Jobs for Iraq: an employment and decent work strategy

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CHAPTER 1. INTRODUCTION

The employment and labour market situation in Iraq has remained extremely precarious. Data from different sources covering the period from 2004 to the end of 2006 suggests that as many as 1.3 to 2 of the 7 million-strong labour force were unemployed. Unemployment among the young (15-24 years), at around 30 per cent, has been nearly double the overall unemployment rate. An analysis of the employment generating impact of the reconstruction effort during these years suggests that against these high levels of unemployment and high growth of the labour force, it did not contribute sufficiently to improving the situation. This book[1] focuses on the critical role of employment and creation of decent work in facilitating peace in Iraq. It argues that reducing the high degree of unemployment could contribute to peace and stability in the lives of people, communities and the country. Iraq's difficult transition process is compounded because of the problematic labour market situation which continues to be a source of grievance and social unrest. Unemployment, especially amongst the young and dislocated workers, feeds the conflict cycle, and in consequence further hampers reconstruction, investment and the creation of jobs.

This book is based on an analysis of the labour market situation and outlines a set of policy measures needed – as far as security conditions allow – first to

[1] A major part of the work on this book was undertaken for the International Employment Conference on "Jobs for the Future of Iraq", held in Amman in December 2004 with further analytical work conducted in 2005 and 2006. Some recent data on unemployment was added to the study in early 2007. The 2004 International Conference was organized and led technically by the ILO within the United Nations Development Group (UNDG) Trust Fund for Iraq. The Conference brought together 145 national and international participants. The Government of Iraq was represented by the Minister of Labour and Planning and by more than 70 representatives from ten ministries and the Central Bank. The Conference was also attended by representatives of Iraq's employers' and workers' organizations, representatives of local authorities, and leading academics and experts. On the international front, all major United Nations agencies involved in the reconstruction of the country were present, as were the World Bank, the International Monetary Fund (IMF), and key international donors (DFID, UK; USAID, USA; JICA, Japan; and the EC). Representatives from main donor countries were also present.

tackle the immediate problem of a very high level of unemployment and then to ensure that economic growth leads to productive, remunerative and decent employment. This requires that the ongoing reconstruction programme create the greatest number of jobs possible. In the medium and long run the goal should be the setting up of a well functioning, efficient, equitable and rights-based labour market which will ensure that the economy moves towards and maintains a high level of employment and creation of decent jobs.

The book also argues that careful consideration should be given to the sequencing of reforms and to put in place appropriate safety nets and an affordable system of social protection. The employment consequences of reform need to be considered in the wider context of tackling massive unemployment. In the medium term, the reform process must be developed in a way that leads to more and better employment opportunities in the private sector.

Amid an increasingly complex security situation, unemployment and precarious work in Iraq are central issues. Beyond the need to restore security and the enforcement of law, proactive interventions and policies for job creation must be part of an integrated strategy for peace and recovery. The problems of violence, lack of development and unemployment are closely intertwined. Failure to address employment and labour market issues in the present crisis would endanger both security and development. Therefore they need to be addressed concurrently to ensure that all citizens and communities have a stake in rebuilding the country.

Within data and other limitations, this book presents key characteristics of the labour market and employment situation and an analysis of the job generating impact of the reconstruction and aid programmes. It identifies critical issues to secure jobs and livelihoods in Iraq. These include the need for active labour market policies, developing strong labour market institutions and creating conditions for the development of micro, small and medium-sized enterprises. It also addresses some overarching issues relevant to Iraq's transition, in particular the challenges of setting up an affordable social protection system and the sequencing of reforms of State-owned enterprises in a manner that minimizes negative impact while ensuring growth of a vibrant private sector.

Giving priority to these areas could contribute to developing sound and sustainable mechanisms for productive and decent employment, even if in a limited way in the present unsettled conditions, but certainly when the security conditions allow them to be fully implemented.

EMPLOYMENT AND DECENT WORK STRATEGY: MAIN POLICY RECOMMENDATIONS

The main policy recommendations that emerge from the study are part of an integrated employment and decent work strategy whose aim is not to create just any employment but Decent Work in which fundamental principles and rights at work are fully respected, which provide productive and adequately remunerative employment, there is an affordable degree of social protection and adequate opportunity for social dialogue between the government, employers' and workers' organizations. In this context the main policy recommendations from the study are as follows:

- Increasing the employment intensity of the reconstruction effort through appropriate choice of techniques and the reorientation of project choices and increased implementation towards local and municipal level activities;
- Adopting a macroeconomic framework which encourages domestic investment, enterprise creation and growth of employment generating sectors through appropriate incentives;
- Investing in skills development and developing a demand-driven training system in order to develop a competitive and diversified economy;
- Strengthening labour market institutions, including workers' and employers' organizations, and practices which, when functioning effectively, will make the path to raising employment levels smoother and address the social dimension of economic reform;
- Making decent employment explicit in the national development strategy and developing the institutional capacity to monitor labour market developments and propose appropriate policy responses;
- Strengthening the growth of small and medium-sized enterprises through reform of the policy and regulatory environment, provision of business development services and microfinance, promoting entrepreneurship among youth, encouraging economic empowerment of women and linking large and medium-sized enterprises;
- Reconstructing of the social security system in the context of transition;
- Seeking the views and support of independent organizations of employers and workers in the formulation and pursuit of employment policy;
- Cooperating with women's organizations in order to promote equal employment opportunities and conditions without any discrimination;
- Preparing the economy to adapt to structural change and absorb new technologies and global competitiveness.

INTERNATIONAL COMPACT WITH IRAQ

A recent development has been the signing in May 2007 of "The International Compact with Iraq" between the Government of Iraq, the United Nations and the World Bank.[2] The Compact is a five-year national plan that includes benchmarks and mutual commitments from both Iraq and the international community with the aim of helping Iraq on the path towards peace, sound governance and economic reconstruction.

The Compact includes a set of economic and social policy benchmarks including in the medium term reducing unemployment by half, doubling the non-agricultural labour force participation of women, developing a multi-pillar social insurance scheme in order to protect the most vulnerable from dislocations caused by economic and political change and the development of an action plan for investment and economic recovery.

It is hoped that the analysis undertaken in this study and the policy conclusions and recommendations based on an analysis of the labour market in Iraq will strengthen the contribution that the United Nations System "Delivering as One" can make towards realizing the goals and benchmarks that have been outlined in the Compact. The "Toolkit for Mainstreaming Employment and Decent Work" recently adopted in April 2007 by the UN system Chief Executives Board for Coordination can also serve as an important tool for realizing this goal.[3]

[2] See the Government of Iraq, United Nations and the World Bank, 2007.

[3] See United Nations, Chief Executives Board for Coordination, 2007.

CHAPTER 2. EMPLOYMENT SITUATION

LABOUR FORCE, EMPLOYMENT AND UNEMPLOYMENT: THE BENCHMARK

This section provides a picture of the labour force, employment and its distribution among major activities and sectors using the benchmark year of 2004. The basic source of information is the Iraq Living Conditions Survey (ILCS), implemented in 2004 by the Iraqi Central Organization for Statistics and Information Technology (COSIT) in cooperation with the United Nations Development Programme (UNDP) and the Norwegian Fafo Institute for Applied International Studies[4]. This is supplemented with the results of the Labour Force Survey (LFS) conducted by COSIT in two phases – the first in September 2003 and the second in July 2004[5] and with some unpublished data from the same source for November-December 2006. Estimates of population size in this section are based on the ILO dataset, which shows a higher aggregate population for Iraq than the ILCS.[6]

The picture put together in the following tables is not claimed to be anything more than a *possible state of affairs* concerning the labour force, employment and its distribution in Iraq during 2004 and 2006. The reality may have differed from this scenario in significant ways and some of those possibilities are raised in

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[4] See United Nations Development Programme, *Iraq Living Conditions Survey, 2004, Volumes I* and *II*, Baghdad, 2005.

[5] The ILO dataset uses the estimates in the United Nations Demographic Yearbook and applies them to the ILCS. At the time the ILCS data were being processed, the UN estimates were not available. The UN estimates of aggregate population are about 3.4 per cent higher than the COSIT estimates. They are also higher than the estimates implied by World Bank's figure shown in *World Development Indicators 2005*. This paper uses the UN estimates simply to ensure consistency with the other papers in this ILO-sponsored project, which uses the UN data.

[6] This, however, makes little real difference to actual employment and unemployment estimates, because the working age population – those 15 years old and above – are almost identical from the two sources.

the discussion below. Given the available information, however, this appears to be not only a possible, but also a *plausible* scenario.

Table 2.1 presents the broad aggregates about population, labour force and employment in 2004. Labour force is usually defined as consisting of those who are 15 or above and either working or looking for work[7]. To this is added those among 15+ age groups who responded to the ILCS (2004) by stating that they were not looking for work, because they believed that there was no work available. These are the so-called "discouraged workers" who have "withdrawn" from the labour force, because they do not expect to find employment. Economists however have long argued that they should actually be included as members of the labour force. In Iraq's case, this argument is strengthened by the unusually low participation rate even after their inclusion, an issue to which we return below.

Table 2.1: Population, labour force, employment and unemployment in Iraq: 2004 (Absolute numbers in thousands)

	Total	Male	Female
Population	28,057	14,207	13,850
Working-age population (15+)	16,447	8,295	8,152
Economically active & looking for employment	6,735	5,613	1,122
Discouraged workers	649	481	168
Total labour force	7,384	6,094	1,290
Participation rate[8] (%)	44.9	73.5	15.8
Employment	6,015	5,037	978
Unemployment rate[9] (%)	18.5	17.3	24.2
Dependency ratio[10]	2.8		

Source: Population and working-age population are from the ILO database. All other estimates are based on the Iraq Living Conditions Survey (2004) data.

Note that the labour force, as a proportion of the population, is extremely small. In other words, the dependency ratio, i.e. the number of individuals supported by a member of the labour force, is exceedingly high – 2.8 – not counting the

[7] Note that no maximum cut-off age, e.g. 65, has been used. The ILCS (2004) has not done so and this section could not have applied such a cut-off age for sectoral employment. There is little evidence that such a cut-off age applies in reality and, even if it did, the error due to its neglect is likely to be small, because the proportion of the population 65 years old and above is low – less than 3 per cent.

[8] *Participation rate* is total labour force as a percentage of working-age population.

[9] *Unemployment rate* is the number of unemployed (the difference between total labour force and the employed) as percentage of total labour force.

[10] *The dependency ratio* is the number of dependents per member of the labour force *not counting the worker him/herself*, i.e. the population divided by the labour force minus one.

worker him/herself. The average ratio for all the Low-Income Countries (LIC), according to the World Bank classification, is 1.22, and for the Middle East and North African (MENA) countries 1.79.[11] This means that even if all the members of the labour force, including the discouraged workers, were fully employed, Iraq's economy would be under the debilitating burden of each worker having to provide for the livelihood of another 2.8 non-workers, which, under similar assumptions, is 130 per cent higher than the burden that would be carried by a worker in an average LIC and 56 per cent higher than the burden carried by a worker in a MENA country.

This disadvantage for Iraq is due to two reasons: an age-structure heavily skewed in favour of the young and a low ratio of labour force to working-age population. The former phenomenon is a general feature of the LIC countries and the MENA region; but it is worse in Iraq. According to UN data, the proportion of the population below 15 years old was more than *41 per cent in Iraq* in 2004. According to the World Development Indicators, the average in 2003 was much smaller: 36.9 per cent in the LIC countries, 34.6 per cent in the MENA countries, and 29.5 per cent in neighbouring Iran (World Bank, 2005)[12]. Among the factors that led to this unfavourable age structure in Iraq are the high birth rate and the high mortality rate for the young in recent wars, especially the Iraq-Iran war of the 1980s (see Annex A). Perhaps the high fertility rate has been the decisive factor. Both Iraq and Iran had high youth mortality throughout the 1980s, but the age structure for Iran suffers from far less of an imbalance and the principal difference between the two countries that seems to explain this phenomenon, is the *difference in birth rate: 18 per thousand in Iran* as compared to *29 per thousand in Iraq*[13].

Skewed age structure is not the only reason for the low ratio of labour force to population. Labour force, as a proportion of working-age population, is also low: just 73.5 per cent for men and 15.8 per cent for women. The following table presents this data for Iraq and for some comparators.

Table 2.2: Labour force participation rate (percentages)

	Male	Female
Low-Income Countries	86.3	54.6
Middle East & North Africa	80.8	34.5
Iran	80.2	33.8
Iraq	73.5	15.8

Source: World Development Indicators 2005

[11] These figures are estimated from the population and labour force data for these country groups shown in the World Bank World Development Indicators 2005.

[12] *World Development Indicators 2005* reports the figure for Iraq in 2003 as 39.4 per cent.

[13] See *World Development Indicators 2005*.

It is worth noting that the participation rates for Iraq actually include the estimated discouraged workers in the labour force while discouraged workers are not included in the same for the comparator cases. Even so, the participation rates are far lower than for the countries that share similar culture and religion. This is true for both men and women, but strikingly so for the latter. While low labour demand may be an important factor, it appears that there are very important supply-side factors at work too. Civil unrest and insecurity may have caused women and, to a lesser extent the population in general, to stay at home. Free food rations may have made such behaviour affordable.

The high unemployment rate has exacerbated the disadvantage due to the high dependency ratio. Including "discouraged workers", who did not identify themselves as members of the labour force, because no job was available, the unemployment rate is 18.5 per cent.

The official national labour force surveys by COSIT have come up with unemployed rates that are substantially higher. In July 2004 they were estimated at 26.8 per cent (see Table 2.3) but the more recent unpublished data for November-December 2006 estimates this at 17.6 per cent (16.28 for males and 22.78 for females) which is nearer the Fafo estimate. The differences between the July 2004 and Fafo estimates are partly explained by the definition used for measuring unemployment (see Annex B) and the sample frame coverage. It is possible that these were corrected for in the November-December 2006 survey.

Given the unsettled conditions in which the surveys took place, any unemployment estimate would have been tentative. The important thing is that, even if we take the unemployment rate estimated on the basis of the ILCS data or the COSIT November-December 2006 survey, it is high by any absolute standard. In most developing countries the rate of open unemployment, measured by surveys of households and labour force, is much lower, typically less than 5 per cent. The high open unemployment rate together with the above factors means that each employed person carried the staggering burden of 3.66 non-working persons on average in 2004.

Table 2.3: Results of labour force survey (LFS) by COSIT: 2003 and 2004 (percentages)

	LFS October 2003	LFS July 2004
Labour force participation rate	44.1	48.5
Unemployment rate	28.1	26.8
Male labour force participation rate	73.7	77.4
Male unemployment rate	30.2	29.4
Female labour force participation rate	14.2	17.9
Female unemployment rate	16.0	15.0

Source: Labour Force Survey (LFS) in September 2003 and July 2004 conducted by the Central Organization for Statistics and Information Technology (COSIT)

Table 2.4: Unemployment rate by age groups – COSIT November-December 2006 (percentages)

Age group	Male	Female	Total
15-19	35.90	25.85	33.73
20-24	24.90	37.70	27.64
25-29	16.51	24.28	18.22
30-34	11.77	21.12	13.67
35-39	8.31	17.86	10.29
40-44	7.70	15.61	9.42
45-49	6.84	11.73	7.88
50-54	8.49	9.82	8.75
55-59	8.67	10.69	9.01
60-64	10.77	6.65	10.29
66 +	7.51	39.88	11.88
Total	**16.28**	**22.78**	**17.64**

Source: COSIT (Unpublished data)

Table 2.5: Unemployment rate by region – COSIT November-December 2006 (percentages)

Governorate	Male	Female	Total
Ninva	25.01	40.08	27.48
Sulymania	5.89	32.96	13.75
Kirkuk	6.43	12.92	7.90
Diyalla	17.64	24.17	18.47
Baghdad	14.82	19.61	15.74
Babil	16.85	11.80	15.05
Kerballa	17.14	26.91	18.53
Wassit	7.26	13.66	8.82
Sallah El-deen	20.90	10.09	18.36
Najaf	15.82	32.97	18.90
Qadesya	19.26	22.26	19.89
Muthana	23.13	21.95	22.94
Theqar	24.68	44.42	27.78
Messan	14.49	38.01	17.91
Basrah	11.54	21.01	12.89
Total	**16.28**	**22.78**	**17.64**

Source: COSIT (Unpublished)

While the open unemployment rate is high, the rate of underemployment, defined as the proportion of employed workers who would like to work longer hours, as given by the ILCS (2004) survey is very low, just 3.5 per cent of those employed. This is quite consistent with the finding in the same survey that the median hours of work per week are high: 48 for men and 35 for women.

Why is the unemployment rate so high?

How should one interpret these unemployment and underemployment rates? The rate of open unemployment is high; and the rate of underemployment, measuring the proportion of those who are currently employed looking for additional hours of work, is very low. These figures are in sharp contrast to the characteristics of the labour market in a typical developing country where the rate of unemployment is low and the rate of open underemployment is very high. A great deal of additional information and analytical research on Iraq's labour market is needed to resolve this issue.

On existing evidence, many of these features in Iraq seem to derive from the *preponderance of formal employment in a highly urbanized labour market in which the State has been the dominant employer*. Compared to a developing country with similar living standards, a much higher proportion of employment in Iraq consists of the formally employed, a very high proportion of whom are on the Government payroll. *Government alone provided employment to 30 per cent of those who have work*. Loss of employment in these categories of workers cannot be hidden in the form of disguised unemployment that predominates elsewhere in the developing world.

But then has job loss not been higher in reality than the surveys show? Indeed, as the ILCS finding shows, the formal loss of jobs due to the war of 2003 and its aftermath may have been limited. This of course does not mean that 82 per cent of the labour force in 2004 was productively employed, as the ILCS survey explains. Most of those employed in the formal sectors, especially those in the State sector, have probably been engaged in little productive employment: many enterprises have simply been shut, while others have been operating at a fraction of their capacity. Much of the labour force has probably been sitting idle much of the time. Despite having full-time jobs as long as they belonged to the payroll, much of the labour force's wages and salaries had lost their real value. No matter how many hours were spent without actually working, they were not seeking additional hours of work. It is in this sense that the rate of open unemployment in 2004 was 18.5 per cent and the rate of underemployment in 2004 was only 3.5 per cent, as the ILCS survey suggests. *Yet the proportion of Iraq's potential human power that was the number of productively employed in 2004 was almost certainly quite low, a situation that has changed little since then*.

SECTORAL DISTRIBUTION OF EMPLOYMENT

According to the ILCS, employment in the mining sector, of which employment in the oil sector is a part, contributed only 0.4 per cent of total employment in 2004. On this evidence, the sector that produced about three-quarters of total GDP in 2005 contributed virtually nothing to the nation's employment.
Much employment is in the "non-traded sectors". In 2004, commodity production in agriculture and manufacturing employed less than a quarter of the population. There are, however, *incongruities* in labour allocation. According to the *ILCS survey*, only 17 per cent of employment was in agriculture and this appears to have changed little over more than a decade (see Table 2.6). Yet, according to other surveys, agriculture's share of non-oil GDP appears to have been high in the past. Thus the share of agriculture in GDP is reported to have been 30.8 per cent for 2000 by the *UN Yearbook of National Accounts Statistics* (2001)[14] and 29.4 per cent for 2003 by COSIT *(Annual Statistical Abstract, 2003)*. According to estimates from the *International Monetary Fund (2005)*, the share of agriculture was even around 40 per cent in 2003. If anything, the share of agriculture in non-oil GDP may have risen in the post-war period. It is unlikely for agriculture to face as much dislocation as non-farm economic activities do during periods of turbulence. If these figures and assumptions even approximately resemble reality, then labour productivity in Iraq's agriculture sector would be much higher than labour productivity in non-agricultural sectors including manufacturing. Whether this represents yet another special feature of Iraq's economy or whether it is a statistical quirk, is for the moment difficult to resolve.

Table 2.6: Sectoral distribution of employment in 2004 (% of total employment)

Agriculture, forestry & fishery	17.0
Manufacturing & mining	7.3
Construction and utilities	10.5
Trade, hotels, restaurants & repair services	21.7
Transport, storage and communications	10.0
Finance and real estate	1.4
Public administration and defence	17.8
Education, health & social work	10.3
Other services	3.8

Source: Iraq Living Conditions Survey, 2004

[14] ILO, *Employment in Iraq: Outstanding Issues*, paper prepared by the ILO for the Conference on Employment in Iraq, Amman, December 2004 (Geneva, November 2004), Table 2.4 quotes these data.

Table 2.7: Employment by type of employer in 2004[15]

	Per Cent	Total (Millions)
Local or central Government including Government companies	29.7	1.794
Private companies	49.2	2.974
Cooperative or joint sector	2.9	0.177
Iraqi army	0.7	0.043
Family business	12.2	0.738
NGOs	3.7	0.222
Private households & others	1.7	0.101

Source: Iraq Living Conditions Survey, 2004

How much turmoil did the war of 2003, the subsequent occupation and aftermath cause to employment in Iraq? It is not possible to document the extent to which *those who were employed before the war* lost jobs and/or moved to new jobs. The ILCS however provides information about how many of *those in employment in 2004* had lost their previous jobs and/or moved from a previously held job. Eighty eight per cent of the employees in the public sector, including local and central Government and Government companies, were employed in the public sector prior to the war. The proportion is 94 per cent for the employees of private companies, 68 per cent for cooperative or joint sector, 95 per cent for family business, 78 per cent for the NGOs and 60 per cent for private household employment. It is only for the Iraqi army that the proportion was low: only 11 per cent of its members in 2004 were employed by the army prior to the war, which could be a result of the decision of the occupying powers in 2003 to discharge Iraq's army of some 400,000 soldiers. *It therefore seems that most people outside the army in 2004 were in the jobs in which they were employed before the war*. The turmoil in terms of formal job loss and involuntary relocation may have been limited. The decline of the economy appears to have taken place long before the war of 2003.[16]

[15] There are small errors, possible due to rounding

[16] Another group most severely affected by post-2003 dislocation were those who lost their jobs through the "de-Baathification" directive initiated by the occupying powers. According to most estimates these were about 30,000-40,000. This directive was relaxed in May 2004.

PROFILING UNEMPLOYMENT

A clear understanding of who is unemployed has important implications for designing the policy response to the unemployment problem. It is also vital to understand that the incidence of unemployment is not equally distributed throughout Iraqi society, but that it affects some groups much more than others. The most affected group in 2004 and in November-December 2006 was young men and women between 15 and 24 years old (Tables 2.8 and 2.4).

Table 2.8: Unemployment rates by age and gender in 2004 including "discouraged workers" (percentages)

	Total	Male	Female
Total	18.4	17.2	24.0
65+	17.1	14.7	31.9
55-64	10.0	9.5	12.5
25-54	12.7	11.2	18.8
15-24	33.4	32.1	40.6

Source: Iraq Living Conditions Survey, 2004

The 2004 ILCS data also suggest that statistically the risk of being unemployed rises with the level of education. Unemployment was as high at 37.2 per cent among *young men with secondary or tertiary education* in 2004. For men of the same age group with no formal education it was at 31.8 per cent. Thus, the problem of youth unemployment is most pressing among youths who have a formal education, but whose skills are not in demand in the labour market at present. Most of the unemployed youths have never worked before and live from family allowances while looking for a job. The overall situation of youth employment in 2004 also stands in contrast to the boom years of the 1970s, when the Government engaged in large-scale programmes to get university graduates a job in the public sector. The long-term implications of this situation are: *little on-the-job training due to the lack of starter-jobs and apprenticeships, a lower rate of investment in work skills, and a lower build-up of human capital*.

Apart from the problem of youth unemployment, Iraq also faces the problem of *lack of female integration into the labour market*. According to the ILCS survey (2004) and the COSIT November-December 2006 results, women were significantly more likely to be unemployed than men. Along the lines of the trend observed for educated men, educated women were also significantly more likely to be unemployed than men and unemployment was highest among female secondary school graduates according to the 2004 ILCS survey. This can be explained by the tendency that less-educated women in Iraq did not usually consider themselves unemployed when they had no access to remunerative employment, as they were not actively seeking work. As the prospect of getting

paid employment was perceived to be very low, they tended to regard themselves as economically outside the labour force rather than as unemployed. This is different for educated women: since public sector employment is regarded as respectable for women they also expressed their desire to work. Thus, lack of employment opportunities for women tends to show up in low labour force participation rates, whereas lack of opportunities for men shows up in the statistics as unemployment (Assaad, 2003, p.128). It is thus likely that when more women will be taking up jobs, the unemployment rate will rise. Nonetheless, even if allowing for some undercounting of women and any statistical distortions that this may cause, there is little doubt about the presence of a large section of women outside the labour force. This, combined with the young demographic composition of the population, is likely to keep the labour market under pressure for the foreseeable future.

EMPLOYMENT, INCOMES, AND POVERTY

Once a middle-income country, Iraq had been slipping into economic decline prior to the current situation and conflict in the context of the Iran-Iraq war, the first Gulf war and sanctions. Although there are very scarce data available on the extent of poverty in the country, it was estimated that in 2004, more than five million Iraqis lived below the poverty line (assuming a 25 million population).[17] The median hourly wage in Iraq in 2004 was Iraqi Dinars 1,042 (US$0.72) for women, compared to Iraqi Dinars 694 (US$ 0.48) for men.[18] In September 2004, the World Food Programme Iraq country office reported that 25 per cent of Iraqi families were still highly dependent on the monthly food rations. These figures point towards the scale of Iraq's poverty problem. However, a word of caution is required concerning the reliability of income figures. Those working in the agricultural sector and in the informal economy are especially likely to have underreported their income.

Table 2.9 presents some evidence on the regional distribution of income for 2003 and 2004. It displays regional income levels *relative to the average national income* in 2003, which is fixed at 100 per cent as a basis for comparison. Looking first at the averages, it can be seen that the North was at 130 per cent. It was thus 30 per cent above the national average in 2003 and its lead increased tremendously to 237 per cent in 2004. The relative position of Baghdad also improved. This would imply that average income levels have been on the rise

[17] "Social Security and Safety Nets in Iraq: Outstanding Issues", Paper prepared by the ILO for the Conference on Jobs for the Future of Iraq, Amman, 12-13 December 2004, Geneva, December 2004, p. 2.

[18] *Iraq Living Conditions Survey 2004, Volume I*, Ministry of Planning and Development Cooperation of Iraq in collaboration with UNDP, Baghdad, 2005, p.104, which suggested that higher median wages for women could be related to the fact that "primarily women with higher education have work, thus are paid more".

Table 2.9: Regional dynamics of income distribution in Iraq, 2003-2004
(Percentages, national average in 2003 = 100)

	2003		2004	
	Average	Median	Average	Median
Southern Iraq	95	105	74	107
Baghdad	84	93	102	100
Central Iraq	105	98	69	96
Northern Iraq	130	99	237	99

Source: Iraq Living Conditions Survey, 2004

since the beginning of 2004, presumably because of the termination of economic sanctions and reconstruction spending.
The median figures, however, tell a different story. As Table 2.9 shows, despite the big increase in average income in the Northern Governorates of Arbil, Dohuk and Sulaimaniya, the median income in the North bore exactly the same relation to the national median income in both years. The discrepancy between average and median income suggests that while the top earners in the North had been doing especially well since the end of the war, there was less movement for those in the middle of the income spectrum. As far as equality of income is concerned, the distribution of incomes has become increasingly dispersed in the North while being comparatively more equitable in the South. However, the absence of high earners in a region is not necessarily a sign of economic strength, even if it makes income distribution more equal. These income differences combined with the fact that some parts of the country had been more severely touched by the conflict than others. Although there was also violence in the Kurdish Northern Governorates of Northern Iraq, its levels were significantly lower then in other parts of the country. This triggered an increase in labour migration within the country away from the conflict ridden Central Iraq.

SUMMARY

Some of the important characteristics of the labour market situation in Iraq between 2004 and 2006 were as follows:

- An extremely high rate of *population growth* resulting in a very young population leading inevitably to a very high rate of labour force growth (4 per cent on average between 1994 and 2004)
- A very *high degree of unemployment* especially among the young (15-24 years) where unemployment rates were over 30 per cent
- In common with a number of other countries in the region a high degree of *gender disparity* in terms of participation rates and employment

- A very low and almost negligible contribution to employment by *large and medium-sized private enterprises*
- The *State sector* accounting for a large share of total employment and virtually monopolizing formal employment

ANNEX TO CHAPTER 2

ANNEX FIGURES 1 AND 2: POPULATION AND THE LABOUR FORCE

A. Demographic trends

Figure 1: Total population (in thousands)

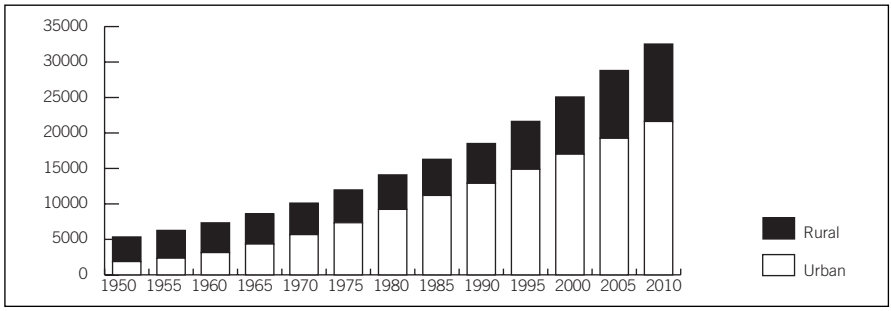
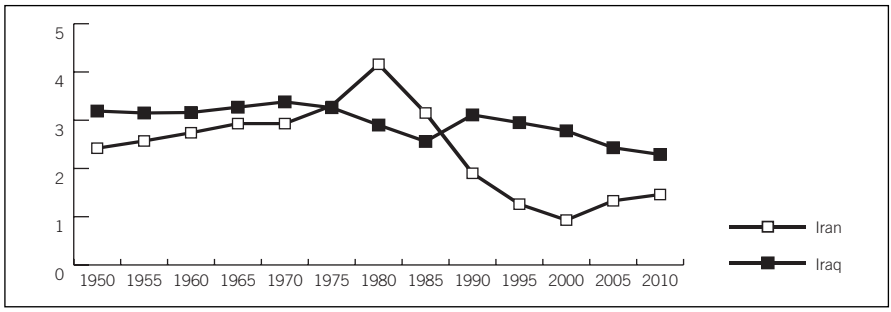


Figure 2: Iraq's population growth rates in comparision (in per cent)



Source: Population Division of the Department of Economic and Social Affairs of the United Nations Secretariat, *World Population Prospects: The 2004 Revision* and *World Urbanization Prospects: The 2003 Revision* http://esa.un.org/unpp

Figure 1 shows how rapidly the population grew between 1950 and 2000, especially in urban areas. Between 1950 and 1980, growth accelerated; since 1980 it has slowed down slightly (see Figure 2). This demographic development suggests that Iraq – as most Arab countries – has been undergoing a demographic transition from high birth rates and high death rates, which characterizes pre-industrial societies, to the equilibrium of low birth and low death rates found in advanced industrial societies. Yet, compared to other countries of the region, Iraq's demographic transition appears to be in an earlier stage. Fertility, for example, declined later and in a less pronounced way than in other countries of the Middle Eastern region. During 1995-2000, an Iraqi woman had an average of five children, whereas an Iranian woman had only three. Some analysts have argued that this comparatively high fertility rate can be linked to poverty and lack of personal security, as poor people tend to generate children to ensure their livelihood when they are old.

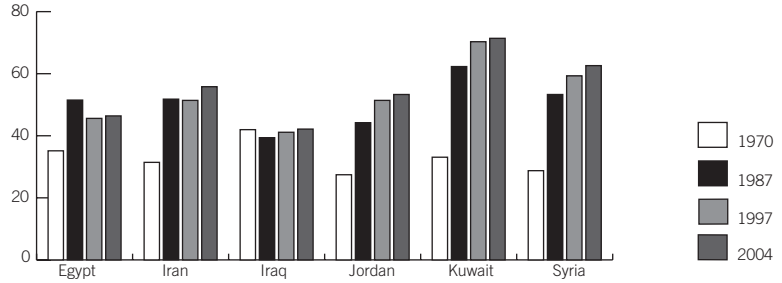
Since the mid-1960s, population growth for the cohort aged 15 – 24 years has been higher than overall population growth, producing tremendous pressure on the Iraqi labour market on the supply side. The Population Division of the UN estimates that only after the year 2015 will youth population growth slow down sufficiently to drop under the overall population growth rate. This is also because expected declines in fertility in the future will be offset by the hoped for improvements in child and maternal health. Iraq's demographic structure also implies a large size of the working age population: as of 2006 Iraq has a working age population of some 17.5 million, rising by some 500,000 a year, while there are 12 million below the working age. Overall, those under 24 years of age represented over 50 per cent of an estimated total population of 29.6 million in 2006. Even under normal circumstances this demographic structure would pose a significant challenge to the Iraqi labour market. It therefore comes as no surprise that Iraq has had considerable difficulties dealing with it, in the context of several wars and an embargo regime.

B. Workforce size and structure

Population growth translates into labour market trends via the labour force participation rate, which is therefore critical to the understanding of the employment situation. The most obvious characteristic of the Iraqi labour force is that participation rates are low. Taking the estimates from the ILCS survey as a baseline yields 70.24 per cent labour force participation for men and only 14.07 per cent for women in 2006. This results in a weighted average score of 42.40 per cent. The labour force participation of women is thus strikingly low, with the only exception of women with higher education and those working in agriculture.[19]

[19] ILO, *Summary of revised estimates of economically active population in Iraq* (2005).

Annex Figure 3: Actual and projected labour force participation regional comparison (percentages)



Source: ILO Laboursta Database, Iraq (summary of revised estimates of economically active population in Iraq (2005)

Figure 3 shows the labour force participation rates in regional comparison. These participation rates have remained remarkably stable over recent decades in Iraq. In Syria, in contrast, labour force participation has more than doubled since the 1970s and is now at around 60 per cent. The reason for this catch-up is mainly an increasing participation of young women workers in the labour market. This has to be seen in the context of changing gender roles with women taking up a more proactive position in society. In Iraq, on the other hand, the participation rate has stagnated at very low levels.

The finding of the ILCS survey that Iraq's labour force participation has not increased was in contrast to expectations, as it was assumed for a long time that female labour force participation was higher in Iraq than in other Arab countries. It was one of the expressed goals of the Baath Party to promote the emancipation of women. However, these attempts were offset by the economic pressure, which held back the absorptive capacity of the labour force, constraining the social modernization that other Middle Eastern countries have witnessed in recent decades. If the conditions in Iraq normalize, the female labour force participation may increase sharply in line with the experience of other Middle Eastern Countries in the 1990s. The scope for increasing female participation in the labour market is immense and will ensure that the pressures on the labour market will be upheld for some time to come.

Diverging estimates of the employment situation: COSIT 2003 and 2004 and Fafo 2004

In 2003 and 2004, three different labour market surveys were conducted: the Iraqi Central Organization for Statistics and Information Technology (COSIT) conducted two Labour Force Surveys (LFS) covering around 25,000 households. In April 2004, COSIT conducted another survey with technical assistance from the Norwegian Fafo Institute covering 21,700 households. This second survey was called the Iraqi Living Conditions Survey (ILCS). It arrived at a quite dissimilar

conclusion to the LFS estimate. While the LFS estimated the unemployment rate to be at 26.8 per cent, the ILCS concluded a much lower unemployment rate of 10.5 per cent. Although there may have been some variation in employment due to seasonal fluctuations, this huge difference cannot be explained by the timing of the surveys alone. It appears that the large discrepancy is largely a result of different methods in the definition and assessment of unemployment. The ILCS survey followed more strictly the ILO conceptualization of unemployment. To qualify as unemployed under this definition, a woman or man has to be of working age, must have actively looked for work, and must not have worked for income or in kind for more than an hour within the reference period of one week. Thus, only those who have performed no work at all are considered "unemployed", while the others are considered "underemployed". Applying this definition to developing countries usually leads to a small number of unemployed and a comparatively large number of underemployed persons.

The Labour Force Survey followed a broader conceptualization of unemployment that allowed for more working hours per week until a person was called "employed". The LFS considered those who had worked less than 15 hours a week "unemployed", as opposed to the one-hour-per week cut-off line of the ILCS. The rationale behind this different cut-off line is that working less than 15 hours is insufficient to make a living in Iraq, as wages are very low.

Another difference concerns the category of the so-called *"discouraged workers"*. These are the people who want a job and are currently available for work but who have given up searching because they believed that there was no work to be found. This concept is based on the premise that the discouraged workers are only temporarily out of the labour market and would be looking for work if there were jobs on offer. As the discouraged workers act in very similar ways to the unemployed, they are included in the category of the "unemployed" in the Labour Force Survey. According to Sletten (2005) the unemployment rate increases by 8 per cent to 18.5 per cent, if the discouraged workers are included into the "unemployed" category. If the "discouraged workers" are included and the cut-off point for "unemployment" is lifted from one hour to 15 hours of work per week, unemployment rises to 22.5 per cent. The difference of this estimate to that of 26.8 per cent put forward by the LFS is thus reduced to only 4 per cent. Sletten (2005) suggests that the remaining four percentage points of difference between the ILCS and the LFS estimates are due to different structures of the questionnaires used by the two surveys.

CHAPTER 3. RECONSTRUCTION AND EMPLOYMENT

INTRODUCTION

The high levels of unemployment and underemployment in Iraq clearly warranted that high priority be given to job creation in the reconstruction programme. Indeed the Government, donors, World Bank and UN agencies identified employment creation as a major objective of the reconstruction programme. It was recognized that reducing the high levels of unemployment especially amongst the young and displaced workers would have a favourable impact on security and on the law and order situation.

The issue this chapter addresses is whether the high priority which was at least overtly being given to job creation was actually reflected in the investment programme being undertaken as part of the reconstruction effort during 2004 and 2005 by the Government, multilateral institutions, donor countries and UN agencies. To find an answer to this question the results of two exercises conducted to evaluate the employment impact of the reconstruction effort were analysed. The first was a macro exercise, which analysed the investment undertaken in 2004 and 2005, and then generated estimates of the numbers of jobs that could have resulted. This was done by examining the available information on estimates of total investment made in these years, the sectors in which it was concentrated and the capital and import intensity of this investment. The methodology suffers from some serious shortcomings including labour-use assumptions based on other countries' experiences. It does however provide some interesting insights on the impact, or lack of it, of the reconstruction effort on the employment and labour market situation.

The second part of this chapter reports on an exercise that the UN undertook during the second half of 2004 to evaluate the extent to which its programme in Iraq reflected sufficiently the high priority it had assigned to the goal of improving the employment situation. The major aim of this "labour audit" or "labour assessment" was to take a sample of projects being implemented by UN agencies in Iraq and examine whether this potential for generating employment was

being fully realized in terms of their labour use and whether there was a possibility of increasing the labour or employment content of these projects either by using different contractual arrangements or more labour intensive techniques of production.

The limitations of both these exercises must be kept in mind when interpreting the results of this analysis. Clearly employment or job creation cannot be the *only* priority assigned in designing the reconstruction programme. The revival of key sectors, for example, oil exports which are vital for revenue generation must have priority, even if the huge investment this would involve would have very little direct impact on the domestic economy in terms of linkages with the rest of the economy or employment generated. Similarly, the clearing of the harbour in the south of the country and making the port operational must again be given high priority even though the machinery needed to do this is highly capital-intensive and labour employed in the operation minimal.

Also one needs to take into account the security and law and order situation where the projects were to be implemented. If the security situation were such that the timeframe for implementation and providing security for those who were to work on the project needed to be kept to a minimum then clearly this would have an impact on the way in which the project was designed and implemented. Again it is difficult to assess the factors which did impact on the choice of projects and their means of implementation. Clearly the geographical location of the project played a part in this decision as did many other factors.

The challenge the reconstruction programme faced was twofold: first to select and implement those projects which would respond to the urgent needs of rebuilding and restoring vital infrastructure, even if this implies the use of capital-intensive technology, as these would be vital for regenerating growth and employment creation in the rest of the economy; second, that those projects, in which there were possibilities for maximizing the employment impact, bidding and contractual arrangements including choice of technology, were so framed in the project design to ensure that such an impact did in fact materialize.

It is the answer to these two challenges that this chapter addresses. But before we do so we examine some of the key principles that have been identified by the ILO in designing an employment-intensive reconstruction programme.

PRIORITIZING EMPLOYMENT IN RECONSTRUCTION

Experience from previous post-war reconstruction suggests that employment must be made one of the central objectives of reconstruction programmes on the premise that reconstruction needs to fulfil both economic and social objectives. Its aim must be not only the reconstruction of physically destroyed assets, but also to address the social needs of the community. Tackling unemployment is generally recognized as a priority issue in this context.

From this standpoint some key principles for reconstruction emerge. Shone (2003) describes them as follows: *first*, the unemployment problem and infra-

structure rehabilitation needs must be addressed concurrently. The choice of technology for undertaking the reconstruction works and the packaging of reconstruction contracts should be done in a way that secures a fair share of the market for local enterprises. Through mainstreaming these labour-based reconstruction techniques, the reconstruction programme itself can become a tool for addressing unemployment and poverty. *Second*, the capacity of the local construction sector needs to be enhanced to respond to the business opportunities arising through reconstruction. Otherwise the weakness of the local business community can impair its ability to duly participate in the reconstruction process. This includes providing credits, business support services, training, and local development strategies. *Third*, the labour-intensive reconstruction should also be used to "build peace" on a community level. Doing projects with a visible impact and significant employment potential can help to diffuse the frustration that nothing is moving. Amid the difficult security context in Iraq it can be hoped that working towards a common goal will help to foster social cohesion, combat passivity and rifts between communities.

EMPLOYMENT AND INFRASTRUCTURE

As is well known, Iraq's economy is dominated by the oil sector, which has traditionally provided about 95 per cent of foreign exchange earnings and a large share of State revenue. In the past the Government used some of these earnings for financing significant investments in the infrastructure. In this respect, Iraq was a leader in the Arab world in the 1970s. Since then, however, Iraq's infrastructure has fallen back to levels comparable with a lower income country. In the wake of the fall of the Baath regime, Iraq's infrastructure was in a debilitated state suffering from decades of underinvestment. Initial advances were made after 2003, principally in restoring oil production capacity, but reconstruction has been stalled by the lack of security. Violence, sabotage and crime have hampered reconstruction efforts. According to recent estimates, only 85 per cent of households have stable access to electricity networks, which only provide some 3 – 6 hours of electricity daily. Only 20 per cent are connected to reliable water and waste-water infrastructure (World Bank, 2006). Thus further investments will be necessary and are estimated in the neighbourhood of US$7 billion. Even under unfavourable conditions, investments of such magnitude are likely to generate a significant number of jobs. Infrastructure reconstruction is therefore the main area in which policy choices can have a favourable impact on the employment situation.

Discussing the link between employment and infrastructure reconstruction one needs to bear in mind that much of it was donor-funded. In 2003, a conference of donors in Madrid pledged over US$32 billion in grants and loans. The assistance was composed of two major funds, the multilateral International Reconstruction Fund Facility for Iraq and a separate fund administered by the US. Of the latter, US$16.7 billion had been obligated by the time of writing (United

States Congress, 2006). It appears that there was no plan to systematically promote Iraqi involvement within the reconstruction programme prior to the Amman Conference in November 2004. This meant that Iraqi participation was left to function on its own rather than being the fundamental and agreed upon principle of all reconstruction efforts. The conditions for realizing the priority objective of job creation were thus not ideal from the outset.

Employment impact of investment in 2004-05

In analysing the employment impact of investment made in 2004-05, a large part of which was donor funded, it needs to be kept in mind that much investment expenditure inevitably goes on the purchase of machinery and equipment from abroad for all sectors, including transport equipment and indeed construction machinery. What one needs to work out in broad terms is what the investment programme undertaken during 2004 and 2005 would imply in terms of wages, purchase of materials, equipment rentals and overheads, and activities in Iraq. The exercise undertaken was broken down into a number of steps. Using IMF (2005) estimates as the baseline for GDP and investment, the estimated imports of capital goods were then subtracted from investment undertaken in 2004 and 2005. This showed that the US$12.6 billion public investment programme for these two years involved around US$4.3 billion to cover activities on the ground, such as procurement of construction material, and wages. We then analysed public and private sector separately. For the public sector we used Government estimates of the sectoral breakdown of public sector investment, and then on assumptions of labour intensity of these sectors calculated the implied expenditure on wages. We then, on the basis of average wages reported by the UN Labour Audit Report and the ILCS (2004), calculated the number of workdays of employment generated.

Based on these steps and given the breakdown into different activities reported by the Government for 2004, we find (see Table 3.1) that during the two years 2004 and 2005 this public investment created 53 million working days per year, or some 200 yearly workdays for 263,000 people. On top of this an additional 50,000 jobs were created in the private sector (See Annex Table 3.1). These figures need to be seen in the context of almost 250,000 new entrants into the labour market during 2004 and 2005 due to labour force growth.[20] The net contribution to reducing the high levels of unemployment was therefore minimal. While recognizing the limitations of this exercise, although it is based mainly on plausible assumptions drawn from other countries, the results do clearly point out that the investment programme as was designed and implemented during 2004 and 2005 was clearly insufficient to overcome or significantly ease the current unemployment and labour market situation.

[20] This is based on data from the ILO Laborsta database, which has been adjusted to the findings of the Iraq Living Conditions Survey.

Table 3.1: Employment intensity of investment: Public sector

US$ millions	2004	2005	2006**
GDP (Real)	25,724.0	26,855.9	28,037.5
Public investment			
Total public investment	5,736.5	6,875.1	7,458.0
Domestically spent investment			
Finance	187.9	225.2	244.3
Internal affairs, security and defence	289.9	347.4	376.9
Transportation and telecommunications	76.1	91.2	99.0
Public works and municipalities	49.8	59.7	64.7
Housing and construction	23.7	28.4	30.8
Industry and mining and planning	18.6	22.2	24.1
Petroleum	514.5	616.6	668.9
Electricity	540.3	647.6	702.5
Health and education	27.0	32.4	35.1
Cross-cutting issues (Labour and social affairs, science, youth, migration)	9.6	11.5	12.5
Other	218.0	261.3	283.4
Total	1,955.5	2,343.6	2,542.3
Wage bill	231.6	277.6	301.2
Employment	240,958	284,799	304,679

Source: IMF (2005) and ILO estimates (See Annex Table 3.1) **Projected

EMPLOYMENT ASSESSMENT SURVEY

While the employment-impact assessment was conducted with the intention of understanding the overall employment impact of reconstruction efforts, the following employment assessment discusses the necessary prerequisites to raise the use of labour in reconstruction. It draws on the common experience that for many construction tasks a choice of techniques can be made that *vary in their mix of expenditure on labour and capital* (e.g. equipment rental, interests, or payments) but provide a similar final product. The assessment is therefore largely a technical exercise, based on the assumption that more jobs could be created through Iraq's reconstruction by means of modifying the technologies utilized for their implementation.

The employment-technology assessment draws on data from two levels. Using standard reported data, the research team first conducted an overall assessment of selected UN-funded projects; and then complemented this data with case studies of 11 individual projects covering a wide range of sectors and sources of

funding. The study was conducted by a staff of Iraqi consultants and government officials under the guidance of an international specialist for labour-based technology. The assessment was based on a standard approach developed by the ILO, which draws on a combination of *review of data* that projects hand in to their funding agencies and an *on-site* appraisal using a standardized checklist. This approach is deemed sufficient by most experts to provide empirical information about the impact of reconstruction programmes on employment.

Table 3.2: Projects reviewed

Project	Funding source
Individual projects:	
Open Educational College, Baghdad	Ministry of Education
Book stores	Ministry of Education
National Centre for Health & Vocational Safety	MOLSA
MOLSA HQ building	MOLSA
Al Sayab Girls' Secondary School	MOLSA
Tequar Primary School	MOLSA
Raw water complexes	UNICEF
Al-Itifia Raw Water Station	UNICEF/US Army
Al-Wathba Raw Water Station	UNICEF/Red Cross
Environmental Cleaning Project (Mosul)	UNICEF
Environmental Cleaning Project (Al Ramadi)	UNICEF
Overall assessments:	
Rehabilitation of 26 schools, 10 technical institutes and one university	UNHABITAT
Rehabilitation of water/sanitation facilities and public buildings	UNDP/Govt. of Japan
Reconstruction and Employment Programme – basic infrastructure repair	UNDP – IREP
Rehabilitation of chlorination production facilities	UNIDO

Source: UN/ILO Iraq Employment Assessment, 2004

Results of the employment-technology assessment

Project characteristics: The available funding for the sample projects totalled US$2.4 million, of which US$1.98 million was allocated to civil works and construction related activities. The average project was around US$0.25 million, the smallest being US$35,110, and the largest over US$1.2 million. Overall, 71 per cent of the contracts used "standard" or conventional civil works implementation and around 15 per cent used either machine or labour-based, equipment-supported technology. The projects were all implemented starting from mid-2003 to the time of assessment during November 2004, with average contract

Table 3.3: Project characteristics

Project duration (days)	106
Current status (% completed)	94
Job creation considered in project design (%)	91
Technology choice:	
– Use of pre-cast/prefab materials (%)	9
– Use of locally made materials (%)	82
– Use of locally available materials (%)	100

Source: ILO, Iraq Employment Assessment, 2004

duration of 106 days. In principle the majority of the projects (91 per cent) incorporated job creation as part the project design and the contracts used a mixture of technologies, all using locally-available materials, with a limited use of prefabrication and pre-cast components. Overall, 71 per cent of the contracts used "standard" civil works implementation methods/technology and around 15 per cent used either machine or labour-based/intensive technology. The employment content would be significantly higher if the projects had used a different technology mix, including labour-based equipment supported methods.

The employment content of the civil works projects (by value) consisted on average of 7 per cent professional staff, 19 per cent skilled, 33 per cent semi-skilled, and 41 per cent unskilled. These proportions are similar to those that would be expected under standard contracting conditions, but they are different from what would be expected using labour-based methods. Overall, wages accounted for around 27 per cent of the contract costs, which is again consistent with the use of standard construction techniques. There was a wide range of daily wage rates for unskilled labour ranging from US$3 – 7 per day.

Main employment indicators: The sample projects all included civil works, but other components were also incorporated, such as mechanical/electrical works (55 per cent of contracts) and equipment and furniture (73 per cent). The data collected allowed a fairly detailed assessment to be made of the total employment created by the projects. The average number of workers per contract was 110, over 90 per cent of whom were youths (aged 15-24), 71 per cent unskilled and 90 per cent fully able-bodied. Very few of the workers were female. Permanent jobs accounted for 7.5 per cent of total employment. Estimates were also made of indirect employment – accounting for approximately an additional 20 per cent of the jobs created through the projects, the majority of which were for services provided before implementation. This result is rather on the low side compared to experiences from projects elsewhere, but may partly be due to the sectoral composition of the projects reviewed.

Civil works expenditure: The average civil works expenditure was also analysed, with labour accounting for 27 per cent on average of contract values, local/imported materials for some 30 per cent, mechanical equipment and tools for

13 per cent, and overheads/preliminaries and profit for around 31 per cent. These average values are similar to what would be expected when using "standard" levels of technology, although the overheads/preliminaries and profit components are approximately 20 per cent higher than would normally be expected reflecting the uncertainties and risks involved with construction activities in Iraq at present.

Table 3.4: Bottlenecks/constraints to implementation procedures (percentages)

– Lack of local participation in project design	18
– Lack of targeting of special groups	0
– Need for more decentralization	27
– Need for better procurement	9
– Need for faster payments	36
– Lack of small and medium enterprises	18
– Lack of access to credit	64
– Lack of material resources	64
– Lack of trained staff	73

Source: ILO, Iraq Employment Assessment, 2004

Project implementation constraints: Questions about the supply of workers indicated that there was an adequate supply of unskilled workers (91 per cent of respondents) and some shortages of skilled workers, but the greatest gaps were in the supply of supervisory staff. The main bottlenecks/constraints in implementation of the projects were identified as (1) lack of trained staff, (2) lack of access to credit and (3) lack of material resources. From these results it can be concluded that training of supervisory staff is one of the main priorities in overcoming project implementation constraints.

Table 3.5: Training required to improve the qualifications of construction personnel (percentages)

– Unskilled (male)	64
– Skilled (male)	100
– Supervisory (male)	73
– Professional (male)	36
– Unskilled (female)	18
– Skilled (female)	18
– Supervisory (female)	27
– Professional (female)	36

Source: ILO, Iraq Employment Assessment, 2004

All project managers interviewed believed that skilled workers needed additional training, and 73 per cent of them demanded more training for male supervisory staff. This result underscores the necessity of additional training for construction personnel.

Other data allowed a detailed assessment of the total employment impact of these projects: The average number of workers per contract was 110, over 90 per cent of whom were youths (aged 15-24), 71 per cent were unskilled, and 90 per cent fully able-bodied. Very few of the workers were female. Permanent jobs accounted only for 7.5 per cent of the total employment.

Key findings: employment assessment

The survey results suggest that the priority that employment should have been given was not adequately reflected in the way the reconstruction effort was planned and implemented. Among the many issues that were analysed, three warrant particular attention:

First, projects in 2004 were seriously underutilizing labour-based technologies. Of the projects reviewed 71 per cent were using "standard" or conventional civil works implementation methods and only 15 per cent labour-based technology. This finding suggests that there would have been wide scope for increasing the employment impact of projects by using more labour-based technologies in their implementation. If the technology mix were changed by adding a conservative 5 per cent of the contract values to be used as wages, the number of jobs would increase by around 22,600 jobs per billion dollars spent. Also for every job created directly using labour based-methods, another 1.6 jobs would be created due to indirect effects. The most significant group employed in construction activities consisted of young people in the 15-24 age range.

Second, the assessment also found that Iraqi enterprises operating on a smaller scale pay more for capital, use it more sparingly, and are thus more labour intensive. In the assessment period there had already been a substantial growth in the number of contractors (30 per cent overall from mid-2003 to November 2004).[21] This implies that splitting up major construction tasks into elements that could be handled efficiently by small and medium-sized enterprises would further stimulate activity in this sector. However, as of 2004, there was still a need to build up capacities for local contractors and to undertake labour intensive construction projects. Skill shortages were found to be a major constraint to productivity – in particular for skilled workers. The survey therefore suggested technical cooperation to focus on capacity building.

Third, the assessment found donor procurement regulations to be an important factor in determining the employment impact of projects. In this context it is

[21] Prior to April 2003 there were around 23,000 contracting organizations, of which 600 were construction companies and the balance were individual contractors.

necessary to bear in mind that much of the assistance for Iraq has been provided through *bilateral* assistance. While multilateral donors and some bilateral ones have rather "liberal" rules allowing for local procurement, this practice is less common among major bilateral donors. While not all donors permit local procurement, some allow for national preferences during bid evaluation. The impact – or the lack of it – of reconstruction on employment in Iraq emphasizes that technical assistance should be provided in untied form, wherever possible.

CREATING AN ENABLING ENVIRONMENT FOR LABOUR-BASED RECONSTRUCTION

If the investment programme is currently insufficient to overcome or ease the current labour market situation the real challenge is to push the reconstruction programme into a more labour intensive direction. In any case, the potential for infrastructure investment will remain high during the coming years. Iraq has made progress in addressing some of these issues: on 30 June 2005, the Government established a tripartite, i.e. including employers' and workers' representatives, Inter-ministerial Board for Employment Creation, which is headed by the Ministry of Labour. One of the agenda items of the Board is to evolve a policy emphasizing labour-based methods and to direct the international support programme in this regard.[22] Within the UN, new regulations have also been adopted to mainstream the use of labour-based technologies. These are important steps but they are not in themselves sufficient to achieve the required impact. Indeed, the challenge will be to mainstream labour-based technologies in all sectors where they can be applied. This would involve abandoning the standard "partition of labour", which means that some projects specifically focus on employment creation, while the bulk of projects disregard employment-related criteria in their project design.

Labour-based policies can provide a framework for the participation of the domestic economy, but they must also be complemented by capacity building for small and medium-sized contractors in order to fulfil their catalytic function. Due to its strong backward linkages into the economy, the construction sector can help trigger an economic dynamism that will eventually be taken over by the private sector. But for this to happen, the local economy needs to establish a "response mechanism" that ensures that private businesses can engage competitively in the reconstruction market. The Government and the donor community need to address this issue by (a) providing *business development services* parallel to reconstruction and by providing an opportunity for small enterprises to invest in the reconstruction market, (b) by providing *counselling and informa-*

[22] Letter entitled "Establishment of an Employment Committee" (Ref 370) from MOLSA, dated 12/7/2005 and a letter of approval from the cabinet office dated 30/7/2005.

tion services for small contractors, and (c) by collaborating with financial institutions to *facilitate contractor access to producer loans*. The local economic development approach has frequently been proven suitable to address these issues in an integrated manner.

ANNEX TO CHAPTER 3

Annex Table 3.1: Employment intensity of investment

US$ millions	2004	2005	2006**
GDP (Real)	25,724.0	26,855.9	28,037.5
A: Public investment			
Total public investment	5,736.5	6,875.1	7,458.0
Domestically spent public investment	1,955.5	2,343.6	2,542.3
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Public works and municipalities	49.8	59.7	64.7
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Cross-cutting issues (labour and social affairs, science, youth, migration)	9.6	11.5	12.5
Other	218.0	261.3	283.4
Total	**1,955.5**	**2,343.6**	**2,542.3**
Wage bill			
Finance (10%)	18.8	22.5	24.4
Internal affairs, security and defence (22%)	63.8	76.4	82.9

US$ millions	2004	2005	2006**
Transportation and telecommunications (15%)	11.4	13.7	14.8
Public works and municipalities (36%)	17.9	21.5	23.3
Housing and construction (37%)	8.8	10.5	11.4
Industry and mining and planning (30%)	5.6	6.7	7.2
Petroleum (5%)	25.7	30.8	33.4
Electricity (5%)	27.0	32.4	35.1
Health and education (40%)	10.8	13.0	14.0
Cross-cutting issues (labour and social affairs, science, youth, migration) (27%)	2.6	3.1	3.4*
Other (18%)	39.2	47.0	51.0
Total	**231.6**	**277.6**	**301.2**
Employment			
Finance	21,345.0	25,228.7	26,989.7
Internal affairs, security and defence	70,299.1	83,089.8	88,889.8
Transportation and telecommunications	15,222.6	17,992.3	19,248.3
Public works and municipalities	18,872.5	22,306.3	23,863.4
Housing and construction	9,240.9	10,922.3	11,684.7
Industry and mining and planning	5,860.6	6,926.9	7,410.4
Petroleum	20,255.6	23,941.0	25,612.2
Electricity	27,015.5	31,930.9	34,159.8
Health and education	9,390.3	11,098.8	11,873.6
Cross-cutting issues (labour and social affairs, science, youth, migration)	2,149.9	2,541.1	2,718.5
Other	41,305.9	48,821.3	52,229.3
Total	**240,958.0**	**284,799.4**	**304,679.5**
B: Private investment			
Total private investment	909.2	949.2	990.9
Agriculture (17%)	154.6	161.4	168.5
Manufacturing and construction (25%)	38.6	40.3	42.1
Trade and services (52%)	20.1	21.0	21.9
Other (6%)	1.2	1.3	1.3
Domestic spent investment (Less import of equipment)			
Agriculture (45%)	69.6	72.6	75.8
Manufacturing and construction (43%)	16.6	17.3	18.1
Trade and services (50%)	10.0	10.5	10.9
Other	0.5	0.6	0.6

US$ millions	2004	2005	2006**
Wage bill			
Agriculture (20%)	13.9	14.5	15.2
Manufacturing and construction (20%)	3.3	3.5	3.6
Trade and services (20%)	2.0	2.1	2.2
Other (20%)	0.1	0.1	0.1
Men working hours			
Agriculture	7,727,975.0	7,925,349.6	8,127,765.2
Manufacturing and construction	791,197.4	811,404.8	832,128.3
Trade and services	873,597.2	895,909.1	918,790.8
Other	43,400.3	44,508.8	45,645.5
Jobs created			
Agriculture	38,639.9	39,626.7	40,638.8
Manufacturing and construction	3,956.0	4,057.0	4,160.6
Trade and services	4,368.0	4,479.5	4,594.0
Other	217.0	222.5	228.2
Total			
Subtotal private	**47,180.8**	**48,385.9**	**49,621.6**
Grand total public and private	**288,138.9**	**333,185.2**	**354,301.1**

Source: IMF and ILO estimates ** Projected

Annex Table 3.2: Impact of changing construction technology
(US$ billions expenditure in jobs)

	% Total by Value	Average Wage US$ per Day	Distribution of Expenditure	Total Workdays per Year*	Workforce (Number of Jobs)
Without change in technology:					
Total Construction Budget			1,000,000,000		
% Used for Labour Costs	27%				
Labour Costs by Level of Skill:			270,000,000		
– Unskilled	41%	4.8	110,207,102	22,873,172	91,493
– Semi-skilled	33%	17.7	89,595,666	5,054,114	20,216
– Skilled	19%	21.8	50,569,431	2,317,766	9,271
– Professional	7%	50.0	19,627,801	392,556	1,570
Total Employment per US$ 1 Billion				30,637,608	122,550
With change in technology and constant wage rates:					
Total Construction Budget			1,000,000,000		
% Used for Labour Costs	32%				
Labour Costs by Level of Skill:			320,000,000		
– Unskilled	41%	4.8	130,615,824	27,108,945	108,436
– Semi-skilled	33%	17.7	106,187,456	5,990,062	23,960
– Skilled	19%	21.8	59,934,141	2,746,981	10,988
– Professional	7%	50.0	23,262,579	465,252	1,861
Total Employment per 1 US$ billion				36,311,239	145,245
Incremental employment for 5% change in labour component					**22,695**
* Workdays per year per worker		200			

CHAPTER 4. LABOUR MARKET POLICIES AND INSTITUTIONS

INTRODUCTION

This chapter turns to labour market policies and institutions as another essential building block of an employment-centred strategy for peace in Iraq. Beyond the immediate need to reverse the trend of growing insecurity, Iraq's reconciliation and recovery process must take a shape that promotes productive employment and decent work in acceptable conditions. This requires strengthening of labour market institutions, which – when functioning effectively – can make the path to economic recovery smoother and allow shocks to the system to be absorbed at less social cost. Such institutions and practices are important for the consensual management of change and for reducing the uncertainty and risk facing workers. They include a realistic and forward-looking approach to training policies, the implementation of active labour market policies (ALMPs)[23] and the availability of labour market information.

The Iraqi Government has been striving to restore labour market institutions amid extraordinarily difficult circumstances. Steps have been taken in the field of employment policy development, strengthening vocational training, providing employment services, and building capacity in key ministries. This has included the establishment of an inter-ministerial council charged with the design of effective policies and programmes for employment creation;[24] also the

[23] ALMPs support employment creation in two basic ways: directly by job-creation measures (e.g. public works and enterprise creation, as well as hiring subsidies) and indirectly by improving employability through training and by ensuring efficient labour exchanges that provide better labour market information and enhanced job matching (See Auer et al., 2005). They also target the young and excluded groups including disabled workers. *Passive* labour market policies on the other hand, are those in which the benefit recipients are not obliged to participate in job training or work schemes, but act as "passive" recipients of a certain allowance, even though active job search is frequently a condition for receiving these benefits.

[24] This refers to the Employment Committee established on 30 July 2006 in the wake of the conference on "Jobs for the Future of Iraq", December 2004. The Committee involves the various ministries concerned as well as representatives of employers' and workers' organizations.

revision of the labour law has been initiated. However, as important as these institutional changes may be, they will not in themselves have a considerable impact. The implementation of an integrated but pragmatic programme is needed, as is argued in this chapter. This theme will be discussed under the headings of: active labour market policies, social dialogue and labour regulation. Given the lack of accessible information on labour market policies, this chapter starts by putting together a sketchy image of ALMPs in Iraq.

ACTIVE LABOUR MARKET POLICIES[25]

In 2003 the Government initiated a major programme to activate the labour market; by 2005, 600,000 job-seekers had registered in employment centres and by March 2007 this figure had increased to 940,000 (see Table 4.1 and 4.2). Many of those registered have received training. Employment centres operate as a constituent part of the Ministry of Labour under its Employment Department and they exist in all governorates of Iraq. Their main duties involve recruitment, job search assistance, vocational counselling, labour market information and outreach.[26] These efforts were made against the background of widespread physical damage in 2003, difficulties in obtaining material, and shortages of machinery and equipment due to the combined impact of looting, violence and a decade of sanctions.

Table 4.1: Number of registered job seekers and placements in the employment centres of MOLSA, March 2007

Governorate	Registered	Placed	Persons placed %
Baghdad	183,787	6,252	3.4
Salah al-Din	51,750	4,043	78.1
Diyala	66,552	6,951	10.5
Kerbala	31,767	9,600	30.2
Najaf	55,096	6,018	10.9
Qadissiya	81,805	26,221	32.1
Wassit (Kut)	51,181	12,893	25.2
Muthanna	18,685	2,177	11.7
Missan	59,731	21,992	36.8
Thi-Qar	72,947	49,579	68.0
Basrah	63,274	17,701	28.0

[25] This section is based on Riyadh Hasan M. Ali (2004), "The role of MOLSA in Promoting Employment in Iraq", paper presented at the International Employment Conference, December 2004 and subsequent update submitted in 2005.

[26] Outreach refers to awareness-raising of the potential benefits of vocational training in the community.

Table 4.1: (continued)

Governorate	Registered	Placed	Persons placed %
Anbar	17,609	8,592	48.8
Babylon	63,715	7,640	12.0
Ninewa	91,338	16,145	17.7
Erbil	10,449	361,000	34.6
Sulaymaniyah	16,077	716,000	4.5
Tameem	48,576	4,657	9.6
Dahuk	1,278	228,000	17.8
Total	**939,041**	**201,766**	**21.5**

Source: Data collected from Ministry of Labour and Social Affairs (MOLSA)

Table 4.2: Number of registered job seekers and placements by MOLSA employment centres 2005

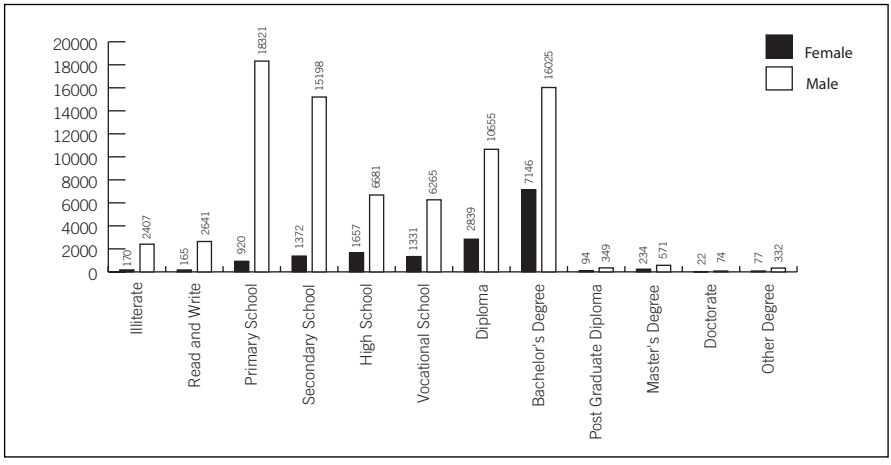
Opened employment centres	Registered job-seekers (thousands)	Persons placed in the labour market (thousands)	Persons placed in the labour market (percentage)
Baghdad	120.1	4.9	4
Tikrit	5.2	3.5	67
Baquba	35.6	6.0	17
Kerbala	12.8	9.5	74
Najaf	15.1	6.0	40
Diwaniyah	58.7	26.9	46
Kut	22.5	12.1	54
Muthanna	18.1	2.1	12
Maysan	58.0	21.9	38
Dhi Qar	59.4	49.0	82
Basrah	39.1	11.3	29
Fallujah	7.6	4.0	52
Ramadi	9.3	3.3	35
Babylon	19.0	7.6	40
Ninewa	48.2	16.1	33
Irbil	8.9	0.3	3
Suleimaniyah	14.1	0.6	4
Kirkuk	47.7	4.5	10
Dohuk	0.8	0.2	18
Total	**600.2**	**189.7**	**32**

Source: Data collected from MOLSA

According to Table 4.1 around 940,000 had registered with an employment centre as seeking work in March 2007 – an increase of almost 50 per cent compared to the figure in 2005 (Table 4.2). The number of registered job seekers in 2007 is fairly large and represents about 12 per cent of the labour force. Of these the number of persons who were placed in the labour market or found employment was around 202,000 or 21.5 per cent of those registered – a decrease of almost one-third from 2005.

Keeping in mind that the country was and is in great turmoil, one has to acknowledge the resilience of Iraqi official agencies to maintain their operations against all odds. Clearly, a certain level of trust in the system is a prerequiste for such high registration rates. Compared to other conflict affected countries – where public institutions are often too weak to function – the basic institutional framework in Iraq is operational, although much of it needs modernization. Wherever possible, international assistance should try to build on these available capacities. The overall picture must be qualified, however, by noting that there are significant regional disparities in the performance of employment services. Table 4.1 indicates that in the Northern and Southern Governorates employment services were working more effectively than in Central Iraq. In Baghdad, for example, only a meagre 3 per cent of around 184,000 registered job-seekers found employment after seeking services of the employment centres.

Figure 4.1: Educational background of job seekers: 2003-2004



Source: ILO (based on Government-reported data)

Figure 4.1 illustrates how difficult it is for many young people to make the transition from schooling to work. Those facing greatest difficulty in finding jobs are essentially graduates and school-dropouts. Of the registered job seekers, 89 per cent are men – reflecting a polarization of labour market behaviour between women and men (see Chapter 2). Providing training for women to facil-

itate greater women's participation in the labour market is therefore a priority for the Ministry of Labour.
Vocational training centres are associated to the Ministries of Industry, Labour and Military Industries, but are also vertically integrated under the auspices of the Training Department of the Ministry of Labour. Subject areas in these centres include car mechanics, wiring, plumbing, languages (English), and food processing.

Table 4.3: Expenditure on active labour market policies (US$ million)

	2004	2005
Labour market training and subsidized employment	74.7	58.8
National Employment Services	18.0	4.5
Public works	125.0	--
Total	217.7	63.3
Total as share of GDP	0.8%	0.2%

Source: World Bank, 2005, *Social protection in transition: Labour policy, safety nets and pensions*

The expenditure on ALMPs in Iraq was at 0.8 per cent of the GDP in 2004 and 0.2 per cent in 2005 (See Table 4.3). In Latin America, an average of 0.4 per cent (and in transition countries 0.65 per cent[27]) of GDP is spent on ALMPs (Auer et al., 2005). In the case of Iraq this relatively high expenditure level partly comes about because of one-time investments, e.g. expenditures to rebuild destroyed machinery and real estate.
Iraq's employment centres and vocational training institutions emerged in the context of a largely State-controlled economy, but are now putting greater emphasis on a "facilitative approach". This means that workers are encouraged and advised to look for a job in the private sector or helped to become self-employed, rather than being referred to a State-owned-enterprise. It is increasingly recognized that the State can no longer hold the responsibility for creating all employment for all citizens. However, one barrier to realizing this vision is the low income and low job quality of the jobs in the private sector. Often private sector jobs do not satisfy the expectations of workers and are therefore rejected by the young as long as they can afford to do so. Thus, improving labour market services must go hand in hand with raising living standards for those working in small enterprises. Training will be a crucial productive link to realizing this objective.

[27] The figure for Latin America refers only to training and employment generation. The figure for transition countries covers all expenditures related to the labour market policy and is an average of the expenditures in the following countries: Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Poland, Russian Federation, Slovakia, and Ukraine.

However, many of these efforts are ad-hoc and improvised in their character. At least formally, the vocational training policy introduced by the previous regime is still in place. The Ministry of Labour is trying to cope with the enormous employment problem using modest means and in an extraordinarily difficult environment. However, the achievements in this field since 2004 highlight the potential of what could be done, if adequate institutional capacity was built up. The ILO provided support to MOLSA during 2003-2006 in strengthening its capacity.

Harnessing opportunities

The extent to which the potential of labour market policies can be tapped will depend on the progress in restoring the efficiency of the employment service system and on its ability to respond to short-term challenges. Among the many issues that need to be adressed the following need special emphasis:[28]

Linking labour market policies with reconciliation. Iraq is currently undergoing a phase of social turmoil and change, which inevitably is adversely affecting the lives of a large part of the population. However, for the future of Iraq it will be critical that all communities have a stake in building and maintaining peace. It is estimated, for example, that through the discharging of the army in 2003 up to 500,000 men have lost a source of stable income. Many also lost their jobs owing to large-scale dismissals in the Ministries of Interior and Information, and in the military industries. Adopting appropriate employment measures for these heterogeneous groups, that range from ordinary soldiers to senior executives of the ministries, poses a difficult challenge. One step the Iraqi Government has taken has been to allow former members of the Baath party to go back into the civil service, but clearly more measures are required. Proactive measures such as wage subsidies, training and re-training, microfinance, and also, to a certain extent, cash for work programmes need to be put in place and, where operating, strengthened or up-scaled if the security situation allows. For some of those dismissed, placement in public-sector jobs may seem the only acceptable form of employment. Thus in recent years, Iraqi authorities have relied on large-scale hiring for the public sector. In part this reflects relying on the so-called "traditional social contract" in Iraq. Care must be taken, however, to balance the widespread desire for public employment with long-term financial sustainability. There is no doubt that finding an appropriate response to this issue is challenging and it may involve difficult trade-offs, but the challenge is one that ought to be faced with carefully thought-through policy responses and practical programmes.

[28] The ILO will be providing technical support in developing the first three of these areas starting early 2007 through a donor-funded programme.

Building institutional capacity: As important as the aforementioned immediate measures may be, the long-term task consists in restoring the capacity of the national system of employment services and vocational training. Currently the agenda continues to be dominated by the need to rehabilitate buildings, procure equipment and develop training materials. Further capacity building is necessary in particular in the area of job matching systems, streamlining registration procedures, and vocational counselling. The goal must be to better coordinate the development of employment services in order to move to a more strategic approach in labour market policy. This effort will have to include training of vocational trainers and other capacity building interventions. A new unit in the Ministry of Labour has been set up to combat child labour. This is clearly an important issue as children are often among the most vulnerable in times of transition and change. Other groups that need to be specially targeted are those who are traumatized or disabled as a consequence of violence, widows with children, and internally-displaced persons.

Moving towards demand driven training systems: There is wide consensus that vocational training should be demand-driven. That is, skills should respond to the scarcity in the labour markets. For wage employment and public sector enterprises skills demand can be forecast to some extent. However, many persons will eventually have to find work in the private sector, which is currently not really being catered for by the vocational training system. Given the large wage and job quality gap with public sector employment, many workers do not yet see the private sector as an option that is worth the effort for acquiring special training. Thus training for the private sector must be accompanied by programmes to improve the job quality in private enterprises, including micro enterprises. Unless this is done in an integrated manner, the combination of insufficient training and lack of product quality can be a vicious circle that keeps private enterprises in a low productivity growth trap. More on-the-job training is required. Many countries have had positive experience with the creation of a steering platform with due participation of social partners – including those that represent small enterprises – to guide the way towards a demand driven vocational-training system. This is especially important as globalization is a reality for Iraq and diversification of the economy has become a strategic need.

Labour market information: The success of labour market measures rests heavily on the performance of labour market information systems. Only when the needs of the labour market are surveyed in an adequate manner, and the information on skill profiles and expectations is properly recorded, can training and other measures become effective. Iraq's service centres already have a database in place, but much more effort and investment is needed to upgrade it to international standards. Improving the system could help to develop more precise labour market information that can be passed on to jobseekers. In the short term, training should emphasise skills in areas where demand exists, such as construction, information technology, and communications. The existing system should be geared to meeting the needs of these sectors. In the medium and long term, it is necessary to conduct targeted surveys (e.g. on youth employment) to

get labour market information that is currently not easily available. To do this successfully close inter-ministerial coordination between the Central Organization for Statistics and Information Technology in MOLSA will be essential.

Box 4.1 UNDP's Iraq Reconstruction and Employment Programme (IREP)

Building on its previous experiences in post-war areas such as Afghanistan and the Balkans, and given the employment situation in Iraq, the UNDP launched IREP with the aim of boosting employment creation through labour-based projects to be implemented across the country.
IREP – funded by Japan, the European Community, United Kingdom, Belgium and Denmark – finances projects designed to create short-term employment to vulnerable groups and increase their participation rate in all stages of the project. This is to be done by working closely with local communities, local government departments and local contractors.

The objectives and strategies of the programme are as follows:

- Create temporary employment for vulnerable groups;
- Increase community participation in project design, planning and implementation;
- Jump-start rehabilitation and restructuring of key public sector enterprises and
- Strengthen national capacity to achieve sound debt management.

According to the United Nations Assistance Mission for Iraq, by January 2005, the IREP had benefited over 23,000 unemployed people in the South of Iraq alone, through the implementation of 168 projects at the cost of US$4.5 million. By mid-2006, over 4.6 million workdays had been generated through 869 projects benefiting over 110,000 unemployed people. Such projects have included road repair, garbage collection, rehabilitation of sewage and sanitation systems and irrigation and rural development.
This programme serves as an important bridge between humanitarian activities and the programme of national reconstruction: it responds to urgent needs at a community level and can lead to significant and lasting changes in living conditions, whilst simultaneously reinforcing the ability of local administrations and communities to work together for positive change in overall living conditions.

Source: http://www.iq.undp.org/economy.html

EMPLOYABILITY AND SKILLS ENHANCEMENT

Vocational education

Vocational education in Iraq is considered part of the system of secondary education. It has existed since the early 20th century, but it was only made a primary policy objective after the Baath Party came into power in 1968. The educational policy currently applied is set by the Free Education Law (1974), which guarantees State coverage of the costs of three years of vocational training as one of the three possible tracks of secondary education (See Table 4.4).

Table 4.4: Vocational training in secondary education: 2004
(percentages)

Secondary school enrolment by school type (16-18 year olds)	Male	Female
Vocational education	7.9	1.9
Towards 6th grade baccalaureate	37.9	28.5
Teacher training	3.1	4.6
Non attendees	61.8	73.1

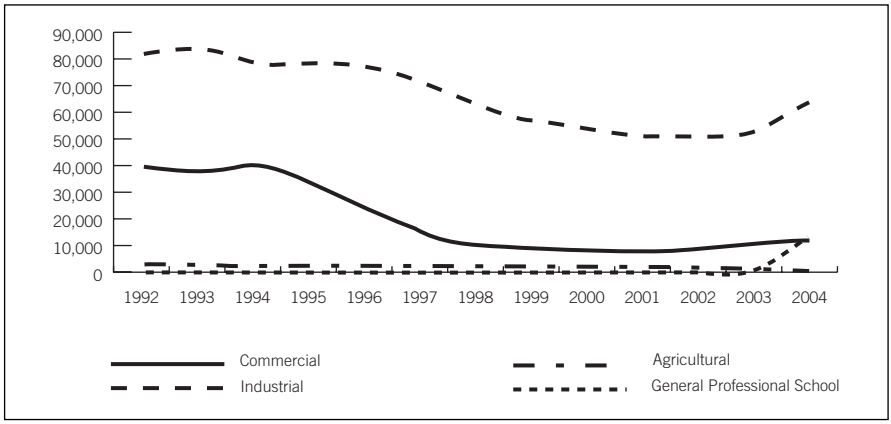
Source: ILO (based on Government-reported data)

After completion of primary and intermediate school, students have the option to take three years of vocational education. The best 10 per cent of these students have an additional option to extend this education through another two years at a technical college. Out of all boys and girls in the 16-18 age group, only 7.9 per cent of boys and 1.9 per cent of girls pursue this option. The reason for this low percentage is the high drop-out rate: 61.8 per cent of all boys and 73.1 per cent of all girls leave school and join the labour force before the age of 19; 37.9 per cent of the boys and 28.5 of the girls pursue further studies at a secondary school leading to a baccalaureate.[29]

Figure 4.2 shows that the enrolment in vocational education has gone down since 1994. This is especially true for industrial and commercial schools. There has been an upward trend since 2003.

[29] ILO, *Iraq's statistical abstracts*, 2004.

Figure 4.2: Enrolment in vocational education in Iraq by subject area



Source: ILO, Iraq Statistical Abstracts 2004. Note that services were interrupted during 2003, but have been resumed since then. The year 2003 is omitted.

Education system

Seen in a broader context, the education system in general is also critical to the question of employment policies. The ILO's Human Resources Development Recommendation, 2004 (No. 195) concerning education, training and lifelong learning[30] stresses the interconnectedness of the skill base of the labour market and the performance of the education system in general. In Iraq, there exists a severe problem that has to do with the poor employability of secondary school graduates in the workforce. It is, for example, more likely for a person who has finished secondary education to become *unemployed* than for those who have dropped out earlier. This is the exact reverse of the experience in the OECD countries, where workers who have finished secondary education are seldom unemployed compared to those with little education.

Prior to 1991, the education system was at the heart of government development plans, with emphasis on higher education and vocational training. Higher education – especially in the scientific and technological fields – was of an international standard. Traditionally, the number of qualified workers, scientists, engineers, and administrators has therefore been among the highest in the Middle East. Over the past two decades, general and vocational education have greatly deteriorated as we shall see next – and not all of this was because of the sanctions, since these started only in 1996.

[30] See ILO (2003), *Learning and Training for Work in the Knowledge Society*, Geneva.

Education is provided by the State free of charge. While primary education (ages 6 to 12) is compulsory, secondary education (ages 12 to 18) is widely available. The latter consists of three years at an intermediary school followed by either three years of secondary school preparing for university, or three years of vocational training preparing for a technical career, or five years at a specially designated school to become a teacher.

Table 4.5: Education and literacy in Iraq in regional perspective

Countries and territories	Adult literacy rate				Primary school enrolment ratio				% of primary school entrants reaching grade 5	Secondary school enrolment ratio 1997-2000* (gross)	
	1990		2000		1997-2000* (gross)		1997-2000* (net)				
	male	female	male	female	male	female	male	female	1995 -1999*	male	female
Iraq	51	20	55	23	111	91	100	86	72	47	29
Egypt	60	34	67	44	103	96	95	90	99	88	83
Iran	72	54	83	69	88	85	74	73	98	81	75
Jordan	90	72	95	84	101	101	93	94	98	86	89
Syria	82	48	88	60	113	105	99	94	92	46	41
Middle East and North Africa	66	39	74	52	95	86	83	75	93	68	62

Source: UNICEF www.unicef.org/files/Table 5_english.xls

Table 4.5 illustrates the decline of Iraq's education system in comparison to neighbouring and comparator countries – Jordan, Egypt, Iran and Syria. Iraq's illiteracy rate for the year 2000 was at 45 per cent for men and 77 per cent for women, which is higher than in any one of the comparator countries. Despite the scarcity of available studies, there are many signs that the literacy rate may even be decreasing, reflecting the deteriorating quality of the educational system. The Iraq Living Conditions Survey, for example, finds that the youth literacy rate (age 15-24) is higher than the literacy rate of the total population, but lower than for the age group 25-34. To a certain extent, this is indicative of the change in the educational system over time and appears to confirm that Iraq's education system is currently on a downward slope. It will be necessary to reverse this trend by restoring and upgrading the schooling system.

Another indicator of a country's human capital and scientific progress is the number of publications produced in refereed recognized international journals (Table 4.6). Arab countries have fallen behind industrialized countries and also behind many Asian developing countries, as demonstrated by the Arab Human Development Report from 2002 (UNDP, 2002).

Table 4.6: Arab science and technology output, papers published in refereed international journals (No. of publications)

	1970-75	1990-95
Iraq	380	931
Egypt	3261	12,072
Jordan	61	1,472
Syria	38	471
Saudi Arabia	126	8,306

Source: UNDP, Arab Region Human Development Report, Statistical Appendix, New York, 2002

Table 4.6 gives some credence to the view that the scientific and technological research capability level of Iraq was comparable or even exceeded many Arab nations in the 1970s. Although Iraq increased its science and technology publications two and a half times, the other countries did much better – Egypt went up by a factor of 3.7, Jordan by 24, Syria by 12, and Saudi Arabia even by 66. There are no reasons to believe that Iraq will not be able to repeat such developments and catch up in the long run.

Box 4.2 Rebuilding statistical capacity in Iraq

Rebuilding statistical capacity is an important contribution to reconstruction and capacity building in Iraq. The effective design of employment and social policy requires data of sound quality that are up-to-date and transparent. Statistical data are often an invaluable source for the different agents in the labour market such as businesses, workers' organizations and job seekers. Although the data situation has improved in the last two years – most notably through the ILCS household survey of 2004 – significant gaps remain. Currently COSIT is the main centre of statistical competence in the Iraqi Government. Major capacity building interventions have been conducted by the ILO and other UN agencies, but more is required. Circumstances permitting, COSIT's employment and unemployment survey should be implemented at more regular intervals and its underlying definitions could be made more explicit. Also, targeted surveys on employers' needs for specific skills and characteristics of youths would be useful for employment purposes. Experience from other countries suggests that close collaboration between the statistical office and other parts of the Government is crucial. This could help the statistical office to become a service provider for all Government agencies.

SOCIAL DIALOGUE AND LABOUR MARKET REGULATION

Important elements for a well functioning labour market are an effective regulatory framework and constructive social dialogue between representatives of employers and workers. Collective bargaining and negotiation can take place at plant, district, sector or national levels, but for industrial relations to be on a sound footing both parties should have the legitimacy of being both representative and independent. This should apply in the private as well as in the public sector. The rules of the negotiating process are set by labour regulations. After 2003, the Iraqi Government made early progress by initiating the revision of the labour law and a draft Labour Code was prepared with ILO assistance, but this has still not been adopted. Also as noted by the ILO Committee on Freedom of Association in October 2005, the laws banning trade unions introduced by the last regime still remain in force. The Committee looked forward to the adoption of the new Labour Code so as to ensure full protection of the right to organize and to bargain collectively for all workers, employers and their organizations in Iraq and ensure that the laws banning trade unions in local and national Governments are repealed.[31]

Development of social dialogue in Iraq

Through a 1958 law (issued in 1959) the rights of workers were recognized in Iraq, and a legal framework for industrial interest intermediation, arbitration and conflict resolution was established. In the late 1980s, however, the Baath regime adopted a different approach leading to a general deterioration of rights. This was noted with regret throughout the 1990s by the ILO Committee of Experts and Committee on Freedom of Association. The draft Labour Code currently under discussion lays down the conditions under which a workers' association must be recognized for bargaining purposes. On such a basis, the social partners can expect to play a consultative role in the formulation of State policy on such issues as unemployment and safety and health measures.

Rules for hiring and employment termination

Labour regulation rules usually set certain minimum standards for hiring and employment termination, although these may need interpretation through negotiation. The rules for dismissal especially must be transparent and practical to ensure compliance and facilitate enforcement. The currently applicable law of 1989 requires companies to make use of an Employment Office, if they wish to recruit workers. It lays down the procedures and time limits to be observed by companies and offices for that purpose. Subject to certain exceptions, companies

[31] See Committee on Freedom of Association Report on the Iraq (Case No. 2453) Report No. 342 *(Vol. LXXXVIX, 2006, Series B, No.2)* http://webfusion.ilo.org/public/db/standards/normes/libsynd/ LSGetParasByCase.cfm

are required to accept workers with suitable qualifications who have been referred to them by the Employment Office (Article 17). Further, employers can only terminate employment relationships if the reason for the termination is down-sizing of the enterprise and after going through an arbitration process. In the new regulatory framework it would be important to combine a degree of flexibility for firms to adjust to changing market conditions while ensuring income and employment security to workers. An important ingredient of success is that the labour market policies be institutionalized.[32] Tripartite social dialogue is necessary for designing and implementing effective labour market policies. Tripartism will aid the acceptance of change, improve the design of regulations and policies and ensure sustainable financing.

The draft Labour Code includes a number of safeguards, so as to avoid abuses to the detriment of the workers. The lack of progress in passing the new law must of course be understood in the light of the exceptional circumstances in Iraq. However, a failure to keep labour law relevant and updated may risk leading to arbitrary ad-hoc decisions and may discourage enforcement. To move towards strengthened institutions both issues must be addressed in parallel: a legal update and greater emphasis on compliance and enforcement. The ultimate priority, however, must be a development towards better respect for the rule of law.

Wage setting

In Iraq, wage setting for public administration and State-owned-enterprises is defined by law. The 1989 Labour Code states that the wage rate shall not be lower than the minimum wage for an unskilled worker, which is fixed at regular intervals by a tripartite committee established by the Ministry of Labour and Social Affairs. The Coalition Provisional Authority established a minimum wage of Iraqi Dinars 69,000 (US$7) per month. However, as the World Bank notes, it is unclear whether the wage is in fact binding on employers and whether it is enforced (World Bank, 2005). The draft Labour Code under discussion raises the possibility for a slightly different approach. According to this proposal, the minimum wage will be fixed by the Government after consultation with a tripartite minimum wage board that will need to be established.

Social partners

Social dialogue is based on a legal framework, but whether it can be effective depends on capable federations of workers' and employers' associations. Social partners can play an important role in industrial relations and in the settling of

[32] The ILO has contributed substantially to the discussion on adjustment, flexibility and workers' protection in the framework of globalized economies. See Auer, P. and Cazes, S. (2003), *Employment stability in an age of flexibility*, ILO Geneva; Cazes, S. and Nesporova A. (2003), *Labour markets in transition: Balancing flexibility and security in Central and Eastern Europe*, ILO, Geneva; Auer, P. Berg, J. and Coulibaly, I (2005), "Is a stable workforce good for productivity", *International Labour Review*, Volume 144/3.

labour disputes, and on this basis they can play a consultative role in the formulation of State policy on such issues as unemployment, safety, and health measures. Since 2003, employers' and workers' organizations have reconstituted themselves. The organization of employers is the Iraqi Federation of Industries. It represents mainly the food processing sectors, basic processing industries, and some other small industrial sectors. The principal functions of the federation are (1) to represent the interest of its members with Government and other authorities, (2) to exchange views with the Government on industrial policies and strategies, and (3) to represent Iraqi employers in tripartite schemes of the Government and in international organizations.

Prior to the take-over of power by the Baath Party, a number of different trade union federations existed. The Baath Party set up a single "official" federation in the 1970s. Thus after 2003, it was recognized that it was necessary for Iraq to re-establish independent unions. There has been some progress in this field, although as noted earlier the International Confederation of Free Trade Unions (ICFTU) and the International Confederation of Arab Trade Unions (ICATU) has filed a complaint with the ILO Committee on Freedom of Association alleging that the authorities have adopted Decree No. 875 which gives the Government control over the finances of existing trade unions and revokes previous arrangements that allowed them to operate without undue interference and harassment from the State and had legitimized free trade unionism for the first time since the 1970s.[33]

In 2005, the three major trade unions that had established themselves signed a joint agreement in Damascus supported by the International Confederation of Arab Trade Unions. According to this agreement they will elect a unified body responsible for representing workers within a tripartite committee of work and social security.

[33] In its recommendations the Committee on Freedom of Association invited the authorities to repeal Decree No. 875 and to enter into full discussions with all concerned parties so that a solution may be found that is satisfactory to all parties concerned and keep it informed of any progress in this respect.

CHAPTER 5. EMPLOYMENT IN SMALL ENTERPRISES

INTRODUCTION

According to recent surveys, 60 per cent of Iraq's working population, or 2.3 million people, earn their living through running or working in a private or family business. Given the large size of Iraqi families, approximately 6.4 million non-workers are thus dependent on these incomes as their sole source of livelihood. These businesses are almost exclusively SMEs. The key to sustainable job creation in Iraq is therefore to focus on small enterprises and their productive development (ILCS, 2004).

This requires a policy that recognizes the central priority of small enterprises as a source of livelihood and sets the right conditions for their growth. At present, the high level of continuous violence poses a fundamental obstacle to investment in the private sector. However, the Iraqi Government needs to act to tackle some of the problems constraining entrepreneurship. Restoring an orderly policy and regulatory environment for SMEs is therefore one of the high priority tasks identified by the Iraqi Higher Council on Employment Creation and is also endorsed by the current National Development Strategy.

This chapter identifies and addresses some relevant issues for improving the policy environment of small enterprises in Iraq. It describes the macroeconomic as well as the legal and policy level factors determining the potential of SMEs to create new employment. It relates them to international best practices and suggests possible ways for the Iraqi Government to improve the situation.

The chapter is organized as follows: it first looks at the *size, employment intensity, and remuneration levels* in the private sector. This is followed by a brief analysis of the *historical role* that the private sector has played over the past decades, and how this has been affected by broader macroeconomic trends and developments.

It then goes on to explore the *policy and regulatory environment*, discussing the fields of business registration, labour relations, and taxation policies. Next, these policy fields are linked to the role of *financial institutions*. Finally, some

recommendations for the design of policies are made to promote employment by means of developing small enterprises.

The state of SMEs in Iraq

The abbreviation SME *for the purpose of this report refers to all establishments with a headcount lower than 30 employees*.[34] All enterprises with one to four workers are considered to be *micro* enterprises and those with five to nine workers *small*. Those with 10 to 29 workers are defined as *medium* sized and those with 30 and more as *large*. By definition, SMEs are *non-agricultural* establishments in private ownership.

The present analysis draws on three statistical sources: (i) The Iraq Living Conditions Survey (ILCS) from 2004, (ii) data drawn from the files of the Iraqi General Taxation Commission (GTC) from 2005 and (iii) a business climate survey conducted in 2004. To date, no establishment survey has been implemented. The data are sufficient, however, to give a tentative overview of the size and sector distributions of employment in small enterprises and their degree of formalization.

Table 5.1: Employment in the private sector by enterprise size and industry: 2004

	Manufacturing and construction		Trade and services		Public administration, education, and health		All	
Micro enterprises (< 5 persons.)	402,064	56%	1,320,543	89%	119,875	77%	1,842,481	78%
Small enterprises (5 to < 10 persons.)	222,733	31%	97,043	7%	18,893	12%	338,669	14%
Medium enterprises (10 to < 30 persons)	77,880	11%	46,316	3%	13,013	8%	137,209	6%
Large enterprises (> 30 persons)	13,649	2%	15,862	1%	3,655	2%	33,166	1%
All	**716,325**		**1,479,765**		**155,435**		**2,351,526**	

Source: ILCS, 2004. The data used are from the files IMIRARoster.saw and IMIRAMain.saw, both dated 26/11/2004.

[34] As there is no nationally accepted and official definition of SMEs in Iraq, the one proposed here is only one of many possibilities. In other countries, it is not unusual to refer to enterprises with up to 99 employees as 'small' – as in Mexico. However, in the case of Iraq, this definition would not be useful as there are only very few private companies on the upper margins of the small enterprise size scale. Widening the definition to companies with up to 100 employees would yield less than one percentage point (about 0.5) of employment in the 'large' size category. In Iraq, it is therefore common to refer to private enterprises with less than 30 workers as 'small and medium-sized'. A survey of industrial establishments conducted in 1983, for example, referred to industrial enterprises with less than 30 employees and less than Iraqi Dinars 100,000 of fixed assets in non-power generating equipment as 'SMEs' (Al-Khudayri, 2002, p.204).

Employment in micro, small and medium-sized enterprises

An overwhelming majority of the people working in private businesses in Iraq work in micro, small and medium-sized enterprises and only a tiny minority in large firms. In the non-agricultural private sector 92 per cent of those employed work in enterprises with less than ten employees. A further six per cent work in enterprises with less than 30 workers, and only one per cent work in enterprises with more than 30 workers. Furthermore, employment within the SME category appears to be concentrated at the lower end of the spectrum. When it comes to size, 78 per cent of those employed in the private sector work in *micro* enterprises with less than five employees (ILCS, 2004).

To a certain extent these observations are also indicative of the *conditions of work* in SMEs, since employment conditions are typically worse and productivity is lower in micro enterprises than in larger ones. An ILO comparative study of seven developing and transitional countries[35] found that jobs in small enterprises are less remunerated, less productive, and of poorer quality on average than jobs in larger enterprises, even after controlling such factors as gender and skills endowment. Considering that the economically weakest members of Iraqi society are usually not unemployed, but in fact part of the working population, it is probable that the poorest urban Iraqis find their source of livelihood in the micro or small enterprise segment.

The ILCS (2004) data on private sector employment also suggest that *women* are relatively underrepresented in SMEs – which is typical for Middle Eastern labour markets. The share of women in large public enterprises and in farms is much higher than their corresponding share in micro, small and medium-sized enterprises. This trend reflects traditional gender roles, in which the civil service tends to be one of the few socially acceptable professions for women. Likewise, working on a family farm or as a white-collar worker in industry has also been an acceptable occupation for women in Middle Eastern societies.

Formal private enterprises in Iraq

In 2005, a total of 1.3 million private companies were registered for taxation purposes in Iraq, and they can therefore be considered as part of the formal economy. This is supported by data from the taxation file of the GTC,[36] which is shown in Table 5.2. The table suggests that SMEs are fairly well included in the taxation system compared to other countries affected by conflict. Yet the high tax-registration rate does not necessarily imply that staff of SMEs are also formalized and have regular employment contracts. It is possible that a considerable number of employees have only informal contracts, even if the enterprises were registered for taxation.

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[35] The countries were Chile, Guinea, Pakistan, Peru, South Africa, United Republic of Tanzania, and Viet Nam (Reinecke & White, 2004).

[36] As of Income Tax Law No. 113 of 1982, para. 2, amended.

According to the data from the GTC, SMEs were concentrated in a few specific subsections and professional categories: the category "taxis and transportation" alone accounted for 30.8 per cent of all registered enterprises – mainly consisting of taxi drivers, of which almost half a million have been registered. Other sizable sub-sectors include trade and to a lesser extent manufacturing and construction. Several points should to be kept in mind when reading the data from the GTC: the data have the advantage of being "official figures" instead of being merely estimated figures. Yet, at the same time, they may have been subject to several biases and uncertainties. First, many small businesses may not have been registered with the taxation office. Second, in some companies more than one person may have been eligible for company income tax under Income Tax Law 113. Furthermore, it is possible that some companies appear several times in the file, as several associates of a limited liability company may have been eligible for company income tax, and these associates may appear in the file as well. The file therefore needs to be read with caution. Yet, the margin of error is not great,

Table 5.2: Entrepreneurs registered with the General Taxation Commission and the Directorate for Industrial Development

	Total	Per cent
Manufacturing and Construction		
Industrial Services and Crafts (Goldsmiths, Tools Maintenance)	10,500	0.8
Furniture Manufacturing and Carpentry Services	4,600	0.3
Food Supply		
– Bakeries	8,000	0.6
– Others	2,700	0.2
Carpentry Factories	1,300	0.1
Garment Industry	2,700	0.2
Construction	41,000	3.1
Foodstuffs	10,700	0.8
Agricultural Industry	2,700	0.2
Carpentry	1,300	0.1
Paper Manufacturing	1,000	0.1
Automobile Related Manufacturing	900	0.1
Rubber and Plastic	600	0.0
Enterprises Registered with the Directorate for Industrial Development	55,000	4.1
Sub Total	**143,000**	**11**

Table 5.2: (continued)

	Total	Per cent
Trade and Services		
Semi Skilled Services (Carpenters, Bakers, Own Account Workers)		
– Freelancers	88,693	6.6
– Private Services	43,686	3.3
– Other	7,421	0.6
Taxi and Transportation		
– Taxi	414,500	30.8
– Pick-up Cars	121,500	9.0
Unclassified Services	44,000	3.3
Transport and Automotive Maintenance	209,500	15.6
Miscellaneous Services		
– Hotels and Restaurants	26,866	2.0
– Body Care Services	16,400	1.2
– Other	27,734	2.1
Specialized Services (Legal Professionals, Technicians)	26,284	2.0
Health Services	24,167	1.8
Literature and Artistic Services	8,400	0.6
Fuel Services	886	0.1
Food Supply Services	65,300	4.9
Wholesale and retail traders		
– Import-Export Retailing	21,600	1.6
– Peddlers/Salespersons	2,600	0.2
– Retailers	2,700	0.2
– Other	5,700	0.4
Clothing and Accessory Retailing	18,000	1.3
Retailing of Manufactured Goods		
– Accessory and Spare Part Retailers	10,000	0.7
– Other	3,900	0.3
Garment Retailers	6,600	0.5
Domestic Retailers	3,700	0.3
Leisure Retailers and Services	475	0.0
Sub Total	**1,200,612**	**89.4**
TOTAL	**1,343,612**	**100.0**

Source: Al Umari & Altimen, 2005

as the data from the ILCS (2004) also suggest a similar number – slightly more than one million SMEs.[37]

The size of the SME sector is one important aspect of the overall picture. Yet, in order to judge whether the extension of SME employment is desirable from a socio-economic perspective, it is necessary to consider the job quality in SMEs. This question is linked directly to the question of poverty alleviation, which is the central objective underlying the current efforts to improve the policy environment for SMEs.

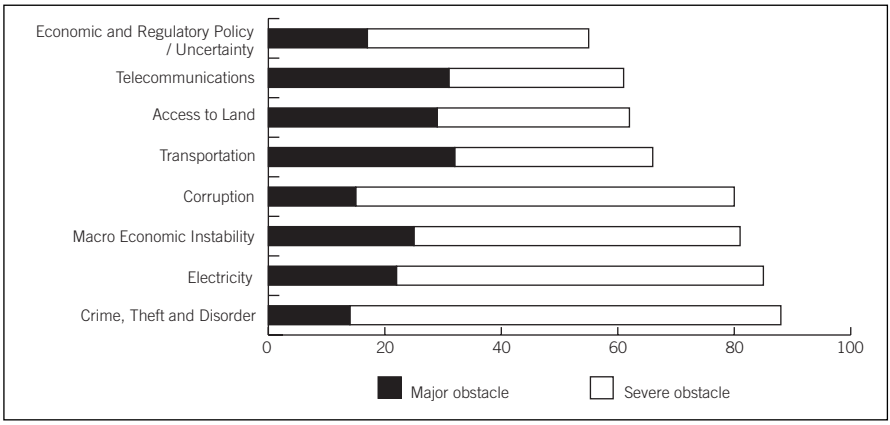
There is little empirical information available on other job quality indicators such as insurance and retirement payments, maternity allowances, sick leave and training. Yet, it can be safely assumed that micro enterprises scored low or at best moderately on all these indicators – almost certainly lower than State-owned enterprises. In general, the educational level of workers is lower in the private sector, and there is a lack of formal training for the skills required to run a small enterprise, since the vocational schools and training centres cater to the needs of State industries and commerce. Training in SMEs is mainly informal and on-the-job. There can be little doubt that the job quality in SMEs in the private sector is perceived as having lower value and prestige than the job quality in the Government sector. This should not be taken to mean that SME employment is inferior and therefore less deserving of the attention of policy makers than larger enterprises. Rather, it shows that small and medium-sized enterprises provide employment to socially disadvantaged groups and that they help to integrate these groups into the labour market. Their potential to provide sustainable and quality employment opportunities must however be improved.

Major business constraints

Figure 5.1 shows that the business regulatory environment (including "uncertainty") is *only one of many factors* that respondents perceived as important to SME development. It is notable that crime, theft and disorder were ranked as some of the most important factors determining the lack of business success, as reported by a survey for which around 700 SMEs in the Southern Governorates were interviewed in February and March 2004 (Economic Institute, 2004). In 2003, the Iraqi-American Chamber of Commerce & Industry conducted a survey for the whole country, resulting in very similar findings. Not surprisingly, crime, theft and

[37] The total number of SMEs (including the non-registered) can be estimated on the basis of the data from the ILCS (2004). Dividing the total number of workers in each size category by the average enterprise size for this category yields an estimate of the number of enterprises within each size category. Using this method would suggest 1,053,482 micro enterprises and 56, 982 small enterprises. However, this estimate is not very accurate for three reasons: first, the estimates are particularly uncertain for the larger enterprises, as respondents are few. Second, as workers in the same enterprise may live close together (e. g. in the case of the company town), standard deviations become large since the ILCS used a cluster sample. Third, workers in large establishments are likely to misreport the number of co-workers, because in many cases they will not know the precise number.

Figure 5.1: Major constraints for business growth in Southern Iraq



Note: The data used is from ECON, Oslo, Norway. A sample of 750 establishments were interviewed for this survey during February and March 2004 covering the provinces of Basra, Al Muthanna and Dhi Qar.

Source: Economic Institute, 2004

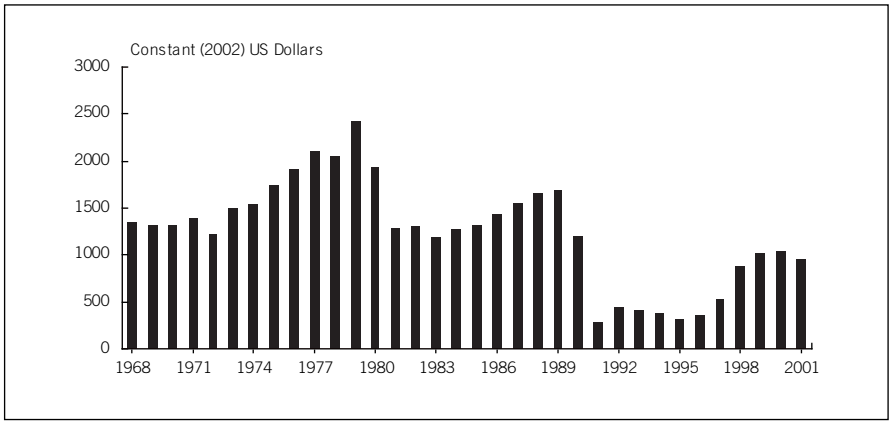
disorder were on top of the list of constraints to growth of private business. Lack of electricity was another significant obstacle. Many small businesses reported frequent power shortages and stable power only few hours a day on average.

DEVELOPMENT OF THE SME SECTOR

Development up to 2003

The development of the SME sector should be seen within the context of the development of the Iraqi economy before 2003. The huge fluctuations of this economy in the period from 1968 to 2001 are depicted in Figure 5.2.[38]

Figure 5.2: Iraqi gross domestic product per capita: 1968 – 2001 (US$ in 2002)



Source: Estimates by COSIT, 2004

Figure 5.2 gives the development of Iraqi GDP per capita between 1968 and 2001 as estimated by the Iraqi Statistical Office. The negative impact of three subsequent wars (1980, 1988, and 1990) and of the embargo regime (from 1990) is clearly visible from this figure, as the economy has been shrinking drastically since 1989 with an equally grave depression in aggregate demand. Once a middle-income country, Iraq was an impoverished country in 2004. The only exceptions to this tragic development were three Northern Governorates (Dohuk, Erbil, and Suleimaniyah), where great losses during the wars were offset by an economic recovery during the 1990s. The lasting economic depression has left many traces on the labour market. One of them has been the increase of SMEs' share in non-agricultural employment. Much of the employment generated during that period was informal, or only partially formal in nature, often of inferior quality compared to the work in larger enterprises.

[38] Levels of annual GDP per capita are obtained by dividing annual GDP at current market prices by the total population. This table is based on market prices of the year 2002 (in US$).

In summary, within the Baathist developmental framework the private sector remained marginalized and was often the last resort source of employment. This resulted in the emergence of a large number of micro and small enterprises but of few enterprises in the middle of the size spectrum (30 – 100 employees). These middle-size enterprises were usually the result of small enterprises growing larger. Typically this occurred because the law of economies of scale or technical innovation gave them a competitive edge against other businesses. However, in the context of two subsequent wars and a strictly monitored economic embargo, the business climate was apparently not suitable for business expansion – and as a consequence businesses remained small. Therefore, up to the present almost no enterprises larger than 30 employees can be found outside of the public sector.

SMEs in post-Baathist Iraq

Since the fall of the Baathist regime in 2003, the macroeconomic environment for SMEs has been influenced by three main factors: *first*, the country had witnessed a paralysis of economic activities due to ongoing conflicts. This paralysis was visible in the deterioration of production establishments suffering from acts of sabotage and looting. *Second,* new business opportunities for SMEs have opened up due to reconstruction and rehabilitation activities as well as to the trade of imported goods[39] that have flooded the markets. Unfortunately, the net result of these two trends has been a further delay of the desperately needed recovery process: SME market opportunities have suffered from a reduction in investment incentives and high-risk costs. Infrastructure reconstruction projects have remained out of reach for small businesses, as contracts were mainly awarded to foreign companies with insufficient Iraqi participation in terms of employment and returns. The *third* major influence has been the continuation of the SME sector as a last resort employer. Those who lost their jobs in the army and law enforcement have often turned to the SME segment as the only remaining source of employment and livelihood. This also includes enterprises that take advantage of the legal gaps and minimal Government control to make quick and easy revenue. Yet, despite these negative circumstances, the Iraqi population has displayed remarkable resilience in dealing with these difficult circumstances. Most surveys conducted to date show some confidence in Iraq's recovery. Public sector salaries have increased dramatically, which in turn has stimulated consumer spending. Import barriers were removed, which appears to have created a boom in the retailing of imported goods. On the other hand, most observers agree that this is not the kind of sustainable economic recovery that Iraq will need to remove the pressure on its labour markets.

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[39] The World Bank Needs Assessment (2003) notes for example that traders are very active and have flooded the market with so called "white goods". This is a term used for all kinds of electronic consumer devices such as washing machines and refrigerators. Some streets have become similar to open-air fairs for consumer goods, for sale at every available location.

Creating an orderly environment for SMEs

According to the ILO Recommendation on Job Creation in Small and Medium-sized Enterprises (1998, No. 189), the most essential prerequisite for small enterprises to grow is an orderly institutional environment. It is further considered vital to find the right balance between the need to remove barriers for business-investment and the need to ensure respect for workers' rights. This means creating institutions that allow small enterprises to move from the periphery to the centre-stage of economic and social development. The following section will discuss constraints to productive development of small and medium-sized enterprises and relate this to international best practice in building sustainable institutions for the productive development of SMEs.

ILO research synthesized in Reinecke and White (2004) shows that small enterprises that comply with registration and licensing requirements create more employment over time than those that do not comply. Some countries have had positive experiences in adopting special SME laws, in which all legal provisions are streamlined in order to reduce the costs of compliance for small enterprises. This usually results in more enterprises that benefit from the many advantages that being part of the private sector entails. In Iraq, these efforts are in their infancy, since Iraq neither had an SME policy nor a well developed strategy for private sector development, and policy has yet to overcome the Baathist legacy. Recently the process of reforming the policy environment for SMEs has been initiated, but care must be taken that the interests of micro enterprises are duly considered in the reform process.

The current business environment is hampered by a lack of legal capabilities in the commercial field to ensure an orderly business environment. This lack of law enforcement is based on unclear, ambiguous and overlapping provisions of business law which make compliance with the law difficult and pushes enterprises into a legal grey zone. The American Coalition Provisional Authority legislation conducted some changes to the business regulations – notably permitting single-member limited liability companies and streamlining some of the registration procedures, but, as further detailed in the Annex to this chapter, some deficiencies persist: in 2004, the registration procedure entailed 11 different steps, and entrepreneurs could expect to wait for 77 days, until formal registration for a medium-sized limited liability company was granted. Also, the law lacked coherent and detailed provisions on rights and obligations of enterprises' sole proprietorship, which is usually the legal status suitable for SMEs. However, these changes did not address Iraq's central problems of legal uncertainty and poor capability to enforce contracts. What is currently most needed is the development of an effective judicial system and sufficient legal capacities to ensure rule of law and the enforcement of contracts.

According to ILO experience, a revision of the regulatory framework should not be conducted in an ad-hoc manner. It rather requires prior assessment of the policy and regulatory framework and due consultation among representatives of employers' and workers' organizations. A central factor in this endeavour is usu-

ally the adoption of an officially recognized definition of small and medium-sized enterprises, followed by an assessment of the impact of the regulatory environment on small enterprises. Considering that the ongoing process of reconstruction is accompanied by the persistence of high levels of violence, the expectations for improvement of the working conditions for those working in SMEs can only be modest. Clearly there is no "quick fix". Yet, considering that SMEs provide employment for the majority of people in the country, including economically weak and marginalized groups, the situation of SMEs nonetheless deserves full attention, as has been recognized in the International Compact for Iraq which aims for the formulation and adoption of a new Commercial Code. A major challenge for the Iraqi labour law is to ensure that jobs in micro and small enterprises are protected and decent. There is clear diversity in the ways labour regulations should apply to small enterprises: While some countries, such as Pakistan, provide that all enterprises below a minimal threshold size are exempt from labour laws, others, such as Chile, extend labour protection to workers in SMEs (Reinecke and White, 2004). The 1987 Iraqi Labour Code provides for universal coverage, but compliance and enforcement remain unsatisfactory. It is often stated that labour law restricts business investment and that it provides a barrier to the growth of small entrepreneurship. Yet ILO research conducted in several countries showed that deregulation of labour laws in this area did not have a positive impact on entrepreneurship. This would suggest that the costs of compliance need to be carefully weighed against potential gains in productivity and workers' welfare. According to ILO experience, general exemptions for SMEs from labour-related laws leave workers unprotected and can result in a growth trap where workers move to the informal sector (or do not provide contracts to their employees) once they reach the threshold size. Therefore the focus should be on simplifying and lowering the cost of compliance. Specific administrative machinery could be established to decide whether differential treatment of small enterprises may be required, with due involvement of the concerned employers' and workers' representatives.[40]

Even if the exact extent to which SMEs ought to be subject to labour law needs further discussion, there appears to be broad consensus that the current Labour Code inherited by the present Iraqi Government is outdated and in need of revision. In 2004, the Government confirmed that such a revision was indeed intended and one of the points on the governmental agenda. The current Labour Code contains many provisions that are impractical for the SME sector and that will, if implemented according to this law, appear to be difficult to implement within the framework of the market economy. In particular, this refers to the regulation in the field of employment termination. The Draft Labour Code seeks to introduce more flexibility in this regard, including by allowing establishments with less than ten regular employees to terminate employment with notice. But it also includes a number of procedural mechanisms to avoid abuses to the

[40] This recommendation is drawn from the ILO draft of the Iraqi Labour Code (Footnote 3, ILO, 2004).

disadvantage of workers, including on the burden of proof required in court when a worker challenges his dismissal.[41] It is essential to recognize that the need to combine flexibility with worker protection does not lead to the lowering of core labour standards. A realistic minimum wage can be a useful point of reference but its level should be determined judiciously in terms of helping the lowest paid workers. Labour inspection is then a very serious responsibility for the Ministry of Labour and Social Affairs. Labour legislation must be applied intelligently to small enterprises, neither forcing firms out of business nor condoning hazardous or underpaid employment.[42]

In the area of social security and safety nets, Law No. 39 of 1971, currently in force on social security, was applied only to private enterprises that employ three or more workers (See Chapter 6). Revision of the law should give due consideration to establishing a minimal size that can be periodically adjusted, with the long-term goal to include all workers and self-employed under social protection schemes. Mandatory social security contributions for the provision of health or retirement benefits often become another contentious issue for small enterprises. The level of contributions may seem high while workers are often unconvinced that they are getting a good return for their money. In such circumstances neither worker nor employer has an interest in contributing and special provisions usually need to be made. Casual workers and the self-employed also need different treatment. The development of smaller-scale schemes of social insurance may be possible.

Table 5.3: Sources of revenue (in US$ million, 2004, 2005, 2006)

	2004		2005		2006	
Personal income tax	10	0.1%	31	0.2%	63	0.3%
Company income tax	21	0.2%	52	0.3%	104	0.5%
Oil revenues	12500	99.8%	19271	99.6%	20104	99.2%
Total	**12531**		**19354**		**20271**	

Source: Government of Iraq 2004 budget

While taxation levels are usually among the key constraints for entrepreneurship, this general rule is only partly relevant for Iraq, as shown in Table 5.3. Despite the attempts of the Government to extend the revenue base of the State, the table shows that company tax revenues in 2004 constituted only a small fraction of the budgetary sources. According to the Government budget, income tax

[41] This is based on the Termination of Employment Convention (No. 158) 1982, which allows some categories of workers to be excluded from its provisions in the event of special problems arising from the size or nature of enterprise. See Arturo Bronstein (2005), *The Iraqi Draft Labour Code*, paper presented at the ICFTU Arab Regional Conference on "Trade Union Rights – Promoting Human Rights at Work"; Amman, 9-10 February 2005.

[42] http://www.solidaritycenter.org/files/ArabRegionalConferenceMarch2005.pdf

was to reach half a percentage point of total Government sources by 2006. Much more important then are taxation tariffs and trade regulations: the Iraqi market is flooded today with various imported goods – many small-scale Iraqi goods and even services face fierce competition. This development may have been unavoidable, but it was certainly accelerated by the adoption of a zero tax regime in 2003. Many Iraqis complain that Iraq exports oil and imports nearly everything else. The agricultural and industrial sectors in particular are suffering from competition from imported goods.

The ILO's Job Creation in Small and Medium-Sized Enterprises Recommendation, 1998 (No. 189) also highlights the importance of a sufficiently broad supporting infrastructure for SMEs. This involves skills training for business start-up and improvement, human resource development, as well as financial support. The reconstruction effort shows some initiatives in this area, but they need to be increased to come close to what the SME sector requires. Another field of action is the need for business partnerships between SMEs and the public sector. This applies to all countries, but in only in few countries is this as important as in Iraq, which continues to be a State-dominated economy. Many countries have had positive experiences counteracting the difficulty that small enterprises often have when they attempt to benefit from public procurement opportunities. It will further be necessary to develop and upscale affordable business development services, which should be made broadly available.

Another major barrier to business development is the underdeveloped, inadequate and underutilized banking system in Iraq. Access to credit and availability of capital are of great concern to SMEs. Findings from questionnaires and interviews show a very limited use of banking and financial services by SMEs and the self-employed. Historically, the banking system in Iraq was unable to cater to the financial needs of private sector development due to the inherent weak capital base of its constituents, and limitations on the banking system's capacity to meet market needs. Credit activities were mostly limited to traditional services such as short and medium-term loans, credit letters and bill discounting. In the absence of an effective formal financial system, small enterprises can only build upon retained profits, street moneylenders (charging exhorbitant fees such as 25-40 per cent per month), or Rotating Savings and Credit Associations (ROCSAs). The latter are groups run by women's circles that provide credit on a mutual basis but are ill-suited to provide finance for business investment purposes.

Major factors behind this failure of access to credit for small enterprises were a backward and limited legal and commercial institutional framework and the exaggerated governmental constraints controlling banking activities. Finance and lending polices adopted by banks are still exclusively commercial, requiring high interest rates and remaining limited to short-term loans with exaggerated guarantees. Security issues are currently exacerbating these limitations. Several cases of kidnapping, reported among industrialists, force entrepreneurs to keep a low profile in their business activities and financial standing. The banking system and capital markets are witnessing major restructuring and develop-

ment. Nineteen private banks have been founded since 2003, along with new governmental, commercial and specialized banks (industrial, agricultural, social and housing) and development funds. The latter include the economic and social fund of the MoPDC, the industrial development fund of the Ministry of Industry (MoI), and the export support fund of the Ministry of Trade (MoT). There are also some donor microfinance projects that act as implementing partners of international aid agencies. If successful these institutions should be upgraded to reach significant impact. Business incubators could act as facilitators to bridge the gap between SMEs and the financial sector. For SMEs to play out their full job-creating potential, steps should be taken to improve the availability of financing to SMEs including credit guarantees and concessionary financing including packages targeted towards micro enterprises.

Box 5.1. Donor funded support for SMEs

A variety of donor funded projects on microfinance and entrepreneurship development for SMEs have been implemented since 2003. These have included the United States Agency for International Development (USAID) assistance programme called the "Community Action Programme", which consists of a variety of projects. These include Agricultural Cooperative Development International/Volunteers in Overseas Cooperative Assistance (ACDI/VOCA) covering the districts of Mosul, Kirkuk and the Iran/Iraq border region, International Relief and Development (IRD) for the greater Baghdad area, and the Community, Habitat, and Finance (CHF-International) for South and South Central Iraq. The latter initiative disbursed funds to 16,000 people with a total volume of US$43 million as of May 2006, and also conducted large training interventions. According to CHF reports, a 99 per cent repayment rate was recorded throughout the life of the programme. Another donor organization is the UK DFID, which is active through its Governance Capacity Building Programme (GCBP) through which it administers the so-called Governorates Development Fund. Other activities include the establishment of a provincial forum for business associations, a business information centre and a business journal. These initiatives are complemented by in-country training courses on "Growing Commercial Ideas", "Enterprise Development" and "Women in Enterprise". According to DFID, by 2006 over 2,000 small-scale entrepreneurs had benefited from these courses. Overall DFID had committed £20.5 million to the GCBP as of March 2006.

Source: Reed (2005) and information collected from reports of donor agencies.

CONCLUSIONS

A concerted and coordinated approach will be necessary to move towards an orderly business environment for SMEs. This process entails a number of elements, such as reducing the cost of compliance with the regulatory framework, linking SMEs up with the formal credit market, empowering local entrepreneurs with better skills, and improving access to Government procurement in reconstruction. Finally, targeted policies are needed for value-chain upgrading. This is spelled out in detail in the Annex to this chapter that draws on the action plan adopted by the UN Iraq Employment Conference in 2004.

All these are important aspects of the business environment. However, the most significant obstacle that must be addressed clearly goes beyond the field of business regulation. To move towards a more orderly business environment Iraq needs to return to the rule of law and ensure contract enforcement. Iraq's SME sector would be best aided by the development of an effective judicial system and sufficient legal capacities to ensure the rule of law and the enforcement of contracts, and freedom from fear. This must be credibly guaranteed by an effective policing and law enforcement system.

ANNEX TO CHAPTER 5

Annex Table 5.1: List of technical recommendations for development of SMEs

	Activities / Objectives
Policy Environment and Development of an Enterprise Culture	• Formation of a technical advisory committee, supported by the Employment Creation Secretariat, and linked to Higher National Council on Employment Creation • Mapping and assessment of the policy and regulatory framework's impact on SMEs with due consideration for micro enterprises • Establishing a sound legal and regulatory framework to focus and manage the reform process • Designing and reform policies for an enabling environment and a proactive SME policy • Fostering compliance with international labour standards, including child labour and other labour standards within SMEs
Sectorial SME Policy	• Focus efforts on promising sectors to foster the growth of SMEs: reconstruction, oil sector, transport and distribution, carpentry, information and communication technologies, tourism, etc.
Industrial Policy and Supporting Infrastructure for SME Development	• Targeted at developing specific factors of production in the SME sector (skills and human resources, credit) • Targeted at fostering development of niche markets and dynamic sectors of activity • Setting up of industrial and new technologies estates • Support private sector investment and partnerships with Ministry of Industry and Minerals in provision of infrastructure

	Activities / Objectives
Regional and Local Policies	• Fiscal policy for SME promotion within targeted zones • Capacity building of local authorities for enabling local business environment. Public private partnership programmes (PPP) to strengthen capacity of local authorities in procuring from and promote SMEs
Association Building	• Strengthening of member-based associations, particularly for women and youth associations, to ensure that their voices are heard
Business Development Services (BDS)	• Promote sustainable, affordable, needs-based and commercially driven Business Development Services for SMEs and specific target groups, such as youth, women, and vulnerable groups.
Credit Lines and Incubators	• Facilitate the provision of credits for SMEs, particularly for strategic sectors such as housing and construction • Setting up of business incubators for reduced infrastructure and business services costs and for wider access to new information and communication technologies
Micro-Credit and Micro-Insurance	• Establishment of micro-credit institutions as implementing partners within partnership programmes between international, national, and local stakeholders. These institutions should be gradually replaced by commercial banking for SMEs (or the upgrading of micro-finance institutions into retail and commercial banking) • Ensuring that capacities are built within new institutions, and that they are aiming towards technical and financial sustainability within a strategic plan • Geographical scope: impoverished regions
Entrepreneurship development and management skills	• Strategic groups: young entrepreneurs, women, ex-soldiers, vulnerable groups • Strategic sectors: promising sectors, construction, housing, small industries, non-agricultural rural sector
Agriculture	• Strengthen the capacity of the Ministry of Agriculture and of its regional and local agencies • Ensure coordination with the Ministry of Labour and the Ministry of Planning for the design and implementation of programmes with a job creation potential
Housing	• Strengthen the capacity of the Ministry of Housing and of its regional and local agencies

	Activities / Objectives
	• Ensure coordination between the Ministries of Labour and Planning for the design and implementation of programmes with a job creation potential
Other Strategic Sectors (industries, new technologies)	• Trade regimes and industrial policies tailored to the restructuring needs of strategic sectors of activity • Inter-ministerial coordination and integrated policies • Vocational Education and Training

Annex Table 5.2: Rough estimate of total SMEs in the private sector, 2004

	Average Size	Estimated Number
Micro Enterprise	1.75	1,053,482
Small Enterprise	5.94	56,982
Medium Enterprise	13.75	9,977
(Large Enterprise)	(43.30)	(248)
Total SMEs		**1,120,441**

Source: ILCS, 2004. The data used is from the files IMIRARoster.saw and IMIRA-MAIN.saw, both dated 26/11/2004.

Annex Table 5.3: Geographical distribution of currently employed persons in the private sector by enterprise size: 2004

	South	Baghdad	Centre	North	All
Micro Enterprise	649,787	522,144	447,839	222,711	1,842,481
Small Enterprise	118,549	88,107	92,588	39,424	338,669
Medium Enterprise	45,552	33,791	36,315	21,551	137,209
Medium Enterprise (external definition) and Large Enterprise	10,359	9,899	8,694	4,214	33,166
All	**824,247**	**653,942**	**585,437**	**287,900**	**2,351,526**

Source: ILCS, 2004.

CHAPTER 6. SOCIAL SECURITY IN IRAQ AND THE WAY FORWARD

INTRODUCTION

Social security is a basic human right and has a key role to play in restoring social cohesion in Iraq's fragile social fabric. Important parts of its population are now facing social exclusion. This is due to the combination of several factors, such as a high unemployment rate, especially among youth, the demobilization of soldiers and militia men, the growing number of war and conflict victims with disabilities and of widows and widowers, and the internal and external displacement of thousands of persons. Peace and stability in Iraq may only be achieved through the implementation of appropriate mechanisms to provide at least some basic degree of protection to those segments of the population that are the most vulnerable. Ongoing conflict and sectarian violence in the country have resulted in the establishment of a climate of insecurity and have hampered efforts to curb widespread poverty. Hence, it is of the utmost importance that social security – as an important tool to prevent and alleviate poverty and as an instrument for sustainable social and economic development[43] – be provided to the Iraqi population in the near future. Lastly, it must be underlined that the establishment of proper social protection mechanisms can play an important part in the development of democracy in Iraq while contributing to the political inclusion and empowerment of the population.[44]

The need for the adoption of coherent social security policies and the implementation of social protection mechanisms and safety nets in Iraq was discussed at the International Employment Conference held in Amman in December 2004. This has been reasserted by representatives of MOLSA and discussed in December 2005 at the ILO Workshop on a Social Security Strategy for Iraq in Geneva.

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[43] Resolution and conclusions concerning social security, International Labour Conference, 89th Session, Geneva, 2001.

[44] ibid.

While in pre-conflict times there were well-established social security schemes providing coverage to both public and private sectors, their application was suspended during the 2003 invasion. In 2003, all schemes were replaced by emergency payments for all. For the reasons described below, such payments are not sustainable in the long run, hence the need to establish effective social security mechanisms through technical assistance and a coordinated effort of the international community and donors.[45] Taking this into consideration, the present chapter will set out an assessment of the situation of social security in Iraq and try to identify the main orientations which should guide any social policy decision taken in respect of the implementation of social security schemes. In the second part, an analysis of the legal, administrative and financial social security background will be conducted, focusing on the main pre-war and current social protection mechanisms and measures, the weaknesses of the social security system in place and the administrative and financial contexts of social security in the country. Finally, in the last part, the main policy considerations will be identified which should guide any reform of the actual social security system and present the way forward.

THE ECONOMIC AND SOCIAL BACKGROUND OF SOCIAL SECURITY

In order to assess the needs and to identify the main priorities in terms of social protection coverage, it is essential to first recall some of the socio-economic characteristics of the country. This involves setting out some data on population, labour market, and economic and financial systems in Iraq that are particularly relevant for social security.

The total population of Iraq in 2005 was estimated at 28.8 million, of which 14.6 million (50.7 per cent) were men and 14.2 (49.3 per cent) women. According to United Nations data for the 2000-2005 period, the life expectancy at birth for men was 57.3 years of age and 60.4 for women. For pension scheme analysis purposes, it may be pointed out that life expectancy at age 60 was 15 years for men and 16 years for women (United Nations, 2005).

A large share of the labour force was engaged in public sector activities. Out of the 6,002,000 employed persons, 1,794,000 (approximately 30 per cent) were employed by the public sector[46] (1,286,000 men and 508,000 women), while the remaining 4,210,000 (approximately 70 per cent) were employed by the private

[45] Such need has been recognized by MOLSA and discussed in December 2005 at the ILO Workshop on a Social Security Strategy for Iraq. As a follow-up, an official request for technical assistance was made by MOLSA to the Social Security Department of the ILO.

[46] References to public-sector employees comprise those employed by the central and local or Government, State-owned enterprises and the Iraqi army.

sector (3,744,000 men and 466,000 women) (ILCS, 2004).[47] Out of these, 2,972,000 were employed by private companies (2,810,000 men and 162,000 women).

According to data provided by MOLSA (2005), the non-working age population of the country in 2004 was approximately 10.7 million, comprised of 1,296,000 State pensioners (public sector workers) and 14,125 social security pensioners (private sector workers).

Concerning the social security coverage of the employed population, the data for 2004 indicates that all public sector employees (1,794,000) were insured under the State pension scheme administered by the Iraqi Ministry of Finance. The same data show that, out of 2,972,000 private company employees, only 80,502, or less than 3 per cent, were registered with MOLSA – responsible for the administration of the social insurance scheme – and thus covered by the scheme (2005). These represented only 1.2 per cent of the economically active population of Iraq in 2004. One of the reasons given by MOLSA for such a low degree of coverage is that, under the law establishing the private sector social security scheme,[48] companies with less than three employees are under no obligation to join the scheme and are not subject to the payment of contributions.[49] The data further indicate that, out of the 80,502 private sector employees registered with MOLSA under the pension scheme, only 35,697 contributed to the social security scheme in the first quarter of 2005.[50] This, it is suggested, is due to the fact that out of the 24,315 private companies registered in the Business Registry of Iraq, only 12,177 were still active in the first quarter of 2005. Thus, it can be deduced that a significant part of the Iraqi labour force works in informal employment without any form of social security protection in the face of risk.[51]

The available data show that per capita income is estimated to have fallen by nearly one half between 2001 and 2004, when it stood at US$780.[52] Iraq is thus considered a low-income country, and, although there are very scarce data available on the extent of poverty in the country, it was estimated that in 2004, more than five million Iraqis lived below the poverty line (out of a 25 million population).[53] The median hourly wage in Iraq in 2004 was Iraqi Dinars

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[47] The results of this survey are also discussed and referred to by MOLSA in a document entitled "Social security for employed labour force in Iraq", December 2005, which was communicated to the ILO and presented by MOLSA representatives at the ILO, Geneva, in December 2005.

[48] Law No. 39/1971.

[49] According to information provided by MOLSA, this provision should soon be amended, providing for the contribution to the pension schemes of all private employers.

[50] MOLSA, "Social security for employed labour force in Iraq", December 2005 (as distributed and presented at the ILO, Geneva, December 2005).

[51] As underlined by MOLSA in "Social security for employed labour force in Iraq", op.cit.

[52] "Social protection in transition: Labour policy, safety nets and pensions", Middle East and North Africa Human Development Unit, World Bank, June 2005 (Draft), p. iii.

[53] "Social security and safety nets in Iraq: Outstanding issues", Paper prepared by the ILO for the Conference on Jobs for the Future of Iraq held in Amman, 12-13 December 2004, Geneva, December 2004, p. 2.

1,042 (US$0.72) for women, compared to Iraqi Dinars 694 (US$0.48) for men.[54] In 2004, wages in the public sector, which corresponded on average to Iraqi Dinars 2,610,000 (with the exclusion of wages of the military and police), were 60 per cent higher than the median, while private sector wages, averaging Iraqi Dinars 540,000 in 2004, were clearly the lowest, often found below 50 per cent of the median hourly wage.[55]

ANALYSIS OF THE LEGAL, ADMINISTRATIVE AND FINANCIAL BACKGROUND OF SOCIAL SECURITY IN IRAQ

Main social protection mechanisms

Presently, there are in Iraq coexisting different mechanisms aiming to provide some degree of social protection to the population. In response to the situation of high unemployment, acute poverty and vulnerability engendered by the conflict, the transitional administration and the Iraqi Government have adopted specific emergency measures. As a result, the country has experienced in recent years a shift in emphasis of social security programmes away from contributory social insurance schemes towards food and other subsidies and social safety nets targeted at basic needs for the most vulnerable.[56]

Public social security schemes

Social security schemes were well established in Iraq before the 2003 war. They were based on social insurance principles under which pensions and other benefits were payable to insured persons upon occurrence of the contingency, subject to compliance with the length of service conditions and the payment of contributions by employers and workers. Two main social insurance schemes similar in their nature and in their benefit programme formed the core of the pre-war social security system and applied to the public and private sectors. Both schemes were designed with technical assistance from the ILO, as defined-benefit arrangements with pay-as-you-go financing.[57] At the onset of the conflict, they covered together about 15 per cent of the labour force, mostly comprised of public sector workers.

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[54] Iraq Living Conditions Survey 2004, Volume I, op.cit., p.104, which suggests that higher median wages for women could be related to the fact that "primarily women with higher education have work, thus are paid more".

[55] "Social protection in transition: Labour policy, safety nets and pensions", op.cit, p. 6 and 93.

[56] "Social security and safety nets in Iraq: Outstanding issues", op.cit.

[57] In a defined-benefit scheme pensions are fixed by law and guaranteed by the Government. The law entitles those who pay into the system a certain amount of benefit, according to a formula that considers both the duration of contribution and levels of income. Pay-as-you-go financing means that the contributions of those who pay into the system in a given year are used to pay the beneficiaries of the same year.

The *State pension system*, established under Law No. 33 of 1966 (Civil Pension Law),[58] provided for the entitlement of public servants, including State and State-owned enterprise employees, to old age, disability and survivor's benefit. Under this scheme, public and semi-public sector workers were entitled to old-age benefit upon completion of 25 years of pensionable service or after reaching 50 years of age, after reaching 55 years of age and completing 30 years of pensionable service, or after reaching 60 years of age, regardless of their period of pensionable service.[59] Mandatory retirement age under this scheme was 63.[60] As an employer, the Government did not contribute to the scheme, which was solely funded by employees' contributions going from 7 to 10 per cent of their monthly salary.[61] As for State-owned enterprises, they had the obligation, as employers, to double the contribution of their employees. Old-age benefit was based on the worker's average salary over a certain period of time and on the period over which a worker had contributed to the scheme.[62]

Two specific schemes were added to the existing State social insurance scheme for the public sector in 1975[63] and 1978[64] to cover the military and security forces.

Mention should also be made of the adoption by the Transitional National Assembly of the Unified Retirement Law, No. 27/2006, on 30 November 2005, which entered into force on 17 January 2006.[65] By adopting this new law, the Iraqi Parliament has unified the various old-age pension schemes applicable to public-sector workers, such as State employees, the military and internal security forces, SOE employees and other workers whose salary is paid by public funds. The new Unified Retirement Law has replaced the pre-war legislation governing the retirement of public sector employees. Under this new scheme, the number of years of service and the level of last salary are used in the calculation of the amount of the benefit, while the legal age for retirement is set at 63 for a person with 25 years of service.

In the *private sector* social insurance was established through the Workers' Pension and Social Security scheme under Law No. 19 of 1971, providing workers in this sector with a range of benefits in respect to a range of contingencies. Under this scheme, old age, invalidity and survivors, and compensation in respect of work injury and invalidity, maternity, and sickness were covered. Law

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[58] See also the amendments to the Civil Pension Law: Law No. 76 of 1989 and Law No. 55 of 1988.

[59] Art. 3(1), (2) and (3), Law No. 33, 1966.

[60] Art. 3(4), Law No. 33, 1966.

[61] The amount of the contribution is determined by the employee's salary level. Art. 5(1), Law No. 33, 1966.

[62] Article 6, Law No. 33, 1966.

[63] Law No. 1, 1975.

[64] Law No. 1, 1978.

[65] Law No. 27/2006, Iraqi Official Gazette, No. 4015, 17 January 2006.

No. 19 of 1971, as amended, applied to all private establishments employing three or more people, with the exclusion of agricultural workers, temporary employees, domestic servants and family labour. The benefit provisions under Law No. 19 are as follows:

Old-age benefit – Under the private sector scheme, the qualifying age for entitlement to the benefit is 60 for men and 55 for women with 20 years of contributions, or any age for men with 30 years of contributions and women having contributed for 25 years. The amount of the benefit corresponds to 2.5 per cent of the average wage of the last three years of work, multiplied by the number of months of contributions and divided by 12, for a monthly minimum of Iraqi Dinars 54 and a maximum of Iraqi Dinars 140. Workers who do not meet the qualifying conditions are entitled to a lump sum corresponding to one month's pension for each year of contributions.

Invalidity benefit – The permanent or long-term loss of at least 35 per cent of a person's working capacity gives him/her entitlement to an invalidity benefit. This is calculated using the same method as old-age benefit and is subject to the same restrictions in terms of minimum and maximum amount. In the event of a partial disability that would be less than 35 per cent of working capacity, the disabled worker is entitled to a fraction of the full benefit proportionate to the assessed degree of incapacity.

Survivor's benefit – In case of the death of the breadwinner, the surviving spouse is entitled, at any age, to a benefit corresponding to 60 per cent of the insured person's old-age pension. Sons of the breadwinner under age 17, under age 27 if students, or without age limit if disabled, and unmarried daughters under age 17 are entitled to a benefit equivalent to 40 per cent of the breadwinner's old-age benefit or to 60 per cent in the case of full orphans. The breadwinner's dependents (mother, father, sister or brother) are entitled to 40 per cent of the breadwinner's pension. The maximum amount of the survivor's benefit is 100 per cent of the breadwinner's pension.

Sickness and maternity benefits – Coverage in case of sickness and maternity is also guaranteed to private sector workers and provided as cash and medical benefits. There is no minimum qualifying period for entitlement to benefits, which amount in the case of sickness to 75 per cent of the worker's average wage during the last three months preceding the onset of the illness, and to 100 per cent of the worker's wage upon occurrence of maternity. Sickness benefit is payable after an 8-day waiting period, during which the employer must pay the full wage, and up to a maximum of six months.[66] As for maternity benefit, it is payable for at least ten weeks, including at least four weeks before the expected date of confinement, which may be extended in case of complications at a rate of 75 per cent of the worker's wage. Maternity leave is covered for up to six

[66] Entitlement to a benefit corresponding to 100 per cent of the worker's wage may be granted for two years in case of an incurable or malignant disease.

months at any time during the first four years of the child's life and up to the fourth child, with a replacement rate of 50 per cent. In addition, a maternity grant is provided for women who leave employment because of pregnancy, as a lump sum corresponding to one month's benefit for each year of contributions. Medical benefits for the two contingencies are provided through Government health centres and hospitals financed by the Labour and Social Security Institute.[67] As for the coverage of workers' dependants in terms of medical benefits, they are equivalent to the benefits to which the insured person is entitled.

Work injury – There is no minimum qualifying period for entitlement to work injury benefit, which amounts to 100 per cent of the wage on which contributions were last paid. In case of temporary disability, the benefit is payable after an 8-day waiting period – during which the insured person is entitled to his/her full wage – and until recovery or certification of permanent disability. Provided that a worker is completely disabled, permanent disability benefits amount to 80 per cent of the average wage in the insured person's profession. Partial disability corresponding to 32 per cent and up is compensated by a percentage of the full pension proportionate to the assessed degree of incapacity, while an incapacity of less than 32 per cent gives entitlement to a lump sum corresponding to four years of partial disability pension. Disabled workers are also entitled to medical benefits such as general medical care, home visits, surgery, specialist care, hospitalization and medicine. As for the benefit to which surviving spouses – widows or dependent disabled widowers – are entitled in the case of the death of the breadwinner as a result of a work injury, it should correspond to 60 per cent of the insured person's permanent total disability pension or to a lump sum equal to four years of the breadwinner's partial disability pension. Orphans and dependants are entitled to a benefit in the same proportion as the standard survivor's benefit (see above).

Common provisions – The legislation requires both workers and employers to contribute to the scheme, in a proportion of 5 per cent of the workers' salary and 12 per cent of the employers' payroll. As an exception, firms operating in the oil sector are required to contribute the equivalent of 25 per cent of the payroll. Such contributions are used for the financing of all benefits covered under the scheme in a prescribed proportion.[68] Under this scheme, all types of benefits are provided

[67] Medical services covered by the scheme include various forms of treatment and consultations, such as: general and specialist care, hospitalization, surgery, medicine, X-rays, appliances, laboratory services and rehabilitation.

[68] According to Article 5 of Law No. 155 of 1971, which amended article 27(b) of the Workers' Pension and Social Security Law No. 39 of 1971, the 12 per cent contribution rate had to be distributed as follows: 1 per cent to the Health Security Section; 3 per cent to the Work Injuries Security Section and 9 per cent to the Pension Security Section. In the case where the employer was required to contribute in a proportion of 25 per cent of the payroll, the rate had to be distributed as follows: 3 per cent to the Health Security Section; 3 per cent to the Work Injuries Security Section; 15 per cent to the Pension Security Section; and 4 per cent to the Services Security Section.

as part of the social insurance system. Their collection and payment is administered by the Pension Fund for Workers,[69] while the administration of the programme is vested with the Labour and Social Security Institute, under the general supervision of the Ministry of Labour and Social Affairs.

Emergency payments

Emergency measures were taken by the Coalition Provisional Authority, in response to the social crisis affecting the country in recent years. In 2003, the Coalition Provisional Authority amended the two laws of 1966 and 1971 by way of administrative decision, replacing pensions under both systems with emergency payments. Simultaneously, reserves for the private sector social security system, which represented at that time Iraqi Dinars 19 billion – less than 0.5 per cent of GDP – were frozen in the Central Bank. From the moment this policy entered into force, payments have been supported from the State budget.

While all payments made in 2003 were of the same amount for everybody,[70] regardless of the length of service and the contributions paid into the scheme, such "flat" payments were replaced in January 2004, by decision of the Ministry of Finance of the Coalition Provisional Authority, by defined payments, increasing the number of years of employment and the grade of pensioners upon retirement. In 2004, benefits ranged between Iraqi Dinars 80,000 (US$53) and Iraqi Dinars 200,000 (US$133).[71]

Other public social safety nets

The main social safety net in Iraq is the Public Distribution System (PDS), which started in 1991 as a programme to distribute domestically-produced food when sanctions were first imposed on the country in the aftermath of the 1990 Gulf War. In 1996, the implementation of the Oil-for-Food Programme under UN supervision allowed Iraq to purchase food and other necessities using the proceeds from oil exports. Under the administration of the Ministry of Trade, the PDS is implemented by State-owned enterprises and private sector companies. It is made available to the entire population for a nominal fee and, as of June 2005, covered more than 90 per cent of Iraqis.[72] According to the WFP, up to a

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[69] Article 14 of the Law No. 29 (1987) of the Ministry of Labour and Social Affairs (Revolutionary Command Council Resolution No. 243, published in the Official Gazette of the Republic of Iraq, 10 June 1987). See also Chapter 3 of the Workers' Pension and Social Security Law No. 39 of 1971.

[70] Emergency payments for the last three quarters of 2003 (April – December) corresponded to US$20 per month (Iraqi Dinars 30,000) and were increased to US$27 (Iraqi Dinars 40,500) in the first quarter of 2004. "Social protection in transition: Labour policy, safety nets and pensions", op.cit.

[71] More precisely, emergency payments were diversified in the first quarter of 2004 in two different amounts: US$67 for individuals having 25 years or more of service and US$50 for individuals having less than 25 years of service. Payments were further diversified in the third quarter of 2004 in four categories, depending on the position and the number of dependents. "Social protection in transition: Labour policy, safety nets and pensions", op.cit, p.48.

[72] ibid, p. viii.

quarter of the Iraqi population was considered to be heavily dependent on the food baskets provided under the PDS for basic nutrition and consumption in 2004.[73] It must be noted that, as of June 2005, the Government, in partnership with major donors, planned to reform the PDS to make it more in accordance with the population's needs.[74]

In addition, cash and in-kind public assistance are primarily provided to the most vulnerable and to demobilized military personnel by MOLSA. Such aid includes cash transfers, training and rehabilitation services, and other in-kind assistance. Under the Family Care Allowance programme, certain categories of families who lack adequate support are provided with a flat monthly cash benefit by MOLSA, regardless of family size. Although there are no means or asset tests for entitlement to the benefit, eligibility is determined on the basis of a person falling into one of the prescribed categories of beneficiaries, which include the blind and disabled unable to work, widowed or divorced women with children and the elderly without pensions. In 2004, 113,000 families benefited from monthly transfers of Iraqi Dinars 30,000 (US$21).[75]

Demobilized military personnel covered under the Government demobilization and reintegration programme are also provided with cash transfers.[76]

As for in-kind assistance, it is mainly provided by MOLSA through institutional care and rehabilitation services, in facilities such as orphanages, institutes for the disabled, cooperatives and elderly homes. In 2004, roughly 6,300 persons benefited from these various forms of assistance.[77]

Lastly, it should be noted that the Government provides important price subsidies, both direct and indirect, to individuals and companies, for services (such as healthcare and education) and commodities (including pharmaceutical supplies, electricity and oil).[78 / 79]

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[73] "Baseline Food Security Analysis in Iraq", World Food Programme, Iraq Office, 2004, p.6.

[74] Iraq's National Development Strategy 2005-2007, Ministry of Planning and Development Cooperation of the Republic of Iraq, 30 June 2005, p. xii.

[75] According to the World Bank (2005), "…the family care benefit given to families amounts to almost 5% of the estimated median income of the lowest quintile of the Iraqi population", "op.cit., p.36

[76] Figures from the 2004 and 2005 budgets indicated that the average benefit provided to demobilized military personnel amounted, for each of these two years, to 17 per cent of the median income of the lowest income quartile. Ibid. p. 36.

[77] ibid, p.37.

[78] According to the World Bank (2005), the cost of supporting commodities and services is very important for the Government and significantly increased between 2004 and 2005. For more information on price subsidies, see "Social protection in transition: Labour policy, safety nets and pensions", op.cit, pp. 32-35.

[79] This chapter does not refer to Zakat-benefits to the poor and needy as insufficient data on them is available.

Financial situation of social security

In 2004, approximately 19 per cent of Iraq's GDP was spent on public social protection measures and the budget planned an increase in spending equivalent to almost 22 per cent of GDP for 2005.[80] In both 2004 and 2005, most of the social protection related resources were allocated to the public food distribution system (approximately 93 per cent of all resources allocated to social protection in 2004 and 21 per cent of Government revenue in 2005).[81] In second place were pension payments, which constituted about 15 per cent of all resources allocated to social protection in 2004, or an estimated 3.5 per cent of GDP,[82] and which, under the 2005 budget, accounted for 5 per cent of GDP.

Flat emergency payments accounted for an increasing part of expenditures from 2003 to 2004, when they represented 3.5 per cent of GDP, following a decision by the Ministry of Finance to award higher payments to pensioners with longer service and higher grades as from January 2004. The provision of the funds necessary to the payments is under the responsibility of the Ministry of Finance, through the Treasury account and with very small contributions from employers and workers.

Weaknesses of the existing social security provisions

The operation and effectiveness of both social security schemes have been significantly impaired in recent years, both in respect of the coverage and range of benefits provided and of the collection and recording of contributions from employers and insured workers.

One of the main areas of concern with the regular pension system consists of the low rate of coverage of private sector workers – less than 3 per cent. The management of the social security system reports high levels of evasion from employers, who allegedly under-report the number of employees to avoid enrolment in the scheme. Also contributing to the low rate of coverage is the fact that an important part of the labour force is underemployed, i.e. individuals in unregistered jobs who report receiving an income (e.g. self-employed, casual or seasonal workers, etc.).

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[80] According to a World Bank Report ("Social protection in transition: Labour policy, safety nets and pensions", op.cit.), "…this is a huge sum of money by any standards. By comparison, OECD countries spend on average just under 14 per cent of their GDP on social protection, while the Middle East and North Africa region averages less than 5 per cent of GDP.

[81] The Republic of Iraq Government General Budget for 2005, Ministry of Finance, Budget Directorate, December, 2004. According to a World Bank report of June 2005, the PDS "is the largest public food programme operating in the world today (…) – absorbing approximately 21 per cent of government revenue" ("Considering the Future of the Iraqi Public Distribution System", Economic and Social Development Unit, Middle East Department, World Bank, 2005, p. 3).

[82] "Social protection in transition: Labour policy, safety nets and pensions", op.cit, p. 47.

According to a MOLSA report,[83] both social security schemes are indebted. With regard to the private sector scheme, this is due, according to MOLSA, to a number of factors. First, the high degree of non-compliance of private companies with the provisions of Law No. 39 of 1971 is believed to have contributed to keeping the number of contributors to the scheme relatively low. In addition, the possibility, under the scheme, for allowances to be deducted from the contributor's salary base before the contribution is calculated has also been identified as a factor for such a low level of participation. MOLSA further mentions the fact that contributions owed by companies to the social security budget are calculated on the basis of workers' salary for the month of January instead of on their monthly salary, as one of the causes of the scheme's deficit. More generally, it is pointed out that the proper functioning of the scheme, which requires the effective recovery of unpaid contributions from private companies, is still hampered by institutional dysfunctions and the overall security problems that affect the country.[84]

It was also pointed out by MOLSA that the coexistence of the public and private sector social insurance schemes became difficult after the war: the dual structure of the pension system was questioned for fostering inequalities between the private and the public sector and for increasing administration costs, "precluding an efficient allocation of resources".[85] Furthermore, the dual structure does not consider any inter-sector transfer for people accumulating years of service in both the State and private economy and thus horizontal labour migration from public to the private sector has been small due to the lack of transferability of pension rights between the two funds, impeding the development of the private sector economy.

In pre-conflict times, the administration of pension schemes was already faced with problems, mainly relating to the "manual outdated administrative systems, with poor record keeping and little accountability".[86] The State pension system faces similar problems due to the manual registration of contributors and contributions and only partial computerization of beneficiaries. As all other public institutions, social security institutions were severely affected by the war and have suffered infrastructure deterioration post-war.[87]

Emergency payments are an important tool in alleviating poverty in conflict situations when it is not possible to maintain formal social security schemes. The eligibility conditions surrounding their payment are necessarily different to those

[83] "Social security for employed labour force in Iraq", December 2005 (as distributed and presented by representatives of the Ministry of Labour and Social Affairs at the ILO, Geneva, in December 2005).

[84] ibid, p. 5.

[85] ibid. p. 50

[86] Iraq's National Development Strategy 2005-2007, op.cit, p. 2.

[87] "Social protection in transition: Labour policy, safety nets and pensions", op.cit., p. 53.

of the pre-conflict formal social security schemes. In particular, levels of payments are in many cases less than an individual would have received from the pension schemes. However, once Iraq moves from a conflict situation into a stable political environment, it will be ready to consider the type of schemes that would be appropriate in a new environment.

DEVELOPMENT OF SOCIAL SECURITY STRATEGIES

It is essential that plans for reconstruction and development include social security in order to support employment generation, and that they are phased in in a way that supports the overall reconstruction plan. The UN strategy recognizes the long-term goal of providing employment and income-generating activities across all sectors. It is proposed that focus should be directed on the restructuring of the economy and on the most vulnerable through the provision of a social safety net that provides a minimum income and access to basic health. Simultaneously, promoting social security coverage in all infrastructure works through specific procurement regulations, and a gradual formalization of employment in small enterprises provides an opportunity for social insurance coverage to be expanded.

Within this broad strategic approach, there will be a need to reconstruct and develop what remains of the national social security system. It is not possible, at this time, to set out what a new system would look like, but it is possible to mention the sort of issues that will need to be addressed. There needs to be a comprehensive review of the existing schemes, social protection priorities, resource prospects to finance social security, and the priority needs and gaps in coverage for social protection.

The Government will have to decide the extent to which resources should be channelled towards the reconstruction of the established pre-war social security system and to what extent they are allocated to structural reform. The case of the Iraqi pension system illustrates this issue.

It is envisaged that a debate should be generated which should encourage consideration and research as to the future development of a reconstructed national social security system. The following paragraphs indicate some of the main issues, which will need to be addressed in the reconstruction process.

Social security standards and legislation

The ILO has already provided technical assistance in the drafting of social security legislation relating to both the public and private sector social security schemes and has also drafted a Labour Code. Discussions on the final structure of this legislation should be based on further discussion, including with employers' and workers' representatives, leading to relevant policy decisions. Legislation should be closely based on international labour standards but the initial emphasis should be on the gradual reconstruction of the social security systems underpinned by a basic level of income support and access to health care.

Social security coverage

The extension of coverage under the social security schemes both in terms of the range of protection and in the numbers of persons protected should be a key element in the development of social security strategies. Gaps in social security coverage are likely to remain significant for some time and this will include many people who have become unemployed or who are working in the informal economy. This may give rise to the need to consider the desirability of special schemes for those in informal employment, the self-employed and also to consider the feasibility of unemployment insurance or benefit. Among those in employment, the social partners will play an important role in designing and implementing new schemes and in modifying established schemes.

Social security financing

The financing of the proposed benefits must be thoroughly studied. A viable solution can be found only through an overall analysis of the social budget, which takes into account the fiscal capacity of the State as a whole. Social insurance schemes, as one component of a national social protection system, can be financed through a variety of methods and each of them can be justified on different grounds. However, they have to be part of an overall national social protection financing strategy. The social stability of the country will also, to a considerable extent, depend on the rapid coverage of a major part of the population under the new social security scheme. To achieve this, the possibility of introducing a universal basic pension scheme to be financed from general revenues or an earmarked proportion of national oil revenues may be an option. Such a scheme should function as a first tier of a national social security system. The second tier could consist of the reformed existing insurance schemes.

Social security administration

The reconstruction of the administration of both the public and private sector schemes, in terms of personnel, equipment and records will be a major task on which the future effectiveness and public acceptability of the scheme will depend. The establishment of the management and of a Board of Directors with tripartite participation will be important. The State should have the overall responsibility for the proper administration of the social security schemes and the due provision of benefits to be provided in compliance with the national legislation.

Clarification of responsibilities for management and administration of social security

Greater priority will need to be given to increasing the capacity and expertise of the social security administration. This implies improvements in the working conditions and in recruitment policies. The administration must consist of able and experienced staff who know social security and who can assume responsibility for its administration and for initiating and managing its reform and recon-

struction. Social security is a national priority and the concept will help establish an understanding throughout the country of the need for mutual support. The Ministry of Labour and Social Affairs does not necessarily need to be directly responsible for running the scheme. Its job should be to bridge the gap between policy making and politics on the one hand and service and delivery on the other

Improvement of the policy building capacity

Many countries have chosen to recognize the need to strengthen the policy making process and administration of their social security system through the separation of functions between the legislative structure of the scheme and its administration and implementation. The social security organization can thus become an autonomous body responsible for running the scheme, with an independent Board of Directors or Trustees who appoint a Managing Director to administer the scheme and as appropriate other experts on administration, computerization, finance, etc. Recruitment of personnel and their training will be a high priority alongside the restoring of records for pensions contributions and benefits payments. Account will need to be taken of the arrangements for the efficient administration of the scheme and, in particular, for financial management and control with regard to both long and short-term responsibilities.

Establishment of an effective computerized system

Iraq certainly needs a fully computerized records system since the records of contributions and benefits paid represent the core of the social security system and in particular one which is based on social insurance principles. The structure of the scheme will require both political and policy considerations and technical expertise. Bridging the gap between policy and administration is an important role for the representatives of the beneficiaries and the contributors and the politicians, so that their interests are taken care of, and accounted for, directly to the Board. The investment of social security funds is thus an important element in the financing of the scheme and it should be recognized that the return on each investment should not be subordinated to political considerations. A special investment committee should be established to ensure that sound decisions are taken on investment management.

Special rules to facilitate entitlement to benefits

It will be important to ensure that adequate provisions are made to provide appropriate benefits in accordance with the provisions and expectations of the existing pre-war social security schemes. Many of those who are, or should be, insured under the social insurance scheme may have gaps in their contribution payment records that represent periods of employment or non-compliance by their employer, or sickness, etc. In order to ensure adequate social protection for persons with limited periods of membership in the scheme when it commences, special arrangements should be made to modify the qualifying conditions for

entitlement to benefit and the rate of benefit. This is particularly the case for those who are close to retirement age.

Reform of the existing scheme has certain implications in that benefit rights especially for pensions will have accrued and also liabilities to pay contributions have not been met. In addition, persons insurable under the schemes have not been insured and paid contributions and many employers have not paid contributions. In other cases, insured persons will have joined the scheme late in life so that they would be unable to qualify for a retirement pension, which usually requires a qualifying period of at least 10 to 15 years. Special rules to assist such persons in attaining a meaningful pension would be desirable.

The disruption of economic activity and the uncertainty of the situation have obvious implications for income generating activities and for family support. This is reflected in the effective coverage of both the private and the public sector social security schemes. Special arrangements may also be made to provide income support, but a strategic approach to the continuation of these schemes will need to be developed to assist gradually in their phasing out and replacement by more effective and structured public systems. Nevertheless there is likely to be a continuing role for private or religious schemes to provide support on a charitable basis to the most vulnerable and, in particular, to those who are outside the scope of the national public schemes.

Need for policy initiatives and legislative reform

Special initiatives will need to be implemented from time to time, with particular reference to global programmes such as the extension of coverage and the promotion of Decent Work. In addition, special plans will need to be made to ensure impact on the objective. Examples are:

- Ensure income replacement for all employees and the self-employed for contingencies such as: retirement, sickness, maternity, employment injury, disability and the death of a breadwinner. This is most important for those whose income is jeopardized or disrupted by inability to provide income from employment.
- Provide *income support* for those without prospects of regular income from employment.
- Consideration of feasibility of introducing an *unemployment insurance* scheme.
- Ensure access to adequate *health care*.

Rights to existing benefits earned during insured membership of the social security scheme should be preserved.

The future of social security in Iraq

The overall strategy envisaged for the development of social security in Iraq is one which seeks to follow several tracks all of which lead to the same destina-

tion – universal coverage. This means a series of reforms aimed both at the existing social security systems and at the benefit schemes themselves. The preceding paragraphs have identified the main issues that will need to be addressed once the reconstruction phase is reached. However, the nature of any reform will be necessarily dependent on how long the existing situation continues.

CHAPTER 7. EMPLOYMENT POLICIES AND STATE-OWNED ENTERPRISE REFORM

Defining and redefining the role of the State in the economy is one of the major points of debate for economic policy in Iraq. As in many other countries of the region, Iraq's economy is dominated by the State. Government alone provides employment to those who have work (See Table 2.7). There are some 192 State -owned enterprises (SOE) in Iraq although exact information on the composition of their output or employment varies widely. In the latter case the estimates range from 500,000 to 800,000 workers.

Iraq drew up its vision in the National Development Strategy (2005) with its focus on revitalizing the private sector and strengthening good governance and improving the security situation. It is a formidable task to move away from a virtually closed economy with enormous State intervention to a market-oriented economy and many specific problems need to be overcome. However, in recent years many States have made the transition from a closed, State-run economy to a market economy. It is advisable to give due regard to the lessons that have been learned in this transition process, when the pathway for Iraq's reform process is being laid out. The first steps of the reform process would inevitably lead to some labour shedding. Careful consideration should be given to the sequencing of reforms and the setting up of appropriate safety nets and social protection measures as outlined in Chapter 6. The employment consequences of reform will need to be considered in the wider context of tackling massive unemployment. How the reform of the SOE in Iraq will affect the number of SOE workers and their welfare will depend on the course and character of SOE reform. So far little by way of a specific blueprint has emerged. Even the World Bank's working paper on SOE reform is almost exclusively concerned with the principles of reform and the guidance derived from reform experience elsewhere rather than an identification of reform policies specific to industries and enterprises in Iraq's public sector.[88] This chapter is also limited to outlining the broad pattern of SOE

[88] World Bank (Finance, Private Sector and Infrastructure Department of Middle East and North Africa Region). *State Owned Enterprises Reform in Iraq, Reconstructing Iraq. Working*

Continued on page 88

reform that it considers both likely and desirable in Iraq and then spelling out its implications for employment. This will be based upon an analysis of SOE and their contribution to employment.

EMPLOYMENT IN STATE-OWNED ENTERPRISES

Table 7.1: Number of State-owned enterprises formerly affiliated with specific Line Ministries

Ministry/Commission	Number of SOEs
Agriculture	10
Electricity	11
Finance	9
Health	1
Housing and Construction	15
Industry and Minerals (MIM)	48
Military Industrial Complex (MIC) (now with MIM)	48
Irrigation	11
Oil	19
Trade	8
Transport and Communication	12
Total	**192**

Source: World Bank (2004)

There are 192 State-owned enterprises in Iraq and 43 enterprises with mixed ownership covering all sectors and economic activities. Surveys of the status of the SOE show that close to 90 per cent of Iraq's industrial capacity "is seriously de-capitalized, asset-starved, obsolescent, and inefficient, saddled with high production costs, as a result of looting, over-staffed and in a state of physical degradation" (World Bank, 2004).[89] These problems are not new, but were already occurring during the sanctions period – largely as a result of the insufficient capitalization of assets and lack of access to input supply. However, events since 2003 have exacerbated this problem. One particular problem is the underutilization of much of the staff: people continue to receive salaries even if they have not enough work to do.

Continued from page 87

Paper No. 2, 26 July 2004, and similarly World Bank (Middle East and North Africa Region, Social and Economic Development Group). *Rebuilding Iraq, Economic Reform and Transition, 2006*.

[89] ibid and DFID (2004), *Iraq's SOE Feasibility Studies*. DFID, London, UK, Mimeo.

Table 7.2: Employment in State-owned enterprises: 2004

Sector/Ministry	Employees	Estimated Salary Expenses 2004		Average monthly salary, USD
		USD, million	ID, billion	
Transportation	30,182	34.7	69.5	95.9
Communications	15,226	30.0	60.3	165.1
Trade	31,186	37.4	74.8	100.0
Water	6,665	9.3	18.6	116.3
Health	3,027	7.1	14.2	196.1
Housing	16,842	20.2	40.4	100.0
Culture	2,521	3.2	6.3	104.4
Agriculture	6,285	11.2	22.5	148.9
Oil	66,964	80.4	160.7	100.0
Electricity	40,000	48.0	96.0	100.0
Finance	9,608	11.7	23.4	101.6
MIM	104,378	186.1	372.3	148.6
MIC	55,913	58.0	116.0	86.4
Total	**388,797**	**537.6**	**1075.1**	**115.2**

Source: Ministry of Finance, General Budget Law FY05, January 2005

Little information is available on employment in SOE in Iraq. One problem that exacerbates the difficulty of coming up with an estimate of SOE employment is the fuzzy line of demarcation between the SOE and the rest of public sector employment, in particular public administration and defence. Before 2003 no distinction was made between public administration and enterprises under supervision of line ministries that engaged in production activities. The only detailed data available that give a detailed break-down of SOE is from 2004, but specialists have suggested that public sector employment was underreported given the disincentive to report staffing levels adequately. If one abstracts from this difficulty and assumes that public administration and defence strictly refer to the categories that should belong to them, then an estimate would be close to 600,000 persons employed in SOE.[90] This large number is partly due to rising staff levels since the end of the war. According to some sources, SOE have increased their staff by more than 30 per cent since the end of the 2003 war. If the estimate of 600,000 workers is correct, then employment in SOE represents close to 8 per cent of total employment and nearly 40 per cent of all public

[90] The draft budget of 2006 provides a number of 580,819 SOE workers as of mid-2006. The growing number is also a reflection of the currently unstable environment. In view of the uncertainties on the street, employment in SOE is often viewed as a last resort of stable and guaranteed employment.

employment in Iraq. Thus employment in SOE represents a large share of the State in production activities of the economy and it has risen since 2003. Indeed, total employment in SOE is substantially larger than the entire employment in all non-farm private enterprises excluding the micro enterprises which employ four or fewer workers.[91] A major change in the level of SOE employment will thus have a significant effect on aggregate employment in Iraq.[92]

PUBLIC SECTOR REFORM

One important fact about Iraq's SOE is that they represent State ownership far beyond what experience around the developing world suggests being the limit of meaningful public intervention. In Iraq, many industrial, agricultural and service enterprises engaged in production activities are under State ownership and control. Experience suggests, however, that State ownership and control should best be limited to infrastructure and other select activities which are characterized by large externalities. Elsewhere, especially in ordinary production activities in industries, agriculture and services, governments would do much better by leaving ownership and operation to the private sector while compensating for any market failure by resorting to standard instruments of intervention: taxes, subsidies and regulation. SOE reform in the long run should restructure the composition of ownership of enterprises in Iraq to fit this pattern.
This does not mean the immediate and straightforward privatization of the enterprises that do not meet the criteria of State ownership. There are many reasons why this is not the case and why the following might be highlighted: at the moment most SOE are either not operating or operating at far below capacity. They are suffering from an acute shortage of investment and material inputs. They also suffer from dislocated infrastructure and lack of security – conditions which make the efficient functioning of a market economy impossible. Given these circumstances, it is impossible to identify the market worth of individual enterprises. Iraq's industries were developed under distorted incentives, without consideration of market or social profitability. It is likely that some of them would still turn out to be socially profitable and some others could become so after restructuring of their techniques and output composition. But it is equally

[91] According to the ILCS, private non-farm enterprises that employed more than four persons each in manufacturing, construction, trade, education, health, and other services together employed 0.640 million workers in 2004.

[92] Note that the share of public employment is high, but substantially lower than in some of Iraq's neighbouring countries. In some countries of the region university graduates used to get guarantees for employment in the public sector. In Iraq, attempts to do the same were limited due to rapid labour force growth and austerity measures introduced during its long-lasting economic crisis. See: Karshenas, Massoud (1997): Macroeconomic Policies, Structural Change and Employment in the Middle East and North Africa, in: Azizur Rahman Khan and M. Muqtada (eds.): *Employment expansion and macroeconomic stability under increasing globalization*, ILO, Geneva.

likely that some, probably many, would never achieve social or market profitability. The problem is that the determination of the prospects of individual enterprises is going to be very difficult, if not downright impossible, under the present circumstances. On the demand side, Iraq's domestic capital market is so undeveloped, and the private sector so weak, that it would be exceedingly difficult to organize an orderly privatization. Even foreign private investors would be extremely reluctant to enter into the market except into the politically-sensitive oil sector. Opinion surveys have established extreme domestic hostility to foreign investors. Given the fragile political situation, this must mean that prudence would dictate the avoidance of privatization of existing enterprises by handing them over to Western private foreign investors in the immediate future. There is the further danger that a fire sale of unprofitable enterprises to private investors will only lead to the misappropriation of assets by powerful bureaucrats operating in the State sector and/or to misuse of assets. Immediate privatization on a large scale is thus not an option.

A much better alternative for the Government is to try to put the enterprises back into production based on social dialogue involving workers in the enterprises, in order to achieve a reasonable level of capacity utilization by making the necessary investment in replacing, modernizing and balancing the assets and by improving access to inputs and markets. Quite apart from the absence of immediate privatization as an alternative, this is an attractive option in that the opportunity cost of continuing to operate the SOE is likely to be relatively low on average. This is the case, because the only form of closure of a State enterprise that is politically feasible is to pay very high termination benefits to the laid-off workers. Wages are already low, partly, even largely, because of the huge consumer subsidy in the form of the 100 per cent food ration provided to a large section of the population. The marginal cost of operating the SOE may thus turn out to be much lower than the observed average cost.

Once the SOE attain a decent level of performance, a strategy for their future might be easier to formulate. In principle it would be desirable to classify them into three categories. The *first category* would comprise all those enterprises that are in infrastructure or similar activities with broad externalities. It would make sense to keep them in the public sector. It might still not be desirable to declare these sectors as public monopolies. Instead they should be opened up for private investment *in new enterprises* so that there is a healthy competition between the SOE and private enterprises. In the *second category* would belong all those enterprises involved in ordinary manufacturing, agricultural and service activities that turn out to be profitable or nearly profitable. These should be privatized by a transparent system of transferring ownership. Finally, in the *third category* would fall all those enterprises that are unlikely to meet the standard of social or market profitability. The continuation of these enterprises by artificial support be it in the form of direct subsidies or a distorted system of incentives, must be avoided.

It is worth emphasizing that the ultimate goal of a vibrant private sector, complemented by a well-functioning role of the State, is best achieved by creating

space for private enterprise to grow, not by the privatization of the existing SOE (see Chapter 5). As the experience of China shows, rapid promotion of the private sector is quite consistent with State ownership kept intact during transition to a market economy. As the experience of the former Soviet Union shows, wholesale privatization, without the creation of a healthy private sector and economic institutions, leads to the collapse of existing State enterprises and creates a highly unequal distribution of ownership of the privatized State enterprises through the dominance of rent seeking by the bureaucrats in State enterprises during the process of privatization.

An obvious question is: how can the SOE succeed in reviving themselves given the current lack of security and disrupted infrastructure? A rhetorical response is that the restoration of security by controlling insurgency and the rehabilitation of the infrastructure by a proper organization of reconstruction are necessary preconditions of any kind of economic revival. These preconditions must be fulfilled to put Iraq on the path of sustained recovery, to be followed by steady and rapid growth that the realization of the potential of this resource-rich country warrants.

The essential validity of this argument can hardly be denied. And yet it does not seem meaningful to argue that no avenue for recovery could be found until these preconditions are fulfilled, if only because the end to the insurgency does not appear to be on the horizon. What strategy for an employment-intensive recovery of Iraq's economy can be visualized in these circumstances? In the next chapter we examine a few basic changes in Iraq's current economic policy that might help bring about such a change.[93]

[93] Hardly any policy in Iraq today can be called a purely economic policy. Economic decisions are inextricably bound with important political decisions.

CHAPTER 8. TOWARDS A STRATEGY OF EMPLOYMENT-INTENSIVE RECOVERY AND DEVELOPMENT

A brief recapitulation of the employment scenario is useful at this stage. Iraq has a very high level of unemployment of between 20 to 30 per cent, combined with a very low "visible" underemployment rate of just over 3 per cent of the employed workforce. While these figures indicate a certain degree of formal access to the payroll, they are highly misleading as indicators of the degree of productive use of available labour resources. In the formal economy, which has a far higher share of the total economy in Iraq than in most developing countries at a comparable level of living, the retention of labour on the payroll is not commensurate with the low levels of production. Productively employed labour is a much smaller proportion of labour resources than is indicated by the employment rates that are implied by the above unemployment and underemployment rates. To increase the productivity of the formally employed workers and then to reduce the observed rates of unemployment and underemployment, there must be rapid recovery and growth of output. This must be the focus of economic and employment policy in the short and medium term. Another unfavourable feature of Iraq's labour market is the extreme employment hostility of the overwhelmingly dominant sector of the economy: oil contributes up to three quarters of GDP but less than one-half of one per cent of employment. Iraq's labour market suffers from serious structural problems which will perpetuate an intolerably high dependency ratio on the employed labour force even if all unemployment and underemployment is eliminated.

Apart from insurgency, there are several identifiable obstacles to short-term recovery and growth of which the most important are: a relatively ineffective reconstruction programme in relation to the employment situation; and a serious lack of incentive for non-oil traded sectors. It is widely reported that the rate of implementation of the reconstruction programme has been slower than resource availability would dictate, thereby preventing an early rehabilitation of the infrastructure. Once again insurgency is blamed as a principal obstacle. Furthermore, as available reports and Chapter 3 suggest, reconstruction, largely implemented by foreign contractors, is mostly focused on the import of equipment and

supplies and very little on the use of Iraqi labour. It seems that to work around insurgency, to improve the rate of utilization of resources, and to increase labour intensity of investment, *reconstruction needs to be indigenized, decentralized*, and depoliticized. Resources for reconstruction, domestic and foreign, should be distributed to as low a level of local administration as possible with encouragement for collaboration among the local administration, employers' and workers' representatives, civil society and the NGOs. Governorates, or some feasible lower level, should be targeted. This automatically means that resources for reconstruction will be under the control of the Iraqi local government although the central government will still have an important coordinating role. This presupposes a geographically balanced distribution of these resources, duly weighted by population densities, irrespective of political differences. This will, it is hoped, facilitate a more effective implementation of programmes and a rapid utilization of resources in those large parts of Iraq where insurgency is limited or under control: the Kurdish north and a good part of the Shiite south-east. Even in the Sunni-dominated central and western parts an emerging civil society and the NGOs at the grassroots level might be able to engage in reconstruction as long as resources are effectively put at their disposal with the minimum of strings attached. Even if the insurgency in this region continues, it might not be directed against the popularly-managed non-political economic reconstruction at the grassroots level. Along with the resources for reconstruction, the operation and management of the State-owned enterprises should also be decentralized to the lowest feasible tier of the Government.

Even if the political problems of Iraq are overcome, there will remain an overwhelming problem of disincentive that afflicts the non-oil tradable sectors of Iraq's economy. Currently only a quarter of GDP is reported to be produced by all non-oil sectors. It appears that much of the non-oil economy consists of services that are non-traded industries and agriculture – the traded and trade-substitute sectors of the economy – produce very little. Quite apart from all the dislocations preceding and following the wars, these activities appear to be afflicted by a massive "Dutch disease"[94] of a kind. With oil revenues and reconstruction funds flowing in, and easy de-facto access to imports, these industries face massive disincentives. They are in need of countervailing support without which they simply cannot grow.

It might be argued that Iraq does not face a "Dutch disease". With the third largest oil reserve in the world, it makes sense to specialize in oil. As its reserve gradually dwindles, the market will bring about a change in the incentive structure for the other industries to become profitable. This argument is flawed. Even if Iraq's oil reserves are inexhaustible, the outcome of the present strategy of the preponderance of oil in the economy will mean a negligible overall output elasticity of employment. Iraq will have to distribute its oil earnings among the population to operate an annuity-based economy leaving the labour force severely

[94] 'Dutch disease' is an economic concept that tries to explain the seeming relationship between the exploitation of natural resources and a decline in the manufacturing sector.

underutilized. There is no contemporary experience of a successful economy operating on this basis. Furthermore, there are far too many uncertainties about the volume of oil reserves and the optimum time pattern of its extraction in Iraq. Sensible planning must provide for incentives for non-oil activities to grow.

The form that support to non-oil industries should take can only be worked out after careful research of alternatives. There are some imperatives and priorities that are however worth noting. The classical kind of import-substituting industrialization, by the imposition of trade restrictions is unlikely to work due to its well known inefficiencies and practical infeasibility in a globalizing world of which Iraq rightly wants to be a part. Instead the policy makers must look for some form of market-friendly method of promotion. One that appears particularly attractive is to tie industrial promotion to employment: *instituting some form of employment subsidy*, e.g. a negative payroll tax. This would increase both profitability and employment of the targeted industries, thereby making growth more employment intensive with the poverty-reducing and inequality-averting consequences that it implies.

Financing of such a policy should not be difficult. Again the details can only be worked out once the necessary information is collected to design such a policy. But consider the following illustrative example: assume that half of all employed workers would qualify for such a subsidy – almost certainly an overestimate – and further assume that the monthly subsidy is US$20 per worker, which would be a fairly high proportion of the average wage rate. The annual cost of such a programme would be US$720 million. This is a small fraction of the cost of the food ration subsidy and, as claimed by some reports, a fraction also of the subsidy to petroleum users, a practice which is highly wasteful, encouraging smuggling out of petroleum. The wage subsidy could easily be financed by an orderly reduction in some of these subsidies which will have its own benefits.

As discussed earlier, even if Iraq's current labour force is fully and productively employed, it will suffer from the crippling burden of every wage earner carrying nearly three dependents. The dependency ratio must be lowered. One aspect of the necessary change involves a *demographic transition to a lower birth rate*. As Iraq emerges from its current transition, it must address this issue. Iran's experience shows that there is nothing in the culture and religion of a country that necessarily prevents a rapid transition to low fertility. The other aspect of required change, namely raising the participation rate of the working-age population, will be helped once a restructuring of subsidies, away from consumption into employment, takes place.

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