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What Saudi Arabia, Iran and Tunisia have in common: The Economy, Stupid!

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Since the beginning of 2018, economic problems have come to a head in three very different states in the region: Saudi Arabia, Iran and Tunisia. As a result, unrest has developed with social and political consequences.

Table 1 below provides an overview of economic conditions in the three countries. Iran is a large oil producer with a very large population. Its economy has been badly affected by sanctions, mismanagement and by large expenditures on the conflicts in Syria and Iraq, as well as the fall in oil prices since 2014. It has also provided support for the Hezbollah in Lebanon and for forces fighting in Yemen. These allocations have become a major burden on the budget and Iranians have called for them to end. Saudi Arabia is one of the world's largest oil producers. It has a mid-size population compared with the rest of the region and high levels of per capita income. One third of its population is made up of foreign workers. Although Saudi Arabia has large foreign currency and oil reserves, its economic wellbeing has been affected by the fall in oil prices, large subsidies and military spending at home and on the Yemen War. Tunisia has a relatively small economy and population as well as very small oil reserves and production. Despite the differences, these three countries have one thing in common: very high levels of youth unemployment, especially among females. Iran and Tunisia have high overall levels of unemployment. They all have low scores on the ease of doing business index. Finally, they all face a water crisis. These factors are connected to the types of economic systems that prevail.

Table 1: Iran, Saudi Arabia and Tunisia: Main Economic Indicators, 2016			
	Iran	Saudi Arabia	Tunisia
GDP ($ billions)	419	646	42
Population (millions)	80	32	11.4
GDP per capita ($)	5,219	20,029	3,684
Oil production (millions of barrels a day)	4.6	12.3	0.063
Unemployment (%)	11.4	5.5	14.7
Male youth unemployment (15-24-years old, %)	23.2	24.3	34.6
Female youth unemployment (15-24-year old, %)	41.3	58.5	40*
Ease of doing business index (out of 190 countries)	124	92	88
Sources: World Bank, British Petroleum			
*2012			

The events of the last month in all three countries were due to deteriorating economic conditions. In early January, the Saudi Arabian authorities arrested 11 princes who had gathered at a royal palace in Riyadh to protest the government's unwillingness to continue paying their utility bills. The government reduced subsidies in order to cut waste and ease pressure on the budget. These arrests follow the detention in November 2017, of dozens of Saudi Arabia's richest and most influential people, including princes and government ministers, at the Ritz-Carlton Hotel in Riyadh. The arrests were ordered by an anti-corruption committee, headed by Crown Prince Mohammed bin Salman. The prince's anti-corruption drive tapped into a popular vein among young Saudis who were bearing the brunt of low oil prices and felt that the kingdom's elite were above the law.

Saudi Arabia must now cope with much lower oil revenues than it obtained before 2014. While the development of the non-oil sector is recognized as essential, oil remains the main source of finance for diversification programs.[1] Oil, gas, refining and petrochemicals industries are capital intensive and generate relatively little employment. Saudis, like other the citizens of other oil-rich Arab states in the Gulf, work mainly in the public sector while foreign workers dominate employment in the private sector. Given the fall in oil revenues, the public sector can no longer guarantee employment for the hundreds of thousands of young people coming entering the labor market. As a result, their high unemployment threatens social and even political stability.

The Saudi budget for 2018 budget was announced in mid-December 2017. The government stated that the economy had contracted by 0.5% in 2017. While the budget allowed for higher spending, the rise was a modest 0.6% in real terms over 2017. In its budget statement the Ministry of Finance projected 2018 spending at $261 billion, a nominal 5.6% increase on the preliminary estimate for 2017. Revenue is forecast to rise by 12.5% to $209 billion. As a result, the deficit is forecast at $52 billion in 2018, or 7.3% of GDP. This compares with a deficit $ 61 billion in 2017.

Development spending will rise by a $36 billion, with $22 billion coming from the Public Investment Fund (PIF) and about $13 billion from the National Development Fund (NDF). Total spending will therefore reach $267 billion. The budget statement does not include a presumed oil price or production level for 2018. It does, however, assume oil revenues of $131 billion, compared with an estimated $117 billion in 2017.

Oil is expected to provide 63% of total revenue in both 2017 and 2018. The budget indicates that this share will fall, as the government's plans to boost non-oil revenue are implemented. A sectoral breakdown shows that spending on military and security continues to absorb a very large share of government expenditure: 32% in 2018 and 37% in 2017. In 2018 the allocation to education is 20%, and health and social development, 15%. The two sectors showing the largest increases are those for "economic resources and programs" and "infrastructure and transport." This fits in with the kingdom's plans to boost the private sector.

In Iran unemployment, especially among the young, is a major problem. Oil plays a large role in the economy, but, as in Saudi Arabia, it does not provide many jobs and when revenues are low the ability of the government to generate jobs is limited.

In January 2018, unrest stemming from economic pressures resulted in protests in numerous cities and towns. These were economic protests, reflecting deep-seated frustration with economic stagnation, mismanagement and corruption, and growing income inequality along with conspicuous concentration of wealth at the top.

The announcement of the 2018-19 budget was one of the factors behind the protests. It was little unchanged from the 2017-18 one, with modest revenue and spending increases. With inflation estimated at 10%, the budget is sharply reduced in real terms.

The general budget allocates $79 billion for ordinary spending, down 6.8% in real terms from the previous year, and $17.3bn on development expenditure, down 27.5%. Development spending was $6.7 billion last year, and the Central Bank of Iran suggests that this will fall to $4.7 billion. Spending on salaries will rise by 11%, representing a modest real increase. The budget allocates $11.4 billion for military expenditure, of which $7 billion goes to the Islamic Revolutionary Guard Corps, $2.7 billion to the army, $1.2 billion to the Ministry of Defense, and $31.2 million to the Basij Resistance Force.

The draft budget was President Rouhani's latest effort to reduce the numbers receiving cash subsidies. It aimed to cut the allocation for cash subsidies from $12.7 billion in 2017-18 to $6.6 billion in 2018-19 by reducing the number of recipients of the $13/month handouts from about 70 million to about 41 million. The budget bill also proposed a 20% increase in the price of gas oil to generate $3.7billion in additional government revenue, as well as an increase in the "departure tax" for nationals from $21 to $64.

The protests reflected the widening gap between large urban centers, especially in the greater-Tehran area, that corresponds roughly to President Rouhani's political base, and the smaller towns and rural regions that tended to support his conservative and hardliner rivals. Protests were concentrated in small towns among the poorer sections of society who had traditionally been the strongest supporters of the hardliners. If the 2009 protests could be labelled as "middle class" then the January 2018 protests were "working class", and hence Iran faces an accumulating crisis. Mismanagement, corruption and the allocation of huge resources for conflicts in the Arab world have denuded the country of resources to such an extent that the regime's own supporters came out in protest.

The protests are not a surprise to those who follow economic developments in Iran. At the beginning of 2017, the IMF stated that the ending of nuclear sanctions under the Joint Comprehensive Plan of Action (JCPOA) has spurred economic growth, but banking system weaknesses, structural bottlenecks, and hesitation by foreign banks to re-establish financial links have held back the expansion of non-oil activity. World Bank business climate indicators show Iran performing poorly in terms of access to credit, protecting minority investors, governance, trading across borders, and resolving insolvency. Global Competitiveness indicators show shortfalls in financial market development, labor market efficiency, and technological readiness. These constraints, combined with the large role of the state, result in a low employment elasticity of nonoil growth (just 0.2). The labor market is unable to absorb new entrants—which average half a million annually over the next five years—with youth and women facing the greatest challenges. The unemployment rate exceeds 12 percent, with female and youth unemployment at 21 and almost 30 percent, respectively. Nearly one-fifth of university graduates are unemployed, and one-third of the youth are neither economically active nor in education. Structural reforms can spur private sector growth and mitigate the effects of fiscal austerity.2 Another factor that has contributed to discontent in rural areas is Iran's disastrous water crisis. Those living in Iran's provincial towns and villages have long been regarded as the backbone of the country's Islamic regime. They tended to be conservative and religious. In the last decade, that has changed. A 14-year drought has emptied villages, with residents moving to nearby cities where they often struggle to find jobs. Access to satellite television and, more important, the mobile internet has widened their world and increased their awareness of inequality and inequity.[3]

One Iranian (émigré) economist has noted that the crisis the result of sanctions and economic mismanagement. The cost of living is very high, "unemployment remains rampant, and economic inequality is not only widening, but also being flaunted by the rich." Rouhani's economic policies, that can be called neo-liberal, have had a negative effect on the working class. Austerity policies reduced inflation but also resulted in job losses. Cutting subsidies resulted in higher energy prices, and the value of cash transfers declined. Other policies favoured businesses and the middle class who mainly live in Teheran but hit the poor, especially in rural areas who were badly affected by drought.[4] (This is very similar to what happened in Syria in the early part of the civil war, when drought caused havoc in rural areas and government policy aggravated the situation.)[5]

Tunisia is still suffering from the legacy of Zine El Abidine Ben Ali's 24 years of misrule. This is manifest in state institutions that are weak and deep public suspicion regarding the continued corruption of state institutions. The campaign of Islamist terror groups against the tourism sector severely damaged the economy and resulted in a further slowdown in growth. The democratically elected government (the only one in the Arab World) is struggling to implement reforms demanded by the IMF in return for $2.9 billion in economic aid. Measures announced in the 2018 budget to raise fuel prices and taxes on many products and services came against a background of food price inflation. With widespread poverty and extremely high rates of unemployment, especially among the young, unrest resulted. In December 2017, the IMF stated that Tunisia's main economic challenge was to make-up for the significant delays in lifting long-standing obstacles to growth and reduce large fiscal and external deficits.[6]

The World Bank noted that the labor force participation rate in Tunisia remains low at about 50 percent, mainly due to very weak participation rate of women of only 26 percent. Unemployment has declined from its peak of 19 percent in 2011 to 15.5 percent in 2016. The majority of the unemployed are low-skilled workers. University graduates have the highest unemployment rate, which increased from 15 percent in 2005 to 23 percent in 2010 and to 31.6 percent in 2016, while female graduate unemployment reached 40.4 percent. Unemployment rates are also much higher in the hinterland than in coastal regions.[7]

Accumulated problems of economic mismanagement, corruption, a lack of transparency led these three very different countries (and many others in the region) to a similar state of crisis. Neither Saudi Arabia nor Iran have the means to achieve all their objectives, including the struggle between them. Saudi Arabia has responded with reforms, but it is not clear if they will lead to the development of the private, non-oil sector or to even more centralized rule. Iran is amid a struggle between those who want reform and those with strong interests in the status quo. It seems that the leadership, Rouhani, and even more importantly, Ayatollah Khamenei realize that change is necessary. In Tunisia the situation is more worrying, because there the Arab World's only democracy is struggling with harsh economic realities that may threaten its political stability.

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[1] For a previous discussion on this topic see Paul Rivlin, "The Saudi Sheikh Up" *Iqtisadi*, Vol. 7, No. 9 November 26, 2017.

[2] *IMF Press Release* (Staff report with statement by the Executive Director for the Islamic Republic of Iran), "Islamic Republic of Iran 2016, Article IV Consultation," IMF Country Report No. 17/62, February 2017.

[3] Thomas Erdbrink, "Hardliners and Reformers Tapped Iranians' Ire—Now Both are Protest Targets," *New York Times*, January 2, 2018; Shoshank Bengali and Ramin Mostaghim, "A long-simmering factor in Iran protests: climate change," *Los Angeles Times*, January, 17, 2018.

[4] Djavad Salehi-Isfahani, "Poverty and living standards in Iran after the nuclear deal," *Djavad Saleh.*com (Blog), January 3, 2018.

[5] Paul Rivlin, "Behind the Tensions in Syria: The Socio-Economic Dimension," *Tel Aviv Notes*, (Vol. 5, Special Edition No. 6) March 29, 2011.

[6] *IMF Press Release*, "IMF Concludes the 2017 Article IV Consultation and Announces Staff-Level Agreement for Completion of Second Review of Tunisia's Extended Fund Facility," (No. 17/490), December 13, 2017.

[7] *World Bank Public Documents*, "Tunisia MEM 2017 English," *n.d*