

ME 101 Lecture 06: The Politics of Economic Reform

Speaker: Ms Rana Karadsheh-Haddad, Moderator: Mr Carl Skadian

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In this lecture, Ms Rana Karadsheh-Haddad spoke about the Middle East's developmental and economic challenges, and examined some potential opportunities in the region. As the regional industry director with the Manufacturing, Agribusiness, and Services team, covering all of the Asia-Pacific within the International Finance Corporation (IFC), she focused on her organisation's efforts and achievements in the Middle East. Part of the World Bank Group, IFC seeks to help economies develop, including through the development of the private sector.

Context and Challenges

Noting that people in Singapore often mostly associate the Middle East with the Gulf Cooperation Council (GCC) countries, Ms Karadsheh-Haddad argued that we should not ignore what happens in the rest of the Middle East, as such events have spill over effects on GCC economies.

Since 2010, countries in the wider Middle East have experienced elements of disruption, mostly driven by the protests of the Arab Spring. In Syria, Libya and Yemen, this has resulted in ongoing conflict, broken states, humanitarian disaster and refugee flows into countries like Jordan and Lebanon. In addition, oil prices have dropped further as a result of Covid-19, the coronavirus pandemic.

There were improvements in 2019, with some macro-economic stabilisation, reconstruction in Iraq and some growth in the region. Despite this, challenges, including high unemployment, especially among youths and females, remained. The Middle East and North Africa region (Mena) has recorded about 1.8 million Covid-19 cases, which raises the question of whether healthcare services in the region will be able to manage the pandemic.

Economic frustration and high unemployment is a recipe for potential political and economic instability, as seen in the Arab Spring, noted Ms Karadsheh-Haddad. The countries with the highest unemployment rates (using 2019 International Labour Organisation estimates) include Libya, Tunisia and Sudan at over 15 per cent.

Water stress, a high poverty rate and a strong presence in the economy by state-owned enterprises (SOEs) are other significant challenges facing the Mena region. In IFC's view, a larger private sector results in better economic activity, more stable economic growth and higher employment rates, but the growth of the private sector is hindered by a large SOE presence. High levels of SOE presence are linked in the region with the presence of natural resources, with Saudi Arabia, Kuwait and Iraq heavily dominated by SOEs.

Looking at the state of the region's economies, Ms Karadsheh-Haddad noted that the World Bank expects a 4.2 per cent decline in GDP for the region in 2020 due to the effects of the pandemic. This places Mena between Europe and Central Asia (at an expected 4.7 per cent contraction), and Sub-

Saharan Africa (at an expected 2.8 per cent contraction), in line with most of the world's regions, which are expected to contract in economic activity. She noted the disparity in economic development within the region, with the GCC countries remaining far wealthier than their non-GCC counterparts in GDP per capita terms.

Several bottlenecks keep the Mena region as a whole low on the World Bank's *Doing Business* rankings. These include issues in resolving insolvency, enforcing contracts, protecting minority investors and difficulty in getting credit. However, it is among the three most improved regions, with the United Arab Emirates (UAE) achieving a ranking of 16th in 2020.

Additional challenges for the region include a stagnating middle class, a category that has, in fact, contracted slightly between 2013 and 2018. Learning outcomes in Mena are also poor, with 9½ years of expected schooling but only 6 learning adjusted years of school in 2018.

Ms Karadsheh-Haddad noted the higher youth female unemployment rate of 43 per cent in the oil exporting countries, such as Saudi Arabia and the UAE, in comparison to the developing oil importers, such as Egypt and Lebanon. Without the luxury of commodities, the latter countries have to employ more of their population, however, at 33 per cent, their youth female unemployment rate is still substantial.

The region also faces a lack of water resources and of heat waves as a result of climate change. These will impact the region's ability to grow food and increase its need for resources to cool homes. Climate change will further exacerbate the high levels of surface water stress in the region.

Security and political risk also remain high in several countries, especially in Syria and Yemen, although many countries in the region face a medium to high level of risk. Political and security risk are a concern to investors as they look to potentially invest in the region. Security and political risk is in general lower in the GCC states, as well as Jordan, Israel and Morocco.

On mitigating economic, political, and security risks, Ms Karadsheh-Haddad noted that many proposed solutions are still difficult to implement, require time to put in place, and do not produce immediate results.

Overall, the Mena region still suffers from its underlying challenges and the aftermath of the economic impact of the Arab Spring. The coronavirus pandemic further threatens to put the region into economic hibernation, a poor and challenging scenario.

Potential Opportunities and Areas of Growth

Moving to examine opportunities and areas of potential growth, Ms Karadsheh-Haddad said Egypt has seen returning levels of foreign direct investment (FDI), benefiting from recent natural gas finds and its large population base. On the other hand, Jordan has seen a decline in FDI as a result of a shift away from serving as a base for reconstruction work in Iraq and increased refugee flows from Syria. FDI in Lebanon is also expected to see a drop in 2020.

She also highlighted the potential of the digital economy to jumpstart economic activity and to allow Mena countries to bypass stages of development. The region has the highest number of mobile subscribers per 100 inhabitants globally, but has a low level of digital payments, indicating that it is not applying the full potential of technology as an economic enabler. This presents an opportunity to invest, but also to employ the more tech-savvy youth, dovetailing with the need to address youth unemployment.

Additionally, there is a growing market for start-up funding, and over 155 institutions have already invested in Mena start-ups. Financial technology, or fintech, is also overtaking e-commerce as the most actively invested industry.

IFC's Strategy in Mena

Elaborating on IFC's strategy to tackle some of Mena's challenges, support the private sector, and intervene and invest in the region, Ms Karadsheh-Haddad said one key challenge is producing productive and sustainable economic opportunities for the 300 million job market entrants expected by 2050. The region needs to go from an old economy of public sector-led jobs to a new economy driven by private sector-led growth, empowered youth and women, technology enabled service delivery, and modern and efficient utilities. IFC's strategy to do so is to advocate investment in developing human capital, embracing the digital transformation and giving room for the private sector to grow.

There is a need to invest in tertiary education to improve the skills and enable the reskilling of youth and women, including through vocational training. Healthcare is another key pillar. Health systems should be strengthened through greater private sector participation and universal healthcare coverage pursued. Social protection systems are also important, and these include social insurance, flexible retirement savings schemes and the challenge of managing the refugee crisis. All are means of investing in human capital to strengthen the enabling environment.

Aspirations for the Mena region include digital broadband access, investment in telecommunications infrastructure, and increasing the utilisation of internet and mobile payments. The development of local platforms for e-commerce should be supported, and inclusive digital connectivity should be ensured to benefit women, refugees and citizens of lagging regions.

There is a desperate need to modernise regulations and utilities. Good roads, infrastructure, access to power and water are critical to economic development. Without goods and the provision of services, industries cannot operate, and jobs will not materialise. The dearth of water availability in the Mena region requires an efficient management of water resources that would benefit from using the best available technology.

In addition, key measures will include supporting private investment, entrepreneurship, and small and medium enterprises (SMEs), including through digital skill development and the use of technology to create opportunities and investment platforms.

Results on the Ground

One of IFC's achievements in the region is its fast-track Covid-19 credit facility, a global initiative launched in March 2020 in Asia to help IFC's clients with the liquidity and working capital solutions critically needed to address the pandemic's economic impact. Of US\$8 billion, US\$1.4 billion has been provided as of 31 August for short-term financing in Africa and the Middle East.

The objective of the facility is to save jobs and protect the most vulnerable, with the eventual aim of supporting the necessary restructuring of markets and the resumption of private sector activity. The long term objective is to support resilience in the operations and balance sheet of companies and sectors.

Some examples include the provision of a US\$100 million debt facility to the Commercial International Bank of Egypt to help SMEs impacted by the pandemic and a US\$9 million debt facility to Jordan's Luminus Group, a vocational technical training provider.

Other results from IFC include support for healthcare modernisation and multi-speciality hospitals in Jordan; the support of renewable energy capacity in Egypt; health and nutrition services in Yemen in partnership with Unicef in aid of 14.6 million people; infrastructure investments in all-weather rural roads in Morocco; Egypt's largest investment in human capital development through a cash-transfer programme benefiting 2.26 million households, 88 per cent of which are headed by women; and the support of developers providing housing for refugees.

Concluding, Ms Karadsheh-Haddad provided a snapshot of IFC's total committed portfolio of US\$4.2 billion in the Mena region, with largest exposures in Egypt (US\$1,565 million), Jordan (US\$973 million) and Lebanon (US\$ 370 million).

Highlights from the Question and Answer Session

Responding to a question on the road-blocks to enacting the development needed to tackle Mena's youth unemployment problem, Ms Karadsheh-Haddad said the business environment and risk perception will continue to be obstacles. However, Mena has seen more capital from regional development banks and more trade between Asia and the non-Gulf countries, and these shifts should translate into economic opportunities.

Asked for her view on oil prices, Ms Karadsheh-Haddad said the shift of the Chinese economy from manufacturing to consumption will shift its demand for commodities, which has previously been a key driver for higher oil prices. She is not bullish on her outlook on oil prices, though she noted that supply disruptions affect prices too, and impacted by geopolitical events, are hard to predict.

Questioned if the World Bank and IFC took a position on Saudi Aramco's initial public offering (IPO), since this involves capital from the private sector going into the public sector in a way almost opposed to the idea of promoting privatisation, Ms Karadsheh-Haddad replied that opening up one's capital base to private investors is generally a good thing, but it is important to ensure the protection of minority investors' interests, although the public requirements of listing help address this concern.

As for the areas where East Asian companies might capitalise on in the Middle East, Ms Karadsheh-Haddad suggested going straight into technology. The high number of mobile users in the Middle East and low level of digital payments is "very much a low-hanging fruit". She also suggested water resource management in particular for Singapore, which has leveraged technology, including through desalination and recycling, to address its water security and safety issues. This is an opportunity given Mena's big need in this respect.

Responding to another question on how Covid-19 has affected the grand economic "Vision" plans of Mena countries, she said the pandemic has hit tourism hard. She believes that economic plans globally are going to have to be relooked in light of the pandemic, including in terms of their industry focus.

Her personal view is that the global economy could take longer to rebound from the pandemic and this could create different structural shifts in terms of trade and consumer behaviour, with a faster move to digital payments. It could be at least 2022 until the world gets back to where it was in 2019. However, a business enabling environment, investments in human capital, healthcare and education will remain important.

For the final question, one participant noted that among the factors that have led to a lack of development in the Middle East were its governance structures, a lack of proper accountable institutions, and corruption, and sought Ms Karadsheh's view on this.

She agreed that governance is important and noted that conversations on governance do take place between international financial institutions and the Mena region. The IFC's engagements with its investee companies come with a governance review. On corruption, the IFC's policy is that events such as money laundering and corruption are events of default, with the issue being black-and-white for IFC.