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# **In Time of Troubles: Challenges and Prospects in the Middle East and North Africa**

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# **In Time of Troubles: Challenges and Prospects in the Middle East and North Africa**

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## **Abstract**

The recent crises concerning food and finances highlight the extreme fragility of the MENA countries and question the sustainability of the development processes. The social stress and economic instability caused by these challenges give a good indication of what might be expected in the future. This paper intends to provide a comprehensive analysis for understanding the major challenges faced by the region and the kind of internal impediments that will need to be dealt with in order to achieve a higher level of economic development and more resilience to external shocks.

JEL codes: O1, N2

Keywords: MENA region, Economic Fragility

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## **1. Introduction**

Throughout its history, the Middle East and North African region (MENA) has managed to maintain a unique geopolitical significance. Its central location at the junction of three continents and its control over main commercial networks had helped to establish the region as the world's leading economic power throughout the 7th-13th centuries.

The region remained relatively cohesive until the 18th century while economic power shifted to northern Europe during the 14th -16th centuries. Europe started surging ahead in the 18th century in the aftermath of the industrial revolution and technological advancement. With the collapse of the Ottoman Empire in late 19th century, most of the region was colonized by Europe powers. By mid 20th century the independent countries of the region had formed a new architecture, ushering in a new era.

Despite the fact that the MENA region no longer has a leadership role, it still holds a unique position. Because of its central location straddling Europe, Africa and Asia as well as its cultural links with more than 1.5 billion people scattered over the world, the Middle East and North Africa area, more than any other region, is still the focus of world attention.

Its high profile may also be explained by the key role the region plays in the global economy. Indeed, two key additional factors have become apparent during the modern period, which ensure that the region remains the world premier geopolitical flashpoint. These include the fact that the world's major reserves of oil are located here, in addition to its important financial resources. Moreover, many experts believe that in the next decades the MENA region will be among the most important areas where renewable energy, including solar energy, will be exploited.

The MENA states have shown serious concern over their economic development since independence. During the 1970s, supported by its natural resources, post-colonial development programmes were implemented to improve the quality of life for the citizenry. Most MENA countries invested in major infrastructure projects, as well as in education and public health. However, as the oil boom started to decline around the end of the 1970s, economic performance gradually weakened, and poverty increased dramatically throughout the region.

The high growth rates in some MENA countries have created the impression of sustainable development, but this is misleading. Many factors indicate that the development process applied

since the 1970s, has failed to deliver its promise. Despite massive investments in infrastructure, in schools and in health, the MENA region in general still suffers from major shortcomings and from development results that are far below expectations.

As a consequence of the excessive reliance on raw material exports for foreign exchange earnings and on foreign markets as a source of industrial products and food items, the region is essentially faced with three challenges: growth volatility, distorted production structure and a mismatch between key economic activities, high unemployment levels, especially among young people, and food security risk. Weak governance and corruption, which have handicapped human and institutional progress in the region, are additional development bottlenecks.

The recent crises concerning food and finances highlight the extreme fragility of the MENA countries and question the sustainability of the development processes. The economic and social impacts of these crises on the economies of the MENA region signal the magnitude of the challenges facing the region and the need to reorient its development policies. The social stress and economic instability caused by these challenges give a good indication of what might be expected in the future.

This paper intends to provide a comprehensive analysis for understanding the major challenges faced by the region and the kind of internal impediments that will need to be dealt with in order to achieve a higher level of economic development and more resilience to external shocks.

The first section of the paper provides a general overview of the Middle East and North Africa. In the second section we try to analyse the reasons for, and the main manifestation of, its vulnerability. The third section concludes and offers the main policy recommendations.

## **2. Overview of the region**

Deepak Nayyar (2009) states that the past can be a pointer for the future and that in order to understand the present better, we need to learn from history. In this section we examine the hypothesis that the recent poor performance of the MENA region is a matter of (bad) choices, not its irrevocable destiny.

## 2.1 MENA region from historical perspective

While MENA countries differ in terms of resource endowments and economic evolution, they share common history and cultural heritage. The MENA region has managed to maintain a unique geopolitical significance throughout its history. Situated at the junction point of three continents, the region was a thriving centre of trade. Control over main commercial networks helped to establish MENA as the world's leading economic power from the 7th to the 13th centuries. Compared to the rest of the world, including Europe, the region was very prosperous: according to Table 1, GDP per capita in the MENA region in the 10th century was the highest of the five country-groups.

**Table1**  
GDP per capita from the first century to the 19<sup>th</sup>  
(1990 International Geary-Khamis dollars)

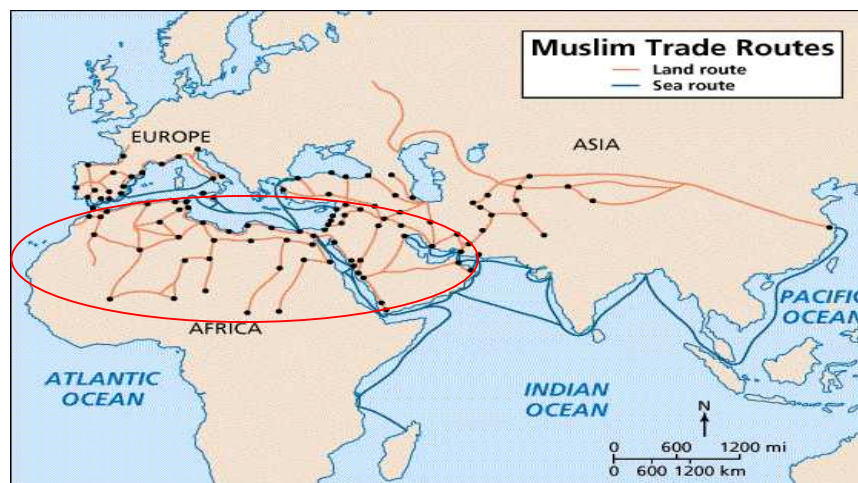
<b>Year</b>	<b>1</b>	<b>1000</b>	<b>1500</b>	<b>1600</b>	<b>1820</b>
<b>Latin American</b>	400	<b>400</b>	416	438	636
<b>Asia</b>	433	<b>447</b>	554	557	604
<b>Africa</b>	472	<b>425</b>	414	422	420
<b>Western Europe</b>	576	<b>427</b>	772	889	1,202
<b>MENA</b>	517	<b>527</b>	485	453	532

Source: Maddison (2003)

MENA's explorers and traders created a prosperous global economy through a commercial network that stretched from the Atlantic Ocean and the Mediterranean to the Indian Ocean and China Sea. Its cities were integrated with no restrictions on the free flow of people, ideas, techniques, goods, and capital (Findlay and O'Rourke, 2007). As Lombard (1975) notes, the region at that time could be perceived of as a series of urban islands, linked by trade routes with the supply of precious metals lubricating the movement of goods and factors of production along these circuits.

**Figure1**

Commercial trade routes during 7<sup>th</sup>-13<sup>th</sup> centuries



An early form of market economy flourished between the 8th and 12th century, due mainly to the development of trade. A monetary system based on a strong, stable and high valued currency (the dinar) was created in the 7th century to facilitate the exchange of goods and production factors (Findlay and O'Rourke, 2007). Innovative new business techniques and forms of business management adapted from different civilizations were promoted during this period by economists, merchants and traders. Scientific advances in many fields such as hygiene, sanitation and medicine resulted in a significant increase in urbanization. According to Lombard (1975: 118) 'This prodigious urban expansion was characterized at first by the creation of towns, some of which rapidly became the largest in the world'.

A modern system of irrigation, based on the knowledge of complex hydraulic and hydrostatic principles, was introduced early in the 9th century,<sup>†</sup> providing the foundation for the region's agricultural revolution (Watson, 1983). The agricultural revolution was based on four key principles: the development of a sophisticated irrigation system, adoption of a scientific approach to improve agricultural techniques, incentives based on a new approach to land ownership that recognized the private property and the introduction of new crops that transformed private farms into enterprises supporting the export industry.

Findlay and O'Rourke (2007) argues that industry and mining were also highly developed. In the Nile valley, for example, flax was the cornerstone of the flourishing linen industry. Major

<sup>†</sup> Crops from Africa such as sorghum, from China (citrus fruits), and numerous crops from India (mangos, rice, cotton and sugar cane), were distributed throughout the region, which previously had not grown these crops (Watson, 1974).

capital-intensive industries, using very advanced technology such as in sugar refining and papermaking, were developed in cities like Andalusia (Ashtor, 1992). The fusion of a variety of cultures and knowledge from many civilizations and the integration of diverse economies during the region's 'golden age' gave birth to the earliest forms of capitalism that were adopted and further advanced in medieval Europe from the 13th century onwards (Labib, 1969; Banaji, 2007).

The Middle East and North Africa remained relatively powerful until the 18th century despite the shift of economic power to northern Europe at the beginning of the 14th century. Erosion of its central position began in the early 14th century. No single explanation for this decline exists, but most historians confirm that the loss of control over global trade and the emergence of Europe as the new global power are the main causes. In addition to external factors, intense internal dissensions, weak central government, declining financial resources were also among the causes that led to the fragmentation of the region and its decline thereafter. By the end of the 19th century most countries in the region were colonized, and during colonialism, the economic development processes became distorted to serve the requirements of the dominant foreign powers. Any local production of commodities which might have competed with the products of the dominant country was forcefully prevented (Alnasrawi, 1987). The evolution of the MENA economies was determined by the needs of the colonial country and its economic system.

By the mid-20th century, the independent countries formed the region's new architecture and a new era began.

It is clear that the economic performance of the region during past centuries was not simply a coincidence but the result of good management of existing capacities combined with the willingness to seize opportunities offered by the favourable global environment.

Although the MENA region no longer has a leadership role, it still maintains a unique position. Because of its central location between Europe, Africa, and Asia and the fact that the locality has the largest heritage relationship of all global regions, with more than one billion people over the world, implies that MENA is still the focus of attention.

Its high profile may also be explained by the key role the region plays in the global economy. Indeed, two additional key factors have become apparent during the modern period, which have ensured the region's position as the premier geopolitical flashpoint of the globe: the world's

major oil reserves are located here, and its financial resources are considerable. Moreover, many experts have recently stated that the MENA region during the next decades will be among the vital areas where renewable energy, including solar energy, will be exploited.

## **2.2 Modern period of MENA region**

After independence, the MENA states had serious concerns for a national industry that would be geared more to their own specific interests as well as to the development of the education and health systems. Financed through natural resources during the 1970s, post-colonial development programmes were implemented to improve the quality of life for citizenry. Most MENA countries invested in major infrastructure projects, education and public health. With the end of oil boom in the 1970s, however, economic performance gradually declined and poverty increased dramatically throughout the region.

Since the late 1980s, many countries have launched important economic reforms in line with programmes prescribed by such international institutions as International Monetary Fund and the World Bank. These reforms essentially were concerned with privatization and trade liberalization, considered to be the tool to improve trading capacities and to attract more foreign direct investment.

The development programmes, implemented in the late 1980s, have succeeded partially to improve economic growth and to adapt the economies of the region to the international environment. Nevertheless, although governments followed the main recommendations of the international institutions, these have been unable to deliver on their promise to their citizens, or to address the substantial deficiencies their economies face. In addition, most countries failed to implement any realistic political reforms to ensure the effective participation of various social stakeholders in the discussion and the implementation of economic reforms.

The current MENA region encompasses 24 independent countries: Algeria, Bahrain, the Comoros, Egypt, Djibouti, Iraq, Jordan, Kuwait, Lebanon, Libya, Mauritania, Morocco, Oman, Palestine, Qatar, Saudi Arabia, Somalia, Sudan, Syria, Tunisia, United Arab Emirates (UAE) and Yemen.

Total surface area is 14.8 million km<sup>2</sup>, making it 44 per cent larger than China, or 3.8 times the size of the European Union. The MENA countries cover 9 per cent of the world's total surface



area and hold 61 per cent of the world's known reserves of oil and 21 per cent of its natural gas. Eight out of the 10 oil-exporting OPEC countries are located in the MENA region (Algeria, Iraq, Kuwait, Libya, Qatar, Saudi Arabia and United Arab Emirates), and in 2004 accounted for 42 per cent of total oil exports in the world.

The population of the MENA region was 325 million in 2008 (World Bank, 2008), indicating that the region is relatively scarcely populated, with a mere 38 inhabitants per km<sup>2</sup>. The most important reason for the low population density is the scarcity of water resources.

The region covers a diverse group of countries, including some very rich and some very poor. It can be divided into three main country-groups, with different economic structures<sup>‡</sup>:

**Table 2**  
Basic indicators for the three groups (2000-07)

	<b>Group</b>		
	<b>Group 1</b>	<b>2</b>	<b>Group 3</b>
<b>Openness</b>	98.53	79.83	75.23
<b>Unemployment rate</b>	6.68	11.38	21.56
<b>Current account balance (% of GDP)</b>	16.59	-2.36	-6.48
<b>GDP/cap (\$ US)</b>	14048.34	2252.26	617.10
<b>Manufacturing, value added (% of GDP)</b>	9.32	15.27	5.18
<b>Fuel exports (% of merchandise exports)</b>	85.11	21.47	
<b>Total reserves in months of imports</b>	9.77	7.23	4.83
<b>Manufactures exports (% of merchandise exports)</b>	6.34	52.37	
<b>Bank liquid reserves to bank assets ratio (%)</b>	18.68	14.86	22.72
<b>Domestic credit provided by banking sector (% of GDP)</b>	41.90	94.16	10.10

Source: World Development Indicators, 2008

First are the oil-producing countries (Saudi Arabia, Kuwait, UAE, Qatar, Oman, Bahrain, Libya, and Algeria) where oil contributes 36 per cent of total value added, 82 per cent of the export revenues and 71 per cent of government fiscal receipts, highlighting that these

<sup>‡</sup> Table A1 in the appendix shows the main characteristics by country for the three groups.

economies are still overwhelmingly dependent on petroleum. While the value added of the petroleum industry represents 36 per cent of the region's aggregate GDP, its contribution to employment, including all petroleum-related activities, is less than 5 per cent. These countries lack a domestic market to meet their needs in terms of consumer and non-consumer goods and have a paucity of financial and capital markets to absorb domestic savings.

The second group is represented by the states that have more diversified but relatively vulnerable economies (Egypt, Jordan, Lebanon, Morocco, Syria, and Tunisia). Indeed, these countries are deeply integrated into the global economy and rely on imports both for consumption and investment. Furthermore, exportation, foreign direct investment, remittances and tourism play a key role in the economic growth and job creation of these countries.

The third group includes the poor countries (Sudan, Yemen, Mauritania, Djibouti, Somalia, and Comoros). This group is affected by serious economic and social problems as a result of inadequate economic and social structures.

Rich cultural heritage, unique geopolitical position, and abundant natural resources, namely oil and natural gas, contrast with the region's low performances in terms of productivity, democratic progress, and human development. Indeed, despite the unprecedented expansion of the hydrocarbon sector in recent years, income levels are low in most MENA countries; performance in the agricultural sector is poor and high rates of unemployment are commonplace. Moreover, the region suffers from serious economic and social instabilities and at least five countries (Iraq, Palestine, Sudan, Somalia and Yemen) are torn by violent internal conflicts<sup>§</sup>.

Many reasons may explain the poor performance of the region, but most experts agree that failure of these modern states to find appropriate strategies to adapt to the constantly changing international environment is the main cause.

In what follows, we attempt to shed some light on the main manifestations and causes of economic vulnerability in the region.

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<sup>§</sup> The Mena region was plagued by political, military and social conflicts during the last several decades. Libya has suffered from the UN sanctions for 8 years (1992-1999), Algeria has suffered from civil conflict for 9 years (1991-2000), Lebanon has suffered from 16-years civil war and 10 -years of external military aggression and Iraq has suffered from 8-years war and 9 years of UN sanctions.

### **3. Main manifestations and causes of vulnerability in MENA region**

The region's economy, with almost 300 million people, is equal to half that of Italy and less than that of Brazil. The region's total manufactures exports represent a mere 40 per cent of the exports of Netherlands and the region's total non-oil exports are lower than those of Finland.

High growth rates in some MENA countries have created the impression of sustainable development, but this is a misconception. Many facts indicate that the development process in the region has achieved its limit, as it has been unable to deliver what was promised. Despite massive investments in infrastructure, in education and in health, the MENA region in general suffers from major shortcomings, and outcomes that far below expectations.

#### **3.1 Main manifestations of vulnerability**

As many international reports have pointed out, the locality tends to be more economically vulnerable, as indicated by manifestations such as considerable GDP fluctuations, distorted economic structure, high unemployment levels and food security risk.

##### *Low growth and high growth volatility*

It is noteworthy that no other region in developing world has so much access to domestic financial resources as MENA region. Despite this advantage, economic growth has been highly disappointing. (The Arab World Competitiveness Report 2002-2003, part 1).

MENA GDP growth rates have lagged behind other regions and, after Sub-Saharan Africa, it has the lowest total GDP, rising from \$199.79 billion in 1975 to \$561.78 billion in 2004, as compared to East Asia and Pacific where GDP rose from \$256.17 billion to \$2,132 billion during the same period. GDP per capita rose from \$1,406 in 1975 to \$1,977 in 2004, while for the same period, in East Asia and Pacific, it rose from \$204 to \$1,140, i.e. an increase of 558 per cent compared to only 35 per cent in the MENA region.

Moreover, World Bank data show that productivity in the MENA region (percentage change in GDP by employed individuals) fell 5.66 per cent in 2000, while East Asia and South Asia recorded an increase of 1.88 and 4.10 per cent, respectively. According to the Arab Knowledge Report (2009), growth performance in the MENA region was very poor in view of the fact that investments valued approximately \$4000 billion in fixed capital formation and more than

\$1,000 billion in human resources have been made during the last two decades. Clearly, much of the capital has been diverted to inefficient uses.

**Table3**

GDP growth rate in MENA region and East Asia & Pacific (percent)

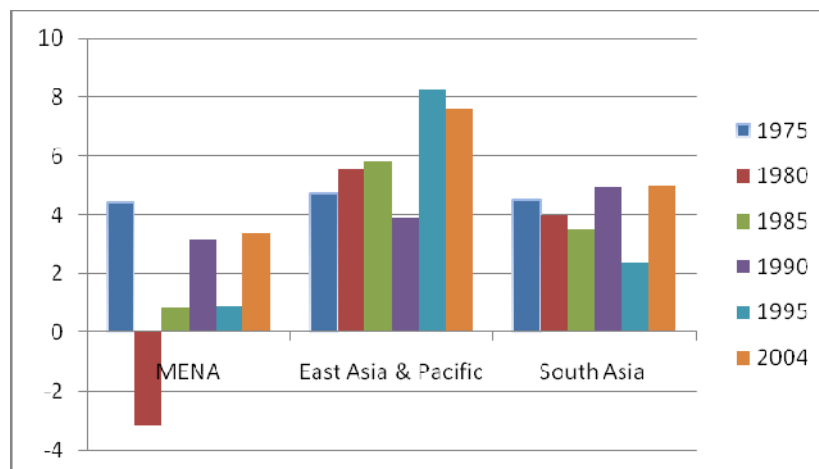
	1970	1980	1985	1990	1995	2000	2003	2004
<b>MENA</b>	7.31	-0.19	4.07	6.71	2.99	3.57	5.23	5.09
<b>East Asia &amp; Pacific</b>	13.16	7.14	7.48	5.75	9.59	7.29	8.18	8.48

Source: World Development indicators, 2008

Growth performance of the MENA states over the period 1975-2004 has been characterized by a higher volatility than in East Asia, caused mainly by the region's overwhelmingly dependence on petroleum. The relative higher growth rates in the 1970s and the first half of the 1980s were largely attributed to a favourable external environment. This situation became reversed in the early 1990s after the oil crash.

**Figure 2**

GDP per capita growth in MENA and other regions (per cent)



Source: World Development indicators, 2008

The weak economic performance is also reflected in the higher volatility of GDP per capita, which grew by 4.41 per cent in 1975, -3.15 per cent in 1980, 0.87 per cent in 1985, 3.15 per cent in 1990, 0.9 per cent in 1995 and 3.34 per cent in 2004.

The higher volatility of GDP growth confirms that MENA region as a whole lacks of effective engines of growth despite that necessary conditions for development, such as infrastructure, are satisfied.

Moreover, in the nine countries that represent about 73 per cent of the total population in the region, the average daily per capita GDP at current prices is less than five dollars, while the average income of 22 per cent of the population is about one dollar a day. According to UNDP (2009)\*\* an estimated 65 million people in the region live in poverty, which means that about 40 per cent of the population in countries included in the sample exist below the poverty line. Furthermore, it has been estimated that approximately 28 million (11 per cent) lack access to improved drinking water and 78 million (25 per cent) have no access to improved sanitation.

*Distorted economic structure*

“Natural resources are not a growth engine on their own and had not proven to be catalyst for other sources of growth for the region as a whole....” (The Arab World Competitiveness Report 2002-2003, part 1).

In general, the region’s economies are oil-dominated and oil is the main source of revenue. Extractive industries represent the largest share of gross domestic product, about 38.8 per cent. Oil revenues represent approximately 60 per cent of total public revenues, but more than 90 per cent in some of the producing oil countries.

The region is also characterized by low production diversification and suffers from an imbalance between the key economic sectors because of its total dependence on exports of crude oil, gas and other minerals for funding economic core activities. The region contributes 3.8 per cent of the world exports, including oil and its derivatives, and 3.1 per cent of the global merchandise trade volume.

**Table 4**  
Production structures in MENA region and other regions

<b>Agriculture, value added (% of GDP)</b>							
				<b>1970s</b>	<b>1980s</b>	<b>1990s</b>	<b>2000s</b>
<b>MENA</b>				16	14	16	15
<b>East Asia &amp; Pacific</b>				32	28	20	13

\*\* Extrapolation is based on a sample of countries representing 65 per cent of the region’s population.

<b>Latin America</b>	12	10	8	6
<b>South Asia</b>	38	32	27	21
<b>Sub-Saharan Africa</b>	20	18	18	17

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**Industry, value added (% of GDP)**

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	<b>1970s</b>	<b>1980s</b>	<b>1990s</b>	<b>2000s</b>
<b>MENA</b>	45	38	33	35
<b>East Asia &amp; Pacific</b>	40	42	43	45
<b>Latin America</b>	38	39	32	32
<b>South Asia</b>	23	25	26	27
<b>Sub-Saharan Africa</b>	32	34	30	31

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**Manufacturing, value added (% of GDP)**

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	<b>1970s</b>	<b>1980s</b>	<b>1990s</b>	<b>2000s</b>
<b>MENA</b>	8	10	11	10
<b>East Asia &amp; Pacific</b>	32	31	30	31
<b>Latin America</b>	27	27	20	18
<b>South Asia</b>	16	16	16	16
<b>Sub-Saharan Africa</b>	17	17	16	14

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**Services, etc., value added (% of GDP)**

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	<b>1970s</b>	<b>1980s</b>	<b>1990s</b>	<b>2000s</b>
<b>MENA</b>	40	48	52	51
<b>East Asia &amp; Pacific</b>	28	31	37	42
<b>Latin America</b>	50	51	61	62
<b>South Asia</b>	39	43	47	52
<b>Sub-Saharan Africa</b>	48	48	52	53

Source: World Development indicators, 2008

As is shown in table 4, MENA seems to be less industrialized in the new millennium than it was decades ago, with the contribution of agriculture to GDP in the 2000s is as it was in the 1970s and the share of the manufacture sector to total GDP the lowest among all regions. The low contributions of agriculture and industry imply that the MENA nations are developing into services-based economies. However, considering the region's low productivity performance, the types of services produced offer little to the advancement of local knowledge and may indicate greater economic fragility. Accordingly, a radical change in the region's development process with a more diversified and flexible production base is more than urgent.

**Table5**

Expenditure on Research and Defense in MENA countries

	<b>Expenditure on research as percentage of 2006 GDP</b>	<b>Military expenditure as percentage of 2005 GDP</b>
<b>Algeria</b>		2.9
<b>Bahrain</b>		3.6
<b>Comoros</b>		
<b>Djibouti</b>		4.2
<b>Egypt</b>	0.20	2.8
<b>Jordan</b>	0.34	5.3
<b>Kuwait</b>	0.18	4.8
<b>Lebanon</b>	0.20	4.5
<b>Libya</b>	0.70	2
<b>Morocco</b>	0.75	4.5
<b>Oman</b>		11.9
<b>Qatar</b>		
<b>SA</b>		8.2
<b>Sudan</b>	0.30	2.3
<b>Syrian</b>		5.1
<b>Tunisia</b>	1.30	1.6
<b>UAE</b>		2
<b>Yemen</b>		7

Source: UNDP (2009)

In addition, the region experiences a wide knowledge deficiency as a result of low public investment in 'research and development' and the failure to promote human resource development and technology transfers. The 2009 United Nations Human Development Report points out that only 0.2 per cent of the MENA region's GDP is at present spent on scientific research, compared to Denmark, France, Switzerland and the United States where the corresponding figure is between 2 and 3.6 per cent. Furthermore, 38 per cent of total population of MENA are still illiterate. According to UNDP (2009) the annual expenditure on scientific research per capita in the region is less than \$10 compared to a corresponding figure of \$575 and \$1304 for Ireland and Finland, respectively. On the other hand, the MENA region spends more than 4.5 per cent of its GDP on defense.

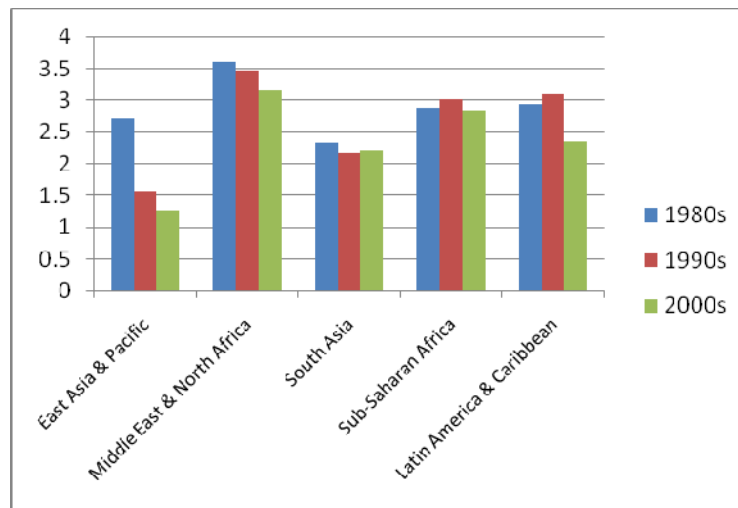
Moreover, over the last two decades braindrain in the region has increased and millions of highly skilled people have immigrated to developed countries, causing a massive economic and social loss in addition to significant development opportunities being missed. According to

estimations by the Arab Labor Organization, losses have increased twentyfold, currently totaling 200 billion dollars versus 11 billion dollars in the 1970s. The region accounts for 31 per cent of the braindrain from developing to developed countries (contributing approximately 50 per cent of the doctors, 23 per cent of the engineers and 5 per cent of the scientists who migrate from the third world). According to many experts, this critical situation is also explained by the region's restrictions on freedom as well as its bureaucracy and corruption.

*High unemployment rates*

The unemployment rate in the region is about 14 per cent, among the highest in the world (UNDP)<sup>††</sup>. Compared to other global regions, the area exhibits the highest rates of labourforce increase over the last three decades (figure 2), making the fact that the unemployment rate for young age groups reaches 40 per cent a major concern.

**Figure3**  
Labor force growth over 1980s, 1990s, and 2000s



Source: World Development indicators, 2008

Unemployment essentially concerns the youth and is linked more to the problem of insertion into the labour market (World Bank, 2004). This situation is typical in countries where education and training systems are not adequately linked to the economic environment. Indeed, graduates, misinformed about the country's working conditions and requirements, have educational profiles that are inconsistent with reality, a fact which makes their first attempt at labour market entry difficult.

<sup>††</sup> Higher unemployment rates confirm that economies of the region are stagnating even if they seem to be basically stable.



The high level of unemployment is a challenge for the region's economies and may be a potential source of social disruption and conflict, particularly as the population will increase to 410-460 million by 2020. Those under the age of 14 years will constitute more than 40 per cent of the total population and the number of job seekers over the next decade will top 39 million. The situation deteriorates further if we include women's growing participation in the workforce, which will put greater pressure on the labour market.

The number of unemployed in the region is expected to increase to 25 million by 2010. The situation worsens when we acknowledge that nearly 5 million new workers hope to enter the labour market annually; the estimated funds needed to provide new jobs for this cohort will exceed \$20 billion annually. If the workforce in the region continues to grow at the same rate, it is estimated that the labourforce will reach 134 million by 2010 and 155 million by 2015. This means that the region should provide 39 million new jobs by 2010, to meet the additional needs for the 17 million job seekers and 22 million new labour-market entrants. By 2015, the need in the region is about 60 million jobs and by 2020 around 105 million jobs. In addition, according to the Arab Labor Organization (2009) a 1 per cent increase per annum in the annual unemployment rate induces a 2.5 per cent loss in total GDP (about \$115 billion).

The fact that the region's countries lack unemployment insurance implies that the social impacts of being jobless are substantial. The problem is particularly severe for the informal sector workers, as these are not registered with the state's institutions, and consequently have no social protection. The problem is most acute in those MENA countries where the informal sector accounts for 90 per cent of economic activity, and is the largest employer of the labour market.

In diversified economies such as Egypt, Morocco and Tunisia, the informal sector is likely to expand, as it may be difficult to promote formal sector employment. The unemployment crisis can be aggravated by low capital flows, a sharp decline in exports, or a slowdown of investment growth in the developed countries. Finding new job opportunities in the MENA region during this decade is more pressing than at any other time in the past. The problem is the biggest in those countries where the risk of increased poverty is most eminent.

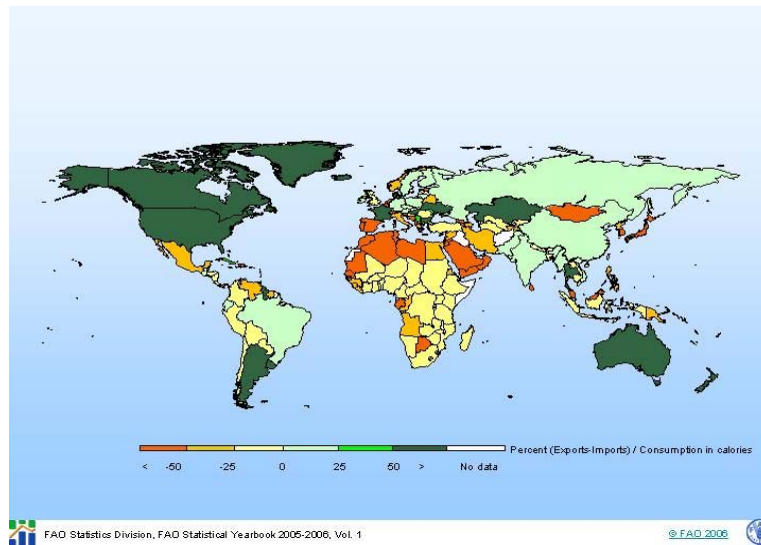
#### *Food security risk*

MENA is one of the most disadvantaged regions of the world with regard to food self-sufficiency (figure 8). It is largely dependent on the import of grain, meat, milk, sugar and oils,

to meet the consumption needs of its population of 300 million. Food deficit is increasing and the reliance on external food sources has become a real constraint for most MENA countries. This will have a significant effect on their ability to achieve economic and social development in general and agricultural development in particular.

**Figure4**

The region is one of the most food-import dependent in the world



For many MENA countries, more than 90 per cent of total food consumption is imported. In 2007, the cereal trade balance recorded a deficit of 58.2 million tons, making the MENA region the largest importers of cereal in the world (FAO 2008).

**Table 6**  
**Net cereal imports and food aid in MENA countries**  
**(% total consumption) 98-00**

<b>Algeria</b>	76.10%
<b>Bahrain</b>	39%
<b>Comoros</b>	
<b>Djibouti</b>	100%
<b>Egypt</b>	33.70%
<b>Jordan</b>	97%
<b>Kuwait</b>	99.60%
<b>Lebanon</b>	88.40%
<b>Libya</b>	89.20%
<b>Mauritania</b>	
<b>Morocco</b>	54.10%
<b>Oman</b>	98%

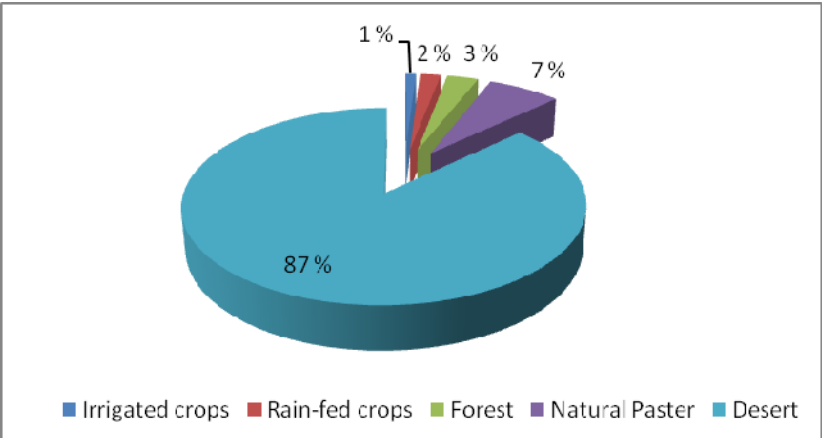
<b>Qatar</b>	95.60%
<b>Saudi A</b>	72.90%
<b>Sudan</b>	12.80%
<b>Syria</b>	21.60%
<b>Tunisia</b>	56.90%
<b>UAE</b>	100%
<b>Yemen</b>	76.30%
<b>Average</b>	70%

Source: FAO 2008, World Resources Institute.

Food safety is a recurring problem that is related, in part, to the geographical characteristics of the region. Indeed, according to World Bank, MENA is one of the world’s most water-scarce regions. The region has a total area of about 14 million km<sup>2</sup>, of which more than 87 per cent is desert. It is characterized by a high dependency on climate-sensitive agriculture and a large share of its population and economic activities are located in flood-prone urban coastal zones. Furthermore, most people are city dwellers, not desert pastoralists.

**Figure5**

Distribution of major land uses for the MENA region



Source: FAO (2008)

Moreover, the region annually exceeds its supply of water from rainfall and river flows, depleting groundwater resources. Accordingly, the availability of water and subsequent agriculture production are expected to diminish (UNDP, 2009). Warren et al. (2006) confirm that by 2025, 80-100 million people in MENA will be exposed to water stress. By 2050 water availability per capita will fall by 50 per cent and there is high potential for food crises due to increasing demand (population) and declining supply factors (precipitation, yields). Indeed, the

growing competition for water is expected to reduce the share of agriculture to 50 per cent by 2050.

The degradation of agriculture is likely to increase unemployment in countries like Comoros, Djibouti, Mauritania, Sudan and Yemen where farm workers constitute 50 per cent of the total labourforce. Gender inequalities are likely to increase because the share of women in the agriculture labourforce in many countries is relatively high (more than 60 per cent)<sup>##</sup>.

**Table 7**  
Population growth and water availability in MENA countries

	<b>Population 1995 (million)</b>	<b>Water per capita 1995</b>	<b>Population 2025 (million)</b>	<b>Water per capita 2025</b>
<b>Algeria</b>	28.1	527	47.3	313
<b>Bahrain</b>	0.6	161	0.9	104
<b>Comoros</b>	0.6	1667	1.3	760
<b>Egypt</b>	62.1	936	95.8	607
<b>Jordan</b>	5.4	318	11.9	144
<b>Kuwait</b>	1.7	95	2.9	47
<b>Lebanon</b>	3	1854	4.4	1261
<b>Libya</b>	5.4	111	12.9	47
<b>Morocco</b>	26.5	1131	39.9	751
<b>Oman</b>	2.2	874	6.5	295
<b>Qatar</b>	0.5	91	0.8	64
<b>Saudi Arabia</b>	18.3	249	42.4	107
<b>Tunisia</b>	9	434	13.5	288
<b>Emirates</b>	2.2	902	3.3	604
<b>Yemen</b>	15	346	39.6	131

Source: *Gardner-Outlaw & Engelman (1997)*

According to World Bank projections for the region, temperatures will increase by 2 degrees C by 2030 (4 degrees C by 2050), so that the sea will rise 20-50 cm and rainfall precipitation will drop 20 to 40 per cent by 2050. Higher temperatures and diminishing precipitation will increase droughts. Indeed, Agoumi (2003) confirms that since the beginning of the 20th century, drought frequency in North Africa has increased from one event every ten years to five or six occurrences. He also adds that between 6 and 25 million people will be exposed to coastal flooding.

<sup>##</sup> See table A2 in appendix.

Increased water competition and low productivity have added to the region’s difficulties to feed its growing population. In addition to the harsh environment, the region needs to deal with inefficiency with regard to food crops and productivity that results in particular from impractical farming methods, and weak training and education. Limited opportunities for financing and lending as well as misguided agricultural policies have resulted in declining farm output. On other hand, harsh living conditions in rural areas, due to the paucity of agricultural and rural development, has triggered massive rural–urban migration.

Coping with the risk of food security will be beyond the capacity of many of the region’s countries and is expected to add new challenges to the social agenda. Deteriorating living conditions of the poor are estimated to revive earlier social tensions and conflicts. It will, therefore, be necessary to introduce an integrated strategy that increases the options for controlling the demand on water resources and for encouraging their efficient usage.

### 3.2 Determinants of economic vulnerability in the MENA region

At least two factors can explain the apparent fragility of the region: high trade exposure associated with high export concentration, and social and political deficiencies.

#### *Heavy reliance on foreign markets*

All MENA economies, regardless of the level of their economic development, exhibit a common characteristic: excessive reliance on raw material exports for foreign exchange earnings, and on foreign markets for their industrial products and food items.

**Table 8**

Main characteristics of the MENA region (2000-07)

	East Asia & Pacific	Latin America	MENA	Sub- Saharan Africa
<b>Workers' remittances (%GDP)</b>	1.39	1.66	6.97	1.71
<b>Food import (% of merchandise imports)</b>	4.97	7.23	16.84	11.36
<b>Fuel export(% of merchandise exports)</b>	7.46	17.51	56.32	36.98
<b>International tourism, receipts (% of total exports)</b>	5.96	6.38	14.13	8.28
<b>Manufactures exports (% of merchandise exports)</b>	79.1	55.35	24.47	31.85

<b>Openness</b>	77.1	44.59	87.89	65.76
<b>Unemployment (% of total labour force)</b>	4.55	9.19	14	

Source: World Development indicators, 2008

Table 5 shows that, compared to other developing regions, the MENA region is more dependent on (i) remittances (accounting for almost 7 per cent of GDP), (ii) international tourism (14 per cent of GDP) and (iii) fuel exports (56 per cent of GDP). It also shows that the region is highly dependent on food imports, importing in general more than 50 per cent of agricultural products. The agricultural trade balance recorded a deficit of US\$25 billion and a food deficit valued at US\$18 billion in 2006.

For most economies, the strong dependence on international markets has resulted in an underdevelopment of local markets. Indeed, it is widely recognized that the proportion of a country's population living in urban areas is highly correlated with the level of income. Urban areas offer economies of scale and richer market structures. Workers in urban areas are individually more productive, and earn more, than their rural counterparts. Consequently, increased urbanization would improve productivity and income per capita.

**Table 9**  
Correlation between GNI per capita and Urbanization  
in MENA region and other regions (1980-2004)

<b>MENA</b>	0.37
<b>East Asia &amp; Pacific</b>	0.95
<b>Latin America</b>	0.95
<b>Sub-Saharan Africa</b>	0.93
<b>South Asia</b>	0.95

Source: Author's calculation

As is shown in table (6), MENA is the only region with a very low correlation between GNI per capita and urbanization, confirming the limited role of local markets in the region's wealth creation<sup>§§</sup>.

Consequently, economic development seems to be fostered not by indigenous economic forces and needs, but rather by the requirements of the industrial economies. The lack of dynamism in the local market and its insignificant contribution to economic development is certainly a major

<sup>§§</sup> Morocco and Tunisia are the exceptions with correlation coefficients of 0.89 and 0.91, respectively.

weakness that needs to be addressed by the region's economies. Moreover, the MENA region has for too long pursued a growth strategy reliant essentially on capital accumulation as engine of growth.

**Table10**

Trade in technological products in MENA countries

	<b>Hi-tech exports as % of total manufactured exports 2006</b>
<b>Algeria</b>	1
<b>Bahrain</b>	2
<b>Comoros</b>	
<b>Djibouti</b>	
<b>Egypt</b>	0.6
<b>Jordan</b>	5.2
<b>Kuwait</b>	1
<b>Lebanon</b>	2.4
<b>Libya</b>	
<b>Mauritania</b>	
<b>Morocco</b>	10.1
<b>Oman</b>	2.2
<b>Qatar</b>	1.2
<b>SA</b>	1.3
<b>Sudan</b>	
<b>Syrian</b>	1
<b>Tunisia</b>	4.9
<b>UAE</b>	10.2
<b>Yemen</b>	

Source: Knowledge Assessment Methodology Data Base, World Bank (2008)

However, high integration in the world economy, *per se*, is not the source of vulnerability. The major problem of the region is its high concentration of exports with a low comparative advantage, and its limited local market size combined with a low level of regional integration. The main exports of the region are raw materials and the technological content of its exports is modest, which reduces their competitiveness and bargaining power. Indeed, the share of hi-tech exports in total manufactured exports in 2005 was, on average, 3.3 per cent. Morocco and EAU recorded the highest level of hi-tech exports at 10 per cent and Egypt the lowest level at 0.6 per cent (table 10); for comparison, it should be mentioned that the corresponding share in Malaysia, for example, is 54.7 per cent (World Bank, 2009).

In addition, the MENA region has lagged behind in terms of regional integration. Indeed, despite the favourable conditions of some of the region's countries and the comparative advantage of geographic proximity to other MENA nations, intra-regional trade is still very low, less than 14 per cent (13 per cent of exports or the equivalent of US\$65 billion, imports 15 per cent, or US\$62 billion). Bahrain, Oman and Yemen are exceptions as they import more than 30 per cent of their needs from the region. The poor results are due to the fact that current integration projects are driven by political considerations instead of a natural process of integration fostered by the market for which geographic proximity is an essential factor.

The concentration of trade and poor regional integration, in conjunction with the paucity of effective mechanisms of coordination and cooperation, make the MENA region relatively vulnerable. Indeed, regional cooperation to overcome the crisis through greater intra-regional trade and funds to support the most affected countries could reduce its consequences and shorten the time needed for recovery. Consequently, a regional strategy to deal with internal as well as external shocks is not going to be easy.

#### *Human and institutional deficiencies*

To a large degree, the ability of any economy to continue to function in the face of unexpected events depends on the institutional structure and the operational systems in place, and the resilience of these. Moreover, it is widely accepted that social relations and institutions contribute to the effective functioning of the economic system. The role of institutions and good governance in promoting economic growth is confirmed by many recent works (see Rodrik, Subramanina and Trebbi, 2002; Easterly and Levine, 1997). For instance, the *Global Competitiveness Report 2009-2010*, considers important pillars of economic development to be the institutional environment and solid institutions that play a crucial role during economic crisis.

Weak governance and corruption are the main bottlenecks handicapping the human and institutional development of the region. Familialism is still important in the MENA region, and favours and kin reciprocities often govern people's interaction (Abu-Laban & Abu-Laban , 1987).



**Table 11**  
Human and Institutional development in MENA countries

	<b>Life expectancy at birth, females (2000-2005)</b>	<b>Literacy rate, all adults (2007)</b>	<b>Corruption perceptions index<sup>***</sup> (Transparency International) (2006)</b>	<b>Government Effectiveness Index<sup>†††</sup> (2007)</b>	<b>Political Stability and Absence of Violence Index<sup>‡‡‡</sup> (2007)</b>
<b>Algeria</b>	72.2	75.4	3.1	-0.52	-1.18
<b>Bahrain</b>	76.5	88.8	5.7	0.41	-0.28
<b>Comoros</b>	65.1	75.1		-1.8	-0.4
<b>Djibouti</b>	54.9			-0.98	-0.05
<b>Egypt</b>	72	66.4	3.3	-0.44	-0.77
<b>Jordan</b>	73.1	91	5.3	0.27	-0.29
<b>Kuwait</b>	79.2	94.5	4.8	0.2	0.4
<b>Lebanon</b>	73.2	89.6	3.6	-0.61	-2.09
<b>Libya</b>	75.7	86.8	2.7	-1.07	0.47
<b>Mauritania</b>	64	55.8	3.1	-0.68	-0.33
<b>Morocco</b>	71.8	55.6	3.2	-0.07	-0.52
<b>Oman</b>	75.9	84.4	5.4	0.38	0.76
<b>Qatar</b>	75.3	93.1	6	0.06	0.81
<b>Saudi Arabia</b>	74	85	3.3	-0.18	-0.59
<b>Sudan</b>	57.8	60.9	2	-1.18	-2.3
<b>Syria</b>	74.9	83.1	2.9	-0.88	-0.61
<b>Tunisia</b>	75.1	77.7	4.6	0.46	0.1
<b>UA E</b>	80.5	90	6.2	0.86	0.76
<b>Yemen</b>	61.8	58.9	2.6	-1.02	-1.48

Source: World Resources Institute.

As is shown in table 8, most MENA countries suffer from bad governance and political instability. Indeed, with a few exceptions, the region is below the world level in terms of government effectiveness and political stability. Moreover, most MENA countries rank poorly in terms of corruption, and TI's Corruption Perceptions Index consistently ranks these nations below the world median.

\*\*\* Units, 10=least corrupt, 0=most corrupt

††† Units: -2.5 worst governance, 0 average, 2.5 best governance

‡‡‡ Units: -2.5 worst governance, 0 average, 2.5 best governance

Low social capital, security and social tensions, conflicts, deteriorated business environment, due to excessive public intervention, and low quality of human capital are additional bottlenecks handicapping development and stability in the region.

In terms of human development, many of the region's nations have achieved higher levels than other developing countries, as indicated by the relatively higher life expectancy for females and literacy rates. However, the recent gains in human development are fragile, and are not built on long-run government policies (Arab NGO network for Development, 2009). Indeed, the provision of public and social services depends on volatile oil revenues. Moreover, in poorer countries of the region the lower life expectancy for females compared to the world average (68 years) reflects a very precarious situation.

In the absence of robust safety networks and well-developed social policies, the number of vulnerable regions and populations may grow sharply, triggering social and political instabilities. Even for the richer countries having adequate financial resources to dampen economic and social impacts of an eventual crisis, the cost will be relatively high due to the lack of good governance. Damage caused by potential crises could be contained if these countries had well-designed institutions. Because of the lack of financial resources and inefficient institutions as well as the lack of effective social policies, the poorer MENA countries may be faced with social tensions.

#### **4. Concluding remarks and policy recommendations**

The MENA region finds itself at a crossroad, faced with new opportunities but also challenged by real social and economic debacles. Development programmes implemented by the different states have failed to deliver significant results, and essential reforms are needed if these are to remain viable in the global economy.

Diversification of the economy continues to be a major challenge for the region in general. Many experts call for urgent action to address the main causes of economic vulnerability in the region and to enhance its resilience to external shocks. Moreover, it becomes vital that MENA countries improve the overall quality of governance and raise their economic competitiveness. Improvements to macroeconomic management as well as institutional reforms are essential to enhance efficiency and facilitate the absorption of new technology.

It is clear that the economic performance of the region during past centuries was not simply a coincidence but the result of good management of existing capacities combined with the willingness to seize opportunities offered by the favourable global environment.

In short, the 'golden age' of the region during the period from the 7th century to the late 13th century can be explained by factors such as:

- First, the region succeeded in promoting a dynamic economy through control of much of worldwide trade and the free movement of goods, people and capital. The mass of wealth generated through large-scale trade provided the financial resources needed for developing the necessary administration, agriculture and industry.
- Second, the strong central power and well-developed administrative system provided an appropriate environment for the smooth conduct of economic activities. Free market system, combined with a strong, stable monetary system, led to economic and social prosperity in the region.
- Third, with new technology and innovative planting and irrigation methods, the agricultural revolution provided the backbone of the region's economic development. Quantitative and qualitative advancement in agricultural production also promoted the development of some basic industries like the sugar and paper industries.

The main conclusion of this paper is the fact that economic and social deficiencies in the MENA region are currently a matter of choice, not its irrevocable destiny. In other words, the region's current, poor economic performance is not an historical fatality but the result of bad policy options made after the end of colonization and the emergence of the modern states. Indeed, despite a wide range of economic reforms having been adopted since the 1970s and late 1980s, the region's economic frameworks remain fragile and dependent on the economic conditions of the industrial countries.

From our analysis, we can conclude that the development process in the region has already reached its limit and can no longer meet the region's needs in terms of development and stability. A new development strategy based on the knowledge economy has become more than urgent in order to establish the foundation for sustained development.

Indeed, despite 35 years of active effort and vast amounts of money, economic achievements have fallen far short of the population's aspirations; the region remains extremely fragile and dependent on the economic conditions and policies of the industrial countries. Even if important

foreign exchange reserves have helped certain countries within the region to overcome many economic crises, the financial cost of support has been relatively high. Moreover, it appears that the fragility of the region could worsen in the future, if account is taken of the risk of greater fluctuations in food and oil prices. The likely depletion of the region's water resources, combined with severe climate changes, will introduce greater challenges.

Despite the apparent heterogeneity of MENA, available financial and human resources are important assets that could, with better management, establish the foundation for sustained development throughout the region. Even if regional integration currently appears to be difficult to achieve, it remains the only option for the region. Geographic proximity may play a key role in promoting economic integration and improving intra-regional trade and investment.

However, geographic proximity *per se* cannot influence trade among neighbouring countries if these are underdeveloped and lack trade potential. Geographic proximity can give an additional stimulus to trade only if the preconditions for dynamic growth exist. Consequently, to improve intra-regional trade among the MENA countries, a dynamic mechanism needs to be envisaged. The emergence of virtuous trade circle among the MENA states needs that leader countries be developed first before attempts at regional integration are made, and the leader would then be utilized by neighbouring nations as a vehicle (pivot country) or an engine for industrialization and development. Intra-regional trade could be used by the lead countries to supplement their international trade in order to overcome the limited size of local markets, thus remedying the scarcity of resources, enhancing production efficiencies by developing economies of scale and achieving higher production capacities as a result of the better allocation of domestic resources. Regional trade can be used by other countries to boost competition in the domestic market and improving terms of trade due to cheaper imports.

In the final analysis, the MENA countries should coordinate their efforts and develop a regional plan for agricultural and industrial investment, and adopt regional projects for improving education and training. Strong, modern institutions could represent a safeguard against future crises as well as develop the capacities of the region to absorb external shocks. Better governance and greater freedom are essential to address the various sources of vulnerability and to increase the resilience of the region. The potential social costs that the region could support justify the need to invest more effort in this direction.

## Appendix

**Table A1:** Main characteristics by country

	<b>Food imports (%imports)</b>	<b>Trade (% of GDP)</b>	<b>Industry (% of GDP)</b>	<b>Fuel exports (%exports)</b>	<b>Domestic credit (% of GDP)</b>	<b>Remittances (%GDP)</b>	<b>External Debt (%GNI)</b>	<b>GDP per capita (PPP)</b>
<b>First Group</b>								
<b>Algeria</b>	20.91	65.17	57.66	97.95	20.39			6736
<b>Bahrain</b>	7.30	38.29		74.65	59.19			25329
<b>Kuwait</b>	16.39	71.85	53.34	93.44	74.96			37818
<b>Oman</b>	10.97	94.60	54.48	85.05	35.46			19064
<b>Qatar</b>	7.70	129.88		89.83	37.85			64262
<b>Saudi Arabia</b>	14.54	157.57	53.09	89.81	54.41			20357
<b>Libya</b>	16.91	79.11			2.33			12396
<b>UAE</b>	33.26	47.58	11.86	67.61	11.54			45896
<b>Second Group</b>								
<b>Egypt</b>	15.52	66.72	27.73	0.38	97.04	4.17	30.85	4504
<b>Jordan</b>	17.00	88.49	23.74	0.26	184.06	21.30	70.53	4095
<b>Lebanon</b>	17.79	98.66	32.38		-3.77	19.48	92.89	9108
<b>Morocco</b>	12.58	61.15	24.66	77.37	12.71	7.66	38.00	3447
<b>Syrian</b>	8.71	93.25	28.89	11.55	72.22	2.16	118.48	3939
<b>Tunisia</b>	7.21	147.44	54.26	67.61	50.57	4.81	68.29	6159
<b>Third Group</b>								
<b>Comoros</b>		51.67	16.21		28.52	3.99	90.99	1110
<b>Djibouti</b>	21.50	60.18	35.61	45.15	103.23	3.69	52.28	1824
<b>Mauritania</b>	11.01	107.65	27.89	3.91	77.94	0.14	145.94	1668
<b>Sudan</b>	16.60	96.07	34.13	67.59	30.90	5.17	93.39	1621
<b>Yemen</b>	25.51	78.25	42.15	94.14	5.77	10.16	45.71	2138

**Table A 2: Share of Agricultural labor force**

	<b>Share of Agricultural labor force in total labor force</b>	<b>Share of female in agricultural labor force</b>
<b>Algeria</b>	23.3	52.2
<b>Bahrain</b>		
<b>Comoros</b>	71.9	50.9
<b>Djibouti</b>	76.9	48.7
<b>Egypt</b>	30.7	48.4
<b>Jordan</b>	10.3	69.7
<b>Kuwait</b>	1.1	1
<b>Lebanon</b>	2.8	39
<b>Libya</b>	4.6	66.3
<b>Mauritania</b>	51.6	51.7
<b>Morocco</b>	33.5	85.2
<b>Oman</b>		
<b>Qatar</b>		
<b>Saudi Arabia</b>	7.5	8.2
<b>Sudan</b>	57.4	38.2
<b>Syria</b>	26.1	65
<b>Tunisia</b>	23.1	41.8
<b>United Arab Emirates</b>	4.1	
<b>Yemen</b>	46.4	44.1

Source: FAO (2008)

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