MEI Insight No. 141

1 March 2016

Middle East Insights

Middle East Institute, National University of Singapore

Development under risk in the Arab World[1]

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Many of the countries that are far from achieving sound economic development, are situated in the Arab World.[2] The worst hit are either in conflict, near conflict or post conflict zones. Even when not in a state of conflict, the fragility of their development is further compounded by the prospect of conflict, which dampens the appetite for productive investment. Their past slow rate of progress is typical of developing small risky markets or capital-scarce structures that have adopted unconditional liberalisation measures (real and not financial capital). For their economic growth, for the most part, these countries still depend on the export earnings of raw material exports or oil (most Arab countries are oil producers). When oil prices fall, economic growth stumbles, and an already poor development showing suffers yet another setback.

Often yesterday's accomplishments are written off by the dislocation caused by war or anti-developmental macroeconomic policies. The latter are policies whose interface with reality does not mobilise idle resources, such as putting more people to work. For the group of risk-saturated and underachieving Arab countries, the crunch on their course of development happens to be fourfold:

Firstly, the determining undercurrent in their development lies in the fact that decision-making circles often involve external forces (any exogenous agencies) for whom another small country being able to develop its productive capabilities in a world consumed by a crisis of overproduction is regarded as unnecessary.

Secondly, the immediate damages of war or the prospects thereof impose a drag on economic, social and institutional development.

Thirdly, although economic growth, rapid industrialisation and technological advancement are indispensable conditions for development, they are pointless when governments constrain popular participation or the capabilities of people to achieve different valuable human functionings, as in achieve their potential.[1]

Fourthly, without income and wealth being more evenly distributed among different sections of society, the demand component that would drive the momentum for auto-generated and knowledge-infused growth falters.

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[1] *Parts of this article were first published on Global Research* :"War, Conflict and Economic Development in the Arab World", 16 February 2016, *http://www.globalresearch.ca/war-conflict-and-economic-development-in-the-arab-world/5508140*

[2] These are non-oil producing as well as oil producing Arab countries.

Most Arab economies grow from 'without' by the incongruous forces of commodity prices, geopolitical rents and political tensions. The fact that they have not harnessed their internal resources for the purpose of development implies that the build-up of development is not part of the national security structure (Industrial and human capacity, including better living standards, enhance security). It also implies that the extent of this separation of security from development is a product of a schismatic social contract, which does not mediate the interests of various social groups within society. Despite hollow growth leading to low 'decent' employment generation and poor development experience over the past few decades, their macroeconomic structure did not change. The historical agency in charge of development reproduced the same policies and conditions time and again. A slow dynamic rise in productivity or negative productivity growth rates, which is the nucleus of wealth creation, indicates an absence of 'growth from within' (endogenous growth) or growth that is based on the infusion of national knowhow capabilities in production.

At times of high oil prices, output per worker 'appears' high and even somewhat astronomical, but when oil revenues are deducted from total income, output growth per worker is more often negative than positive. This is a pernicious result because it means that the productive capital stock per worker, or equipment of the modern technology type that grows from the need to capitalise both capital and labour to meet higher demand, is not rising.[2] The positive developmental impact of an oil price windfall resulting from a transient rise in commodity prices is either a token-like stabilisation measure, given the type of social contract, or is continuously sapped by persistent tensions or by institutional squandering arising as a by-product of conflict or as a result of an impertinent macro policy, or a policy that does not match the particularity of Arab economies. With respect to the last point, the synergy that would arise as a result of incremental value-added growth attendant on productivity growth, which would, in turn, drive the introduction of knowledge into production, is clearly missing. In other words, because these economies are not growing by their own means, they need not link their scientific output to their production structure. The whole point of nationalising jobs or synchronising labour for the requirements of capital is meaningless when the virtuous circle of productivity growth cum economic growth has not taken root.

It is true, but more like a truism, to assert that reviving the debilitated economies requires an end to conflicts and the creation of a politically stable environment conducive to both domestic and foreign investment – investment of the higher output to capital ratio type – along with a rising internal demand component in the national economy. Yet, as true as this assertion may seem, the regional security arrangement is now anchored in a continuous war condition related to more acute international divisions. On the national political scene, a process of 'selective democracy' similar to those practiced in ancient times – as opposed to a universal one – which enshrines the right of the few at the expense of the many appears to further take hold. On the economic side, it is now evident that macroeconomic policies continue to be of the neoliberal genre market, favouring private over public interests. Although it is practical to develop macroeconomic policies that envisage development under the shadow of risk, the interface between external shocks/conflicts and the national economy under the current state of tensions is based almost entirely on the non-existent assumption of a level playing field and risk-free environment. If the elephant in the room – as in the wars and the lopsided institutional context – Is overlooked, the case may be that it is no longer myopia on the part of the

agency of development that is causing past errors to be continuously repeated, but the lack of will to develop.

In *operational* terms, the problem of development in such risky contexts has to address the issue of managing the macro-economy subject to a plethora of economic and extra-economic constraints of which, principally, a risk level/insecurity reproduced conjointly by regional and extra-regional agents overshadows the course of events. That is to say which are the principal variables that should be addressed to produce healthier growth and development. It is never easy to separate politics from economics, but in small developing countries exposed to risk, the operational problematic prioritises 'politics' or the decision making level of policy as the control variable. Past and current policies**,** some of which are reviewed below, overlook the interrelatedness and the structure of determination between politics and economics.

Previous recipes for economic reform intended to crowd in political reform as a result of oiling the market machinery for a frictionless welfare maximising outcome, occurred only on the pages of textbooks. Moving from the public to the private sector and from closed to open economies did not shift resources into more competitive areas. According to the World Bank, the Arab share of manufacturing in investment is declining almost everywhere, and the share of manufacturing in GDP is lower than that in all other developing regions except Sub-Saharan Africa (World Bank 2011; World Development Indicators various years). The share of high-technology exports from total manufactured exports in the Arab World is at around 1 to 2 percentage points, below the rank of Sub-Saharan Africa – including South Africa, which is around 5 per cent (World Development Indicators various years; World Bank 2011).[3]

Capping supply capacity, which is essential to promote competition, Arab countries remained almost entirely dependent on raw material exports and did not diversify. For fast neoliberal reformers and slow reformers alike, the present condition of low oil price combined with low output growth is telling; showing how past and present parochial policies have failed to identify the principal conduit of regional development, which is overdetermined by the region's mode of integration into the global economy through oil and war. Not that there are exceptions to the rule of development failures, but in case there is an odd achiever, the explanation of developmental success could be carried out more fittingly on geopolitical grounds than it would be on economic grounds.

In retrospect, the case may have been that most may have needed to liberalise trade, but not willy-nilly as they have done. Trade liberalisation could have been selective and conditional and within their own respective regions first such that their negotiating position and accession into the global economy does not come at the expense of national industry and food security for instance. Arab countries import more than half their food consumption and some food dependent and cash-strapped countries have to borrow to buy their basic foods.[4] In a politically tense atmosphere, East Asia's successful experience shows that being choosy about what to liberalise and only in relation to developing the national industry and to what the big trading partners do creates the condition for development enhancing growth.

It may have been valid that there needs to be a boost to the environment for the growth and development of the private sector, but such a position has viewed the public/private investment relationship as antagonistic. Practically, for public investment to crowd out private investment is nearly impossible.[5] When the risks to private returns are high, and potential resources are plenty, a better managed public sector can act as a quasi-

insurer of private undertakings. The public sector crowds in the private sector.

It is also true that there needs to be a diversification away from primary products. However, as regionalism and/or transforming countries into a regional building-blocs to expand markets requires at least the promotion of investment in intraregional infrastructure, given the low rate of Arab regional integration, moving away from oil appears to not have been taken seriously. Other leading indicators of unsuccessful diversification include the lack of complementarities that tie physical to human capital and the minimal contribution of knowledge to production in the composition of Arab growth: the sort of industrial expansion that requires greater markets or that integrates with other markets to grow.

When it comes to policy in this class of risk exposed countries, macroeconomic questions have to be put differently. There is already the inherited weakness of being born a late developer, small and insecure into a world where being the opposite of these matters in the race for development. Consider why it is that when revenues from the export of primary commodities rise, the rate of retained savings dwindles afterwards, as in the aid paradox.[3] The policy set up is such that as consumption rises, steadily eroding reserves, less and less savings are left for investment in production when oil revenues fall. One can dwell on the point, but what is important to realise is that an economic contraction/expansion could be triggered by an external shock, however, its magnitude and duration is determined by the adequacy of economic policy and the efficiency of institutions. The prolonged and substantial economic contraction in most Arab countries, therefore, raises serious questions regarding the decision making process behind the whole macroeconomic constellation, including why institutions knew way back that they had to diversify and yet failed persistently.

Macro policies are interrelated and questions about their efficacies beg their own answers. For instance, to what extent is the problem of unemployment in some of these countries an outcome of monetary policy that targets low rates of inflation with no regard to unemployment? To what extent is the problem of stagflation in some countries an outcome of a policy-mix of increasing short term interest rates along with national currency devaluations? To what extent has the adverse impact of a chronically high rate of unemployment aggravated the contraction triggered by an external shock (falling oil price) and thus created a debilitating path dependence (they stay on the same undesirable path)? The answer to all three questions may boil down to the fact that a country cannot peg to the dollar under an open capital account, and still hold on to an effective monetary policy. As labour share from total income fell as a result of lacking labour representation, inflation and wage compression, the steadying of the national currency against the dollar channelled wealth not only up within the same society, it also sent it abroad. If corruption is defined as the diversion of public wealth to private use, the past and still ongoing monetary policy under open capital account regime, which was in fact not only legal but also supported by major international financial institutions, is the epitome of corruption.

One may argue that freeing the environment to invest could have been a boon. However, without an investment guiding institution and an insurance framework

[3] Pouring financial aid into developing countries may produce undesirable outcomes because once aid dwindles, the growth momentum follows suit. Griffin, K. (1970) "Foreign Capital, Domestic Savings and Economics Development", *Bulletin of the Oxford University Institute of Economics and Statistics,* Vol. 32, No. 2.

underwriting force majeure attributed losses, small, risky and fragmented markets channelled investment into short gestating capital or non-productive activity. Cutting public sector employment and spending did not improve employment conditions. Alongside public sector cuts, deindustrialisation reduced the rate of decent job creation far below the rate of new entrants into the labour force.[6] Hence, rising unemployment and poverty were deliberate and necessary outcomes of policy. Welfare in this instance was not decided within a context in which private interests aim to serve the betterment of public interests. The institutional context and its rules are such that the intersection of private and public interests stand to be more contradictory than complimentary. In an imbroglio, which is overdetermined by a constellation of extra-national institutional decision making arrangements (the neoliberal ideology and its institutions) whose end is not necessarily the welfare of the region, developing countries stand to benefit from being discerning in their choice of policies. In retrospect, past social efficiency criteria under selective openness, in which social investment pays back for itself through programmes of long term development, has outperformed the current neoliberal economic efficiency criterion of fantastic marginal magnitudes making prices 'right' for growth.

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