

THE ECONOMIC IMPERATIVES OF THE ARAB SPRING

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Framing the Issue

The Arab Spring constitutes the most important political and economic transitions since the end of communism in Europe. But the world has not found an effective way to channel its support for the reformers in Arab states into economic assistance.

The economic dimension of the transition, moreover, has been all but neglected. While much has been made of the demands for freedom and human rights by protesters, a strong economic rationale is driving Arab citizens to support democracy. A survey of Egyptians conducted this past summer, for example, finds that almost two-thirds of respondents defined the most essential characteristic of democracy as either a low level of inequality or the provision of basic necessities for all citizens. More than 80 percent say that “the economy” is Egypt’s greatest challenge. This is the heart of the matter: if the economies fail to deliver, democracy will fail.

The G-20 can play an important role in promoting much-needed engagement between reforming Arab states and the rest of the world. When the reformist mood last spread through the Arab world some four decades ago,

it coincided with the emergence of economic protection, planning and redistribution. Today, circumstances have changed. Arab economies—less competitive and productive than other middle-income countries—face the prospects of transition during the worst years for the global economy since the Great Depression. And the Arab economies themselves have failed to deliver in recent decades. They relied too much on economic rents rather than production, and on cronyism rather than inclusion. When they reformed—as they were forced to do in the 1990s—they did so half-heartedly and in ways that enriched a small ruling clique. These failures created deep aversions to economic liberalization that persist today.

Policy Considerations

Despite differences among Arab economies, they face four common economic challenges.

First, the challenge of economic reform in the Arab world is foremost a problem of state building. The public sector has acted as the lynchpin of a political-economic system designed to support redistribution and equity. While

these policies improved the health, educational attainment, and living standards of Arab citizens for many years, they also entrenched cronies and enriched a small elite. They have also become increasingly unaffordable. So ingrained in public opinion is the role of the state in the economy, that large percentages of Arab publics prefer government jobs over private sector jobs, despite long waiting lists for public sector employment. Even among Arab youth, large pluralities express preferences for government jobs. Key reforms in the public sector require both fiscal consolidation as well as institutional fixes—increasing access and representation in policymaking, improving the effectiveness of poorly-functioning bureaucracies to deliver public services and controlling corruption.

Second, the disproportionate burdens of adjustment heaped on Arab youth cannot be sustained. Almost two-thirds of the population in the Arab world is under the age of 30. They, unlike older generations whose entitlements are largely protected, face the prospect of longer periods of unemployment or underemployment as well as much greater economic vulnerability, having lost many of subsidies that their elders can still claim. More importantly, the Arab education system is one of the most underperforming in the world. Returns to schooling at primary and lower secondary levels are nearly zero, while they are high at the university level. But for the majority of youth who do not attend university, there is little else. They are left without the requisite skills and training needed to compete in global labor markets.

Third, Arab economies must diversify. Moving beyond an exclusive reliance on oil and gas exports, remittances, and tourism will require gaining the confidence of foreign and domestic investors and entrepreneurs, while creating a favorable environment for all businesses, big and small, to invest, create jobs and expand. Equally important, the business community must regain the confidence of society. The natural advocate of a good government, the merchant class, has not been as a strong voice for change in Arab states. Alliances between rulers and business elites have for too long been part of a mutually-beneficial mechanism for distributing rents rather than an engine of growth. And the organizations that have often prodded reforms in other coun-

tries—entrepreneurs' and business associations—are weak, unrepresentative and captured.

Finally, the relative isolation of Arab economies—both from each other and from the world—must end. Much more should be done to take advantage of opportunities offered by both regional and global markets. Unfortunately, cooperation has a poor record in the Arab world. Intra-regional trade among Arab states is barely one-tenth of total trade. In addition to political divisions between Arab states, the impediments consist of uneven levels of import protection, high nontariff barriers, bad trade logistics, and large gaps between bound and applied tariff rates.

Action Items for the G-20

In previous transitions in other parts of the world, the international community has played a valuable role in providing financial resources and anchors to support multi-year reform programs. Such programs help build confidence and shape expectations in a way that crowds in private investments. In the post-Arab Spring, this may be complicated. The resources available from the international community are largely in the form of loans, not grants, and those are less valuable for countries struggling to maintain fiscal discipline.

More importantly, there is significant resentment against the forces that supported and perpetuated the old regimes—in particular, the international financial institutions and aid agencies that provided the largesse to these Arab states.

Some potential action items for the G-20 include:

- Develop regional assistance tracks to complement the country-specific tracks typically used in development cooperation. A regional approach may be better-suited to addressing the economic and political needs of Arab states.
- Establish a regional development agency that is focused on the issues of transition in the Arab world. The agency should play a leading role on trade and logistics facilitation, regional infrastructure financing and support to the private sector.

- Revive an expanded Barcelona Process and Union-for-the-Mediterranean initiative. These initiatives were designed to build political, economic and social partnerships between the European Union and its southern Mediterranean neighbors, focusing on creating free trade areas, removing most tariff and non-tariff barriers, as well as providing for the elimination of investment obstacles and easier technology flows.
- Better coordinate international assistance efforts, modulated to country circumstances. Reformers in countries such as Morocco and Tunisia, where transitions have thus far been less disruptive, may be able to capitalize on windows of opportunity and move rapidly. But in Egypt, Libya and other countries still engaged in political transitions, the situation facing reformers is less clear.