Iqtisadi
Middle East Economy

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The Arab Spring and the Economic Winter

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Economics played a significant part in the outbreak of the Arab Spring: the main factors were high rates of unemployment, especially among the young; rising food prices; corruption and poverty. High oil prices –which benefited Middle East oil producers – also added to pressures. Little, if anything, that has been done since the Arab Spring started to ameliorate these problems. Furthermore, food prices are rising again on international markets. The collapse of economic growth has led to deteriorating conditions on labor markets and higher unemployment. This edition of *Iqtisadi* reviews economic conditions in some of the non-oil Arab states.

Egypt and Tunisia’s economies remain in the doldrums following regime change. For Jordan and the Palestinian Authority, growth has stalled; in Yemen and Syria, conflict is destroying the economy. All these countries are now threatened by rising food prices, as is Morocco where growth has been somewhat stronger. Lebanon's economy is affected by strife in Syria and growth is weak there too. All of these countries face budgetary and, to a lesser extent, balance of payments pressures, because of the high costs of imported food and fuel.

The international economy is in recession; the European Union is one of the worst affected regions. Europe is a key market for Arab countries as well as the most important source of their tourism revenues. As a result of the recession, the demand for Arab countries' exports has declined and tourism revenues in Egypt, Jordan, Tunisia and Morocco have been badly hit.

Egypt's economy is stagnating. It is badly in need of reforms but the new Islamic government of President Morsi has been cautious in the extreme. The 15 percent pay rise for the public sector announced by the new government was reminiscent of the policies of the Mubarak regime and does nothing except compensate for accelerating inflation. Egypt has received funds from the Gulf and financial help from the US, which have helped to stabilize the foreign exchange reserves, but an agreement with the International Monetary Fund (IMF) has not been signed. This means not only that Egypt has not received aid from the IMF but that it so far refused to commit to policies favored by the Fund.

When he came into office in June, President Morsi announced a 100-day program that aimed to improve internal security, the flow of traffic in Cairo, the collection and disposal of rubbish, and the supply of bread and fuel. Apart from some improvements in security (with the notable exception of Sinai), he has failed.

Prior to the public sector wage rise, the July 2012–June 2013 budget had a planned deficit equal to 7.6 percent of GDP. The final outcome is likely to be significantly higher given rising costs, especially subsidies for fuel and food.

Jordan's economy, which suffered from the chaos in Iraq, is now threatened by the civil war in Syria. This has worsened the budget crisis and forced the country to rely increasingly on financial support from the US and the Gulf. The government was forced to spend at least $500 million to cover a fuel shortage that resulted from the sabotage of the pipeline through the Sinai carrying subsidized gas from Egypt to Jordan. It has provided large subsidies on foodstuffs and fuel; as international prices rose, so their costs increased. The energy subsidy increased from just over one percent of GDP in 2010 to 6.25 percent in 2011. As a result, the budget deficit has risen as has borrowing, causing higher interest payments. This, in turn, put more pressure on the budget. In addition, public sector wages and pensions have been increased.

In response, the Gulf Cooperation Council (GCC) and the US have provided Jordan with increased aid. The GCC has allocated $1.25 billion and the US has provided $700 million while the IMF has agreed to loan Jordan $2 billion.

While higher oil prices mean larger revenues for Arab oil producers in the Gulf, this has enabled them to provide financial assistance to Jordan, which they consider a strategic ally. Higher oil prices have also made possible more foreign investment and larger remittances from Jordanians working in the Gulf.

While foreign aid has temporarily plugged budgetary and balance of payments holes, the structural problems facing the economy remain formidable. In 2010, the official unemployment rate was 12.5 percent and that for young people aged 15-24 years was 28 percent. As many do not enter the labor force, the participation rate is only 40 percent. According to the IMF, Jordan needs to create 800,000 jobs between 2010 and 2020 to absorb the currently unemployed and to employ new entrants to the labor market. This would require economic growth of 9.3 percent a year compared with an average of 6.1 percent in 2000-2010. Even that achievement would leave the employment-to-working-age population ratio in 2020 at the very low rate of 43 percent.

Morocco is also suffering from a larger budget deficit resulting from rising subsidies and increases in public sector wages and pensions. Economic growth has slowed and the growth rate is likely to be about 2.5 percent in 2012 compared with five percent in 2011. This is due to the poor harvest and the slowdown in exports resulting from the recession in Europe. Agriculture accounts for 40 percent of employment; low rainfalls resulting in a poor harvest have a major impact on the economy. The recession in Europe threatens the volume of remittances sent home by emigrant workers. These are likely to reach $8 billion in 2012 and are the largest source of foreign revenue in Morocco. In recent years they have played a key role in reducing poverty both by providing funds for millions of families and by reducing pressure on the labor market.

Unemployment, especially among the young, is high and without a sustained acceleration of growth, it will not fall significantly.

The Tunisian president, Moncef Marzouki, warned in July that if economic reforms are not implemented, there could be a "revolution within the revolution." The most pressing issues are unemployment, particularly that of jobless university graduates, who have been taking to the streets since the revolution. Tunisia also faces sharp regional disparities that affect the rural interior and some urban areas. In addition, the government has yet to clean up the corrupt practices of the previous regime's patrons. This is despite the publication of plans for wide-ranging reforms including a five year plan for the period 2012-2016.

In 2011, Tunisia's GDP fell by 1.8 percent, despite a good harvest and agricultural growth of nine percent. Private sector activity, especially investment, fell as a result of the demonstrations and regime change. Public sector spending held up, partly to prevent the recession from deepening. Thousands of Tunisian workers left Libya when conflict broke out, but when they returned home, few of them could find work. As a result, unemployment rose to 19 percent and that among young people reached 42 percent.

The GDP growth rate in 2012 is forecast to improve modestly to 2.7 percent. The budget deficit is likely to reach nine percent of GDP in 2012 compared with 3.5 percent in 2011 as a result of large spending on food and fuel subsidies as well as increases in public sector wages and pensions. The latter were increased to cover rises in the inflation rate due to higher food and fuel costs.

The external position has also deteriorated: the current account deficit widened to 7.3 percent of GDP in 2011 from 4.8 percent of GDP in 2010. In 2011, tourism receipts fell by 33 percent and foreign direct investment inflows declined by 26 percent. The international reserves of the central bank fell from $9.5 billion at the end of 2010 to $7.5 billion at the end of 2011. By the spring of 2012, they had fallen further to $6.9 billion (equivalent to 3.5 months of imports).

Syria's economy is being wrecked by war. Hundreds of thousands of Syrians have fled to Turkey, Jordan and Lebanon. Up to three million people face the threat of famine due to losses in the agricultural sector (estimated at $2 billion). Since the conflict began, tourism has stopped and the country has lost revenues that in 2010 brought in $8.3 billion.

Oil has also been a major source of export earnings but international sanctions have resulted in losses of up to $4 billion a year. Sanctions have also have led to a reduction in foreign trade and investment and to the stopping of large scale investment projects, although these were unlikely in the state of war prevailing in the country.

Damage has been inflicted on industrial facilities, oil and gas pipelines, electric power facilities and railway tracks along which fuel tanks were transported. One of Syria's largest refineries at Homs has been paralyzed as have many other installations. In July, the authorities assessed the damage caused by the war at $11 billion –about $650 million a month. The foreign exchange reserves have fallen by 50 percent, from $18 billion before the conflict to $9 billion or less. Total financial collapse has been prevented by Iran, which has provided billions of dollars of support.

In contrast to Libya, which has managed to restore its pre-conflict oil production level, Syria is not a major oil producer. Prior to the war, the country produced only 0.4 million barrels of oil a day and received about $4 billion a year from exports.

Foreign tourism, a key area in the country's revenues, has suffered losses. It will be hard to return to the former glory of being a tourist country and to restore the greatly damaged agricultural sector. Estimates of the conflict's effect on the economy in 2012 range from falls in GDP of between 10 to 18 percent. Even the higher figure may be an underestimate.

In the aftermath of the Arab Spring, the non-oil Arab states are suffering. Economic growth has sharply decelerated, budget deficits have increased, the balance of payments has weakened and foreign exchange reserves have fallen. The population and labor force continue to grow as does the need for reform, but the Arab regimes' room for maneuver has narrowed.

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