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**Macroeconomic policies and
employment in Jordan:
Tackling the paradox of job-poor
growth**

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Employment
Policy
Department

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Preface

The primary goal of the ILO is to contribute, with member States, to achieve full and productive employment and decent work for all, including women and young people, a goal embedded in the ILO Declaration 2008 on *Social Justice for a Fair Globalization*, and¹ which has now been widely adopted by the international community.

In order to support member States and the social partners to reach the goal, the ILO pursues a Decent Work Agenda which comprises four interrelated areas: Respect for fundamental worker's rights and international labour standards, employment promotion, social protection and social dialogue. Explanations of this integrated approach and related challenges are contained in a number of key documents: in those explaining and elaborating the concept of decent work², in the Employment Policy Convention, 1964 (No. 122), and in the Global Employment Agenda.

The Global Employment Agenda was developed by the ILO through tripartite consensus of its Governing Body's Employment and Social Policy Committee. Since its adoption in 2003 it has been further articulated and made more operational and today it constitutes the basic framework through which the ILO pursues the objective of placing employment at the centre of economic and social policies.³

The Employment Sector is fully engaged in the implementation of the Global Employment Agenda, and is doing so through a large range of technical support and capacity building activities, advisory services and policy research. As part of its research and publications programme, the Employment Sector promotes knowledge-generation around key policy issues and topics conforming to the core elements of the Global Employment Agenda and the Decent Work Agenda. The Sector's publications consist of books, monographs, working papers, employment reports and policy briefs.⁴

The *Employment Working Papers* series is designed to disseminate the main findings of research initiatives undertaken by the various departments and programmes of the Sector. The working papers are intended to encourage exchange of ideas and to stimulate debate. The views expressed are the responsibility of the author(s) and do not necessarily represent those of the ILO.

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¹ See http://www.ilo.org/public/english/bureau/dgo/download/dg_announce_en.pdf

² See the successive Reports of the Director-General to the International Labour Conference: *Decent work* (1999); *Reducing the decent work deficit: A global challenge* (2001); *Working out of poverty* (2003).

³ See <http://www.ilo.org/gea>. And in particular: *Implementing the Global Employment Agenda: Employment strategies in support of decent work*, "Vision" document, ILO, 2006.

⁴ See <http://www.ilo.org/employment>.

Foreword

At the 99th session of the International Labour Conference, constituents endorsed the need to promote a ‘pro-employment’ macroeconomic framework. It was felt that the current framework, while making an important contribution to the goal of macroeconomic stability, paid insufficient attention to the way in which macroeconomic policy instruments either helped or hindered employment creation and poverty reduction. In the standard framework that has evolved since the days of the structural adjustment programmes of the 1980s and 1990s, and that has remained intact during the 2000s, the emphasis is on attaining key nominal targets pertaining to debts, deficits and inflation. The rationale is that attaining such targets in the medium to long run will engender a predictable macroeconomic environment that is crucial for supporting growth and hence employment creation. It now appears that macroeconomic stability is necessary, but by no means sufficient to engender inclusive, job-rich growth.

The Employment Policy Department has been endeavouring to identify existing constraints in the macroeconomic policy instruments that may hinder generation of full and productive employment, and to suggest a way forward for job-rich growth. A series of country case studies has been conducted, and the current case study of Jordan represents one result. The country case study analyzes recent macroeconomic performance, shows their relationship with employment outcomes or lack thereof, reviews the existing programmes on employment and social safety nets, and reflects the views of the ILO constituency and other key national stakeholders that were collected through interviews and consultations.

The current study analyzes the impact of recent macroeconomic policy shifts on the Jordanian labour market. One of the main lessons learned for Jordanian policymakers is that while conventional economic reforms, oriented toward stabilization programmes, may lead to some level of macroeconomic stability, they may not necessarily lead to a reduction in unemployment. Despite steady increase in real GDP growth rate in the 2000s and a surge in foreign investment, unemployment rate remains at around 12 – 15 per cent. The highest unemployment rates are recorded among women and the highly skilled. Poverty continues to affect around one-third of the population. At the same time, trade liberalization has resulted in more job destruction than job creation. Export-oriented production in the Qualifying Industrial Zones (QIZs) with the U.S. led to employment of low-cost migrant workers than creating employment opportunities for the Jordanian labour force. High unemployment rate is likely to persist, and its decline may occur only when the latent reserve of labour starts to become short. The paper identifies reduction in voluntary unemployment, which constitutes the bulk of unemployment in Jordan, as a target of policies to raise productivity and wages. The main challenge facing the Jordanian economy is to overturn the job-poor nature of the economic growth strategy. In this regard, the paper suggests adjustments to a set of macroeconomic and structural policy measures, to ensure better employment opportunities, conditions of work and pay.

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1. Introduction

The current study analyzes the impact of recent macroeconomic policy shifts on the Jordanian labour market. The aim is to assess the extent to which the macroeconomic efforts of the last two decades have resulted in generation of productive and decent employment among the Jordanian labour force. It will demonstrate that Jordan has suffered from a jobless growth strategy, whereby economic growth and employment generation have not resulted in increased employment among Jordanians. The nature of the challenges facing the Jordanian labour market and the recent years' macroeconomic growth strategies call for key structural shifts in economic policies in order to generate better quality and more decent employment opportunities for the national labour force.

These structural shifts will influence the nature and composition of growth across the economy, making it more employment-intensive and, possibly, more pro-poor. An in-depth understanding of the real challenges facing the Jordanian labour market and their source is of utmost importance to the generation of productive and decent employment opportunities. It is only in such context that a role can be defined for macroeconomic policies in reducing Jordan's consistently high levels of unemployment. The 2008-09 global economic downturn reinforced the need to rethink macroeconomic objectives and policies *combined with* a new set of structural policies, which could maximize the employment potentials of each macroeconomic policy shift.

Jordan is a small, lower middle-income country, with a relatively open economy. It has experienced an accelerated pace of economic change brought about by global economic integration and liberalization policies. The 1990s marked the dominance of macroeconomic and trade liberalization in the Jordanian economy, leading to increasing levels of GDP growth and a much-idealized macroeconomic stability as manifested in low inflation, a stable currency, and a real GDP growth in excess of 8 percent by 2005. In a short time, Jordan entered into an Association Agreement with the European Union, signed a Free Trade Agreement with the United States and successfully joined the World Trade Organization.

However, despite these trends, high rates of unemployment and poverty continue to persist in the country. Unemployment remains at around 12-15 percent, with the highest unemployment rates recorded among women and the highly skilled. Meanwhile, poverty was still affecting 13.3 per cent of the population in 2008. It is suggested here that this arises from the inability of the growth strategy to address some of the key challenges facing the Jordanian labour market. These challenges are a result of the nature of Jordanian economic growth as well as its geopolitical position. Among them are, first, high levels of immigrant labour flows to Jordan that have fundamentally changed the composition of the labour market. Migrant workers constitute on average 20 percent of the Jordanian labour force. According to official statistics, between 2001 and 2005 there were approximately 300,000 migrant workers in Jordan filling 62.8 percent of the newly created jobs. By 2009, the number of migrant workers had risen to 335,708 (Al Manar, 2010a). This has increased unemployment, while pushing the wages down, making employment opportunities less attractive to those 'inactive' members of the labour force.

The second challenge facing the Jordanian labour market is the insufficient number of jobs created. The liberalization of the economy during the course of the 1990s resulted in more job destruction than job creation. Privatization of firms resulted in a large number of small private enterprises with limited employment-generation capacities. The nature of export-oriented production, for example in the Qualifying Industrial Zones (QIZs), has implied more unskilled jobs for migrant workers. Hence, the jobs created by exports have not exceeded the number of jobs that have been lost due to imports.

The third challenge is the quality of jobs, which are available in the market. There is a clear mismatch between the skills of the young and highly educated Jordanians and the jobs, which are available in the market. This, to a large extent, questions the composition of growth and the nature of jobs, which have resulted from this growth in recent years.

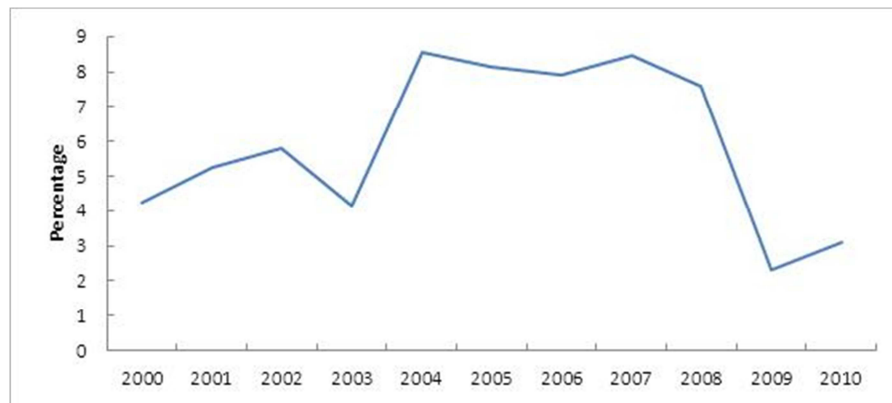
Finally, lack of viable, productive and decent employment at home has led many highly skilled Jordanians to seek employment abroad, with long-term implications for the economy's human capital. The recent global economic crisis has only aggravated these pre-existing features of the Jordanian labour market. Hence, what is required in order to alleviate the unemployment bottlenecks is not a set of policy responses to the crisis *per se* but instead a set of structural changes in all spheres of macroeconomic, trade and labour policies in order to maximize the creation of productive employment opportunities for Jordanians.

In order to explore the above themes in detail, the current study will first present a brief account of the recent developments in the Jordanian economy. This is followed by a discussion of the challenges facing the Jordanian labour market. The study will then analyze the recent macroeconomic policies in Jordan and their impact on the labour market, highlighting the insufficiency of macroeconomic policies in Jordan to generate productive and decent employment opportunities and the need for structural policies in all socio-economic spheres aimed at removing the obstacles to generation of full, productive and decent employment. The study will conclude with a set of broad policy recommendations to this effect.

2. The Jordanian economy: recent trends

Recent years have brought about major changes to the structure of the Jordanian economy, originating from regional political and economic turmoil, the introduction of IMF-led stabilization programmes, and finally, the global economic crisis of 2008-09. In terms of investment and GDP, the Jordanian economy has performed well in recent years. Private foreign investment has increased dramatically since 2001, triggered by soaring oil profits in the Gulf countries and the immigration of wealthy Iraqis in recent years. Annual GDP growth increased from 3.5 percent during 1996-2000 to 6 percent during 2000-05 (World Bank, 2008:2).

Figure 1. GDP, Constant (percentage change)



Source: Central bank of Jordan, 2010.

However, evidence suggests that growth has not translated into a diversified economic structure and a reduction of unemployment and poverty rates. In recent years, Jordan has particularly focused on growth of its external sector, through an export-led strategy, an Association Agreement with the European Union, a Free Trade Agreement with the US and membership of the World Trade Organization. Although these have resulted in high levels of exports, they have failed to produce sufficient and decent jobs and have exposed the economy to the fluctuating waves of international finance and commerce.

Close economic and trade ties with the region, with half of Jordan's exports and a quarter of its imports taking place with its neighbours, has made the economy vulnerable also to regional economic and political fluctuations. This vulnerability to external factors is reinforced by Jordan's traditional reliance on external sources of finance, such as worker remittances and foreign aid – something, which limits the government's policy space when it comes to macroeconomic planning.

In response to the late-1980s' economic collapse in the wake of a severe debt crisis, which resulted in a decline in remittances and aid and exports to the region, Jordan accepted an International Monetary Fund (IMF) adjustment package, which included a devaluation of the *Jordanian Dinar* (JD) by 50 percent, as well as substantial removal of government subsidies. The programmes initially failed to stabilize the economy, leading to a currency and banking crisis as a result of the radical nature of the capital account and exchange rate regime liberalization advocated by the IMF. This rapid pace of liberalization, together with a host of political uncertainties related to Jordan's relationship with the West Bank, undermined investors' confidence and resulted in increased capital flight (El-Said et al., 2006). Within a year, the currency had depreciated by 50 percent and the banking sector was experiencing a crisis. In 1989, the economy contracted by 13.5 percent.

The subsequent decline in the role of the state in the economy, in line with a tight monetary and fiscal policy prescription, had a particularly dire effect on the agricultural

sector, where input subsidies were removed without any public sector investment in the sector. Together with only around 6 percent arable land and one of the lowest water availability rates in the world, Jordan's reliance on the agricultural sector as a source of output as well as input for the industrial sector has been very limited. As a result, in 2000, agriculture constituted only around 3.8 percent of GDP, whereas services (including finance, real estate, transport, communications and government services) and industry (including mining and quarrying) constituted 70.4 percent and 25.8 percent of GDP, respectively. This shift in economic activity has been reflected in the composition of employment, as shown in the table below. As the table suggests, employment in the agricultural sector has declined by more than 44 percent, whereas it has experienced major increases of over 180 percent and 100 percent in the real estate and health and social work sectors, respectively (Al Manar, 2010b).

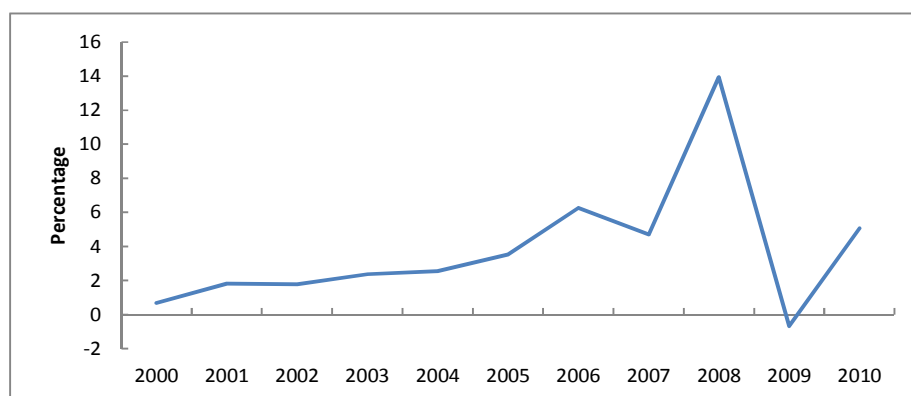
Table 1. Employment of Jordanians by Economic Activity 1995 and 2006 (excluding the Armed Forces)

<i>Economic activity</i>	<i>Employment (000)</i>		<i>Change in employment 1995-2006 (%)</i>	<i>Employment share (%) in</i>	
	<i>1995</i>	<i>2006</i>		<i>1995</i>	<i>2006</i>
Agriculture	49.5	27.6	-44.2	7.2	2.9
Mining & Quarrying	7.8	6.1	-21.8	1.1	0.6
Manufacturing	96.0	114.2	19.0	13.9	12.0
Electric, Gas and Water Supply	13.4	14.2	6.0	1.9	1.5
Construction	55.0	60.9	10.7	8.0	6.4
Wholesale and Retail Trade	116.4	179.1	53.9	16.9	18.8
Hotels and Restaurants	12.4	23.8	91.9	1.8	2.5
Transportation	79.8	98.6	23.6	11.6	10.3
Financial Intermediation	16.2	21.5	32.7	2.4	2.3
Real Estate, Renting and Business Activities	18.4	52.2	183.7	2.7	5.5
Public Administration and Compulsory Social Security	67.8	83.8	23.6	9.8	8.8
Education	93.6	154.8	65.4	13.6	16.2
Health and Social Work	27.2	54.8	101.5	3.9	5.7
Other Community, Social & Personal Services	35.6	62.5	75.6	5.2	6.6
TOTAL EMPLOYMENT	689.1	954.1	38.5	100.0	100.0

Source: Al Manar, 2010b.

Although the reforms resulted in a decline in the fiscal deficit, inflation, and currency fluctuations, in later years they failed to lead to a full economic recovery, leaving the per capita incomes stagnant. In terms of 'stabilization', inflation was kept well below 5 percent between 2000 and 2005, since then inflation has increased, spiking at 13.9 percent in 2008. In 2010, inflation hovered at around 5 percent.

Figure 2. Inflation (percentage change)



Source: Central Bank of Jordan, 2010.

With an exchange rate fixed to the U.S. dollar since 1995, the Jordanian Dinar has shown signs of stability for much of the ensuing period. However, the decline in the value of the US dollar during the 2008-09 global economic crisis raises worrying questions about the long-term consequences, particularly for the current and capital accounts, of this close association with the dollar. Real GDP growth has shown a relatively upward trend in recent years, rising from 4.1 percent in 2003 to 8.6 percent in 2004 and remaining between 7.6 and 8.6 until 2008. In 2009, real GDP growth decelerated, notably, to 2.3 percent per year. However, tight monetary policy, a small domestic market, and vulnerability to regional instability have all discouraged domestic investment in the economy, leaving the government with high levels of debt, which reached 105 percent of GDP in 2000.

External debt constituted 84 percent of GDP in the same year. By 2010, net outstanding domestic public debt stood at 34.5 percent of GDP and external public debt constituted around 23 percent of GDP, leaving net public debt at around 57 percent of GDP. Labour productivity in this period fell to very low levels (Central Bank of Jordan, 2011:36). World Bank studies show that most of Jordan's growth during the 1990s and early 2000s was originated from expansion of capital and labour, inflow of migrant workers and high levels of foreign assistance, and *not* due to higher productivity. This highlights the limited progress in Jordan's economic competitiveness, leaving unemployment and poverty as its major socio-economic problems (World Bank, 2008).

The impact of the global financial crisis on the Jordanian economy came with some delay, as Jordan is not a major global investor and not an oil-producing country. Hence, the country avoided entering a recession after 2008, although real GDP growth fell from 7.5 percent in 2008 to a mere 2.5 percent in 2009 (ILO, 2010). The initial impact of the crisis was somewhat mitigated due to some of the stabilization policies adopted by the Jordanian government in recent years: for example, the Central Bank of Jordan's efforts aimed at stabilizing the banking and monetary systems.⁵ Although the IMF stated that, 'the Jordanian economy has proved resilient to the global economic downturn, thanks to sound economic management and prudent supervision of the kingdom's financial sector', the impact of the crisis was gradually felt by the economy, particularly through its impact on the remittances, access to regional grants and investment opportunities (Dimou, 2010).

Although the oil price boom of 2002-08 increased the remittance flows, revenues from tourism and regional development assistance, it also led to a higher import bill due to a heavy reliance on imports of oil and gas, which reach up to 23 percent of GDP. As a result, Jordan initially benefited from lower commodity and fuel prices following the global financial crisis. The lower oil prices resulted in a saving of 10 percent of the country's GDP in 2009 (Brach and Loewe, 2010). However, soon the structure of the economy revealed its vulnerability to the regional and global economic slowdown. As a major recipient of external financing in the form of remittances, regional and foreign assistance, and loans, the decline in economic activity of the regional oil-exporting countries started to have an effect on the inflow of these external resource flows to Jordan. According to the Arab Labour Organization estimates, the economic crisis resulted in an overall 19 percent decline in employment opportunities across the Arab world in 2009, possibly creating a 30 percent decline in demand for Arab labour in the Gulf countries (GMG, 2010). The return of many

⁵ For example, via measures such as setting 12 percent as a percentage for capital adequacy (as opposed to the standard rate of 7 percent), which protected the banks from many financial problems and the possibility of bankruptcy. In addition, following the global financial crisis, all banks were requested to disclose all their toxic papers in order to monitor any potentially growing problems in the banking system. These papers amounted to USD 40 million, which is small compared to the USD 1 billion profits of these banks in 2008 (See Dimou, 2010).

Jordanian workers from the Gulf countries, following the decline in economic activity, together with the influx of more than a million Iraqi refugees in recent years, and high levels of land speculation resulted in a 10 percent decline in the levels of remittances in 2009, high levels of unemployment and over-investment in real estate. Between 2008 and 2009, the number of Jordanian companies who filed with the Ministry of Labour (MoL) for mass layoffs tripled from 13 to 32 (ILO, 2010). By 2009, foreign aid alone had dropped by 87.8 percent. The fall in real GDP growth was mainly due to weaker activity in finance, manufacturing, and trade sectors. While an increase in capital spending – to support domestic activity – was largely offset by lower commodity subsidies, a cyclical weakening in domestic revenues and a dramatic downturn in external grants induced a widening of the overall deficit by more than 3 percentage points of GDP, reaching 8.5 percent of GDP in 2009. As a result, the debt-to-GDP ratio rose to about 56 percent by the end of 2009 (Brach and Loewe, 2010).

According to more recent data from the Department of Statistics (DOS), the growth of the national economy showed a positive trend in 2010, thanks to the improvements in regional and global conditions and the growth of services and export-oriented sectors. At a sectoral level, some sectors witnessed a marked improvement, particularly mining and quarrying, which picked up strongly, recording a real growth rate of 24.4 percent compared to a contraction amounting to 24 percent a year earlier. Transport and communications, trade, restaurants and hotels and finance, insurance, real estate and business services also witnessed major growth improvements. In contrast, the construction sector experienced a noticeable contraction amounting to 6.7 percent compared to a growth rate of 13.5 percent a year earlier (Central Bank of Jordan, 2011).

In order to minimize the negative effects of the above trends on the labour market and to protect workers against the adverse consequences of the economic instabilities, it is crucial for the post-crisis macroeconomic policies to be formulated in close coordination with labour market policies. Jordan's Executive Development Program (EDP) for 2011-13 has set employment creation as one of its top priorities, aimed at 'stimulating economic growth, increasing the welfare of Jordanians by reducing poverty and creating jobs through sustained and broadly shared growth, while achieving fiscal sustainability and external balance through boosting investments and enhancing exports'.

Although the EDP places much emphasis on 'maintaining fiscal and monetary stability', it does so by highlighting the role of 'increasing self-reliance' in achieving such objective – a welcomed policy tone, which points towards creation of domestic sources of growth and economic stability, which are likely to result in more sustainable job creation opportunities. The EDP further emphasizes 'developing the public sector and human resources and increasing their productivity' while 'synchronizing education with labour market requirements' (Ministry of Planning and International Cooperation, 2010a). All of these point towards the government's realization and recognition of the need to focus on improving the state of the labour market through increasing reliance on domestic sources of growth.

The 'Arab Spring' factor

The 'Arab Spring' has posed yet a new challenge to Jordan's volatile macroeconomic and employment structures. Political unrest across the Arab world since late 2010 has pushed Jordan to dramatically increase government spending on public sector salaries, food (USD 550 million) and energy subsidies and the social safety network, in an effort to avoid domestic protests by improving the situation of the country's poor and unemployed. The initial round of extra government spending was expanded in August 2011 by an additional JD 584 million for social welfare payments and food subsidies. Hence, in 2011 government spending exceeded its original JD 6.95 billion by over JD 700 million, raising the estimates of the budget deficit from 5.5 percent to nearly 7 percent of the GDP. A further blow to state finances came from a record energy bill that is expected to top USD 4.5 billion after

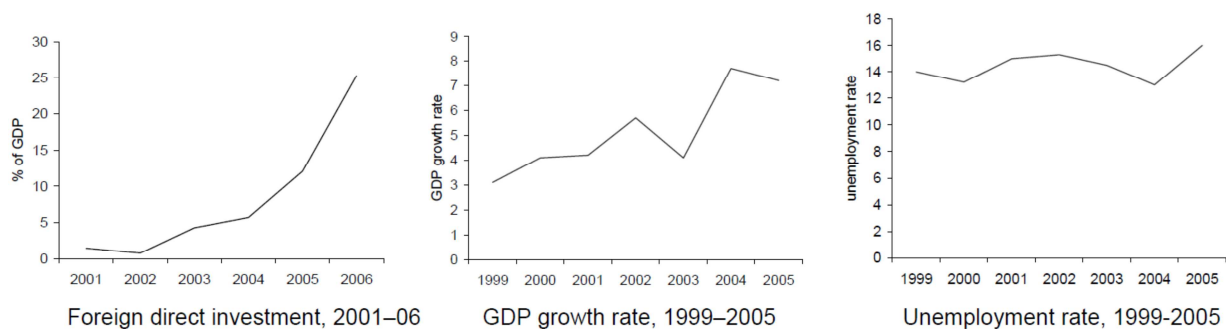
the disruption of Egyptian gas supplies to Jordan due to sabotage of the pipeline in the Sinai region following the political unrests in Egypt in early 2011. As a result, the kingdom was forced to switch to more expensive diesel fuel to generate electricity. Together with the debt incurred by the national electric power company, the government debt levels this autumn went beyond the legal limit set by Jordan of 60 percent, according to the finance ministry.

Still struggling to recover from the global financial crisis of 2008-09, the economy of Jordan is expected to grow at around 3 percent in 2011, much slower than the average 7 percent seen over the last decade. In mid-2011, the government attempted to finance the growing deficit through getting funds from the central bank, a move that raised much criticism from those fearing the jeopardy of the CBJ's independence. The USD 1.44 billion in foreign grants received by the kingdom in 2011, following a dip in foreign aid during the global financial crisis, has contributed greatly to covering the increased public expenditure, ensuring that the 2011 budget deficit target of JD 1.160 billion or 5.5 percent of GDP is met.

3. Labour market and employment in Jordan

In Jordan around 180,000 Jordanians were unemployed in 2009; at the same time, more than 335,000 non-Jordanians were working in the kingdom during the same year. These numbers highlight a critical paradox in the country's labour market: while demand for labour is high, most job vacancies are filled by migrant workers or remain unfilled, leaving many Jordanians unemployed over long periods of time. Existence of such deep structural problems in the labour market implies that economic growth *per se* will not be sufficient to reduce the levels of unemployment. It also explains to some extent why GDP and foreign direct investment (FDI) growth in recent years has not resulted in lower unemployment, as shown in the figure below. The government's strategy in recent years has been to attract foreign investment and generate growth to create 46,000 additional jobs per year, with the expectation that this will reduce unemployment to 6.8 percent by 2017 (World Bank, 2008:2). Indeed, in line with the government's unemployment reduction strategy, GDP growth has generated a substantial number of new jobs: from 2000 to 2005, the Jordanian economy created between 24,000 and 44,000 additional jobs per year. However, unemployment did not decline but fluctuated around a fairly high level of 14 percent. This is despite the low ratio of labour force to population, which is a product of the large pre-working age population as well as low levels of female participation. In recent years, more than half of new jobs created in the economy have been filled by migrant workers.

Figure 3. Paradox: Strong investment and GDP growth, but high unemployment



Source: World Bank, 2008:i.

High rates of population growth have resulted in a labour force growth rate of about 4 to 5 percent annually, with more than 50,000 entrants to the labour market each year, resulting in unemployment rates ranging from 12 to 16 percent. Statistics show that in 2009, of the total number of unemployed, more than 58 percent were below the age of 29 (Al Manar, 2010). Unemployment is particularly high among the educated youth and women. Despite the government's extensive and subsidised health and education programme, its lack of targeting has resulted in a segmented labour market characterized by high unemployment amongst the highly educated. More than 80 percent of the unemployed men are educated at the secondary level and above, and as much as 75 percent of the unemployed women have an intermediate and university level education (Al Manar, 2010). Moreover, despite measures such as compulsory education through grade 10 and stricter child labour laws, women's participation in economic activities is still far below that of men. They also face higher unemployment and lower wages, resulting in high female employment in the informal economy.

It is worth mentioning that the severity of the unemployment problem in Jordan is to some extent disguised by the low labour force participation rate of women with less than higher education. Jordan has one of the lowest labour force participation rates of those above 15 in the world: 64 percent for males and 14 percent for females. The female participation rate declines even further when it comes to females with less than higher

education – something which could be due to a host of factors, particularly the very low wages on offer in the private sector resulting from the excess supply of labour (ILO, 2010). This implies that, even if the rate of job creation accelerates, the present high rates of unemployment are likely to persist given the current quality and wage structure of the labour market. If labour demand increases, any improvement in working conditions, most especially rates of pay, is likely to generate an increase in labour supply, as those previously economically inactive find the rewards of employment more attractive. As a consequence, unemployment rates will decline slowly, if at all, until the latent reserve of labour is exhausted. To this should be added a further challenge, which relates to the construction sector, which has been the driving force behind much of recent economic growth in Jordan. The construction sector is typically the most volatile major sector of any economy. Propelled by investments from remittances, the wealth of Iraqi immigrants and other factors, the construction sector has been a force for growth. However, the activity in the sector is bound to slow down in the near future, leading to a large-scale loss of jobs.

Hence, a continuation of the government's macroeconomic and labour policies in the future will perhaps lead to further growth in terms of GDP and investment, and even jobs, but may not lead to reduction of unemployment. In this context, the government's macroeconomic policies need to be formulated carefully in coordination with the employment priorities of the labour market in order to meet the demands of the Jordanian labour force.

Below, we highlight some of the major structural features of the Jordanian labour market, which need to be taken into account carefully when devising macroeconomic policies with the aim of reducing unemployment. These include the job destruction caused by the recent wave of economic liberalization and stabilization programmes; the significant share of migrant workers; high levels of emigration of Jordanian labour; low quality of jobs available in the market and infrastructure; and the expansion of the employment in the informal economy.

Job destruction after liberalisation

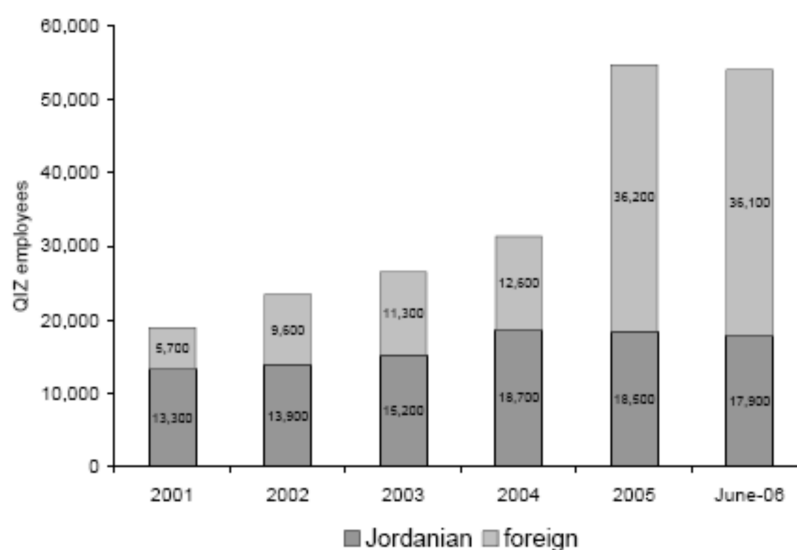
Various elements of Jordan's macroeconomic stabilization policies of the last two decades have resulted in higher levels of job destruction than job creation. One of these factors has been Jordan's drive towards fiscal consolidation and privatization. The public sector has been traditionally one of the largest employers in the Jordanian labour market. The relatively higher wages, social protection entitlements and lack of viable private sector employment opportunity has for long made the public sector a favoured choice of the new entrants to the labour market, particularly women. Female applicants for public sector forces reached 64 percent of the total in 2003. However, a reduction in the size of the government civil servant wage bill and a move towards privatization has been among the major economic 'reforms' of recent years. Jordan's rate of privatization has been faster than many regional economies, helped by its trade agreements with the US and Europe, yet the nature of this privatization process has not been employment-friendly.

Another factor, which has resulted in high levels of job destruction in recent years, is the nature of government's investment and trade strategies. Economic liberalization and export promotion in Jordan has particularly focused on low manufacturing sectors, such as apparel manufacturing, that offer poor working conditions, making them less attractive to domestic workers. The sudden and unprotected inflow of cheaper imports has undermined many domestic producers, pushing them out of business or directly affecting the employment and wages of their workers. Jordan's Qualifying Industrial Zones (QIZs) with the US are another element of Jordan's trade and investment policy that though attracting high levels of investment, have had devastating consequences for employment of nationals. To be eligible for free access to the U.S. market, products from the QIZs have to have at least 8 percent Israeli content, 11.7 percent Jordanian content, and a total content from

Israel, Jordan, West Bank and Gaza, and/or the United States of at least 35 percent (Nazzal, 2005).

Though many have argued that QIZs have resulted in more jobs and higher foreign exchange reserves due to higher exports, the real impact of the QIZs on the Jordanian economy should be assessed on the basis of wages paid and on increases in *domestic* investment through spillover effects and re-investment of the profits in the Jordanian economy. Figures from the Jordan Investment Board (JIB) show that 88 percent of capital invested in the QIZs is from foreign firms. In addition, more than half of the workers in QIZs are migrant workers (see Figure 4 below). Amongst the Jordanian workers, the majority are women who are paid lower wages. Finally, most of the goods produced in these trade zones are low level manufacturing products such as low cost clothing destined for the American market, which have low value-added and hardly represent a real diversification of Jordan's productive structure. In a drive to reduce the costs of production, wages and working conditions are being depressed in these trade zones, resulting in higher employment of migrant workers who are willing to accept such conditions. The decline in real wages in Jordan in recent years is an indication of the impact of migrant workers in turning Jordan's labour-surplus economy into a low-skilled, low productivity, low wage equilibrium. This in turn requires a combined macroeconomic and labour policy effort aimed at generating high value added jobs with wages in line with expectations of the Jordanians. This would be also important in order to attract the large number of skilled Jordanian labour force currently working abroad.

Figure 4. Employment in QIZs, 2001–06



Source: World Bank, 2008:34.

Though many have argued that QIZs have resulted in more jobs and higher foreign exchange reserves due to higher exports, the real impact of the QIZs on the Jordanian economy should be assessed on the basis of wages paid and on increases in *domestic* investment through spill over effects and re-investment of the profits in the Jordanian economy. Figures from the Jordan Investment Board (JIB) show that 88 percent of capital invested in the QIZs is from foreign firms. In addition, more than half of the workers in QIZs are migrant workers (see figure 4 below). Amongst the Jordanian workers, the majority are women who are paid lower wages. Finally, most of the goods produced in these trade zones are low level manufacturing products such as low cost clothing destined for the American market, which have low value-added and hardly represent a real diversification of Jordan's productive structure. In a drive to reduce the costs of production, wages and working conditions are being depressed in these trade zones, resulting in higher employment of migrant workers who are willing to accept such conditions

Quality of jobs

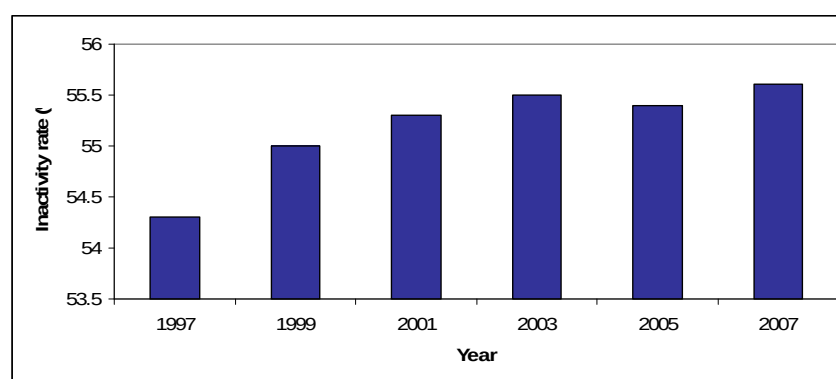
The growth of the Jordanian economy has been concentrated in sectors, which do not offer 'high quality' jobs to the educated Jordanian labour force. In other words, there is a mismatch between the labour market demand and the skills and educational backgrounds of the workers. The young, mostly educated Jordanians, do not show any interest in adopting the low-skilled, manual jobs offered by the mining manufacturers or the QIZs, as these not only have no association with their subject of study but are also low-paid, offer poor working conditions and lack social security. According to official statistics, only 42 percent of the labour force in Jordan is covered by the social security system. The surge in the rate of inflation in recent years has further dampened the already low wages, which dominate in these sectors, making them even more unattractive to the skilled labour force.

Jordanian workers' refusal to accept low-wage employment is often attributed to their high 'expectations' about their employment prospects and earning potential. However, as argued below, rather than being a matter of unrealistic 'expectations', this highlights the mismatch between the high levels of education, training and experience of the labour force and the prevailing low wages on offer in the economy. Evidence shows that Jordanians would be ready to accept even unpleasant jobs if they paid well enough (World Bank, 2008). This phenomenon has led to high levels of 'voluntary unemployment' – something, which cannot be easily reduced by boosting investment and GDP. A survey conducted by the University of Jordan's Center for Strategic Studies shows that around 54 percent of the unemployed fall in the category of the 'voluntarily unemployed' (World Bank, 2008:17).⁶ An increase in economic growth may lead to a partial reduction in the number of those 'involuntarily' unemployed, but is insufficient to reduce 'voluntary' unemployment. The jobs that have been created in the QIZs, which are characterized by low pay and offer poor working conditions, have gone to migrant workers who are willing to accept them. Hence, in its policies, the government needs to distinguish between these two groups of unemployed and target specific policies aimed at raising the productivity and wages of employment opportunities in order to attract the voluntarily unemployed, who constitute the bulk of the unemployment pool in Jordan. This in return requires further diversification of the economy and increase in the productivity and competitiveness of the employment-intensive sectors to ensure better employment conditions and pay.

One of the consequences of the low quality of available jobs in the economy is the high rate of 'inactivity' in the labour market. According to its official definition, individuals are considered to be outside the labour force, or 'inactive', if they are neither employed nor unemployed, that is, not actively seeking work. Figure 5 shows the high rate of economic inactivity in Jordan. The latest figures show that as of 2011, 'there are around 3.5 million people aged between 16 and 64 who are eligible for work, out of them 1.4 million are economically active and 2.1 million are inactive, 30 percent of them are students' (Obeidat, 2011). This highlights lack of decent and productive employment opportunities, which could encourage Jordanians to seek employment.

⁶ When unemployed Jordanian workers were asked about their willingness to accept jobs from a list of widely available jobs at prevailing wages, about 46 percent of respondents indicated a willingness to accept at least one of the jobs. The other 54 percent of unemployed Jordanians want to work, but not at available jobs – unless the pay were significantly more than presently offered. The attraction of civil service jobs and income support from family members (more than three in four unemployed Jordanians (76 percent) live with their parents and only one in four belongs to the lowest expenditure quintile, and significant numbers of unemployed individuals belong to Jordan's wealthiest families) are two factors which allow them this choice (World Bank, 2008).

Figure 5. Inactivity Rates in Jordan, 1997-2007



Source: Saif, 2009:15

The low quality and attractiveness of jobs offered in the Jordanian labour market are further demonstrated through the large number of the ‘working poor’, which refers to those who work for under USD 2 a day. In the case of Jordan, 7.5 percent of the population between 1997 and 2007, and 13 percent of those employed during 1997-2003, constituted the working poor (Saif, 2009:16).

Table 2. Jordan Poverty Indicators

	1997	2002	2008
Poverty line	366 JD	392 JD	680 JD (2.8 JD/day)
Poverty rate	21.3%	14.2%	13.3%

Source: World Bank, 2002 and 2010.

The high levels of voluntary unemployment and ‘inactivity’ in the labour market are reinforced by the relatively high reservation wages of Jordanians, which stem from the expectations of obtaining higher-paid public sector jobs and receiving income support from their families. The expectations of civil service jobs, which pay higher wages on average than the private sector, reinforces the unemployed person’s hesitation in accepting existing low-wage jobs. In theory, the lowest monthly pay in the public sector should be JD 206, far above the private sector minimum of JD 150. This is attributable to the provision of a cost of living allowance of JD 90 and a living standard improvement allowance of about JD 40. In addition, public sector employment offers greater job security. Thus, it is highly attractive, particularly for those with low levels of education.

The contrast between the conditions of public and private sector employment for those with basic education is such that new entrants to the labour force are willing to remain unemployed in the hope that they will find a job in the public sector. Having said this, it should be mentioned that holders of bachelor’s degrees have always been the largest section of the labour force employed by the public sector. Figures from 2007 show that 45 percent of the 165,032 public sector employees held a bachelor’s degree and 15 percent had less than secondary-level education (Al Manar, 2010). Although the pace of government hiring has slowed, Jordan’s civil service continues to expand. New hires crept up from about 7,000 in 2001 to nearly 9,000 in 2004 and just over 11,000 in 2007. Meanwhile, even a larger number of people file applications for employment with the Civil Service Bureau: about 20 percent of all unemployed individuals and 45 percent of unemployed women apply to the Civil Service Bureau. The latest figures show that in 2007, nearly 180,000 people applied for public sector jobs, out of which only 6 percent were appointed (Al Manar, 2010). This ratio has remained constant – a clear indication of the attractiveness of public sector employment *as well as* the public sector’s inability to expand its wage bill.

Table 3. Annual distribution of Jordanian employees by sector (percentage)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Public	37.2	34.8	34.9	35.4	35.0	36.1	36.6	37.9	38.6	37.9
Private	61.8	64.4	64.3	63.9	64.4	63.2	62.8	61.6	61.1	61.5
Other	1.1	0.8	0.8	0.8	0.7	0.7	0.6	0.6	0.3	0.5

Source: Al Manar, 2010.

There are, however, drawbacks to public sector employment. The flatness of the education-earnings profile in the public sector⁷ and its willingness to hire a significant number of people without completed secondary education and to pay them generously often reduces the incentive to finish secondary education and pursue higher education. This can undermine the labour productivity and human capital of the economy to the detriment of future economic expansion and diversification. So many males terminate their education at the basic level, when staying in school for a further two years and earning the secondary school-leaving certificate might significantly improve their prospects. The generous pay offered to the less-educated may reduce inequality among public sector employees, or between less-educated employees in the public and private sectors, but it exacerbates inequality between them and their counterparts who are not successful in obtaining public sector employment. Therefore, for a labour surplus economy, a healthy wage structure and an appropriate level of public sector wage are essential in creating the right incentives in the labour market and preventing unnecessary constraints on government revenues, particularly in the post-financial crisis era.

Although the above sectors should be taken into account in the government's overall employment strategy, it is essential to remember that unemployment is a macroeconomic problem that cannot be resolved by mere supply-side policies relating to earnings differentials or education. Measures to re-align public and private sector pay cannot be expected to have any immediate effect on the unemployment problem, in so far as it is caused by an insufficiency in the aggregate demand for labour. Most recently, the government of Jordan has announced a national strategy for employment through 'striking a balance between demand and supply in the labour market' (Obeidat, 2011). Although establishing funds to 'support small and medium enterprises' can lead to some levels of employment creation, it is an increase in and diversification of domestic and international demand for goods and services produced by the Jordanian economy, which would play a more important role in generating further and more sustainable employment levels.

Realizing the 'dangerous' nature of very high rates of economic inactivity amongst the labour force and its ability to 'limit the state's ability to combat poverty and unemployment', the government has proposed the introduction of structural policies in the areas of support to SMEs, introduction of more decent jobs, greater coordination between the demand and supply in the labour market, and a revision of the government's labour immigration policy (Obeidat, 2011). The above has been recognised to some extent in the government's Executive Development Programme 2011-13, which highlights the importance of rejuvenating investment in the neglected agricultural sector to ensure its

⁷ The reason for the flatness in public sector earnings profiles is, of course, that major components of earnings, the cost of living allowance and the living standards improvement allowance are minimally related to education.

‘sustainable development’ and contribution to unemployment reduction. To ‘increase self-reliance and improve the agricultural trade balance’ and to ‘promote economic opportunities for agricultural producers and benefit from local and international trade opportunities’ are among some of the government objectives in this respect (Ministry of Planning and International Cooperation, 2010).

Similarly in the area of investment in industry and trade, the EDP aims to ‘provide an enabling environment for business and investment, and enhance the competitiveness of the national economy on local, regional and international fronts’, ‘provide new job opportunities’ and ‘upgrade and modernize the industrial sector’ with the aim of expanding its capacity and competitiveness. The government aims to adopt policies which ‘enhance partnership between the public and private sectors’ in industry and trade, ‘support the industrial sector (Industrial Policy), and promote local industries’ (Ministry of Planning and International Cooperation, 2010). Both these agricultural and industrial policies have the potential to expand the economy’s employment generating capacity.

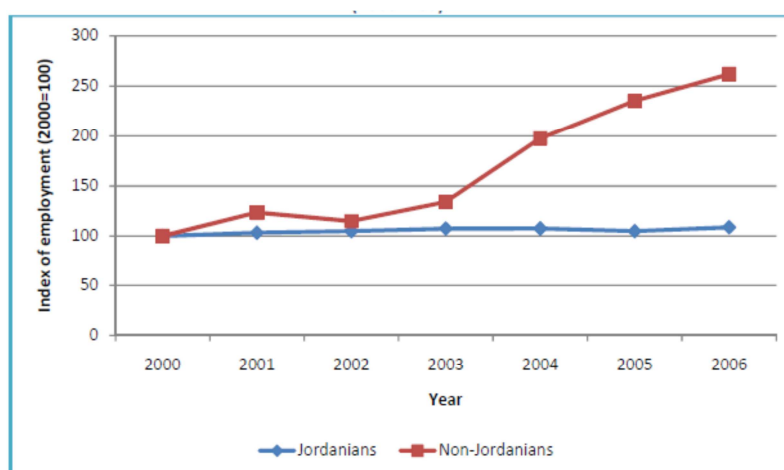
Although the policies aimed at expansion of trade, industry and agriculture have the potential to increase employment opportunities in these sectors, the EDP’s approach to employment generation fails to address the issue of unemployment as a standalone issue and considers it as a spill-over of expansion of other economic sectors.

Migrant Workers

Jordan’s trade and investment liberalization policies and the drive towards expanding competitiveness through a race-to-the-bottom in terms of reducing wages and prices of other inputs has in some cases resulted in low-paid jobs created by foreign investments which dominate Jordan’s trade and investment scene, particularly in the QIZs. These low-paid jobs were often filled by migrant workers who would be ready to accept the low wages and poor working conditions prevailing in these employment categories. The working conditions in these export zones have been repeatedly criticised by various international organizations which have accused them of violating labour rights (National Labour Committee, 2006). In addition, the poor conditions offered in the QIZs have encouraged the expansion of the informal economy.

Several of the sectors with the highest GDP growth in recent years, including manufacturing and construction, have produced a large number of low-skilled, low-wage jobs that were unattractive to Jordanian workers and were, hence, picked up by migrants (Figure 6). A similar trend has happened in the agricultural sector. This has led to a net decrease in jobs for Jordanians. According to the DOS, during 2000 to 2005 between 52 to 63 percent of newly created jobs were filled by migrants. As a result of this trend, in 2009, foreign workers in Jordan numbered more than 335,000, far more than the number of unemployed Jordanians which stood at 180,000 in the same year – see Table 4 below (Al Manar, 2010a). Migrant workers are mainly young men with low levels of education from other countries in the region, particularly Iraq, Palestine, and Egypt. The exact number of migrant workers in Jordan is estimated at about 20 percent of the Jordanian labour force. They are often concentrated in the export zones as well as the agriculture, construction and manufacturing sectors (see Tables 5 and 6).

Figure 6. Employment of Jordanian and non-Jordanians working in Jordan, 2000-2006 (2000=100)



Source: Al Manar, 2010b.

Table 4. Comparison of the number of Jordanian unemployed and migrant workers

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Registered foreign workers	110,580	136,573	127,181	148,823	218,756	261,781	289,730	313,196	303,325	335,708
Unemployed Jordanians	143,730	158,566	171,430	164,431	144,236	177,359	171,390	172,203	170,114	180,284
Employed Jordanians	908,314	920,042	951,612	969,171	1,012,734	1,023,681	1,055,847	1,140,446	1,172,701	1,220,521

Source: Al Manar, 2010 and 2010a.

Table 5. Employment of migrants working in Jordan by economic activity, 2000 and 2006

<i>Economic activity</i>	Employment (000s)		As % of total employment in the economic activity	
	2000	2006	2000	2006
Agriculture	30.5	68.3	37.5	71.2
Mining & Quarrying	2.3	2.9	20.2	32.5
Manufacturing	16.8	69.7	13.7	37.9
Electric, Gas and Water Supply	0.2	0.2	1.3	1.4
Construction	20.2	44.3	22.9	42.1
Wholesale and Retail Trade	10.3	19.4	5.9	9.8
Hotels and Restaurants	7.2	15.2	25.5	39.0
Transportation	1.8	2.0	1.8	2.0
Financial Intermediation	0.9	1.9	4.2	8.3
Real Estate, Renting and Business Activities	1.6	1.9	5.1	3.6
Public Administration and Compulsory Social Security	0.3	0.2	0.5	0.2
Education	1.1	1.4	0.8	0.9
Health and Social Work	0.4	1.2	0.9	2.1
Other Community, Social & Personal Services	17.0	61.0	23.9	49.4
Total	110.6	289.7	11.2	23.3

Source: Al Manar, 2010b.

Table 6. Distribution (percent) of the employment of Jordanians and Non-Jordanians by economic activity in 2000 and 2006 (excluding the Armed Forces)

<i>Economic activity</i>	Jordanians		Non-Jordanians	
	2000	2006	2000	2006
Agriculture	5.8	2.9	27.6	23.6
Mining & Quarrying	1.0	0.6	2.1	1.0
Manufacturing	12.1	12.0	15.2	24.1
Electric, Gas and Water Supply	1.6	1.5	0.2	0.1
Construction	7.7	6.4	18.3	15.3
Wholesale and Retail Trade	18.9	18.8	9.3	6.7
Hotels and Restaurants	2.4	2.5	6.5	5.3
Transportation	11.1	10.3	1.6	0.7
Financial Intermediation	2.2	2.3	0.8	0.7
Real Estate, Renting and Business Activities	3.4	5.5	1.5	0.7
Public Administration and Compulsory Social Security	8.4	8.8	0.3	0.1
Education	14.1	16.2	1.0	0.5
Health and Social Work	4.8	5.7	0.4	0.4
Other Community, Social & Personal Services	6.2	6.6	15.4	21.1
Total	100.0	100.0	100.0	100.0

Source: Al Manar, 2010b.

In general, migrant workers are less skilled and have received less training than Jordanian workers, but their readiness to accept jobs with low salaries and poor working conditions and their general flexibility make them a favourable option for most employers. Furthermore, Jordanians' expectations of employment opportunities that satisfy their academic and professional qualifications have made them less 'employable'. Nonetheless, improving the quality of education continues to be important in promoting relevant fields of specialisation. Among university study fields, unemployment rates in agriculture, veterinary, and educational specializations have remained twice as high as those of engineers and health care workers. Although highlighting the lack of informative mechanisms and a mismatch between supply and demand in the labour market, this is also an indication of low levels of output and productivity in such sectors, which could potentially be a source of employment. The government's 2011-13 EDP aims to 'provide opportunities for universal education and ensuring equality and fairness in educational services both quantitatively and qualitatively'; to 'equip students with the skills and knowledge needed by the knowledge-based economy', and to elevate the 'quality level of higher education and its outputs' (Ministry of Planning and International Cooperation, 2010a).

More recently, the government's National Strategy for Employment has set out plans for replacing migrant workers with Jordanian workers. In the short-term it aims to replace guest workers with local labour, particularly in the services, hospitality, water, electricity, health, construction and trade sectors, whereas in the medium term, this strategy will expand to the sectors of mining, industry and agriculture. Parallel to this, the government aims to boost investments in sectors and industries which employ the majority of Jordanians in order to also ensure a dynamic expansion of employment opportunities in the country (Obeidat, 2011). This is a highly valuable objective as long as the government focuses on expansion of the economy's capacity for generation of productive, high-wage, decent employment opportunities in a wide array of economic sectors.

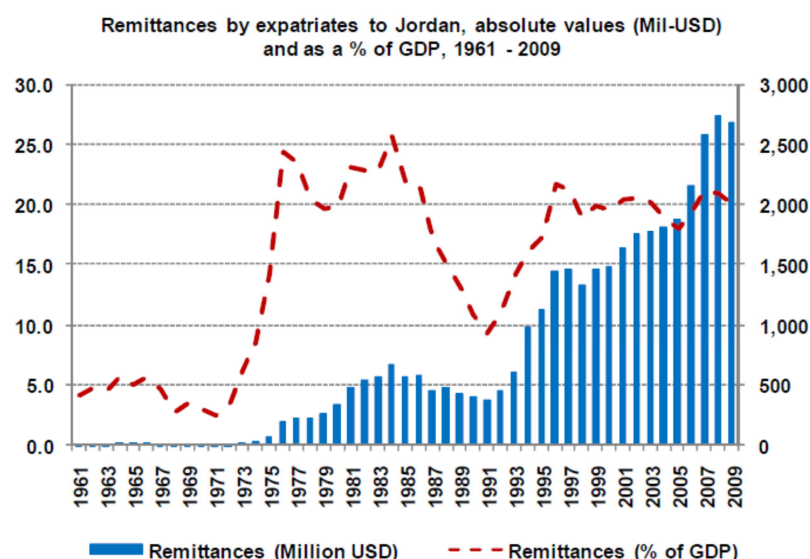
The new Provisional Amended Labour Law aims to better organize and regulate the employment of non-Jordanians, and include clauses on domestic workers. However, while under the new Social Security Law all workers in Jordan can be potentially covered by

social security regardless of their nationality, this does not seem to benefit domestic workers, most of whom are migrants. Under the ‘Jordanisation’ policies of the Jordanian government, agriculture and construction were considered as the first sectors where Jordanians could start replacing migrant workers (by offering to subsidize the salaries and social security contributions of Jordanian employees). Similar policies were also implemented across the QIZs: any company that hires a new Jordanian is eligible to hire two migrant workers with an exemption of permit fees. Finally, in partnership with the private sector, the Ministry of Labour establishes a number of agreements with some of the occupational sectors to facilitate the replacement of migrant workers with Jordanians by setting some targets for the shares of these two groups in company workforces.

Emigration of skilled Jordanian labour

Jordan is a country, which relies heavily on ‘external’ sources of revenue, including remittances from Jordanians who have gone abroad in search of better employment opportunities. Since the early-1970s and the first oil boom, Jordan has been exporting a large number of workers to the oil-exporting Gulf countries, providing high levels of remittances for the Jordanian economy. In 2009, remittance constituted 20 percent of Jordan’s GDP (Figure 7).

Figure 7. Remittances by expatriates to Jordan, absolute values (USD, millions)



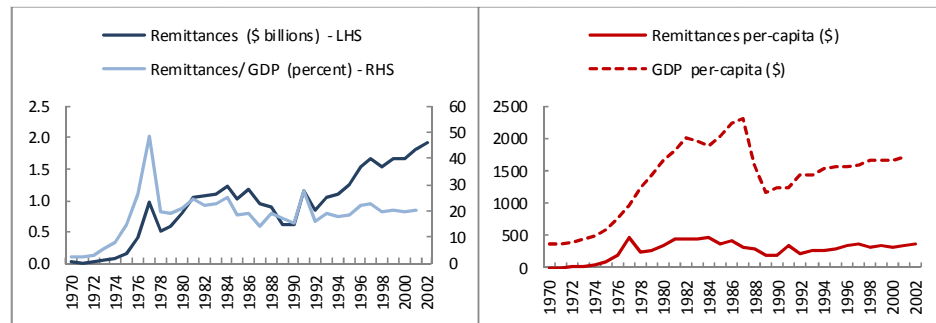
Source: CARIM, 2010:3

Following the Gulf War, around 300,000 Jordanians who had sought employment in the oil-rich Gulf economies since the late-1980s, returned home. As a result, there was a sudden disruption of remittances and aid flows from the oil-rich Gulf economies. In addition, the gradual increase in migrant workers from other regions in the Gulf countries, which began in the mid-1980s, also contributed to a steady decline in remittances observed until the mid-1990s. Furthermore, following the Gulf War, Jordan’s exports were largely affected given Iraq was one of its main trading partners. This was further worsened by the fall in exports to other Arab countries during the war.

The Gulf war had a major direct bearing on all the sectors of the Jordanian economy, as well as the labour market, resulting in an unemployment rate of nearly 30 percent and an increase in the poverty rate to 33 percent. The gradual normalisation of political relations between Jordan and the Gulf countries in the years, which followed resulted in the resumption and full recovery of remittances which reached almost USD 2 billion in 2002.

Since then, remittances have on average constituted 20 percent of GDP. Figure 8 below shows the significance of remittances in the Jordanian economy during the period 1970-2002, highlighting that remittances have been the main source of foreign exchange. Indeed, if remittances in kind and unrecorded remittances are also included, their significance would increase even further. Some argue that the actual level of remittances can be as much as 60 percent to three times higher than the official figures (El-Sakka, 2005).

Figure 8. Remittances in Jordan 1970-2002



Source: El-Sakka, 2005:8.

The emigration of Jordanian workers has also led to labour shortage at home, fuelling larger scale entrance of migrant workers, and deprived the economy of essential skills and human capital. According to the Ministry of Labour, in 2008, about 4.9 percent of the total Jordanian population lived abroad. Estimates from the International Labour Organization (ILO) indicate that around 600,000 Jordanians, half the size of the Jordanian labour force at home, work abroad and are often employed in skill-intensive jobs. This is an indication of an 'imbalanced skills situation' whereby, local supply of skills exceeds local demand for skills at wages on offer in the local economy. The decline of oil prices and economic activity in many of the oil-exporting economies following the global economic crisis of 2008-09, resulted in a decline in employment opportunities in the Arab region by around 20 percent in 2009, with demand for labour declining by 30 percent (GMG, 2010). As a result of these developments, remittances to Jordan decreased by about 10 percent during 2009, with many of those workers who stayed behind in the Gulf countries having to accept lower wages and poor working conditions. Furthermore, some estimates show that the outflow of remittances by migrant workers have offset the remittances sent in by Jordanians abroad. This calls for an emphasis on reforming structural policies (macro, industrial, trade, business and taxation, for example) aimed at moving the economy towards high productivity, high wage equilibrium that is more capable of absorbing the country's skilled labour supply.

Recent government policies related to labour exports from Jordan have been focused on channelling more remittances through official routes in order to maximize their use for the country's macroeconomic stability, rather than focusing on generating attractive jobs for the expatriate Jordanians. Jordan's fixed exchange rate regime enhances the role of remittances on the growth of monetary aggregates through the liquidity in the banking system and the balance of payment surpluses. Remittances have been one of the main sources of foreign exchange in Jordan, helping to finance the balance of payment gaps. In addition, according to the IMF, remittances are equivalent to more than 40 percent of exports of goods and services, largely offsetting Jordan's trade deficit. Thus, the country's monetary, fiscal and trade performance to a large extent hinge on the level and stability of the remittances. In other words, in Jordan, the nature of labour flows plays a key role in determining economic performance and macroeconomic stability rather than the other way around.

Evidence has also shown that remittances, as a form of unearned income or rent, can reduce labour supply by acting as a disincentive for other members of the recipient

households to work. This can lead both to a decline in labour force participation and an increase in unemployment. Furthermore, a recent study by the IMF (2006) argues that remittances have had a significant impact on Jordan's real exchange rate, hence reducing Jordan's competitiveness. Remittances have the potential to induce a real exchange rate appreciation, widen the current-account deficit, weaken monetary control, contribute to inflationary pressures, and result in sectoral misallocation of investment. In addition, in Jordan, remittance income accrues primarily to middle- and high-income families, as most of those who emigrate tend to be well educated and from prosperous families. As a result, remittances are greater for wealthier households than for poor ones and contribute little to reducing poverty levels and inequality in Jordan.

Informal Economy

Jordan's economic growth has failed to produce sufficient formal employment that provides social protection for its workers. Thus, employment in the informal economy has gained much importance. According to unofficial estimates, the informal economy accounts for about 20 percent of GDP and employs about 25 percent of the workers. The jobs created in the formal economy are inadequate for the 50-60 thousand new entrants to the labour market each year. Other reasons behind the growth of the informal economy in Jordan are the high rates of poverty (14.7 percent in 2005) (Shawabkeh, 2007); a high rate of population growth, especially inflated by large inflows of refugees; the mismatch between the skills of the labour force and the demands of the economy; the bureaucratic tax procedures and licensing requirements for setting up businesses, and the unforeseen costs involved in establishing a formal business; the higher standards of living in urban areas and the labour flight from rural to urban centres; and the acceleration of the privatization and restructuring programmes, which have resulted in large scale job losses. The drive towards privatization and minimizing of public enterprises has resulted in a large number of private establishments.

According to the Department of Statistics, micro (1 – 4 workers) and small (5 – 19 workers) enterprises constitute 98 percent of all firms in Jordan (ETF, 2005). These firms are responsible for around half to two-thirds of private sector employment in Jordan. Apart from very limited potentials for employment generation, this private sector structure also limits the resources available for workers in terms of training, career development, and social security. Therefore, added to the prominent presence of non-Jordanian workers, the Jordanian labour market is also segmented between formal employment in the public and private sector and employment in the informal economy with very low mobility between the two areas.

The informal economy is said to be growing faster than the formal economy, as indicated by low official levels of labour participation rate (25 percent), creating most of the new jobs, with migrant workers and women constituting around 75 percent of employees in this sector. These are mainly agricultural workers, home-workers, domestic employees, the self-employed, unpaid family workers, and workers in unregistered enterprises as well as the QIZs. Since the employers in the informal economy do not pay taxes, they do not benefit from various labour and business regulations; hence, leaving workers with inadequate protection and social security, lower wages, lack of application of international and national labour laws, lack of occupational safety standards, and harsh working conditions. Although the informal economy provides a cushioning effect at times of economic downturn, low working standards minimize the positive effects of the informal economy employment. Labour laws need to be amended to protect the rights of the workers and a minimum wage in the informal economy, many of whom work in the QIZs. Although desirable, provision of training and rehabilitation to the workers in the informal economy is insufficient for moving workers to the formal labour market, as it is the unavailability of productive and decent employment opportunities, rather than labour skills that is the real obstacle to this move.

One of the main reasons driving the poor to avoid licensing and formalizing their businesses is the high taxes imposed by the government. There are many types of taxes imposed on the various business sectors, under various names, such as income. The absence of government support and subsidy programmes has also created a significant impact on the existence of informal businesses in Jordan. Lack of any subsidy programmes for the commercial, industrial, agricultural and services sectors to help with setting up start-up businesses, 'formalizing' the unlicensed business sector and giving them legal status, reduces the number of business entities, which operate in the formal market. The need for subsidizing programmes is particularly vital to cope with the increasing costs of industrial and agricultural production when natural and economic resources are becoming increasingly scarce. Finally, the numerous obstacles facing the poor during the process of litigation involving their business, particularly the high court fees, is a further prohibitive factor. For example, the Jordanian administrative law does not provide for quasi-judicial bodies in the various governmental institutions, which could help setting up businesses or protect poor citizens' rights in disputes.

Social protection

As mentioned earlier, social security has been lacking for the majority of workers in Jordan; this includes the majority of those in the private sector, a large section of agricultural workers, the workers in the informal economy, and of course the migrants. There are two sets of social protection systems in place: contributory and non-contributory schemes. In recent years the government has attempted to expand its social protection to the above groups, and also to consolidate both schemes into one social security system in order to increase the efficiency and coverage of the benefits to workers. Less than 1 percent of GDP (and declining) is being spent on non-contributory social protection, and a total of just over 8 percent of GDP on social expenditure excluding education. Contributory-based social protection schemes, such as pension and social security, comprise 62 percent of total expenditures on social protection and are the main source of income for 28 percent of households.

The Social Security Corporation (SSC), a government agency, administers pension arrangements for all Jordanian nationals employed in establishments with five or more workers. Prior to 1995, government employees had a different system, but since that date, new recruits have been subject to the same arrangements as private sector workers. It is a defined benefit scheme, with employees contributing 5.5 percent of total salary to the pension fund and employers contributing 9 percent. Employers contribute a further 2 percent to the fund to cover workplace insurance. Establishments with fewer than five workers may contract into the scheme voluntarily, as may individuals not otherwise covered. Individuals so doing, must pay both the employee and employer contributions. When disaggregating by gender, only one out of ten females of working age are insured with the SSC compared with more than one out of five males of working age. This is an indication of both the lower female labour participation, as well as a lack of universal provision. In addition, the concentration of women is much higher in the informal economy and agricultural sectors, both of which suffer from lower wages, poor working conditions and non-existent social security. In addition, the self-employed are also not fully covered in these social security schemes. In view of this, the government has recognized the need for changes particularly to the contributory social protection schemes.

Many consider Jordan's social security pension system as extremely generous and possibly a disincentive to employment. However, even the World Bank has argued that the 'existing social protection programmes in Jordan do not appear to create major disincentives to work' (Razzaz, et al, 2008:14). There is no evidence that in Jordan, the National Aid Fund (NAF), social security, and severance pay policies keep the unemployed from accepting existing jobs. NAF is a major non-contributory social protection scheme, which provides cash assistance and support to poor families. The categories of individuals

eligible for NAF tend to be outside the labour force. Thus there are few unemployed beneficiaries, and for them evidence shows that receiving NAF benefits does not have a significant effect on labour-force participation and does not raise the likelihood of unemployment. The social security pension system in Jordan is also considered to be unsustainably generous in terms of its overall benefit level and early retirement provisions that allow beneficiaries to retire at age 45 with only minor reductions in their monthly pension. The early retirement pension is said to lead to a sharp decline in employment around the age of 45. However, the impact of this on the overall unemployment levels in the country will be minimal since the majority of the labour force and unemployment is concentrated among the youth. Evidence shows that unemployment rates are very low for those over 40 (Razzaz, et al., 2008). Hence, the pension system does not have a large impact on unemployment. As for workers who are made redundant and are eligible for 'Income support for the unemployed', severance pay policies are considered unlikely to create significant disincentives to accepting employment because the total received in severance pay is shown to be unrelated to the duration of unemployment.

Although the recent global economic crisis has resulted in unrealized losses of 20.4 percent for Jordan's largest investor and administrator of social security benefits, the SSC, the government extended social services to vulnerable groups through targeted policies to support poor families and the unemployed (World Bank, 2008). A new Social Security Law was passed in 2010 that made provisions for unemployment, insurance, maternity insurance coverage of the health insurance to the poor and unemployed. In view of the sudden increase in unemployment following the crisis and the lack of formal employment opportunities in the economy, a 'temporary' law was also passed to extend social security coverage to informal workers. In the same year, the monthly minimum wage rose from USD 155 to USD 211, and the funding for NAF increased by USD 28 million. The government has also aimed at setting up unemployment insurance savings accounts for those workers who have built up sufficient savings in their individual accounts. A programme to support low-skilled workers has been especially beneficial to women in the agricultural sector and aims to boost female self-employment.

The government's EDP 2011-13 calls for a 'comprehensive and effective social security system for the poor' aimed at 'empowering economically-poor factions and create sustainable local economies' and 'linking monetary aid provided to the poor to the conditions of enabling them and improving their living standard' (Ministry of Planning and International Cooperation, 2010). As the existing programmes are reformed, it is important to ensure that social protection reforms increase rather than reduce incentives to work. Introducing unemployment insurance and improving the targeting of the NAF (to cover the working poor) are both valuable reforms, yet can potentially introduce disincentives to work. These can be minimized through establishing careful links to programmes that permit monitoring of beneficiaries' job search and their acceptance of job offers. However, Jordan's budget constraints mean that it will not be able to expand and upgrade social protection programmes sufficiently within its current fiscal envelope. As will be discussed later, such social reforms have wide fiscal implications and their implementation has at points suffered from the government's fiscal consolidation policies. For this reason, the composition of government's social spending needs to be carefully examined and re-prioritized with the aim of targeting the unemployed and the poor. In line with this, for example, in 2010 UNICEF suggested that the Jordanian government should consider phasing out its Liquid Petroleum Gas (LPG) and wheat subsidies to reduce the subsidy burden particularly given the fact that the wealthiest quintiles receive a disproportionate share of the LPG subsidy (UNICEF, 2010).

4. Macroeconomic stabilisation and employment

As discussed earlier, since the late-1980s Jordan has received large loans from international financial institutions, particularly the IMF and the World Bank. The stabilization and reform programmes, which came with these loans, dominated macroeconomic policy making until very recently. The 1991 Gulf War, as well as the more recent Iraq war, further altered the stability of the Jordanian economy due to its high levels of dependence on remittances and external financial flows, all of which were severely disrupted as a result of these wars. Although in-kind and financial aid from the regional governments has helped to cover part of this deficit, the growth rate has often struggled to recover following these uncertainties. Despite goals of stimulating macroeconomic stability and creating further employment opportunities, the IMF programmes have been more successful in achieving some indicators of stabilization, such as lower inflation, strengthening of the trade sector and reducing the government's fiscal expenditure, rather than achieving sustainable employment and poverty objectives. The main elements of the IMF-led stabilization programmes have been policies to boost domestic saving and investment, wide-ranging structural reforms in the fiscal, monetary and external sectors, legal institutional reforms and privatization, containing current expenditures, improving the efficiency of the tax system, reducing subsidies while making them more targeted, and supporting the exchange rate peg through active interest rate and international reserves management policies.

However, realizing the limits of these policies in achieving the country's social objectives, as well as the political challenges of selling these programmes to a population of mainly jobless 'returnees' from the Gulf States, the IMF gradually adjusted some of its programmes with the aim of reducing their contradictory nature. For example, their 1996 programme allowed for an increase in real per capita consumption, in order to 'partially reverse sharp declines in the preceding years and, together with expanding employment opportunities, make the programme 'politically more acceptable' and 'socially more sustainable'. The 1999 Extended Fund Facility-supported programme also aimed to create a balance between further fiscal sustainability, and 'avoidance of undue recessionary effects from rapid contraction' (IMF, 2004:7). More recent IMF programmes became more aligned with Jordan's Plan for Social and Economic Transformation (PSET), adopted by the government in 2001, which highlights the need to improve the quality and standard of living of the population through attraction of higher private sector investment and human resource development, while maintaining the macroeconomic stability. A Stand-By Arrangement (SBA), which expired in July 2004, marked the official end of Jordan's reliance on IMF loans; however, the country still maintains a close relationship with the Fund in the context of *ex post* monitoring and technical assistance.

The nature of the government's macroeconomic policies is all the more critical in the context of the further challenges posed to the Jordanian economy and employment following the global financial crisis. At this juncture, protection of domestic demand is of crucial importance to economic stability and viable employment generation. For that matter, the nature and pace of any fiscal consolidation strategies, an attention to the accommodative nature of monetary policy in view of the inflationary pressures, and creation of carefully-designed subsidy programmes can protect both businesses and workers against the adverse effects of the crisis. The rest of this paper explores the impact of Jordan's macroeconomic policies in recent years on the levels of employment.

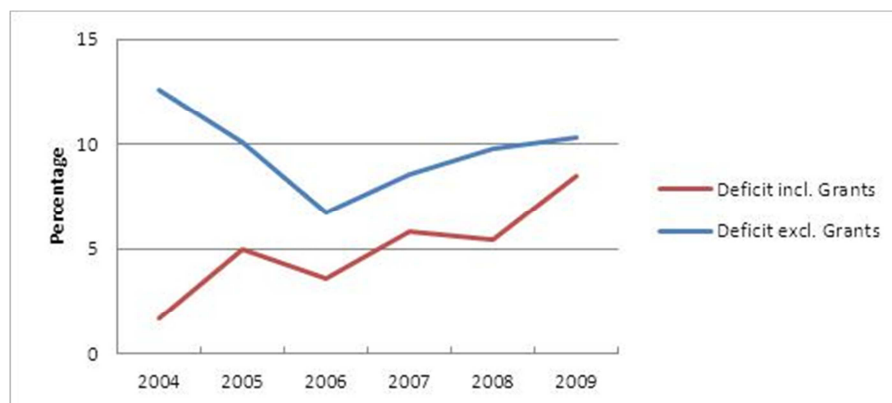
Fiscal policy

As mentioned earlier, fiscal policy reform has been a component of Jordan's recent macroeconomic policy framework. Fuelled by various forms of grants, loans and foreign assistance from the regional countries, as well as international organizations, the Jordanian government's expenditure has stood at around 40 percent of GDP over the past two decades (Ramachandran, 2004:3). This level of fiscal spending has been both helped and threatened by changes in oil prices. However, in order to maintain its spending on social services, particularly in the face of politically unpopular contractionary economic reforms, the government has always maintained its current expenditure levels at the expense of reducing capital. High levels of government expenditure on public employment, health and education have been components of government's 'social contract'.

During this period, IMF called for a reduction in the size of the government expenditure, whereas the World Bank placed a greater emphasis on increasing the quality and efficiency of government expenditure. According to the IMF, the austerity measures led by the IMF and implemented by the government improved its fiscal balance in the immediate post-debt crisis era, registering a surplus of 1.2 percent in 1992, excluding grants. Although the government's fiscal status came under pressure following the 1991 Gulf War, due to a sudden decline in Arab aid, as well as remittances, by 1999 the fiscal deficit had declined to 2.4 percent of GDP, including grants, and 5.8 percent without them. By this year, the total government debt was halved from over 200 percent of GDP in 1989 to 100 percent of GDP by 1999 (Maziad, 2009:10). The resumption of remittances in later years meant that by 2003, they amounted to JD 1.4 billion, offsetting 80 percent of the country's merchandise trade deficit (Luxford, 2004).

An important development in recent years is a change in the composition of the country's debt structure. According to the IMF, since 2000, public debt has moved from external to domestic debt, with the share of foreign currency debt falling from over 80 percent of total debt in 2001 to below 50 percent in 2008, reducing the economy's vulnerability to external shocks and exchange rate pressures (Maziad, 2009:17). The government's decision to finance its budget deficit through issuing bonds and treasury bills, rather than relying on external borrowing explains the decline in the levels of Jordan's external public debt to 24.2 percent of GDP by the end of 2008, compared to an internal public debt of 32.6 percent of GDP. This perhaps to some extent, explains the delayed and relatively smaller impact of the global financial crisis on the Jordanian economy. The budget deficit in 2008 reached 4.9 percent of GDP, compared to 5.1 percent a year before (Ministry of Planning and International Cooperation, 2010). Figure 9 below shows the government's budget deficit trends in recent years.

Figure 9. Budget Deficit, 2004-2009 (in percent of GDP)



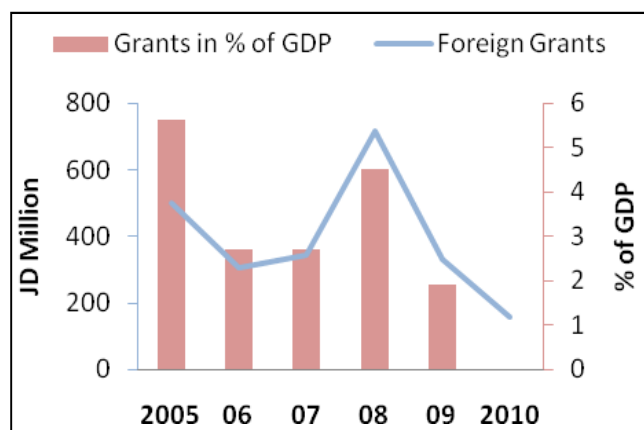
Source: IMF Article IV Staff Reports.

The aim of much of the fiscal reform programmes over the past two decades have been to reduce the size of public sector expenditure, particularly in the area of civil service wage bills, health and education, with the aim of increasing efficiency. However, these tasks have remained challenging, particularly in the absence of a viable private sector, which could act as an alternative source of employment for the 40 percent of the labour force, which is employed by the government (Al Manar, 2010). A large part of Jordan's private sector has been created as a result of privatization of public companies, such as Jordan's cement and telecommunications companies, rather than setting up of new private businesses and entities. As a result, this form of privatization has done little to generate new employment opportunities as it merely shifts the ownership of the company from public to the private sector. If anything, in an attempt to increase worker efficiency and reduce costs, the private owners may in fact reduce the size of their labour force. Rather than generating new jobs, the private sector has tried, at best, to accommodate some of the unexpected waves of 'returnees' following each regional economic or political upheaval.

Meanwhile, the focus of fiscal consolidation has been placed on minimizing the cost of labour. But a lowering of wages for the public sector workers is likely to have a direct bearing on their purchasing power and demand levels. Lower levels of expected demand in the economy can in turn reduce the levels of activity and investment in the economy's productive capacity, which in turn has the potential to produce even more employment. Therefore, a reduction in public sector wage bills can threaten the country's demand base, something, which can be one of the viable future sources of growth and employment.

Jordan's dependence on foreign aid still constitutes a worrying trend for the government's fiscal situation: foreign aid and grants constituted around USD 1 billion in 2009 alone (ISSA, 2010:6). Figure 10 below demonstrates the significance of foreign grants in Jordan's GDP in recent years. When these grants are taken out of the budget, the government's finances show signs of worry. To this should be added the country's debt due to multilateral and bilateral creditors. This is further problematic given the country's weak tax structure: income tax ranges from 5-25 percent with the average taxpayer paying a marginal rate of 5 percent.

Figure 10. Foreign grants, 2005-2010 (in JD million and percent of GDP)



Source: ILO, 2010:17.

In response to the global financial crisis, the Jordanian government panicked into adopting fiscal consolidation measures such as removal of fuel subsidies in early 2008 at a time when food prices were rising. The IMF recommended further expenditure-reducing austerity measures in order to cut the country's fiscal deficit, which had expanded by 3 percent in 2009, to reach 8.5 percent of GDP by year-end. The Fund argued that although the Jordanian economy suffered from lower trade and external financing as a result of the global crisis, the spending cuts, which took place in 2010, achieved a good level of fiscal consolidation, which will push down the fiscal deficit to around 6 percent of the GDP by

the end of 2010. The IMF recommends further reform of the tax system and substantial fiscal consolidation, mainly from the spending side involving greater prioritization of capital spending and savings in current expenditures, including from containment of the public sector wage bill and reductions in the operating costs of public institutions and independent agencies. Additional revenue measures were also introduced in June 2010, including raising indirect taxes on petroleum and other commodities (IMF, 2010).

However, the impact of such tight fiscal policy is quite worrisome, particularly in terms of employment. This is particularly the case since, as will be seen below, the burden of government's fiscal adjustment has fallen on capital expenditures with far-reaching growth and employment implications. Aware of the potentially destructive impact of a tight fiscal policy in the post-crisis setting and to cushion the impact of the crisis and rising prices on households, the government of Jordan began to implement some expansionary fiscal measures such as subsidies to local wheat and barley farmers, fixing the price of bread, and eliminating profit margins on basic commodities. The government also increased the salaries of public sector employees, civil servant workers, military and security personnel. Other measures aimed at protecting the labour market were the expansion of social safety net transfers, including direct cash payments to non-government workers or pensioners with an average per family income of less than USD 1,400 per year, plus an increase in payments to the beneficiaries of the National Aid Fund (NAF). Furthermore, the new Social Security Law has introduced an indexing mechanism, which provides for annual adjustments of pensions in payments to the inflation rate, which accelerated in recent years due to increase in prices of oil and food internationally, in order to protect the pensioners' purchasing power. Finally, and significantly, Jordan's minimum wage was raised in 2008 from JD100 to JD150 (ILO, 2010).

To enhance the employment benefits of government's fiscal policy decisions, the Ministry of Labour has introduced a number of policies aimed at maximizing the employment impact of fiscal policies. For example, during the post-crisis situation, the government has aimed at reducing labour costs by meeting some of the employers' outlay for training, social security contributions and wages. In order to maximize the impact of these initiatives, the Ministry of Labour has started targeting agriculture and construction with incentives and subsidies for companies to hire Jordanians in order to help Jordanian job-seekers replace the large number of migrant workers in these sectors. In coordination with MoL, the government also aims to facilitate skills development through provision of further vocational training to move into an advanced technological level and providing training for teachers that would correspond to the needs of the labour market. Furthermore, MoL has established a programme to subsidise labour costs to Jordanians employed in different sectors, such as agriculture, by topping up the salaries of Jordanians by JD 80 a month for up to six months and paying fully or in part the employees social security contribution.

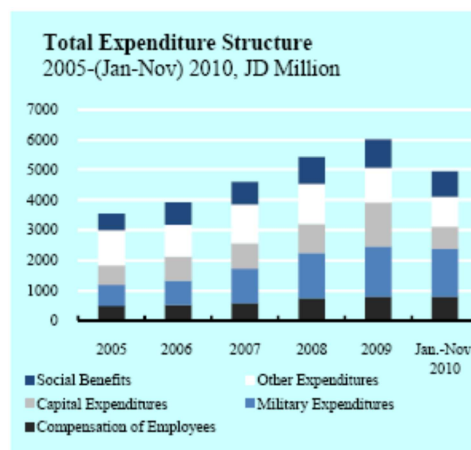
It is then crucial, in a post-crisis phase, for the state to carefully formulate its fiscal policy with the aim of protecting the labour market and living standards in the context of volatile regional and global economic circumstances. Furthermore, given that the global financial crisis highlighted the risks of relying on international markets as a main source of revenue, Jordan's future growth and development strategy should be focused on developing the country's domestic demand base as a more secure market and source of revenue. In line with this, tight fiscal policy may in fact hamper domestic demand.

Government revenues (including grants) increased by nearly 3 percent in 2010 compared to 2009, driven mainly by the increase in both foreign grants and domestic revenues by JD 58.6 million and JD 53.0 million, respectively. Domestic revenues increased by 1.4 percent in 2010 as result of the rise in the proceeds of 'tax revenues' and 'pension contributions'. According to Central Bank's figures, tax revenues increased by more than JD 63 million in 2010, accounting for 70.4 percent of domestic revenues. The general sales taxes on goods and services also increased by 16.5 percent in 2010. On the

other hand, the proceeds from ‘income and profit taxes’ declined by 18.7 percent in this year, which was a result of the slow pace of the real economic growth registered in 2009 and its impact on companies’ profits (Central Bank of Jordan, 2011).

Public expenditures declined by more than 1.5 percent in 2010 to stand at JD 4.9 billion, which was due to a 28 percent drop in capital expenditures with long-term implications for growth and employment-generation in the economy. For example, a freezing of public sector employment can aggravate the volatile employment situation regardless of the desirable fiscal effect of such policy. A 5.2 percent increase in current expenditures was due to the rise in the compensation of the civil sector's employees (wages, salaries and social security contributions) and military expenditures. Increases in external and internal interest payments, as well as goods subsidies, which rose due to the increase in world commodity prices, added to the increase in current expenditure. Meanwhile, ‘social benefit expenditures’ only increased by JD 5.7 million. The substantial decline in capital expenditure of more than 28 percent, equivalent to more than JD 284 million, implied that by the end of 2010, total capital expenditure stood at JD 731.9 million (Central Bank of Jordan, 2011). Figure 11 shows the changes in the composition of public expenditure in recent years.

Figure 11. Composition of total public expenditure, 2005-2010 (in JD million)

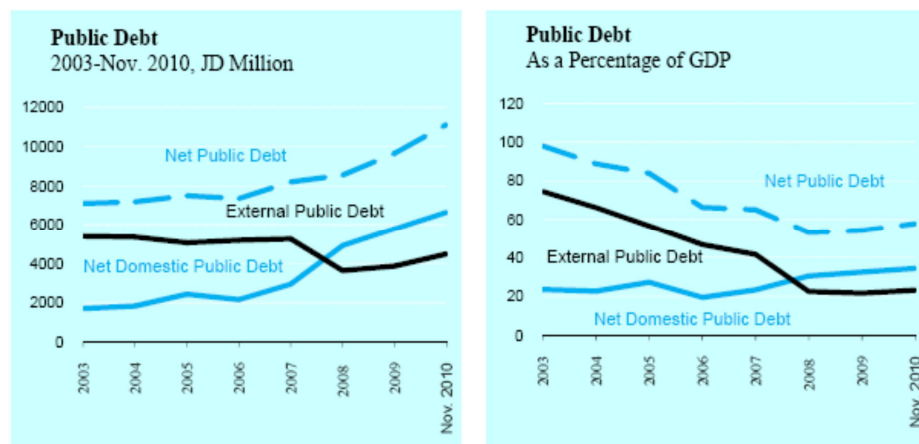


Source: Central Bank of Jordan, 2011:33.

The government’s proactive fiscal response to the crisis, in terms of an increase in public sector wages and institutional improvements, resulted in increase in the budget deficit which stimulated a number of fiscal consolidation measures by the government. For example, all public institutions were required to cut their operating expenses by 20 percent, including cutting the salaries of the ministerial team (ILO, 2010). Furthermore, new public sector recruitments were frozen in most sectors. Hence, by 2010 there was a decline in the general budget deficit, including foreign grants, standing at around JD 786 million compared to the 2009 figure of JD 973 million. This decline was also due to a decline in domestic demand which could potentially hamper future economic activity and employment generation. Net outstanding domestic public debt (budgetary and own-budget) stood at 34.5 percent of GDP, reflecting an increase of JD 852 million during 2010. External public debt also experienced an increase of JD 619.9 million, constituting 23.3 percent of GDP – see Figure 12 below (Central Bank of Jordan, 2011). Gross outstanding domestic public debt of the government (budgetary and own-budget agencies) reached more than JD 7.8 billion, or 40.7 percent of GDP. This was a result of the increase in the budgetary domestic public debt as well as the gross outstanding domestic public debt for own-budget agencies. Net public debt (domestic and external) increased in 2010 to reach more than JD 11.1 billion, or 57.8 percent of GDP, by the end of 2010. It is worth mentioning in this respect that the amended Public Debt Management Law for 2008 sets new ceilings on public debt. According to the introduced amendments, net outstanding

domestic public debt and outstanding external public debt shall not exceed 40 percent of GDP for each. In addition, total outstanding public debt shall not exceed 60 percent of GDP (Central Bank of Jordan, 2011).

Figure 12. Public Debt



Source: Central Bank of Jordan, 2011:35.

The government's EDP (2011-13) sets as one of its priorities the 'reduction of public debt aimed at maintaining financial stability and increase self-reliance'. In addition, in early 2011, the government of Jordan announced a series of fiscal measures aimed at 'alleviating the economic difficulties, improving the living conditions of citizens, as well as meeting the challenge of rising world prices and mitigating its impact on local prices' (Central Bank of Jordan, 2011). These measures include, among others, increasing the cost of living allowance for employees and retirees in both civil and military sectors; allocating JD 20 million to implement services and income-generating projects in underprivileged areas; approving special conditions allowing hiring in the ministries of education, health, social development and women's affairs outside the standard framework of selecting and hiring employees in government positions, as a result of which 20 percent of the jobs listed under the Manpower Tables will be allocated for the diploma holders from underprivileged areas (Ministry of Planning and International Cooperation, 2010a).

In addition, the government has signed a number of grants and loan agreements in order to fill the funding gap left by the fiscal deficit. The government has, among others, signed four grant agreements extended by the United States Agency for International Development (USAID) in the amount of USD 100 million, aimed at supporting development priority projects included in the Budget Law in order to reduce the fiscal deficit. The funding will also aim to cover a number of projects to stimulate trade, improve the investment environment, create jobs for Jordanians, and support the youth and fight poverty. Other grants and agreements have been secured from the Japan International Cooperation Agency's (JICA), the United Nations Children's Fund (UNICEF), and the Jordanian-Egyptian Fajr Company. Although useful sources of short-term financing of government deficit and debt, in the long-term Jordan needs to focus on *domestic* sources of deficit financing. If anything, reliance on external sources of revenue, such as grants and remittances, has been one of the factors, which have often increased the vulnerability of the Jordanian economy towards regional and global political and economic trends. Therefore, developing domestic sources of revenues will not only act as a more sustainable source of government revenue, but also, by developing domestic demand, can expand the economy's capacity for generating more sustainable employment opportunities. For this to materialize, there needs to be an explicit government employment strategy and a strong coordination mechanism that will enhance the linkages between labour market policies and trade and industrial policies.

Monetary and exchange rate policy

Autonomy of monetary policy in Jordan has often been marginalized as a result of a number of factors, including fixed exchange rate, the fluctuating flow of remittances and aid flows, as well as the monetary policy conditionalities of the IMF. The debt and currency crisis of the late-1980s gave rise to a restructuring of the Jordanian monetary system with the aim of giving more autonomy to the Central Bank. Aid flows and remittances are the country's largest sources of foreign exchange, which given the fixed exchange rate regime of the country, have an important impact on the country's balance of payment and hence are key to an analysis of Jordan's monetary policy. The erratic nature of these flows as determined by regional economic and political trends has often reduced the government or Central Bank's ability for long-term monetary policy planning. In addition, remittances directly affect the liquidity levels in the banking system and hence, impact the conduct of monetary policy.

Foreign aid constituted 42 percent of total government revenue until 1983, while remittances averaged 22 percent of GDP annually until 1983. It was the decline in aid and remittances, following the decline in oil prices in the early 1980s that resulted in economic recession and heavy external borrowing. Foreign debt increased by an annual average of 17 percent between 1983 and 1987, reaching a peak of 164 percent of GDP in 1988. When adding domestic debt⁸, the total government debt reached a staggering 203 percent of GDP that year (Maziad, 2009:5). Together with the government's expansionary monetary and fiscal policies aimed at maintaining government expenditure and access to services, as well as the chronic dependence of the economy on foreign capital, the unsustainably high levels of debt resulted in an exchange rate crisis in 1989-90 and a sharp devaluation of the fixed exchange rate.

As a result of the above trends, the average real GDP growth rate of 13 percent, which dominated until 1982 declined drastically to 1.5 percent in 1988, with a further 10 percent contraction in 1989 following the crisis (Maziad, 2009:5). The subsequent programme of macroeconomic stabilization aimed at restoring exchange rate stability, reducing the accumulated debt, enhancing monetary policy instruments and the independence of the Central Bank. Since the government also recognised that one of the main causes of the crisis was 'borrowing from the Central Bank', further fiscal discipline and the enforcement of limitation on Central Bank financing of the budget deficit became critical components of the post-crisis reform period (Maziad, 2009:6).

Tighter monetary policy was introduced in the form of higher interest rates and reserve ratios. The Central Bank of Jordan also increased its discount rate from 5.75 percent to 7 percent in 1988 and 8.5 percent in 1989. The interest rate structure was liberalized in 1990, resulting in higher lending rate of 12 percent later that year. Monetary policy continued to be tightened during the 1990s, while credit to the government and overall domestic credit started to decline, while money supply growth stayed limited to 3 percent. It is argued that a fixed exchange rate helped Jordan in maintaining price stability and attracting foreign capital and investment, particularly from the region (Maziad, 2009:9).

The government has continued to exercise its monetary policy through interest rate adjustments and market operations to contain inflationary pressures generated from high oil prices and the global financial crisis. The surge in food and fuel prices led to a spike in

⁸ The CBJ's lending to the government systematically exceeded the 20 percent (of government revenues) limit since 1980; between 1983 and 1990, average annual CBJ lending to the government was 52 percent of revenues, reaching a peak of 95 percent in 1989 (Maziad, 2009:8).

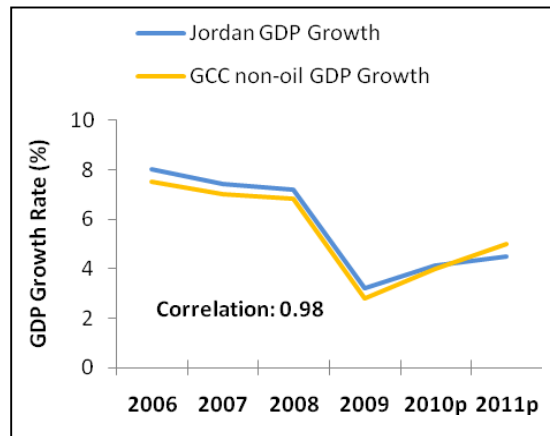
inflation, which reached nearly 14 percent in 2008. When these pressures eased, inflation declined. During these years, the CBJ adopted a cautious monetary policy, which aimed at controlling inflation, protecting the exchange rate and stimulating economic activity at a time of global economic downturn. In order to control the levels of liquidity in the market, the CBJ stopped issuing certificates of deposits, which resulted in an increase in the level of domestic liquidity by 6.7 percentage points, to reach 17.3 percent in 2008 compared to a year before (Ministry of Planning and International Cooperation, 2010).

Following the global financial crisis, Jordan experienced a slowdown in credit activity, with the crisis highlighting Jordan's vulnerability to sudden increases in its budget deficit and public debt. Jordan's fixed exchange rate, its dependence on the US dollar, and the widening of the interest differential between monetary policy rates in Jordan and the United States, reflecting Jordan's tighter monetary policy in the wake of the global financial crisis, were behind this slowdown of credit flows. According to official figures, 'credit facilities given by banks to individuals plunged by 4.9 percent during the first seven months of 2009 compared to the same period in 2008' (Ammon News, 2009). The government's 'reactionary response' to the crisis, as reflected in tighter grip on lending and tougher lending standards exercised by banks, further reduced credit. The relatively higher policy rate in Jordan also attracted excess reserves to the CBJ, further discouraging lending to the real sector. This poses challenges for a country that is largely relying on the public sector for provision of employment opportunities.

This conservative lending policy at the time of crisis resulted in closure of dozens of small and medium-sized projects and businesses, which were unable to obtain loans, further deepening the impact of the crisis. In the face of these threats, the Central bank of Jordan (CBJ) adopted a policy of easing which was conducted between November 2008 and February 2010 with the aim of stimulating credit supply, facilitating lending and increasing the credit flows. This also narrowed the gap between policy rates in Jordan and the United States, and increased the supply of bank credit (Poghosyan, 2010). Major components of this expansionary monetary policy included full guarantee of all bank deposits, pre-emptive actions such as decreases in the discount rate and reductions in obligatory reserves on deposits, a reduction in policy interest rate by 250 basis points between August 2008 and July 2009, and a freeze on the issuance of CBJ certificates of deposits that resulted in an increase of extra liquidity in the banks by JD 3 billion (ILO, 2010). Other policies such as expansion of credit for microenterprises through specific projects and the Development and Employment Fund aimed at protecting the labour market at the time of crisis.

One of the major shortages of credit that Jordan is likely to face in the post global financial crisis era is likely to originate from the future of funding from the Gulf States. The sharp decline in the economic activity of countries such as the United Arab Emirates, signals the possibility of unstable future oil-funded investments in the Jordanian economy. During the second half of 2008, inward FDI flows to Jordan declined by 64 percent mainly due to the freezing of investments by the Gulf investors (Brach and Loewe, 2010). It is also possible to expect further flight of Gulf investment from Jordan in search of more profitable (and cheaper) investment opportunities in the US and Europe, particularly in the real estate sector. The implications of such capital flight will be disastrous for the Jordanian economy and its labour market, which rely so much on external capital flows to the economy. The figure below shows how closely correlated Jordan's economic activity is with that of the Gulf countries.

Figure 13. Correlation between GCC and Jordanian economic growth



Source: ILO, 2010:17.

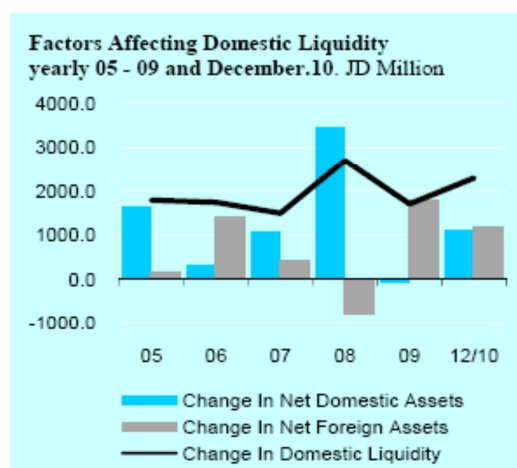
The decline in investor confidence, following the crisis, resulted in a sharp drop in the Amman Stock Exchange (ASE) in 2008, leading to the government and large banks assuring the investors of the health of the country's financial sector. Maintaining the confidence of local and international investors is crucial to Jordan's economy, which is largely dependent on 'external' sources of income such as trade, foreign assistance and FDI. The vulnerability of international banks to the global financial crisis led the government to adopt banking policies to strengthen the risk management capabilities of the banking institutions. Setting a capital adequacy ratio of 12 percent (compared to an international standard rate of 8 percent) in 2008 protected the banks against the financial crisis and the high risks of bankruptcy. In the immediate outbreak of the global financial crisis, the banks were requested to disclose all their toxic papers, which amounted to USD 40 million, which was minimal compared to the profits made by them in the same year (Dimou, 2010). In addition, the government fully guaranteed all bank deposits in local and foreign currencies, as well as inter-bank lending over 2008-10. November 2008 to February 2010 constituted a period of monetary easing by the Jordanian government.

Figures show that the CBJ's foreign currency reserves increased by USD 1,362.2 million, or 12.5 percent, at the end of 2010 compared to their level at the end of 2009, standing at USD 12,241.2 million. This level of reserves is equivalent to around 8.5 months of the Kingdom's imports of goods and services. Domestic liquidity grew by JD 2,293.4 million, or 11.5 percent, during the same period, reaching JD 22,306.7 million – as shown in Figure 15 below (Central Bank of Jordan, 2011). This increased liquidity was reflected in the banking sector activities: the outstanding balance of credit facilities extended by licensed banks increased by 8.5 percent at the end of 2010 compared to the previous year, reaching JD 14.5 billion. The increase in the extended credit facilities took place particularly for the sectors of construction, general trade, industry and public services and utilities; which increased by 22.6 percent, 11.9 percent, 17 percent, and 14.6 percent, respectively, compared to their levels at the end of 2009. The credit facilities extended to individuals experienced a drop of nearly 7 percent, compared to a year earlier (Central Bank of Jordan, 2011). Similarly, total deposits at licensed banks increased by 10.9 percent.

During 2010, there was an increase in both net domestic assets and net foreign assets held by the banking system (Central Bank of Jordan, 2011). Securing 'monetary and banking stability in the Kingdom' are among the top priorities of the Jordan's EDP (2011-13). In line with this, the government aims to 'peg the Jordanian dinar's exchange rate to the US dollar', increase 'knowledge of capital market issues and investment in it in addition to strengthening the culture of investment in stocks and promotion of the national capital at local, Arab and international levels', and generally, to exert 'continued efforts to strengthen the capital market' (Ministry of Planning and International Cooperation, 2010a).

The focus on ‘stabilization’ of the Jordanian monetary system has been only partially successful in protecting the economy against changes in the international interest and exchange rate markets – particularly, given Jordan’s increasing integration into the global economy and its dependence on the US dollar. This overwhelming focus on stabilization of monetary variables has diverted attention away from other socio-economic objectives, such as the creation of viable and high quality employment opportunities within the Jordanian economy, which in the long-run could reduce the instability of the country’s capital flows generated by remittances. As mentioned, Jordan’s 2011-13 Executive Development Plan has argued for price stability with the aim of benefiting employment and promoting investment (Ministry of Planning and International Cooperation, 2010a).

Figure 14. Domestic Liquidity, 2005-2010 (in JD million)



Source: Ministry of Planning and International Cooperation, 2010a: 11.

Trade liberalisation

Given the small size of the Jordanian economy, external trade has been emphasised as an important component of the economy with wide-ranging implications for the government’s fiscal and monetary policies. In the 1980s, quantitative restrictions covered 40 percent of domestic manufacturing and more than 65 percent of the total import value. Jordan’s complicated and highly variable tariff structure in this period implied a maximum tariff rate of 318 percent and an average weighted tariff rate of 19 percent (Saif, 2009:12). Around 51 percent of all imports were exempted from import duty and about 40 percent of imports were subject to quantitative restrictions. Under the guidance of the World Bank, the government adopted several policy changes aimed at liberalizing the trade sector. Over the years, it replaced most of the quantitative restrictions and import bans with tariffs, began rationalizing the tariff structure, making sure that the measures did not adversely affect revenues to avoid undermining the stabilization objective. The government also lifted most price controls, except on some essential commodities, mostly food items. Along with these measures, the government abandoned the fixed exchange rate, moving it to a managed float.

Jordan’s accession to the WTO in 2000 reinforced the pace of trade reform and liberalization. In 2004, the average weighted import tariff rate of 13 percent, a maximum rate of 30 percent, and a standard deviation of 15.7 percent featured the now more simplified Jordanian tariff structure (Saif, 2009:12). Non-tariff barriers and exemptions from import duties have now been eliminated significantly. The depreciation of the real effective exchange rate (REER) by 16.5 percent by the end of 2007 compared to 2002 has resulted in further exports in this period. This has to some extent also reflected the strong export performance of textile and apparel sectors, which benefit from US duty- and quota-

free access, making Jordan one of the top10 apparel exporters to the US in 2006. As a result of these developments, trade in Jordan has increased substantially since 1995, both in absolute terms, as well as a percentage of the GDP. As seen in Table 7, between 1997 and 2007, exports rose from around 20 percent of GDP to around 28 percent. However, the increase in imports was even more pronounced, rising from 56.6 percent of GDP in 1997 to 82.9 percent in 2007.

Table 7. Jordan's Trade Performance, 1997-2007

	1997	1999	2001	2003	2005	2007
GDP ⁹	5137.6	5767.3	6363.8	7228.7	9012.2	11721.5
Dom. Exports¹⁰	1067.2	1051.3	1352.4	1675.1	2570.2	3183.7
Dom. Exports (percent GDP)¹¹	20.8	18.2	21.3	23.2	28.5	27.8
Imports¹²	2908.1	2635.2	3453.7	4072.0	7442.9	9722.2
Imports (percent GDP)¹³	56.6	45.7	54.3	56.3	82.6	82.9
Trade Deficit (percent GDP)	-31.2	-23.0	-22.4	-19.6	-39.5	-39.3
Vol. of Trade (percent GDP)	77.4	63.9	75.6	79.5	111.1	110.1

Source: Saif, 2009:18

The increase in exports since the mid-1990s was led by an increase in exports of manufacturing, particularly in the labour-intensive manufacturing of clothes, which expanded twenty-fold between 1999 and 2005, as it benefited from advantages under QIZs relative to other countries (Saif, 2009:20). Other export commodities include food and animals, crude materials, and chemicals. However, this increase in exports has been more than outweighed by an increase in competition from imports, particularly in manufactured goods and equipment. One of the main imports to the Jordanian economy is oil-related fuel, which has experienced exponential increase in price since 2003 and cessation of access to subsidized fuel from Iraq and the Gulf. The higher cost of fuel together with increased competition from imports has threatened the survival of small domestic producers and their workers.

As seen above, between the mid-1990s and early-2000s, a decline in imports and an increase in exports led to a narrowing of the trade deficit. However, since 2003, the deficit as a share of GDP increased dramatically, due to large increases in imports –largely due to the rise in oil prices following the Iraq war and the stagnation of exports. Although exports increased in later years, the much higher increase in imports did not allow for a recovery of the trade deficit. Furthermore, the evolution of global terms of trade in 2007 and disruptions in mining sector production have resulted in an even larger trade deficit. The external current account deteriorated during 2004-05 and 2007, as a result of high levels of imports,

⁹ Nominal GDP at market prices, in JD millions.

¹⁰ Central Bank of Jordan, Monthly Statistical Bulletins, Table 33 (34): Summary of External Trade Developments.

¹¹ Ibid.

¹² Includes imports of non-resident agencies.

¹³ Ibid.

as well as the increase in the international food and fuel prices, which preceded the global economic crisis. The widening trade deficit together with the fluctuations in foreign assistance, have resulted in a widening of Jordan's current account deficit, reaching 17.5 percent of GDP in 2007. Although Jordan has often received the much needed financing to fill this deficit, the sources of this financing – foreign assistance, FDI and remittances – are far from stable external sources of revenue. This has been reflected in wild swings in Jordan's current account in recent years.

Any positive impact of trade liberalization on employment generation for Jordanian workers has been very limited and at times even negative. In addition, the impact of trade liberalization and export promotion varies by sector. For example, sectors such as manufacture of apparel have benefited from the liberalization of trade. Two sectors with the highest employment potentials are apparel and chemical manufacturing. Apparel manufacturing contributes to around 7 percent of all employment in Jordan and has experienced a job growth rate of over 33 percent during 2001-06. The Qualifying Industrial Zones (QIZs) presented an important opportunity for textile and clothing manufacturers from other countries to circumvent their quota restrictions. The production processes in the QIZs are primarily cutting, sewing, trimming, ironing, and packaging – all low-investment and labour-intensive processes. However, although the exports from this sector constitute more than a quarter of Jordan's total exports, wages and labour productivity remain very low. In 2003 for example, the average monthly wage for a QIZs worker was JD 130 compared to an average of JD 260 in the industrial sector (Saif, 2009). It is, however, worth mentioning that since these factories are located mainly outside of Amman, they employ mainly female workers especially from the rural areas who are entering the labour market for the first time.

Although QIZs have been responsible for a large share of the growth in exports and employment in Jordan since 2000, this trend has contributed little to employment of Jordanian workers. The share of QIZs' exports in total exports grew from 0.2 percent in 1999 to almost 28 percent in 2005, generating 54,000 new jobs during the same period, about one-third of which have been taken by Jordanian workers. Among the Jordanian workers who hold QIZs jobs, nearly two-thirds are women, many of whom are holding their first job. While these jobs provide significant benefits to the workers' families, the impact on unemployment has been negligible, as these women were unlikely to be in the labour force before being hired. The number of migrant workers, most of whom are on temporary contracts, swelled after 2004, when the government decreased work permit fees for migrant workers employed at the QIZs from the usual JD 300 per year to JD 150 (Razzaz et al., 2008). In addition, the QIZs provide few, if any, linkages to other parts of the economy and, therefore, have had little indirect job-creation effect. It is worth mentioning that following the global economic crisis Jordan experienced a decline in the economic activity of the QIZs, as investors began to relocate to competitor regional economies, resulting in a 20 percent decline in exports from the QIZs and a 23 percent decline in the employment of Jordanians in QIZs between 2008 and 2009 (ILO, 2010).

Diversification of Jordan's trade profile is one of the major challenges facing the external sector and its employment creation potential. Jordan's export basket remains narrowly based, and is concentrated in three sectors: chemicals (fertilizers and pharmaceuticals), clothing, and food products. In 2010, the main export commodities were clothes, potash, 'medical and pharmaceutical products', vegetables, fertilisers and phosphate – together constituting around 60 percent of total exports in 2010 (Central Bank of Jordan, 2011). This trade structure is not conducive to employment creation opportunities. The apparel and food industries have lost part of their competitiveness in recent years and their demand levels grow slowly, hence generating narrow profits for producers. Jordan's concentration in clothing has also led to only moderate increases in employment of Jordanians, with most of the jobs generated being low quality and low-wage categories. Finally, given the high levels of water scarcity in Jordan, agriculture can be an

unpredictable export base, with most of its jobs filled by migrant workers who are willing to accept the sector's predominantly low wages and poor working conditions.

Although chemical manufacturing does not create as many jobs as the apparel manufacturing, wages are often higher in the former – in most cases up to 50 percent higher than the average wage in the industrial sector as a whole. This, together with the high levels of productivity in this sector highlights the potentials of this sector for creating high quality jobs. Mining and quarrying is another sector with small scale but high wage employment potentials. Despite its capital-intensive nature, this sector relies on Jordan's main natural resources and also benefits from concessions for the private investors, making it a sector with potentials for expansion. Food production, though not a major source of exports, is another branch of the manufacturing with high potentials for employment generation. Agriculture has been one of the traditional sources of employment in Jordan. Agriculture's contribution to the GDP has declined from 6-7 percent in the early-1990s to around 2-3 percent during 2000-07. Water shortages, flight of workers to urban areas domestically and internationally in search of better jobs, liberalization of the agriculture and food sector, have resulted in the decline of this sector. By 2009, agriculture employed only 2.8 percent of total employed Jordanians, following a steady decline in recent years (Al Manar, 2010). As a result of this, most of the food consumed in Jordan has been imported, as Jordanian producers have lost competition in traditional fruit and vegetable categories. Low wages and working conditions, as well as lack of adequate employment laws and social protection for agricultural workers, have resulted in a departure of Jordanian workers from this sector and their replacement by migrant workers. The nationwide Agricultural Strategy, which started in 2009 aimed to 'upgrade the agricultural sector and assist workers in this field' through taxes on imports of some products and infrastructural projects to assist the agricultural production and exports (Jordan Times, 2009). In addition, the government's initiative entitled, 'Support Programme for the Unemployed and Agriculture Workers' aims to increase job opportunities for low-skilled agricultural workers, especially women.

In the wake of the global economic crisis, although the current account is likely to improve, a deficit is likely to persist thanks to an appreciation of the exchange rate in response to the fuel price hikes, pushing up the prices and reducing the competitiveness of Jordanian exports. During the first seven months of 2009, Jordan's exports and re-exports dropped by 15.6 percent, compared to the same period in 2008. This had a direct impact on the state of Jordan's industrial sector, which is one of the major contributors to the Jordanian economy. The value of total merchandise exports (domestic exports *plus* re-exports) increased by around 10 percent during 2010 to reach JD 4.5 billion. Similarly, the value of merchandise imports increased by around 8 percent, totalling JD 9.9 billion. As a result, the trade deficit expanded and the current account recorded a deficit of JD 579.9 million or 4 percent of GDP in 2010, slightly lower than the 2009 figures (Central Bank of Jordan, 2011).

Capital controls and investment in Jordan

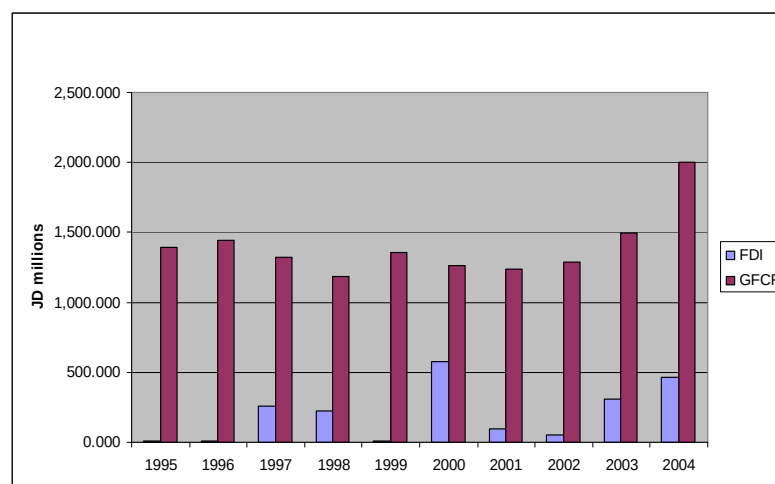
Jordan is an economy, which is highly dependent on external capital flows as the main source of government revenue. The levels of FDI not only influence the state of the economy but also have important consequences for employment, wages and working conditions of workers. The socio-economic instabilities that Jordan has been subject to in recent years, together with lack of internal investment-friendly infrastructure, have traditionally undermined Jordan's attractiveness to potential investors, particularly those from abroad. In 1990, Jordan still had fairly extensive capital controls in place. Export receipts were controlled, although inward capital movements were not restricted (including FDI), but permissions were required for outward flows. Repatriation of inward FDI capital was subject to approval. In 1994-95 the requirements regarding export receipts were liberalized, and in 1997 most controls on capital transactions were abolished although some minor restrictions were added in the following years.

The Jordan Investment Board (JIB) has in recent years attempted to provide various financial incentives and legal exemptions for domestic and foreign investors. There has been much effort in simplifying registration and licensing of investment projects. The Investment Promotion Law (IPL) of 2006 further aimed at removing the regulatory and bureaucratic obstacles to investment in Jordan.

According to the CBJ's most recent monthly reports, investments benefiting from the IPL totalled JD 1.7 billion during 2010, of which 13.5 percent were foreign investments, compared to JD 1.8 billion a year earlier (Central Bank of Jordan, 2011). According to the JIB, the levels of employment in some FDI sectors have increased in recent years; these include tourism (from 11,200 in 1999 to 44,000 in 2005), pharmaceutical manufacture (expected to grow to 7,000 by 2012) and the food and beverage manufacturing sector (expected to reach 54,000 employees by 2012) (Saif, 2009:29). The JIB also highlights employment growth in the communications sector, which added 5,094 employees in 2004 alone. However, given that the primary goal of JIB is to attract the maximum amount of investment in the country, the quality of the employment opportunities generated is of secondary importance to them.

As seen in the figure below, FDI was negligible till the late-1990s, amounting to less than JD 12 million each year, or less than 1 percent of total investment. In 2000, investment in privatized public entities increased, reflected in the unusually high levels of FDI. FDI started to increase sharply since 2002, from a low of 3.9 percent of total investment reaching (JD 58 million) to 17 percent (JD 309 million) and 18 percent (JD 461 million) of total investment in 2003 and 2004, respectively. By 2005, it had reached over JD 1 billion (Saif, 2009:25). FDI has been concentrated in three main areas: the QIZs and Special Economic Zones, which allows unrestricted access to the US market; the mining sector, which has become more attractive in recent years due to the increases in commodity prices; and services and other emerging sectors 'oriented to regional markets and clients', including tourism and medical services (IMF, 2008).

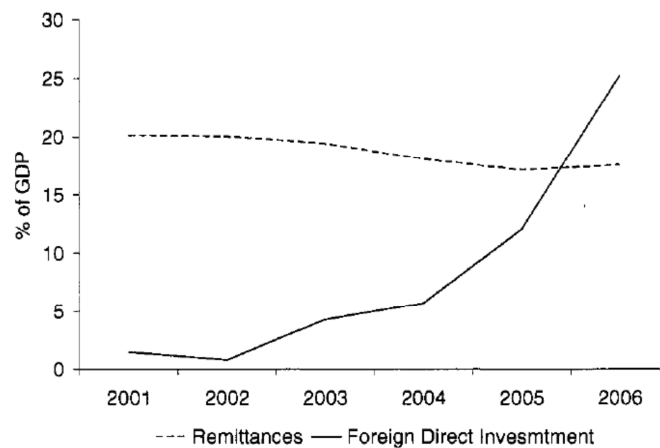
Figure 15. Jordan's FDI and Gross Fixed Capital Formation



Source: Saif, 2009:25.

A recent report by the United Nations Conference on Trade and Development (UNCTAD, 2006) ranked Jordan among the top 20 most attractive countries for FDI, due to its recent privatization of power, water, transport, and telecommunications services. However, despite the currently high levels of private foreign investment (figure 16), which have flooded the economy since 2001 because of soaring oil profits in the region and immigration of wealthy Iraqis, this may not be a sustainable trend. Oil-exporting Arab states have provided 96 percent of Jordan's total external financing in recent years, a trend which is likely to shift towards more investors from Asia in the coming years.

Figure 16. Performance in attracting external financing, 2001-06



Source: World Bank, 2008:25.

Despite these increases in the levels of investment, the impact of this on the labour market has not been as important and beneficial as expected. Higher levels of FDI may not only potentially provide workers with more employment opportunities but can also increase the total factor productivity of workers. However, as will be seen in the case of Jordan, the nature of the FDI, the sectors in which it has been concentrated, and the subsequent loss of local industries and investors have all minimized its beneficial employment and wage potentials. Also, if foreign investors switch to imported products as their inputs, put pressure on local wages through the forces of competition and hiring of cheaper foreign labour, and repatriate their profits abroad, they can harm the local economy and the country's capital flows, further reducing labour demand and wages. By raising the price-elasticity of labour demand, even relatively small increases in domestic wages due to FDI capital flows may cause a steep decline in labour demand. The ability of foreign investors to outsource cheaper foreign workers further reduces the bargaining power of local workers. Although evidence from around the world points to the fact that compared to domestic investment foreign investment can produce fewer jobs, in the case of Jordan, foreign investment has resulted in generation of low skill jobs.

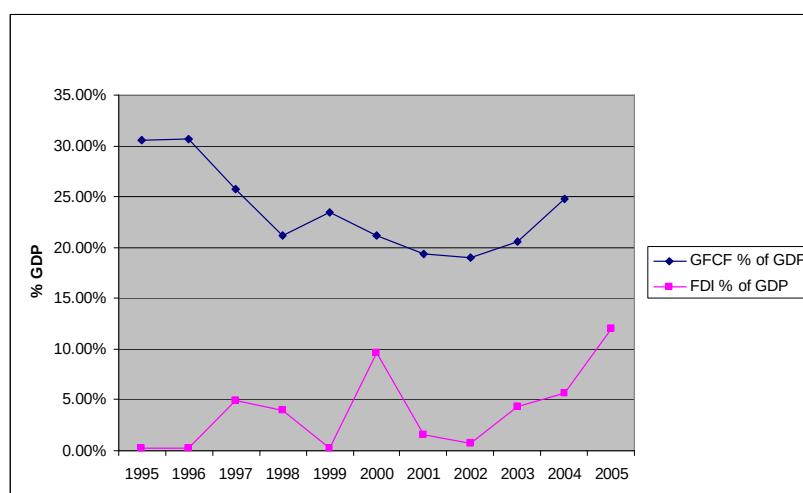
A large share of investment in Jordan goes into activities that do not directly generate jobs. For example, more than 35 percent of the FDI received in 2005 consisted of purchases of existing company assets (including the large privatization programme) by foreign investors, and about 15 percent comprised of purchases of land and real estate. Nevertheless, capital investment – that is, investment in assets (plant and equipment) directly involved in production that can generate jobs – continued to grow, reaching 24 percent of GDP in 2005. Furthermore, since mid-2004, about JD 492 million has been invested in the QIZs by foreign as well as domestic investors. However, given that in 2006 67 percent of the QIZs' workers were non-Jordanians, aided by Jordan's FDI structure and the option it gives to QIZs employers to bring foreign labour, much of the spillover employment effects of the foreign investment in QIZs is allocated to non-Jordanian workers and is 'outsourced' immediately (CARIM, 2010). These free trade zones allow for exemptions from personal income tax, as well as social services tax for non-Jordanian workers, and licensing fees for construction and land taxes.

Although some of these taxes were modified as a result of Jordan's membership of the WTO, there are several factors, which still result in lower wages and poor working conditions for the predominantly non-Jordanians working in the QIZs. Migrant workers often do not get paid on time; are not covered by the Labour Law while also prohibited from joining labour unions; in many cases they have longer working hours and sub-standard working conditions; and, are threatened by deportation since their immigration matters are often incomplete and controlled by their employer. In addition, the inflow of

un-skilled migrants employed under poor working conditions has put downward pressure on wages and has decreased worker bargaining power.

Although the levels of private domestic investment declined by half during the initial phase of macroeconomic reforms, from 26 percent of GDP to 11 percent between 1993 and 1998, ‘non-residential’ investment based on remittances, grew in this period. As the figure below demonstrates, the absolute levels of Gross Fixed Capital Formation (GFCF) declined from about 30 percent of GDP in the mid-1990s to around 20 percent in 2000. However, since then, the levels of domestic investment have increased and stayed strong. Domestic Jordanian investment grew from 19 percent of GDP in 2002 to almost 25 percent in 2004. In fact, latest annual figures show that in 2010, domestic investment that benefited from IPL¹⁴ accounts for 86.5 percent of total investments (JD 1.4 billion), while foreign investments accounted for the remaining 13.5 percent (Central Bank of Jordan, 2011). The relatively higher growth of FDI than GFCF as a percentage of the country’s GDP, as shown in the figure below, is an indication of the very low initial levels of FDI in the Jordanian economy compared to other economies of the region.

Figure 17. FDI and GFCF, 1995-2005 (in percent of GDP)



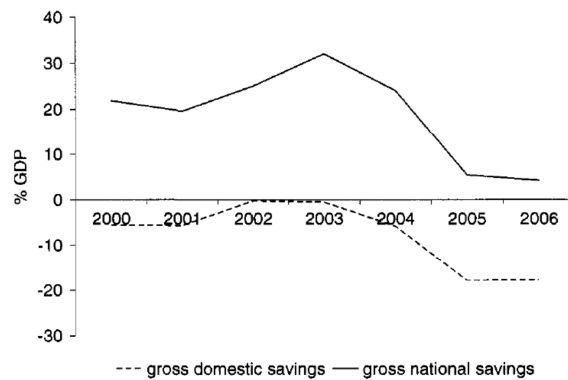
Source: Saif, 2009:26.

Financed by remittances and foreign aid, Jordan’s domestic investment has also failed to generate more employment, as it is often concentrated in non-productive sectors. As of 2010, investment in the ‘hotels’ sector accounted for 41.6 percent of the overall domestic investment, followed by the sectors of industry, ‘leisure and recreational compounds’, transportation, hospitals and agriculture, which accounted for 35.6 percent, 15.3 percent, 4.3 percent, 1.8 percent and 1.4 percent, respectively (Central Bank of Jordan, 2011). Much of the remittances from the Jordanian workers abroad have been invested in real estate, with little spill over effects to the rest of the economy in terms of revenues or employment creation.

¹⁴ It is worth noting that the nature and coverage of investments benefiting from the IPL differ from those of the Foreign Direct Investment (FDI) statistics in the balance of payments. The first indicator measures the size of planned investments by both domestic and foreign investors in a number of targeted economic sectors in accordance with the IPL, while FDI statistics measure the actual size of capital inflows from the outside world in various sectors, including the real estate sector.

One of the issues, which need to be taken into account regarding investment, particularly from foreign sources, is its impact on domestic savings. Reliance on foreign investment may become an important cause for concern in the future, given Jordan's low savings rate. As the figure below shows, gross national savings¹⁵ (which includes remittances) remains positive but has fallen as a share of GDP over the years and is among the lowest in the world. Gross domestic savings have been negative for many years. Low levels of domestic saving will weaken both the domestic demand base in the long run, as well as the resources available for expanding domestic investment levels. As argued before, particularly for a country like Jordan with high levels of dependence on external sources of finance, developing domestic sources of demand, investment and revenue should be among the top priorities of the government's economic development strategy. In order to reduce its vulnerability to shocks from flows of remittances and FDI, the government has taken steps to reduce its stock of outstanding debt and its current spending. Reliance on foreign investment will continue, but care should be taken to minimize vulnerabilities by maintaining high reserves of foreign exchange at the Central Bank and in controlling inflation.

Figure 18. Gross national savings and gross domestic savings, 2000-06



Source: World Bank, 2008:26.

The creation of new businesses is said to be crucial to job creation, export diversification and competitiveness. Cumbersome business licensing and permits requirements also make it difficult to start a business. While not the most important constraint faced by businesses, access to financing was identified as severe or major constraint by a third of small businesses. In recent years, the government has worked on encouraging small and medium enterprises and promoting public-private partnerships (PPPs) for its large infrastructure projects, such as the \$12 billion Jordan Red Sea Project and the \$5 billion National Railway (IISS, 2010). PPPs have been complicated by the financial crisis and the decline in investor confidence, pushing the government to step in to mitigate the risk by injecting equity and subsidies to sustain these projects. Jordan's answer has been to remove barriers and restrictions to market entry and to improve competitiveness. The governments could provide more up-front equity in projects and offer better revenue enhancement schemes, development rights and even subsidies to attract private investors.

In the light of the 2011 political uprisings taking place across the Arab countries, it is likely that the subsequent instability could destabilise the investment and capital flows in Jordan too, leading to a deterioration of the operating environment for businesses and

¹⁵ Gross national savings is the sum of gross domestic savings and net foreign savings.

investors. This could further widen the already large balance of payment deficit of the country, leading to a significant decline in official foreign exchange reserves or an increase in the levels of public debt. In order to maintain political stability in the light of recent events, it is likely that the government may opt for a relaxed fiscal policy in the coming months – a policy response similar to that of the post-economic crisis era. Already in January 2011, the government announced a hike in salaries and pensions along with a reduction in fuel taxes and a lowering of subsidised food prices (Trade Arabia, 2011). Although this can lead to some improvements in the living standards of the Jordanians, such a politically motivated (as opposed to economically-driven) policy may not be sustainable and can threaten the overall state of Jordan's public finances and the already large government debt level of around 60 percent of the GDP.

5. Conclusion and policy recommendations

The above analysis has highlighted a number of structural weaknesses in the Jordanian economy and labour market. These weaknesses stem mainly from the particularities of the Jordanian labour market and the economy's over-dependence on external capital flows. Economic reform and stabilisation strategies of recent years have not been able to address these structural weaknesses but have, in some cases, worsen them. One of the main lessons for Jordanian policy makers in recent years is that while conventional economic reforms may lead to some level of macroeconomic stability, they may not necessarily lead to a reduction in national unemployment.

The reasons for this are twofold: first, the country's growth strategies should be formulated within a developmental framework, which aims at diversifying the economy's structure, increasing productive investment in *domestic* economic sectors with high employment potential, and reducing the country's over dependence on external sources of revenue; second, there is a need for identification of the major challenges facing the Jordanian labour market and a careful analysis of the policies required in order to tackle the causes of these challenges – many such policies may well fall outside of the realm of macroeconomic policies. Therefore, in order to ensure that macroeconomic stability in fact benefits the majority of the Jordanian population, it is essential to work within a developmental framework in which economic diversification and creation of productive and decent employment opportunities are amongst the major objectives. In such framework, macroeconomic policies are some of the tools, which can be adopted and formulated in such way to achieve these objectives.

As mentioned earlier, most of Jordan's growth during the 1990s and the 2000s originated from the expansion of capital and labour force (mainly in the form of migrant workers), and not from higher levels of productivity in the economy. The relatively healthy levels of GDP and investment growth in the economy, despite creation of some jobs, have not brought about higher levels of employment for the *Jordanian* labour force, leaving unemployment and poverty as Jordan's major socio-economic problems. Therefore, the main task in the Jordanian economy is to overturn the related structural problems of the economic growth strategy, in view of the particular nature of the labour market in this country. For example, the low participation rates in the labour market mean that the existing economic policies aimed at expanding growth and investment will not be sufficient to reduce unemployment, they will, at best, encourage the labour market participation of those previously economically inactive. This implies that the present problem of a high rate of unemployment is likely to persist, and that unemployment rates will decline slowly, if at all, until the latent reserve of labour is exhausted. Hence, in order to speed up this process and to reduce the number of those unemployed, more targeted structural policies are required.

The broad areas of policy priority should be a more efficient allocation of investment and government resources in employment-intensive sectors, reduction of the labour market segregation, minimising the mismatch between the skills of the labour force and the demands of the labour market, and creation of a strong domestic demand base as a driving force for economic growth, particularly in the post-crisis era, which has exposed Jordan's vulnerability to regional and international waves of aid, remittances and capital flows. This requires structural shifts in the country's macroeconomic spheres in order to achieve the above objectives. Below are some areas which merit careful attention in this regard and which have been discussed in detail earlier in the paper:

- *Reducing voluntary unemployment:* increased economic growth in the country may lead to a reduction in the number of those 'involuntarily' unemployed, but is insufficient to reduce unemployment among those 'voluntarily unemployed' – who constitute the bulk of the unemployed in Jordan. Hence, it is vital for the government to distinguish between these two groups of unemployed persons, and to target specific policies aimed at raising the

productivity and wages of employment opportunities in order to attract those voluntarily unemployed. This, in return, requires further diversification of the economy and increase in the productivity and competitiveness of the employment-intensive sectors to ensure better employment conditions and pay. In line with this, trade, investment, industrial and agricultural policies need to be revised with the aim of increasing these sectors' competitiveness, productivity and capacity for high quality employment creation for the Jordanian labour force.

- *Rethinking the government's labour immigration policy:* given the significance of migrant workers for the Jordanian labour force, it is important that the government coordinates its labour immigration policies with its macroeconomic and labour market policies, as well as its employment strategy. Following from a long phase of relaxed government immigration policies, which have often provided strong incentives for immigration of migrant workers to Jordan, the government's national strategy for employment announced in March 2011 sets out as its objective the replacing of guest workers with local labour in most sectors of the economy over the next decade. Having said that, it should be borne in mind that although useful in the short- and medium-terms, policies aimed at increasing the employment of Jordanians relative to migrants should go beyond educational and 'immigration' policies, and focus on boosting demand by increasing the capacity of the economy for generating productive, high-wage, decent employment opportunities in a wide array of economic sectors.
- *Reducing dependence on external sources of revenue:* Jordan's reliance and over-dependence on external sources of financing such as aid, FDI, and remittances, is one of the major weaknesses of the economy, which has made it vulnerable to regional and global waves of economic and political uncertainty. For example, as discussed earlier, remittances, as a form of unearned income or rent, can reduce labour supply by acting as a disincentive for other members of the recipient households to work. They can also have a significant impact on appreciating Jordan's real exchange rate, hence reducing Jordan's competitiveness and widening its current-account deficit. Similarly, foreign investment and aid flows can be erratic and not necessarily promoting backward and forward linkages with the local economy. In order to move away from this dependency, the government needs to focus its efforts on expanding the scale, productivity and competitiveness of domestic industries and investment projects. Developing domestic sources of revenues will not only act as a more sustainable source of government revenue, but also, by developing domestic demand, can expand the economy's capacity for generating more sustainable employment opportunities.
- *Maintaining government expenditure:* in response to the 2008-09 global economic crisis, the government of Jordan has been encouraged to adopt further measures aimed at fiscal consolidation through cutting expenditure. However, in this post-crisis phase, such austerity measures should be taken with much caution, ensuring that strategic sectors such as social protection, education, active labour market policies and financial mechanisms to support entrepreneurship are protected from future cuts and even strengthened to ensure a quicker and more job-rich recovery. In addition, maintaining government expenditure at this point in time is essential for preserving (and expanding) the levels of domestic demand as a more solid basis for future growth and employment generation.
- *Fiscal expenditure vital given the state of the private sector:* Maintaining government expenditure is even more vital given the weak state of the private sector in Jordan. As discussed in this paper, privatisation in Jordan has done little to generate new employment opportunities, as it has largely been a result of a shift in the ownership of the companies from public to the private sector. In addition, the small size of the private sector firms, with micro- and small enterprises constituting 98 percent of all firms in Jordan, and their attempt to increase worker efficiency through reducing costs, limit the employment capacities of this sector. In this situation, given the high rates of unemployment, any

government fiscal consolidation will undoubtedly focus on reducing the cost of labour rather than its quantity. This, in turn, has the danger of reducing the levels of purchasing power and demand in the economy, hence, encouraging further voluntary unemployment.

- *Protecting social protection expenditure:* As discussed in this paper, there is no evidence that Jordan's relatively generous social security system has caused a disincentive to employment. However, sustainability and expansion of such a system needs to be considered carefully, given the levels of fiscal deficit and the high levels of demand on government expenditure in the aftermath of the global economic crisis and following the recent political unrest across the Arab world. Furthermore, proposed reforms of the social protection policies need to focus on increasing the efficiency of the *composition* of the social protection structure, aimed at not only creating an incentive to employment by making employment opportunities more secure and attractive, but also to encourage links to programs that permit monitoring of beneficiaries' job search and their acceptance of job offers.
- *Rethinking the dependence on the US dollar:* following the global financial crisis, Jordan experienced a slowdown in credit activity. Jordan's fixed exchange rate, its dependence on the US dollar, and the widening of the interest differential between monetary policy rates in Jordan and the United States were behind the slowdown of credit flows in the Jordanian economy. Given the decline in the value of dollar in recent years and its risks for the Jordanian financial structure, the government of Jordan needs to review the Dinar's peg to the US dollar and avoid further tightening of monetary policy in order to stimulate more lending and investment in the economy. The government's conservative lending policy has resulted in the closure of dozens of small and medium-sized projects and businesses, which have not been able to obtain loans. Such a policy can only deepen the recent global economic crisis. Hence, the Jordanian government needs to adopt policies, which would stimulate credit supply, facilitate lending and increase the credit flows.
- *FDI for employment creation:* high levels of FDI in Jordan have not been accompanied with notable employment creation for the Jordanian labour force. This has been to a large extent due to the composition of this foreign investment and the type of economic activities and employment opportunities that they have given rise to. FDI has been concentrated in three main areas in recent years: the QIZs, the mining sector, and services and other emerging sectors 'oriented to regional markets and clients', including tourism and medical services. The low wages and poor working conditions at these basic manufacturing and services sectors have made them unattractive to the predominantly skilled Jordanian workers. In addition, the foreign investor's desire to minimise their costs and the low levels of spill over from these investments to the rest of the economy have further limited their contribution to employment creation. Therefore, a revision of the foreign investment policy, one of the main pillars of Jordan's recent economic growth, is vital in order to increase its employment spillovers. In line with this, the government needs to strengthen the links between Jordan's trade and investment policies to the local economy and labour market through enhancing the forward and backward linkages and encouraging more Jordanian investment in high value-added sectors, which have the potential for creation of productive and decent employment.
- *Promoting domestic investment:* In the long-term, the government needs to reduce its overdependence on foreign investment and replace it with more secure and sustainable (domestic) sources of revenue. As seen earlier, financed by remittances and foreign aid, Jordan's domestic investment has also failed to generate more employment, as it is often concentrated in non-productive sectors such as construction, housing and finance. A renewed concentration of investment in high productivity industrial, agricultural and services sectors, as well as high value-added exports, can enhance the employment potentials of domestic investment flows. In addition, the sources of financing domestic

investment need to move away from external funding to domestic resources. In line with this, the government needs to increase the levels of domestic savings. The current low levels of savings in Jordan can be a cause for concern, given the country's over-reliance on foreign investment. Healthy levels of savings will not only feed into the country's domestic investment but also strengthen the demand base in the long run. Hence, the government needs to reassess its banking, interest rate and investment policies in order to stimulate larger levels of savings, and strengthen the link between these savings and productive investment opportunities.

- *Trade diversification:* The composition of Jordan's trade and trade policy has so far failed to generate sufficient and decent employment opportunities, given its concentration on basic manufacturing, low-wage chemicals, clothing, and food products. Hence, trade diversification into high value-added products should be on top of the country's trade policy agenda. Furthermore, given that much of Jordan's recent trade has taken place through the QIZs, which have primarily employed migrant workers, a closer coordination between the country's trade, investment and immigration policies are required in order to increase the chances of the Jordanian workers and the local economy benefiting from expansion of the trading sector.
- *Supporting small businesses:* while aware of the limited employment generating potentials of SMEs, maintaining the financial and regulatory support to these businesses is important in preserving their existing employment levels and to possibly allow for their further expansion. Hence, tight fiscal and monetary policies at this juncture of post-crisis environment can endanger employment opportunities in these firms. As mentioned above, by reducing lending and credit flows, the government's tight monetary policy has already pushed many SMEs out of business, adding to the country's already heavy unemployment burden. In line with this, the government's objective, as set out in the 2011-13 Executive Development Plan, of increasing funding opportunities to support small and medium projects for individuals and institutions, especially in the poorest areas, is a welcome move.
- *Labour supply and demand coordination:* finally, an important component of the government's employment creation strategy should focus on the labour market policies and a closer coordination between the labour demands in the economy and what the labour market supplies. The government's 2011 national strategy for employment also acknowledges the importance of striking a balance between demand and supply in the labour market. In line with this, the government should improve the employability and job prospects, particularly of the young, educated, female and poor sections of the labour market, while moving them to the top of the social protection agenda. Closer collaboration among service providers will be important to avoid a fragmented system in which young people leave school without skills, a job, or a plan for obtaining either. In addition, more systematic linking of social protection schemes to labour market programs will be required. These schemes require further government funding and a need for a wider fiscal and monetary policy space.

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