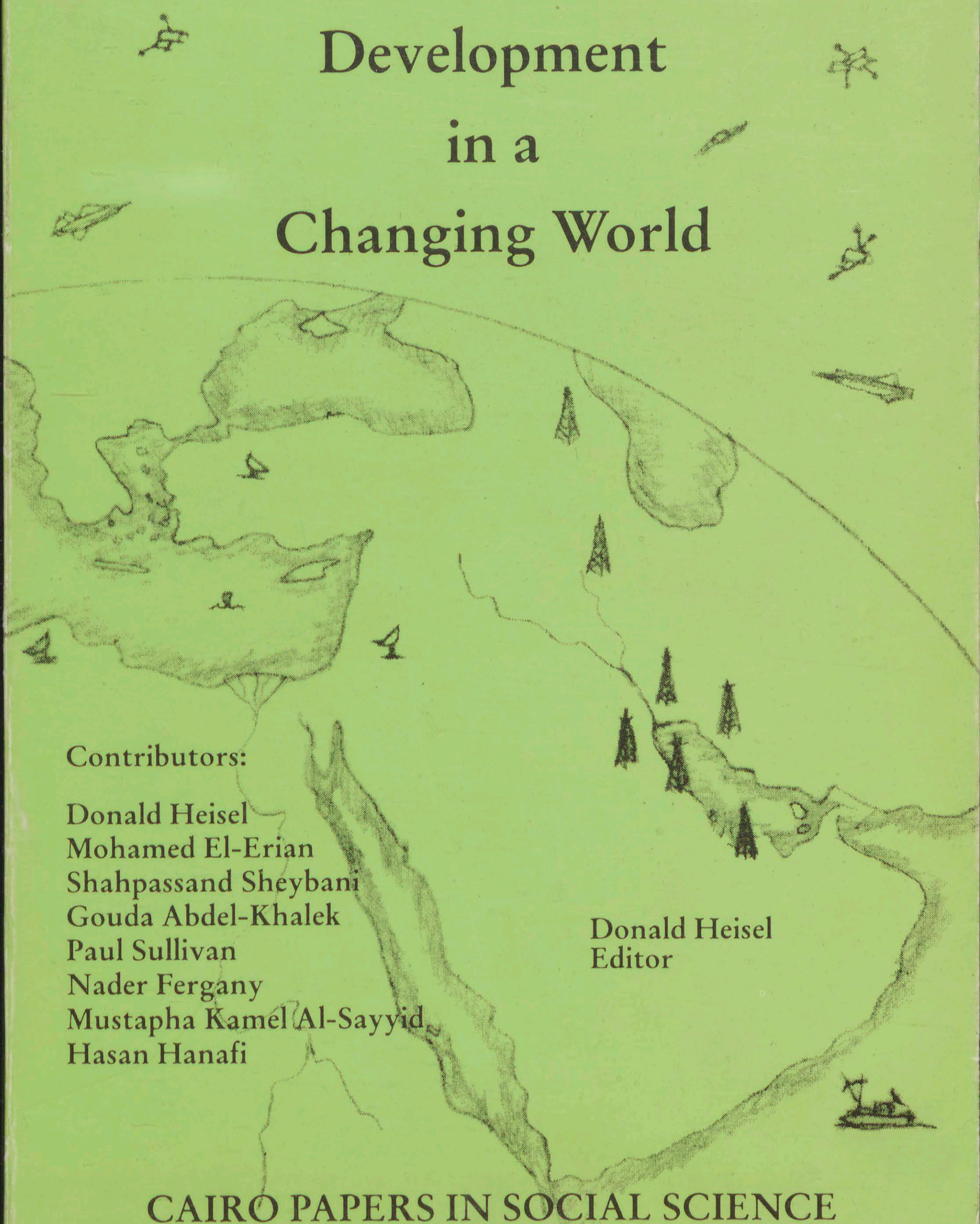
1998

Introduction (The MIddle East and Development in a Changing World)

Donald Heisel

The Middle East and Development in a Changing World



Contributors:

Donald Heisel
Mohamed El-Erian
Shahpassand Sheybani
Gouda Abdel-Khalek
Paul Sullivan
Nader Fergany
Mustapha Kamel Al-Sayyid
Hasan Hanafi

Donald Heisel
Editor

CAIRO PAPERS IN SOCIAL SCIENCE
Volume 20, Number 2

INTRODUCTION

DONALD HEISEL

Globalization of the economy has become a topic of widespread discussion, in business, academic and political circles. Indeed, it has become something of a cliché, a justification for all kinds of good and bad policies and an explanation for all kinds of good and bad conditions. Globalization has come to be so widely used that it is in danger of losing any very precise analytic meaning.

But just because the concept is widely used and sometimes misused does not at all mean that it has no relevance. Clearly, the world economy, and political and social conditions as well, have changed in some of their most basic characteristics during the last decade or so, and the word "globalization" serves reasonably well to describe the process. In technical jargon, there has been a paradigm shift.

The list of changes is familiar:

- A marked move away from direct governmental intervention in the economy. Governments are far less likely now to centrally plan or even try to fine-tune their economies than during most of the years following the end of World War II.
- Greater emphasis on privatization, in one form or another. Concurrently, economies are increasingly being opened to global or regional markets, although usually with more enthusiasm for exports than for imports.
- New centers of economic force, especially in East and South East Asia.
- A profoundly altered balance of political and military power as a result of the dissolution of the Soviet Union.
- Declining relevance of the view of the world as essentially the arena of East-West and North-South confrontations.
- New technologies, especially in information processing, but also in fields such as agriculture and industry, with important consequences for labor force needs and the international division of labor.

Unfortunately, familiarity with these changes at the global level does not contribute much to understanding or offer much guidance for action at the national or the regional levels. However, both understanding and guidance are crucial. Changes as great as those listed have potentially grave consequences for any country or region. And as in any new social or economic situation of this sort, the consequences can be beneficial for some, but acutely painful for others.

In order to better foresee the specific impact of globalization in Egypt and the Arab region, and to devise a sensible strategy to maximize benefits there, it is useful to examine some key elements in the process. The topics here concern: flows of capital, production and exchange of goods, people as producers and as consumers, exchange of ideas in the form of technology and broader social values, and the political structures in which relations between nations take place. Each of the papers presented in this volume focuses on one of these topics, as they relate to Egypt and the other countries of the Arab region.

The paper by El-Erian and Sheybani provides an essential overview of global trends in capital flows to developing countries over the last two decades. They show how the flows have changed in quantity, character and direction. During the early 1990s, the size of the flows has increased dramatically, averaging some 50 per cent more than at the time on the previous peak in the later 1980s. The composition of the flows has also changed. In the late 1970s and early 1980s, the capital needed to finance development in the countries of Asia, Africa and Latin America predominantly took the form of voluntary commercial bank loans. Then, among other things as a result of the debt crisis in Mexico in 1982, that flow was drastically reduced. By the later 1980s, bank loans had been substantially supplemented by direct investment and purchase of bonds and equities issued by firms in the developing countries.

Thus, the total amount of capital available to invest in development, and the variety of terms under which it can be obtained, have both increased significantly in recent years. At the same time, the funds were far from equally used by countries in all of the regions. The Asian countries used by far the greatest share and Latin America most of the rest. The Arab countries, and the countries of sub-Saharan Africa, participated very little in the renewed flow of funds of the 1990s. As El-Erian and Sheybani observe, the Arab countries have been largely bypassed by the process of globalization and integration of international capital markets. The authors go on to suggest that the low level of investment plus the inefficiency of the investments that were made have contributed to the disappointing economic growth performance of the Arab region.

Nevertheless, El-Erian and Sheybani conclude with the observation that in a substantial number of Arab countries, there are the beginnings of a change for the better. These countries have strengthened their structural reform policies and their relations with international capital markets. They point to such positive steps in Tunisia, Egypt, Lebanon and Kuwait.

In a detailed analysis, Gouda Abdel-Khalek examines the specific structural reform policies adopted by Egypt during the 1990s. He demonstrates clearly that the consequences of any such policy will depend a great deal on precisely which steps are taken, and that devising an appropriate strategy requires close attention to the unique situation found in each country that undertakes reform. To put the matter most simply, one prescription cannot suffice to treat all conditions.

In the late 1980s, Egypt found itself in an economic crisis that induced it to turn to the International Monetary Fund and the World Bank for assistance. An agreement was reached with those two agencies in 1991, setting forth the basis of Egypt's Economic Reform and Structural Adjustment Program (ERSAP). In his paper, Abdel-Khalek nicely summarizes the terms of the Program in its five main areas of activity: Macroeconomic reform, public enterprise reform, domestic price liberalization, foreign trade liberalization, private sector reform and the establishment of a Social Fund for Development. As can readily be seen, the broad policies agreed to and being implemented are similar to those adopted by many other developing countries.

Abdel-Khalek then analyzes in greater depth a particularly important component of ERSAP, the foreign exchange regime and financial liberalization. An essential measure for any move in the direction of a more open economy is relatively unimpeded foreign exchange, a step taken by Egypt at the beginning of its economic reform. In association with that step, the Egyptian pound was pegged to the American dollar, and the interest rates that banks were permitted to pay were decontrolled. As a result of these measures, interest rates on pound deposits in Egyptian banks rose sharply between 1991 and 1993. Substantial deposits were attracted from both domestic sources and abroad by the high rates, especially since the returns could if necessary be converted back into dollars. That inflow in turn tended to push up the value of the pound.

To ameliorate the upward pressure on the pound the Egyptian Central Bank intervened, buying dollars in exchange for pounds. Then, in order to keep the large number of pounds that was being injected into the economy from generating inflation, the government issued treasury bills paying very attractive interest rates. The end result of the exchange rate measures was thus large scale interest payments to bond holders, not necessarily a highly productive form of investment nor one that has particularly beneficial effects on income distribution. The general lesson that Abdel-Khalek demonstrates is that an effective response to globalization is not merely a matter of opening to world markets, but precisely how a country goes about doing so.

The papers by El-Erian and Sheybani and by Abdel-Khalek deal primarily with the question of capital flows in the process of globalization. The next essential topic is production and marketing of goods. With respect to its impact on the countries of the Arab region, by far the single most important internationally traded good during the last three decades has been oil. Paul Sullivan's paper provides a thorough review of the issues concerned with the region's involvement in oil production and marketing.

In addition to a rich compilation of essential background information about oil production and marketing in North Africa and the Middle East, Sullivan presents three important general propositions. First, he demonstrates that the oil production industry of the region inevitably links it to the global economy. The sheer volume of oil that is currently produced in the region, the size of known reserves, and the comparatively low costs of lifting and refining all combine to make this by far the world's most important oil producer. In effect, the oil-producing countries of the Arab region, and those that participate in the industry through trans-shipment of oil to world markets are already playing a major role in the global economy.

Second, in assessing the likely future role of the region as a leading oil producer, Sullivan shows that there is little basis for expecting its global importance to diminish. In all of the other known oil-producing regions of the world, there are greater limitations or disadvantages of one kind or another. Nowhere else, including the Central Asian countries of the former

Soviet Union, are known and probable reserves as great as in the countries of the Arab region. Costs of exploration, lifting and refining are usually higher elsewhere. And for many potential producers, especially those of Central Asia, essential infrastructure including pipelines for export to world markets are only beginning to be built. The construction needed to bring these countries to a major role in world oil markets will be costly and time-consuming. Thus, it is more than reasonable to expect the countries of the Arab region that are directly involved in the oil industry to continue for the foreseeable future to play their leading role in the world economy.

Thirdly, however, Sullivan points out that the oil industry is vulnerable to a variety of different kinds of fluctuations and disruptions, and that no matter how large, oil revenues do not automatically lead to economic and social development. The revenues are of course subject to price changes on the world markets, which like those of any other primary commodity can be very large indeed, and at times very disadvantageous to the producer. In addition, oil fields and shipment networks are particularly vulnerable.

But an even more important question is how the enormous revenues that oil can generate are put to use. Sullivan argues that up to the present, the record of how they were used has in many cases been rather disappointing. The windfalls have not at all been used in a manner that would most support development; too often their use has led to the condition that has come to be known as the "Dutch disease". An excessive proportion of the oil revenues is devoted to consumption; development of productive capacity is neglected. A rentier mentality comes to prevail. But the system cannot be sustained. And once again, the lesson demonstrated is that in order to develop, it is not enough to simply have the capital that may be produced by oil or any other primary product, it is even more a matter of how the capital is used.

In his paper, Nader Fergany explores in depth some of the key conditions beyond the sheer availability of capital that must be dealt with if development in the global context is to be achieved in the Arab region. To do so, he uses the conceptual framework of "human development", focussing in particular on education and employment. In addition to examining prevailing conditions, he assesses future prospects for human development as the countries of the region proceed to privatize their economies.

Fergany begins by showing that although current expenditures on education as a proportion of gross domestic product in the Arab region tend to be among the highest in the world, the stock of educated persons remains seriously deficient. This condition is largely explained by the gross inadequacy of the educational systems in the past. However, he goes on to show that even with the greater spending of more recent years, the educational investment in absolute dollar terms remains comparatively very low. In addition, he indicates that access to education is especially inadequate for girls and for children of poor families in general. Even more serious, in Egypt for example, he gives evidence that the quality of education provided in the government schools (which supply more than 90 per cent of all primary school places) may well have declined in recent years.

Fergany indicates that the situation in the Arab region is similarly unfavorable with respect to employment. He suggests that for the region as a whole, the open unemployment rate is on the order of 15 per cent. And in some countries the rate is believed to be even higher: 21 per cent in Algeria, 33 in Iraq and 48 in the West Bank and Gaza. In addition, although rather more difficult to quantify, underemployment is generally believed to be an even more serious problem. For example, it is estimated that in Egypt the proportion of workers who are underemployed or overqualified for their jobs may be as high as two-thirds.

Unemployment and underemployment are exacerbated by both past and present policies. Fergany argues that a leading cause is that international aid and private sector development have generally been capital-intensive. In addition, governments have given up trying to guarantee jobs to all. Thus, the labor markets are unable to create employment sufficient to meet the needs of a rapidly growing labor force.

Furthermore, Fergany views the thrust toward privatization as unlikely to help resolve either the educational or the unemployment problems. He indicates that to simply impose free markets in what he refers to as "a sea of market imperfections", as found in much of the Arab region, is likely to reinforce rather than eliminate the imperfections.

Fergany suggests that ultimately a complete revision of the educational system and the labor markets will be called for. To achieve this goal, an essential step will be a thorough reform of the civil service, leading to higher productivity and a more efficient and just system of taxation. Another essential measure will be to overcome the prevailing fragmentation and vulnerability of the Arab region by means of revitalized cooperation between Arab states.

The prospects for such cooperation between Arab states, and of other possible new models of international cooperation, are thoughtfully appraised by Mustapha Kamel Al-Sayyid. In his paper, he identifies four leading contenders for the regional structure within which the Arab countries can approach globalization.

Al-Sayyid observes that two of the four contenders are based on initiatives largely from within the Arab region, and the other two from outside. The two contenders from within are Arab nationalism and what he refers to as the Islamist project.

Arab nationalism has deep roots in the region's history. In more recent times, it took a high position on the region's agenda in the late 1950s, beginning with the initiative of Nasser when Egypt and Syria merged for a time to create the United Arab Republic. Al-Sayyid identifies a second essentially region-wide flourishing of Arab nationalism in October 1973, as Egypt and Syria fought Israel to recover territory lost in 1967. Following those two events, the movement has lost momentum. The nationalism of individual countries plus the split among countries and within population sentiment that arose at the time of the Second Gulf War have weakened pan-Arab nationalism. Nonetheless, it remains a potent aspiration throughout the Arab world.

Like Arab nationalism, the Islamist initiative also has its roots deep in the history of the region. Its more extreme version calls for a restoration of the Caliphate, and takes the form of armed struggle against the existing government. A tragic example can be seen in Algeria at the present time. A less extreme version calls for the reform of societies and of existing governments, as inspired explicitly by Islamic ideals. In addition to reform, its agenda includes development of a more independent foreign policy, particularly towards the USA and Israel. Recently, the government of Turkey launched an initiative to create a formal grouping of eight Islamic countries; only one Arab country, Egypt, was included among the eight. Given recent changes in the government in Turkey, the doubts expressed by Al-Sayyid about any very significant long-term impact of this movement appear to be well justified.

It is noteworthy that the two initiatives that Al-Sayyid identifies as having their origin within the Arab region are articulated around ethno-linguistic and religious principles. In contrast, the other two initiatives give greater prominence to economic matters.

The Euro-Med project brings together in a formal organization the countries of the European Union with twelve countries of the Mediterranean. The organization dates back to the early 1970s when the countries of the then European Community launched a program mainly focused on economic cooperation with a number of Arab countries. The program continued to develop, culminating in the adoption of the Barcelona Declaration of November 1995. In addition to the members of the European Union and the Arab countries of North Africa and the Eastern Mediterranean, the signatory countries include Israel, Turkey, Malta and Cyprus. Libya is excluded.

The Declaration formalizes an agreement to establish a free trade area by the year 2010, commits the European Union to provide financial assistance to its partners (ECU 4.7 billion during the period 1995-1999), and to humanitarian and cultural cooperation. The Declaration also establishes a formal mechanism for follow-up activities. Al-Sayyid demonstrates that the Euro-Med initiative has become a political and economic reality in the region.

At the same time, he observes that from the perspective of the Arab members, it has some negative elements. The Euro-Med initiative was launched by its European members to deal with their own priority issues rather than with the concerns of the Arab or other non-European members. The Southern Europeans wanted to establish an economic and political counter-balance to offset the importance of the East European countries, where Germany was seen as having a privileged role. They also wanted to devise steps that would reduce the pressure for south to north migration. The Europeans (and perhaps some of the Arab countries as well) see the Euro-Med initiative as a response to the United States' development of NAFTA and Japan's cultivation of its markets in East and South-East Asia. Also, the Barcelona Agreement includes some Arab states, but excludes others, thus challenging Arab unity. Finally, there is some anxiety that any economic agreement between more and less developed countries will work against the interests of the latter.

The fourth structure considered by Al-Sayyid is essentially an initiative of the United States. In the early 1990s, as part of a follow-up to the Madrid Peace Conference, five international committees were established to encourage consultation and cooperation on leading political and economic issues confronted by the countries of North Africa and the Middle East. Participation included a large number of Arab states, Israel, the European Union, Japan, Russia the United States and Canada. By about the end of 1993, when these committees failed to produce results, the United States pressed for the development of an alternative approach in a series of regional meetings on economic cooperation. This time there was to be the direct involvement of members of the business community as well as representatives of governments.

The alternative agreed to at a meeting in Casablanca in 1994 called for the establishment of a Middle East and North Africa (MENA) Economic Community, the creation of a MENA Development Bank, a regional tourist board and a Regional Chamber of Commerce and Business Council. Al-Sayyid observes that some progress toward the realization of these measures has been made; establishment of the MENA Development Bank has proceeded. However, progress on all four measures has been greatly impeded by the stagnation in moves to resolve the Arab-Israeli dispute.

In his overall appraisal, Al-Sayyid concludes that none of the four programs is likely to proceed easily to realization. He suggests that the Euro-Med project may be the most likely to move ahead, albeit without a great deal of enthusiasm at the grass roots level. The least likely to achieve its goals is the Islamist project; it faces the strongest opposition both from within the countries of the region and from outside. In general, Al-Sayyid's analysis points to the conclusion that if more effective involvement in the global economy depends on the development of some form of regional intergovernmental organization, the task will be the more difficult. No such effective organization appears likely to emerge in the near future.

In the final paper presented in this volume, Hassan Hanafi moves away from the narrower question of the impact of globalization, and takes up the more general issue of the relationship between socio-political ideologies and development. He uses Egypt as a case study, covering the early-1920s to the present.

Hanafi describes the main features of the three successive ideologies that predominated in Egyptian society: liberalism, from the early 1920s to the Revolution of 1952; socialism, from 1952 to 1974; and capitalism, from 1974 to the present. He shows that the three ideologies were notably different in many of their prescriptions for social policy. Nevertheless, he concludes that all three shared a crucial common characteristic in that they were imposed on Egyptian society from top down. Each served to privilege some segment of the middle or upper classes, but the ideologies neither significantly influenced the thinking of the great majority of the population nor greatly benefited it. Hanafi's analysis points to some of the difficulties that may occur as socio-philosophical ideas migrate across national and cultural frontiers. Ideas, like other imports, may be used to greater advantage by some members of the community than by others.

Each of the six papers presented in this volume provides a valuable insight into one or another of the ways that globalization is having an impact on the Arab region. Taken together, they demonstrate very clearly that an effective response to the challenge--the risks and the opportunities--of globalization is difficult. The process is many-sided, and so the response will have to be as well. No one measure can suffice, and no one research discipline can produce all of the understanding needed.

The papers presented in this volume were originally presented to the Cairo Papers in Social Science Symposium held at the American University in Cairo, 23 October 1996.