TIMELY ACTION BY THE G-20 CAN HELP MIDDLE EASTERN COUNTRIES HELP THEMSELVES

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Framing the Issue

As nations begin to recover from the worldwide recession sparked by the 2008 financial crisis, the Middle East hopes to continue where its macroeconomic performance had left off, with record levels of growth and job creation. However, in order for this to occur, the G-20 needs to support policies that promote continued private sector job growth in the Middle East as well as trade reform that addresses global imbalances and public sector reform that precludes future budget crises in the region. Saud Arabia, as the region's sole representative at the G-20 Summit in Seoul, has a critical role in bringing to the table these priority areas that affect the Middle East and North Africa.

The enduring challenge facing countries in the Middle East is high levels of unemployment, which had recently begun to improve before the onset of the 2008 global financial crisis. Leading up the financial crisis, the years from 2000 to 2008 witnessed the highest levels of sustained economic growth for the region in the past 30 years. This boom in the region saw exports and foreign investment rise dramatically, budget deficits shrink, and such strong overall macroeconomic performance that unemployment, the perennial Middle Eastern macroeconomic weakness, fell more dramatically than at any time in its recent history. In Morocco, for example, the unemployment rate fell to less than 10 percent for the first time in 35 years. However, despite improvements in overall unemployment levels, this period of rapid economic growth did not resolve the region's education and youth employment problems, and countries entered the global slowdown with large pre-existing hurdles, including high rates of youth unemployment and deteriorating job quality.

The 2008 global economic crisis and the regional crisis brought on by the sovereign debt crisis in Dubai in late 2009 threatened to reverse the macroeconomic advances that were supported by the boom. Fortunately, the Middle East was not as severely affected as other regions by the global slowdown and has managed to weather the crisis with relatively strong growth rates. But, the factors that prevented a recession in the region, including high public spending and lack of integration with the global economy, are now impeding the region's rapid recovery. According to the World Bank's most recent Regional Economic Outlook, the region's sustained growth during the recovery depends on global developments and improved emerging market demand. The G-20 has the ability to assist the Middle East during the recovery phase through guidance and policy support in three areas: trade reform, public sector reform and private sector development.

Policy Considerations

Trade imbalances are a key focus of the G-20 Summit agenda. If the Middle East is going to benefit from the global recovery, it must have support in reducing the large non-oil current account deficits that still exist in most countries in the region. For example, even with a robust tourism sector, Egypt is forecasted to have a record current account deficit in 2010. Specific policies that promote better global trade balances by eliminating currency distortions could improve the balance of trade outlook for the region. However, the most important single factor for improving trade in the short run would be to ensure macroeconomic stability in southern Europe. The fall in Middle East exports has been largely driven by lower demand in Europe; and any continued debt crisis such as those currently being experienced by Greece and Ireland and that threaten Spain and Portugal will harm Middle East trade prospects tremendously. By weakening the euro, these fiscal crises in Europe decrease the competitiveness of Middle Eastern exports.

Another vital area for G-20 assistance to the Middle East, and one that should be addressed during the Summit, comes in the area of public sector reform. Many G-20 nations are reforming their public sector labor market policies due to fiscal crises. Middle Eastern governments have long attempted to offer social protection through bloated public sector payrolls that offer lifetime jobs with generous wages and benefits. The concern is that without a fiscal crisis, governments in the Middle East postpone making difficult decisions about restructuring their public sectors and reversing the perverse incentives that make jobs in the public sector the preferred employment for young graduates. These incentives push young people toward getting an education simply for the credentials needed for government jobs rather than pursuing education and opportunities for skills development as part of a dynamic and productive workforce. The lessons of the current budget crisis in many G-20 countries should not be lost on the Middle East. While Saudi Arabia is the only official member of the G-20 from the Middle East, other countries in the region can work with the G-20 to develop a broad agenda of public sector reform that can avert future fiscal crises brought on by overly-generous public sectors.

The third area that should be addressed by G-20 countries during the Summit is the need for a growing and dynamic private sector. In order for reforms concerning trade and international financial flows to have a direct impact on the Middle East, the private sector needs to be able to respond effectively to international incentives and signals produced by a competitive global economy. The Middle East has too often relied on the public sector to be the engine of job growth, and this is no longer sustainable. However, the private sector is currently hampered by a regulatory environment that makes it exceedingly costly to hire new workers and expand operations. The private sector in the Middle East is also constrained by limited access to capital and reduced access to markets. Guidance and specific initiatives aimed at developing the private sector in the Middle East can go a long way toward helping private sector firms expand their markets and connect with larger businesses within the value chain of production. This will spur job creation and help in reducing the dependence of young people in the Middle East for government jobs. Given that young people in the Middle East who are without jobs in countries like Lebanon, Morocco and Algeria are likely to seek out job opportunities in Europe, many members of the G-20 have an interest in ensuring that there is sufficient private sector job creation in the Middle East. The G-20 SME Finance Challenge represents a positive step in supporting private sector development in the Middle East and other regions. The G-20 should continue to engage multilateral and bilateral organizations in working together in toward addressing the constraints in private sector development. In the Middle East in particular, the G-20 can capitalize on momentum of the entrepreneurship agenda initiated by President Obama's Cairo speech and the Presidential Summit on Entrepreneurship held last spring to address these challenges.

Action Items for the G-20

The three areas of trade reform, public sector restructuring and private sector development are difficult to tackle and require intra-regional collaboration to devise concrete policy solutions. Saudi Arabia should take the lead in convening a post-G-20 Arab Summit that would bring together leaders from the region to discuss policy reform measures to expand private sector opportunities and better trade integration that would promote long-term growth opportunities for the Middle East.