

**Summary:** The events related to the Arab Spring are having a considerable economic impact on Middle East and North African countries. Oil-exporting states like the Gulf states and Algeria experienced a tremendous growth in their national income, partially due to increasing oil prices, and are investing that money in social programs. Nonexporting states like Tunisia, Syria, and Egypt, on the other hand, lost part of their income and are now deeply in need of foreign aid to proceed in their path towards democracy. Facing those challenges, and with their preeminence threatened by emerging powers like the BRICS states (Brazil, Russia, India, China, and South Africa) and Turkey, the Western powers need to redefine their economic and political strategy if they want to maintain their leading position in the area.

## The Economy in the Arab Uprisings: Difficulties and Transformations

By Giorgio S. Frankel

### The Emergency

As emphasized by the International Monetary Fund and other major economic players, Egypt, Tunisia, and Libya are in the throes of an economic emergency. They are in dire need of new resources and aid to the tune of tens of billions of euros. Their current economic and financial crises might compromise their already difficult transition to democracy. At the same time, this could threaten the balance of power in the Northern Mediterranean and the Middle East, both key areas for global stability.

In particular for Egypt, more than Tunisia, the test is decisive from several diverse perspectives: the relaunching of the economy, the ability of the Western powers to maintain their influence in the area, and institutional and political reforms. In other words, in Egypt, as in Tunisia, it is not a question of merely overcoming a critical economic phase, but of a profound modification of the economic model keeping pace with political and institutional reforms. The

same is also somewhat true for the “rentier” states of Algeria and Libya.

The United States and Europe have natural responsibilities to play an active leadership role in these processes. If they want to maintain their influence in the Mediterranean basin, this leadership must be implemented in a rapid and substantial way. A huge amount of resources has to be mobilized, there must be greater opening to markets, and technical and human aid must be made available. A few months after the start of the Arab revolution, it is quite legitimate to question whether the West is able to provide adequate answers to these challenges. Europe and the United States are embroiled in the seemingly never-ending crises in their own economies, and resources available for foreign intervention are diminishing dramatically. Moreover, Western leadership is threatened by flourishing partners, namely China and India, not to mention Turkey’s grand ambitions. Finally, the ever more destabilizing

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wave of the Israeli-Palestine conflict continues to exert a detrimental impact.

## The Economic Consequences of the Uprisings

On a global scale, the crisis in Libya and the partial halting of its crude oil export has led to such a surge in oil prices that the recovery of the global economy is at risk. If after Libya the uprising had also infected Algeria and the Arab oil-producing and -exporting countries of the Persian Gulf (about 25 percent of the entire amount of oil traded at the international level), there would have been a danger of a worldwide oil crisis with incalculable repercussions.

As far as the economic impact of the unrest in the area is concerned, the International Monetary Fund (IMF) and the Institute of International Finance (IIF) in Washington have classified countries into two main categories.

The first category consists of oil-exporting countries and the second, nonoil-exporting countries. The first category includes an important sub-group made up of the Persian Gulf producers, i.e. the six member states of the Gulf Cooperation Council (GCC). While largely avoiding (for the moment) the danger of rebellion, Gulf countries have actually derived considerable economic advantage thanks to the increases in crude oil prices, partly caused by the Arab Spring itself. According to the IMF, GCC countries as a whole could record a growth rate of 7.8 percent for 2011, with a substantial surplus in the state balance and, more important, in the current accounts. The IIF foresees a surplus amounting to the almost astronomical figure of \$1.7 trillion. This would endow these countries with striking economic and financial power on a global, not merely Middle Eastern, scale.

Non-GCC oil exporters, Algeria in the lead, will also show good growth rates: an average of 5.2 percent in 2011 and 6.0 percent in 2012, except for Libya (estimates and forecasts are not available), thanks also to a strong recovery in the oil production sector in Iraq. Yemen, on the other hand, is a small oil-exporting, relatively poor country (with a GDP of only \$20-30 billion and a population of more than 20 million) is one of the countries most affected by the uprisings. According to the IIF, in 2011, it will have negative growth of 4 percent as compared with +7.0 percent in 2010.

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Thanks to increased income from oil, countries in this first category are in a position to finance public spending programs aimed at calming their populations and reducing the danger of protest and uprisings. Saudi Arabia in particular has upped social spending (minimum wage, social benefits, income support) and has announced two vast long term social intervention projects, to the overall value of more than \$120 billion, equating to around 30 percent of GDP in 2010. This would suggest that the Saudi royal family does not underestimate the dangers of an uprising.

In addition, since the onset of the Arab Spring, the Gulf Cooperation Council (GCC) has decided to set up a special fund of \$20 billion for development aid, divided in equal parts over a ten-year period between Bahrain and Oman, both members of the GCC but less wealthy than the others and both hit by waves of protest. This initiative indicates just how much the GCC intends to increase internal cohesion in order to tackle the revolution, and tries to position itself as an economically and financially very powerful “Sunni block,” with leadership ambitions in the Middle East, as well as globally.

## For the Other Countries in the Region, Economies in Recession

The second category is made up of nonoil exporting Arab countries. The uprisings had varying degrees of negative consequences for them: slowdown or collapse of economic growth, further increases in unemployment, double-digit inflation, slump in investments, fall in remittances from foreign workers, and crises in various economic sectors, among them tourism (Egypt, Syria, Tunisia), textiles (Tunisia and Egypt), halting of major construction projects (Egypt and Tunisia).

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According to IIF projections, the initial impact of the Arab uprisings has exerted a relatively severe blow of negative economic growth: -0.5 percent in 2011, compared with 4.4 percent estimated for 2010. The data refers to all countries in this group. The main problems affect Egypt, -2.5 percent; Syria, -3.0 percent; and Tunisia, -1.5 percent. IIF forecasts indicate that these countries might return to positive growth in 2012, which might nevertheless be an unbalanced growth. Thus, in the current situation of severe economic imbalance, any future growth might aggravate the discrepancies in income and backwardness in certain areas. The effects on the situation, which is already socially and politically tense, could be with inflammatory.

## Structural Problems

Even before the uprisings, a considerable part of the Arab economies was afflicted by serious structural problems. Unemployment rates were high, reaching levels of about 25 percent among young people and over 30 percent among women. According to the International Labour Organization, the Middle East and North Africa have the highest unemployment rate in the world. Job creation remains insufficient to meet demand.

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There is also widespread corruption, lack of transparency, and inefficiency in public bureaucracy. In some countries, privatization and deregulation policies have only benefited a limited circle connected to political power.

## Food Security

Algeria, Libya, Egypt, and, to a lesser extent, Morocco and Tunisia are dependent on foreign imports for many basic foods, particularly cereals: for example, 35 percent of wheat traded at an international level, whose prices are subject to the fluctuations of world markets.

Egypt, with its population of just over 80 million, is forced to import approximately 50 percent of its food requirements. In the period between May 2010 and April 2011, the cost of food in Egypt rose by more than 20 percent. For a significant slice of the population, food spending accounts for a substantial share of its income. Bread, which is the staple for much of the population, is sold at subsidized prices. Import forecasts in 2011/12 reach 9.5 million tons, which confirms Egypt as the top-ranking global importer. Hikes in bread prices have always triggered protests throughout the country. The issue of bread prices has often caused Egypt to run afoul of the International Monetary Fund, which for decades has been exerting pressure on Cairo to abolish, or at least reduce, the subsidies. It would be tricky for the Egyptian authorities to raise the price of bread now without risking a fresh round of unrest. In a mid-May interview, a minister warned that Egypt could not afford, under circumstances, to reduce subsidies on bread and other staples, including fuel. In the 2010/2011 budget, subsidies account for about 25 percent of public spending.

## Dependence on Tourism

The economies of Algeria and Libya present the typical problems of “rentier” oil states: income controlled by a narrow elite, concentration of power, and hypertrophy of public sector and imports. For the economies of Tunisia, Egypt, Syria, and to a lesser extent Morocco, tourism represents the driving sector.

In Egypt, tourism employs almost 2 million workers, generates 11 percent of GDP, almost 50 percent of the export of services, and is the principal source of foreign currency, accounting for 20 percent of the total. Egypt forecast a growth of 10 percent and more in tourism for 2011. However, in May the Egyptian authorities announced that the sector was experiencing a deep crisis. Tourist figures for the first quarter show a downturn of approximately 45 percent.

In Tunisia, tourism provides employment for approximately 400,000 people and, in normal times, it generates 6-8 percent of GDP and represents the main source of foreign currency.

Finally in Syria, which a few years ago based its growth strategy on tourism and foreign investment — two sectors that demand political stability and peace — there was a 40

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percent increase in the number of tourists in 2011, generating just over \$8 billion. The country has been the recipient of \$2.5 billion in direct foreign investment. Damascus had planned to attract \$55 billion in direct foreign investment for the five-year period 2011-2015., but recent unrest makes such forecasts doubtful.

It is likely that tourism will be the first sector to recover once the post-uprising situation has stabilized in the region. The experiences of other tourist destinations afflicted by internal crises or struck by natural disasters shows that tourists decrease significantly at first, then gradually return to previous levels when the emergency is over. In May, Cairo announced special incentives favoring international tourism companies in order to relaunch the industry. The Tunisian government, in conjunction with a network of tour operators, has developed an emergency plan to boost the sector: “I love Tunisia.”

### The Transition

In the face of such difficulties, the transition governments have the arduous task of reconciling needs of different or even conflicting natures. They must bear in mind that after an uprising, the population expects a rapid improvement in living standards and, above all, greater job opportunities. They must maintain social cohesion and political stability while responding to the demands for a more open economy, which does not favor a narrow group of elites, and a bold fight against corruption and privilege. At the same time, they must improve the system of social protections. Such policies require an increase in public spending and budget deficits.

In an interview with the Egyptian daily *Al Ahram*, IMF official Ratna Sahay acknowledged that “this is not the opportune moment to cut funding for food and fuel since prices have risen dramatically and such a move would hit the poorest.” Sahay nevertheless underlined that the subsidies policy practiced in Egypt and other countries is inefficient, since it benefits everyone (even the rich), and it should be replaced with a “safety network” targeted at helping those in greater need.

Egypt is certainly not an isolated case. After the explosion of the Arab Spring, other governments in the region increased their budget allocations to subsidizing basic necessities and other “social” programs.

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In 2011, Morocco will allocate 10 percent of investment funds to subsidies “We will protect the purchasing power of the citizens at any cost,” said a government spokesman. This is in addition to other social initiatives, including an increase in minimum guaranteed wage and the creation of new positions in the public sector. Oman, which, along with Bahrain, has benefited from the huge aid package from the GCC, will recruit 50,000 in the public sector and will pay a monthly unemployment benefit. Bahrain has announced a local government building program of almost \$7 billion. In the United Arab Emirates, a campaign to freeze the prices of 400 products in 70 hypermarkets is underway. And Saudi Arabia, as already mentioned, has announced a long-term program of social intervention, which equates to almost 30 percent of GDP.

On the other hand, governments should undertake policies of recovery to relaunch their economies that are welcomed by the international economic and financial institutions, including donor countries and foreign investors, who will push the countries under discussion to institute fiscal discipline and will insist on the adoption of reforms and economic policies that are favorable to the private sector, the market economy, and the opening to the world economy.

There is another emergency. The ousted political leaders and their families, with numerous hangers-on, have taken possession of sizable shares of the economies of their countries, and have accumulated enormous wealth abroad.

The same is true for other regimes that might be overthrown before long. Post-revolution political leadership will

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have to reform their respective national economic systems, deciding where to direct funds and wealth confiscated from the now defunct power classes. Recent experience suggests that a portion of the wealth of deposed leaders might be returned to the state, while another part could be privatized. At the same time, it is important to avoid the repetition of the serious mistakes made at the time of privatization in ex-communist countries. Vital economic and industrial activities and other goods to be privatized must not be acquired at ridiculous prices by groups of speculators, who might even be representatives of the deposed leaders.

### International Aid

At first blush, the direct commitment from Western countries of \$10 billion seems relatively limited. A further \$20 billion should be forthcoming, mostly from the international institutions — IMF, World Bank, and the Islamic Investment Bank — in the form of loans. The oil-producing states of the Gulf should supply the remaining \$10 billion.

The conditional form is obligatory. Saudi Arabia, which has not hidden its disapproval for Mubarak's "abandonment," is worried about a spread of the Arab Spring, as demonstrated by events in Bahrain. They have not yet set precise conditions for the loans.

The budgets of both Tunisia and Egypt are extremely uncertain, and their debts are running high. Reports on the two countries from the IMF and the World Bank have not identified any great deviations in new economic policies. Their priorities replicate those that necessitated structural adjustment plans. Are we facing a new edition of structural adjustment? Not in the short term. It is probable that international institutions will not impose strict conditions on Egypt and Tunisia, at least not at this stage. FEMISE, a network of economic researchers in the Mediterranean area headed by Institut Méditerranéen (IMED) in Marseilles, has openly advised against conditions on loans that are too restrictive and criteria that are too rigid in the short run.

The requests for aid from the transition governments are higher than the announced figures. The Tunisian prime minister, who attended the G8 summit in May 2011 along with his Egyptian counterpart, indicated that his country needs \$25 billion over five years, including \$5 billion immediately. "The only payback we can offer is democracy."

The central question is whether Western powers will be able to find the necessary resources to play a key role in the economic reconstruction and restructuring of the Middle East. This poses a second question: do they have a shared "grand strategy" to guide policies in the era of the Arab Revolt?

### Toward a New Regional Order

While transition cannot be envisaged in a brief period and the level of uncertainty is considerable, the geo-political position of the area is already changing.

## Are we facing a new edition of structural adjustment? Not in the short term.

The "emerging" BRICS powers of Brazil, Russia, India, China, and South Africa are already active in the area with ever-increasing economic and geopolitical interests. China, in particular, with its cash reserves amounting to approximately \$3 trillion, could, without great sacrifice, finance the bail-out and relaunch of Egypt and Tunisia, maybe even of other countries, and supply them with the products and infrastructure they need, as is already happening in Algeria and Libya. And they can do all this without imposing particular political conditions, or a specific economic "model."

The first international initiatives in post-Mubarak Egypt would seem to indicate that the country wants to re-establish its central role on the Middle Eastern stage with a more dynamic and independent foreign policy than under the previous regime.

The GCC countries are also very ambitious, and in the near future they might opt for a more decisive economic and perhaps also monetary integration policy, attracting other Mediterranean countries.

The already started "Common Mid-Eastern Market" (formed by Turkey, Syria, Lebanon, and Jordan) could be consolidated and, according to some analysts, be joined by Egypt. For the moment, uncertainty about the fate of Syria

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and the forthcoming decisions that Jordan will take about membership in GCC are hanging over this project. Should this market become a reality, it could bring about fundamental geo-economic changes in the region, and play a significant role in the global context.

Finally, there is no doubt that a change in the economic model for the Mahgreb countries will necessitate a different relationship among the national economies. Currently trade between Algeria, Morocco, and Tunisia is insignificant when compared to that with Europe. Political conflicts, particularly between Algeria and Morocco, continue to weigh on the full creation of a common market.

### **“A Window of Opportunity” for the West**

Following the Arab Spring, the EU should have a great strategic interest in reviving the EuroMed program, which foresaw, among other things, a free trade zone and the accompanying economic integration. Such integration would undoubtedly contribute to the stability and socio-economic growth of the Mediterranean region, to guaranteeing EU energy supplies, and to the internationalization of the euro. This cooperation could lead to the solutions for many regional conflict situations. However, prospects for the relaunch of the EuroMed partnership should be considered in the light of the fact that over recent years, the Arab Gulf states have overtaken the EU and the United States as main investors in Mediterranean Arab countries.

If the GCC actually do pursue their economic and monetary integration projects, they will have a vested interest in strengthening their economic and financial presence in the Middle East and North Africa, and in promoting the use of their currency in transactions with other Arab countries.

The GCC countries seem to be committed to establishing closer cooperation ties with Asia and in particular with China, with widespread implications not only for import-export issues, but also changing the geo-economic prospects for the region.

In addition, a Turkish-influenced “Middle East Common Market” could prove to be a new hurdle in the attempts to relaunch the EuroMed program, because the two projects would overlap from the point of view of membership, competences, and goals.

Finally, it is necessary to bear in mind the growing economic activity in the Middle East and North Africa of the BRICS countries. In a recent brief study, the African Development Bank stated that by the end of 2009, the BRICS had already invested \$70-90 billion in North Africa. The BRICS countries are interested in importing oil and other natural resources, exporting their ever-growing range of products (including cars, civil and military aircraft, and electronic equipment), and investing in production plants.

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Nonetheless, the events of the Arab Spring would suggest that the BRICS countries, particularly China and Russia have a relatively limited margin of initiative and capacity to intervene. In this initial phase, the policies to mobilize financial aid for Egypt and Tunisia were mainly pursued by the Western powers.

The May 2011 Deauville meeting of the G8, where aid amounting to approximately \$40 billion was announced, was just a Euro-American show. Russia, although a G8 member, remained on the sidelines. Since China and the other BRICS countries are not members of the group, they did not play any role.

The issue of financial aid and other forms of assistance for Middle East and North African countries offers the United States and the European Union the opportunity to re-establish their economic and financial (as well as political and cultural) relationship with the countries of the region on a

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completely new basis. This requires the Western powers to draft a new “doctrine” to guide the dialogue and cooperation with those countries, while bearing in mind the peculiarities of the Arab revolutions, the difficulties of future economic (as well as political) “transition,” and the possible new political identities that will grow in the post-revolution Arab world. In this context, it is also necessary to engage in dialogue about models of economic policy, growth and development, and inclusion in the global economy. Such models have to be more coherent with the reality of the countries under discussion and with their objective priorities.

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It is highly likely that this “window of opportunity” will not remain open for long. The margins for maneuvering for Western powers and their ability to influence the economic decisions of the countries of the Middle East and North Africa could prove relatively limited, given the great resources available of the region and the future policies of BRICS countries and Turkey and their interests in this macro-area.

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