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**THE CHANGING PATTERNS OF WEALTH
ACCUMULATION AND DISTRIBUTION UNDER
ECONOMIC REFORM IN THE ARAB WORLD**

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THE CHANGING PATTERNS OF WEALTH ACCUMULATION AND DISTRIBUTION UNDER ECONOMIC REFORM IN THE ARAB WORLD

by Maria Cristina Paciello*

1. Background

In the 1960s and 1970s, with rare exceptions, Arab countries pursued import substituting industrialization (ISI) strategies to varying degrees, with different ideological underpinnings, and involving central planning and a large public sector. Egypt, Algeria and Tunisia pursued ISI more resolutely.¹ During the period, the Arab region experienced relatively high growth rates and poverty was reduced. However, by the middle of the 1970s, the problems of ISI, compounded by the problems of the state sector, were becoming increasingly apparent.² The infant industries had difficulties growing up and becoming internationally competitive because of their high costs. They were, in general, highly capital-intensive, and even in the best of circumstances, did not provide large numbers of jobs.³ However, the quadrupling of the international price of oil in 1973 led to a major economic boom in the Arab region, thus postponing the need for structural reforms. Both oil and non-oil countries shared in the massive transfer of rents that characterized the period. For the latter, the benefits of the oil boom were partly redistributed to the population through various channels: migration, remittances, high wages and generous welfare policies.

Following the end of the oil boom, economic growth slowed down in all countries of the Arab region. The end of the Cold War, rising economic difficulties associated with serious foreign debt problems and falling oil prices, forced all Arab countries – without exception – to implement some form of economic liberalisation. Countries like Morocco, Tunisia, Egypt and Algeria agreed to externally imposed macroeconomic stabilization programs with formal assistance from the International Monetary Fund (IMF) and the World Bank (WB) in return for international financial flows. In other countries, like Lebanon, Syria and oil producer monarchies, market-oriented reforms were carried out without a formal arrangement with the IMF, but still inspired by the recipes advocated by the Bretton Woods Institutions. Since the end of the Cold War, the restructuring of the global economy – both in terms of production and finance – has thus resulted in growing vulnerability on the part of the Arab states to external pressures for liberalisation and privatisation. International actors such as the IMF and WB have become strongly involved in prescribing country policy in the region, by channelling important resources to Arab countries in the form of multilateral and bilateral grants, debt rescheduling and write offs. Other actors like the World Trade Organisation (WTO) and the European Union (EU) have also pushed Arab countries to open up their

¹ Richards, Alan, and John Waterbury (1998). *A Political Economy of the Middle East*. Westview Press, Boulder, Colorado.

² Owen, Roger, and Sevket Pamuk (1998). *A History of Middle East Economies in the Twentieth Century*. I.B. Tauris, London.

³ Richards, Alan, and John Waterbury (1998). *A Political Economy of the Middle East*. Westview Press, Boulder, Colorado.

economies. The EU, in particular, has been an important source of multilateral credit, and especially since 1995 has been enticing southern Mediterranean regimes to reduce tariffs with the promise of substantially higher EU credits to offset lost customs revenues.

2. Research focus

There is agreement that the scope and the progress of economic liberalisation reforms in the Arab region have been more limited than in other parts of the world. The implementation of structural reform measures has been gradual and slow, and the public sector still dominates most Arab economies. Despite undertaking reforms to remove protection and increase reliance on market forces, Arab economies, with the exception of Gulf countries, have remained relatively protected. Privatisation of public enterprises has generally been selective, and the financial sector remains under close and centralised governmental control. Much of the literature on economic reforms in the Arab region has thus tended to explain why it lags behind other regions in terms of economic reforms. Moreover, although there is evidence that in the last decade living standards and labour market outcomes in most

Arab countries have been negatively affected, analysis of the effects of economic reforms in the Arab region has generally focused on issues of economic efficiency, while neglecting issues of distribution, marginalisation and wealth accumulation. So, little attention has been paid to the fact that economic reforms, albeit marked by caution and gradualism, are contributing to a reorganisation of the state's role and its economic functions, with important implications on the processes of wealth accumulation and distribution. This project intends to explore some of the key dynamics and consequences of the reorganisation of the state's economic functions in the Arab region, by looking at three areas of major change: i) the modalities of wealth accumulation and distribution; ii) the role of the state in the provision of social welfare services; iii) state-labour relations.

2.1 Modalities of wealth accumulation and distribution under economic reforms

One of the main features of the production pattern prevailing in Arab countries is high dependence on the extraction of raw materials, especially oil and natural gas, and reliance upon different types of external rents (location rents, strategic rents, migration rents and political rents coming from the acquisition of foreign aid). Nine Arab countries (Bahrain, Kuwait, Oman, United Arab Emirates, Libya, Qatar, Saudi Arabia, Iraq and Algeria) can be categorised as oil dependent economies. Egypt, Syria and Tunisia had substantial revenues at their disposal during the oil boom, although the oil sector is now less important. Algeria, Morocco, Tunisia, Jordan, and Syria also account for about one third of the world's phosphate production, while remittances play an important role in the economies of Algeria, Morocco, Tunisia, Egypt, Jordan and Lebanon. In a rentier mode of production, the economic surplus originates neither from investment nor labour, but is generated as the result of natural and other advantages. Rents do not have to be reinvested in the society's production process and are allocated on purely political terms, namely clientelism, patronage and proximity to the state. As is commonly argued, the rentier mode of production has deeply influenced the dynamics

of political and economic development in the Arab region, albeit to different degrees in different countries. From a political point of view, it has contributed to reinforcing authoritarianism and to discouraging political participation.⁴ The considerable amount of state revenues accruing to rentier states in the form of oil and external rents has served to reduce the state's need to levy taxes from its citizens, thereby weakening the link between the ruler and the ruled. From an economic point of view, Arab governments have tended to overlook the need for diversifying their economies and implementing long terms structural reforms as they take those revenues for granted. In addition, dependency on rents has encouraged rent seeking and other unproductive activities. Resources are allocated because of personal contacts to political decision makers rather than because of labour, personal capability or merit.

In the 1983-2000 period, oil and other related rents generally declined, although Arab countries continue to be dependent on rents to finance a substantial part of the government budget. In the face of resource shortages, inflows tied to economic reform programs have actually provided a way out of the fiscal crisis and new opportunities for Arab ruling elites' to accumulate wealth, thus reinforcing their ability to maintain control over strategic rents and their allocation. For example, although EU funds to North Africa are designed to bolster private enterprise and support privatisation, only a relatively small percentage of them are destined for private companies, and it is North African governments that determine the actual beneficiaries.⁵ Moreover, economic reforms

have been used mainly by ruling elites as a strategic tool for maintaining and reorganising the system of privileges that has served them. Although the pace and methods of privatisation policies have differed in Arab countries, such reforms have largely implied a shift in patronage networks from the public to the private sector, allowing for the persistence of existing regimes and the formation of crony capitalists rather than competitive markets. In Morocco, for example, "personalisation" of the public sector

masquerading as privatisation has directly benefited the royal family and entrepreneurs affiliated with it.⁶ In addition, in order to gain the necessary backing for selective economic reforms while maintaining control over economic liberalisation, ruling elites have co-opted new economic actors, with the result that new monopolies and oligopolies have emerged, and crony capitalism has accelerated. As Dillman (2001) notes, through economic reforms "the more they [regimes] 'deregulate', the more they 're-regulate' by determining precisely who can most easily benefit from change and join distributional coalitions to tap profits in the market".⁷ In Egypt, Mubarak has diversified the crony capitalism system that he inherited from Sadat to generate the patronage and provide the controls over economic liberalisation required for the regime to retain its support within the state, while appearing to adopt the Washington Consensus. In Morocco, the monarchy has built and strengthened a pro-reform coalition composed of two critical groups of winners in the economic reform process: large Moroccan private

⁴ UNDP (2004). Arab Human Development Report 2004. UNDP, New York.

⁵ Dillman, Bradford (2001), "Facing the Market in North Africa". *The Middle East Journal* 55 (2): 198-215.

⁶ *Ibid.*

⁷ *Ibid.*

sector capitalists and rural notables.⁸

Fiscal policy is also an important instrument through which ruling elites can maintain/re-regulate the political arrangement through the logic of extraction and redistribution. In a context of increasing shortage of rents and external pressures to accelerate trade integration, Arab governments have introduced some changes to their tax system. However, the quickest and politically least disturbing way of reforming the tax system has been through an increase in indirect taxes on consumption, such as value added tax. The increased weight of indirect taxes on massive consumption goods is likely to reduce the real disposable income of the poorest sectors of the population and to have a negative impact on income distribution. At the same time, income and corporate taxes have remained negligible or have been reduced, while tax evasion, especially among influential groups, is on the increase. Lebanon is a case in point: the top marginal tax rate on profits was reduced from 50 percent to 10 percent and the corporation tax rate became a flat 10 percent, while indirect taxes increased continuously in the 1990s.⁹ While this regressive tax system was seen as a major cause of the hardships faced by the majority of the population, it provided the ruling elites with the revenues for financing rent-seeking activities. In Egypt, fiscal reform, which was primarily influenced by external pressures, also favoured the continuity of pre-reform privileges by serving the interests of well connected major enterprises and owners of capital.¹⁰

Finally, despite the conditionality associated with multilateral credits and debt rescheduling, economic reforms have not been able to alter the production structure of Arab countries, which has remained almost as undiversified as it was in the 1970s. Money has continued to be spent on construction and services, the local and private capacity of production remains limited, and the share of manufacturing in export has declined or stagnated. This may suggest that economic reforms have not reduced incentives for rent seeking and other unproductive activities. In this context, how the rise in oil prices in the recent years is likely to affect the economic and political dynamics of changes in the Arab region needs to be investigated.

2.2 *The role of the state in the provision of social welfare services*

From the 1950s through the 1970s, governments in the Arab region, albeit to different extents, progressively redistributed income from the upper to the lower strata through land reforms, universal food subsidies and free access to education. The ruling elites used the welfare state as an instrument of power to create national unity and a social base of support among the formal working class and middle class. With structural adjustment programs, Arab governments, with the exception of Algeria, did not cut social spending as drastically as other countries, at least over the period for which data are available. However, there is evidence that the social policies

⁸ Richards, Alan, and John Waterbury (1998), *A Political Economy of the Middle East*. Westview Press, Boulder, Colorado.

⁹ Dibeh, Ghassan (2005), *The Political Economy of Postwar Reconstruction in Lebanon*, July, Research Paper 2005/44, WIDER.

¹⁰ See Kienle, Eberhard (2005), 'Reconciling Privilege and Reform: Fiscal Policy in Egypt, 1991-2000', in Heydeman S., *Networks of Privilege in the Middle East, The Politics of Economic Reform Revisited*. Palgrave.

of the past have been challenged by declining rents and by the neo-liberal agenda.¹¹ Countries are increasingly unable to finance or sustain their previous levels of health, educational and welfare services. For example, in Egypt, while in the 1990s, there was an evident increase in education expenditure, the health budget remained under-funded at a low 1.3 per cent of GDP. In Lebanon, public expenditures increased on both health and education until 1998, but after that, the growth of debt, debt servicing and the state's fiscal crisis caused a diversion of resources away from reconstruction and social expenditures.¹² Moreover, social spending has not been sufficient to prevent deterioration in the quality of health and educational services because too much of it is going to pay the salaries of the large number of public employees. In addition, there is evidence that, although health care and education are still free, private expenditure on those services is on the increase, in particular for the poor. Private tuition, for example, has become even more indispensable to obtain good grades in public examinations for access to higher education, especially in disciplines considered most likely to lead to better professional and career prospects. These disciplines are thus becoming almost exclusively the preserve of the privileged.¹³

In this context, the state is reorganising by increasingly delegating its social welfare functions to private and informal actors. This can be seen by the proliferation of non-governmental organizations (NGOs) in the Arab countries since the 1990s, many of which are Islamic and deliver social services that the state is no longer able to provide, but also by the return of semi-private charity institutions and the increasing importance of informal networks among the poor as a mechanism for the allocation of resources. It is commonly argued that the appearance of these private actors enhances citizen participation, helps build civil society and fosters democratisation. Yet, country studies have shown that the appearance of these extra-state actors, apparently in opposition or competition with the state itself, does not necessarily challenge state control on wealth accumulation and distribution. While many of the Islamic NGOs have helped to recruit their beneficiaries to Islamist politics, NGOs have been generally co-opted with the aim of either widening the regime's power base or directly controlling society. The Tunisian case may be an example of implementation of social policies to create or maintain national and state security. NGOs and district committees were formed to oversee and provide social services mainly for the purposes of controlling and containing the 'dangerous areas' prone to Islamist recruitment and activity.¹⁴ As for the informal networks, while increasingly competing with state-controlled top-down schemes and with markets, they do not put state authority into question. As Singerman (1995) shows for Egypt, informal networks represent a form of participation that is "tacitly tolerated by the state, unless they become vehicles for opposition and resistance or merely work against the interests of state policy".¹⁵

The appearance of various private/semi-public institutions established by key political figures to organise aid provided by private sources to the needy can be seen as an example of the ongoing process of state restructuring that implies increasing reliance on

¹¹ See, for example, Karshenas, Massoud (2006), *Social Policy in the Middle East: Economic, Political and Gender Dynamics*, Palgrave.

¹² Dibeh, Ghassan (2005), *The Political Economy of Postwar Reconstruction in Lebanon*, July, Research Paper 2005/44, WIDER.

¹³ UNDP (2002). *Arab Human Development Report 2002*. UNDP, New York.

¹⁴ Karshenas, Massoud (2006), *Social Policy in the Middle East: Economic, Political and Gender Dynamics*, Palgrave.

¹⁵ Singerman, Diane (1995), *Avenues of Participation*, Princeton: Princeton University Press.

indirect/private modes of government, but not necessarily a decline in the capacity of the state, understood as a system of power. In Morocco, the Mohammed V and Hassan II Funds, created respectively in 1998 and 1999, are indeed agencies autonomous from the government, but under the patronage of the King. The ambiguous nature – neither private nor public – of such agencies allows the King to ingratiate himself with the public opinion, while at the same time de-responsibilising the state with respect to citizens' social rights. In Tunisia, the presidential programme called 26-26 National Solidarity Fund designed to benefit low

income groups receives money from obligatory “gifts” by citizens and businesses as well as the government budget. Moreover, it does not contribute to the national budget and it is the President who decides how to invest the funds. The programme is thus a tool in the hands of the president for reinforcing his legitimacy in the eyes of the beneficiaries and for maintaining control over businessmen and other influential people.¹⁶ Indeed, the latter risk being excluded from access to economic opportunities if they refuse to contribute to the fund.

Finally, the declining role of the state in the provision of social welfare services has probably caused the growing marginalisation of the initial constituents of the populist state from the processes of wealth distribution. Moreover, while the current social protection system is hardly sufficient to reach all deserving people, the number of weaker social groups is increasing because of significantly increased unemployment, lack of job creation and deterioration of real wage rates. These factors are likely to create their own local dynamics, increasing internal opposition to incumbent regimes and social conflict, as well as reinforcing clientelist social relations and informal networks of solidarity (family, religious etc).

2.3 Changing state labour relations

Most of the studies on Arab labour markets in the 1990s agree that there has been a rise in unemployment, a deterioration of real wage rates and growth in the number of people working in informal labour market. In the light of the above, it becomes important to understand how state labour relations have been changing in the last decade under the pressure of economic reforms and globalisation. Before the end of the oil boom, governments in the Arab countries pursued generous employment policies in the public sector, albeit to different degrees, that helped to provide job opportunities to a growing part of the population in the region. This also meant that a large part of the labour force became eligible for formal modes of social protection. During the first phases of structural adjustment policies largely in response to policies to reduce the size of budget deficits, Arab countries, again to different degrees, gradually started reducing the size of their public sectors. In the mid-1990s, in some countries, the state was still playing a major role as employer, but, efforts at reducing public sector employment, especially in state-owned enterprises, intensified after then. By the end of the 1990s, the role of public sector employment as a tool for promoting more equal distribution and ensuring social mobility had become questionable.

Structural adjustment policies were unable to create sufficient jobs to keep pace with the steady increase in the work force. The obligation to liberalise trade and reduce customs duties as a result of joining the WTO and the EU-Mediterranean partnership

¹⁶ Hibou, Beatrice (1999), “Tunisie: le coût d’un ‘miracle’” *Critique Internationale*, n° 4 été.

agreements also exposed local industries to unequal competition, resulting in increased rates of closure of many industrial units or in further informalisation of the labour market. Moreover, under competitive pressures associated with globalisation, Arab governments started implementing measures to favour capital at the expense of labour. This tendency appears clearly in the Arab countries' attempts at creating free trade zones that provide tax exemptions and other incentives to foreign companies. For example, Jordan started attracting FDI after 1996 with its Investment Promotion Law, including the non-Jordanian Investment Regulation of 1997 as well as the 'Qualifying Industrial Zones' project, launched in 1998 and by granting preferential access to the US market. Most Arab countries also began to revise their labour laws to introduce more labour market flexibility in the second half of the 1990s: in 1996, Algeria amended the labour law it passed in 1990; Tunisia and Jordan approved a new labour code in 1996, while Egypt and Morocco did so in 2003.¹⁷ Yet, in order to minimize social conflict at a time when unemployment and social tensions are on the increase, the states are also re-configuring labour relations, with the result that trade unions are losing ground everywhere in the Arab region. In Morocco, while the state is retreating from the sphere of labour relations, it is actually reinforcing its control over trade unions, by depoliticizing and privatising social conflicts. A new approach based on social dialogue with the unions translated into the signature in 1996 of an agreement between the government, the unions and the General Confederation of Moroccan Enterprises (GCME). In this context, the new labour code calls for the involvement of a new actor - the employer- in the process of social negotiation, which becomes a private affair between him and the worker.¹⁸ Finally, under pressure from the World Bank, some Arab countries have recently started to reform their pension and social insurance systems shifting the responsibility to insure against the increased risks and uncertainties of globalisation from government to individual.

3. Research areas/methodology

Based on the foregoing, **the dynamics and consequences of the reorganisation of the Arab state in the economic sector can be best investigated through the analysis of three areas of research: i) *the modalities of wealth accumulation and redistribution; ii) the role of the state in the provision of social welfare services; iii) state-labour relations.***

The main general questions that the research project plans to investigate are:

- How are ruling coalitions reorganising in the context of economic reforms?
- How is the social basis of Arab regimes changing in that context?
- Who gains and who loses from the process of the state's economic reorganisation?
- How are global structural trends and international/regional actors affecting the process of the state's economic reorganisation in the Arab World?

¹⁷ ILO, Natlex database, http://www.ilo.org/dyn/natlex/natlex_browse.home

¹⁸ Catusse Myriam 1998, "De La Lutte des classes au Dialogue social. Réflexions sur les recompositions des relations professionnelles au Maroc", *Monde arabe-Maghreb-Machrek* 162, La Documentation française: 18-38.

Periodisation

In terms of time focus, while not neglecting an historical perspective, it would be important to look at what has been happening since the mid-late 1990s. This is because structural reforms have accelerated since then and few studies cover that period. For example, from 2000-03, privatisation activity in the Arab region increased greatly in terms of the value of assets sold, led by the sale of telecommunications systems in Jordan, Morocco and Saudi Arabia and several other large sales (the tobacco monopoly in Morocco; cement companies in a large number of countries) that generated significant sums. Also with regard to trade liberalisation, many Arab countries started committing to further liberalising their trade regime in the second half of the 1990s. Morocco joined the EU Mediterranean Partnership in 1996 and signed the U.S.-Morocco Free Trade Agreement in 2004, while Egypt and Lebanon signed Euro-Mediterranean Association Agreements respectively in 2001 and 2002.

An actor's based framework

The three research areas can be studied by looking at the interaction between the different actors involved in the process of economic reorganisation of the Arab state, namely between ruling elites and international/regional actors (the IMF, the WB, the EU, etc) as well as between various internal actors (e.g. ruling elites, entrepreneurs, NGOs, exporters, new interest groups benefiting from accelerated structural reforms, workers, trade unions, public employees, importers, etc.).

i) Modalities of wealth accumulation and redistribution under economic reforms

This research area aims at investigating how economic reforms (e.g. fiscal policy, privatisation etc) and global trends (e.g. the rise in oil prices, etc) have affected the process of wealth accumulation and redistribution, and in particular, whether or not they have reinforced Arab ruling elites' control over resources as well as the politics/logics of rent seeking.

The main questions to be asked are:

- How have economic reforms and global trends impacted on the way economic surplus is produced, distributed and invested?
- How have economic reforms affected ruling elites' control over wealth accumulation and redistribution as well as the politics of rent-seeking?

ii) The role of the state in the provision of social welfare services

This research area aims at understanding how, under economic reforms, the role of the state is restructuring in the provision of social welfare and what the implications are of such changes on wealth distribution and political dynamics in Arab countries.

The main questions to be addressed:

- How is the role of the state changing in social welfare provision?
- What are the distributive implications of such changes?
- How are social cohesion and ruling elites' legitimacy affected?

iii) State-labour relations

This area of research seeks to highlight how state labour relations have been changing under the pressure of economic reforms and globalisation.

The main questions to be addressed are:

- How are state labour relations restructuring under the pressure of economic reforms and globalisation?
- How are changes in state labour relations likely to impact on economic distribution and social cohesion?

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