidate countries, as a policy tool in the framework of closer economic co-operation and integration. These Joint Assessments have contributed to the identification of employment policies that were better geared to the requirements of accession to the EU and the economic reforms that this entails. They have become reference documents for employment policies in these countries, and have contributed to the mainstreaming of employment concerns into a wide range of policy decisions. In fact, the Joint Assessments are part of a three-step exercise: an analysis and understanding of what is happening in terms of employment, a joint assessment of policy priorities, and an annual progress report on implementation of these priorities.

Participants reflected on the possibility of developing a similar type of Joint Assessment on Employment Policies between the Commission and the Mediterranean partners. In addition to the current high level of unemployment, establishing a free-trade zone with the EU entails a period of economic transition, which may entail dislocation and friction in labour markets, especially in the later stages of tariff dismantling when import-substitution industries will be affected. Policies should be put in place to facilitate transition and enhance adaptability in labour markets (labour legislation and regulation, vocational training, wage bargaining, taxation issues). Female labour force participation should be encouraged.

Employment issues and policies will no doubt play a major role in the successful implementation of the Association Agreements and the Free Trade Zone. Successful implementation requires that an equitable balance be found between the economic and social aspects of the Agreements. Employment policies constitute one of the major links between these two. In this respect, the EU's own experience as well as the experience of the EU's candidate member states may be of use to the Mediterranean partners. In particular, the "Joint Assessments" on employment policy issues could help to focus policy makers' minds on employment policy concerns that typically come up in economic transition. It would be useful to reflect on migration issues within the framework of Joint Assessments with the Mediterranean partners. Migration should not be seen as a substitute for domestic labour market reforms in the Mediterranean partner economies however.



3. Overall conclusions

Subjects retained for follow-up and further investigations:

Housing: At several points in the meeting, the housing sector, being one of the most labour intensive sectors with considerable potential for job creation, was mentioned. Housing development offers very significant prospects for growth in view of prevailing demographic forces and high unsatisfied demand in some countries: a young population, with fast growing working age population, will fuel demand for housing. Housing development can be made self-financing, provided the necessary institutional reforms have been put in place: real estate property should be titled, enforceable and transferable; an operational and efficient mortgage market must be put in place, which can then form the basis of a long-term credit market. It is recommended that the situation with regard to housing market institutions and policies in the region be further investigated, in view of possible more concrete action in the framework of Euro-Mediterranean co-operation to facilitate the move towards self-financing housing development.

Joint Assessments on Employment Policies: Economic transition in the Mediterranean partner economies in the wake of the implementation of the Free Trade Zone may produce transitory dislocation and tensions in labour markets. The EU's own experience, as well as that of the EU's candidate member states, demonstrates the value of in-depth analysis of employment and labour market issues and the design of active policies to facilitate transition, to ensure that the implementation of the Association Agreements contributes to improvements in the social welfare in the region. In this context, the Commission will explore the possibility to launch a few pilot Joint Assessments on Employment and Labour Market issues and policies with the Mediterranean partners. Migration will take an obvious place in these assessments, through it should not be considered as a substitute for the reform of labour markets in the Mediterranean partner economies.

Acceleration of economic growth: the causes and consequences of an economic growth deficit in the region were explored during the meeting. Participants emphasised the need to create an environment conducive to private investment in the Mediterranean partner economies, as this should be one of the most important sources of financing for economic growth. In order to make the region a more attractive destination for domestic as well as foreign investments, productivity and the rate of return on investments should increase through a sustained effort at structural reforms. Markets should become more efficient and open to competition, transaction costs should be lowered, and the governance of private property rights should be further improved. In line with the conclusions from the Reinforced Economic Dialogue meeting in October 2001, it is recommended that the Commission study, in collaboration with the Partners, institutional reforms and prepare a report for next year's Meeting of Experts on Economic Transition.



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EU financing for investments in the Mediterranean Partner economies: Several speakers at the meeting expressed their satisfaction with the establishment of a Euro-Mediterranean Investment Facility at the EIB as a step forward and possibly a step towards the establishment of a dedicated Euro-Mediterranean investment bank.

Note to this Euromed Report:

The discussions on the possible economic impact of 11 September events that took place during the meeting were based on the document *Possible economic consequences of the events of 11 September 2001: towards a Mediterranean perspective*, that was presented to the experts in advance. This document has been published in the Euromed Report issue 49.

(http://europa.eu.int/comm/external_relations/euromed/publication.htm).