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Domestic Public Resources in the Arab Region: Where Do We Stand?

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Outline

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Abstract

The paper assesses the recent trends in domestic public resources in the Arab countries, with a focus on taxation systems, and provides a baseline in this context toward monitoring the commitments of countries according to the Addis Ababa Action Agenda (AAAA). The analysis suggests that the share of revenues (excluding grants) to GDP in the Arab region, on average, is about 36 per cent, which is slightly lower than that of the average of the 'advanced economies' in 2014. But the volatility of the revenues in the Arab region is apparent as compared to that of the 'advanced region' or any other region of the world.

There is large disparity between the 'oil-rich' and 'oil-poor' countries in terms of their revenue mobilisation or available fiscal space at the contemporary period. Excluding grants, the average revenue to GDP of the 'oil-poor' countries is only about 20 per cent in 2014, and it has witnessed a declining trend since 2008. The revenue to GDP ratio of the 'oil-rich' countries is among the best in the World, around 40 per cent in 2014, but the fluctuation in revenues is apparent due to swings in oil prices. The oil revenues may not be sustainable in the long run, owing to the downward pressure on oil prices as well as depletion of oil and gas resources.

The Arab countries are in a typical situation. Giving importance to the two sides of the fiscal balance in formulating policy – revenue and expenditure – can minimize the distortions and benefit output as well as fiscal space. Increasing domestic revenue mobilization by all possible means is a priority for most countries in the region. Simultaneously, fiscal expenditures can be spent efficiently to promote the target of economic diversification and increase revenue mobilization in a long term perspective. This paper discusses some policy proposals, with a focus on raising domestic revenue mobilisation in the Arab region.

1. Introduction

Financing is important for the Arab region for progressing toward achieving the 2030 agenda for sustainable development, and also for meeting the immediate need of rebuilding the loss of capital stock in the conflict-affected countries. The cumulative financing requirements for selected Arab countries to achieve sustained growth during 2015-2030 are estimated at $3.6 trillion,[2] which may be much larger if cost related to environmental degradation and conflicts are added. With the ongoing crises in Syria and some other parts of the region, the gap between the requirement and the existing financing availability are widening. The latest ESCWA estimates suggest that conflicts in the region have led to a net loss of $614 billion in economic activity, and an aggregate fiscal deficit of $243 billion during 2011-2016.[3] Conflicts have worsened other economic and social indicators, such as debt, unemployment, corruption and poverty. In addition to crises in several parts of the region, the worsening fiscal situation of major regional donors of the Gulf Cooperation Council (GCC) countries, due to unfavorable oil prices, pose a major concern to easy access to finance for the Arab countries.

Under these circumstances, it is important for Arab countries to consider an integrated approach to the two sides of the fiscal balance: revenue and expenditure. Raising revenues is not easy and quick. Governments often resort to reducing public expenditure in order to correct the fiscal imbalances in the short run. However, expenditure reducing options in order for attaining fiscal balance is no more an ideal choice of the countries in the region, given that the Arab governments need to address the challenges of increasing poverty and unemployment in recent years. The contemporary economic situation of the countries, being affected by shocks that have led to economic downturns, calls for expansionary macroeconomic policies to pick up the slack in aggregate demand and to create decent jobs in order to absorb the growing labour force. In addition, there is a greater need of financing for achieving the SDGs in 2030.

Meeting the increasing expenditure, at present and in the long term period, requires raising revenue from within the country by all possible means. This is particularly significant because external development aid as a source of finance for the developing countries of the region has fallen short of the commitments in the past, and in any case aid is inadequate to bridge the development deficits in the region.[4] Developed countries have been struggling to boost their economic growth and to create jobs for their citizens, particularly after the global economic downturn in 2008. Therefore, there is less likelihood that they could increase development aid for financing the SDGs in the developing world. It could be an

[2] ESCWA, 2015e.
[3] ESCWA, 2016b.
[4] UN and LAS, 2013.

achievement by itself if the developed countries can keep their commitment to achieve the target of 0.7 per cent of ODA/GNI to developing countries, as envisaged in the SDG 17. Nevertheless, the Addis Ababa Action Agenda (AAAA) has explicitly emphasised on harnessing domestic public resources as a central component of financing the Agenda 2030 on Sustainable Development and the member states have agreed to it. Therefore, increasing domestic revenues is important for meeting the rising expenditure needs in the developing Arab countries to sustain growth along with inclusive development in line with the required progress toward achieving the SDGs.

In this context, this paper takes a stock of the recent trends in domestic revenue mobilization in the Arab countries, with a focus on taxation systems, as a baseline exercise toward monitoring the commitments of countries according to the AAAA. In doing so, the paper uses the new official database of IMF World Revenue Longitudinal Data (IMF WoRLD), and compliments it with national data (compiled from Ministry of Finance of respective Arab countries) as appropriate and relevant. The paper assesses the domestic revenue capacities of the countries by tax and non-tax resources, including oil and gas revenues, in the following section 2. The section 3 explains some of the key constraints that affect growth and domestic resources sustainability. The section 4 discusses main policy proposals toward mobilising domestic public resources, particularly through reforming tax systems, reducing illicit financing flows and harnessing public-private partnerships. Of course, broader aspects of cross-border cooperation or international cooperation on financing, trade and technology transfer are other important aspects of raising domestic public resources, as stated in the AAAA, but those aspects are beyond the scope of this paper. Finally, the section 5 presents the findings as they emerge from the analysis.

2. Trends in domestic revenue mobilisation: 'Oil-rich' and 'Oil-poor' countries

The paper took into consideration the period between 2005 to the latest year of data availability for assessing revenue trends in the past ten years or so. In fact, the mid 2000s were the years of high and relatively stable growth in the Arab region (on average 7.7 per cent during 2004-06) and the oil price was at an increasing trend during the 2000s until the global economic crises in 2008. The proposition is to examine the revenues trends from the good years of growth until the latest year, where several parts of the region are amidst conflicts and crises situations.

Arab countries can be broadly grouped into two clusters in terms of major sources of revenue collection: 1) from oil and gas sectors, which is generally known as hydrocarbon-based resources, and 2) form non-oil and gas sectors, which is mainly taxes. The first cluster will be the Gulf Cooperation Council (GCC) countries along with Algeria, Iraq and Libya, whose major source of revenue is the oil and gas sector. For instance, the share of oil and gas revenue in Saudi Arabia is around 90 per cent of the total revenue (Annex Table 1). Except for Algeria and United Arab Emirates, the share of tax component of the revenues is small and is mainly from corporations related to oil and gas sector. For the purpose of analysis in this paper, these countries are referred as 'oil-rich' countries.

The second cluster of the countries is referred here as the 'oil-poor' countries that are poor on oil and gas or hydrocarbon-based resources and they rely on a mixture of sources of revenue collection but mainly on taxes (Annex Table 2). On average, in the tax systems in 'oil-poor' countries, around 50 percent of revenue is collected from indirect taxes. [5] These countries typically face more constraints on fiscal space than the 'oil-rich' countries, although some of them are in the middle and upper middle income category such as Tunisia, Jordan, Morocco and Egypt. These countries have been facing significant development challenges in recent years to tackle high unemployment, increasing poverty, lack of adequate social protection and so on. In addition, some of the 'oil-poor' countries are the low income countries (LDCs), such as Comoros, Djibouti, Mauritania, Sudan and Yemen who have huge development deficits and they were off-track on the MDGs. Therefore, mobilizing larger fiscal space for meeting development needs is a key priority for these countries.

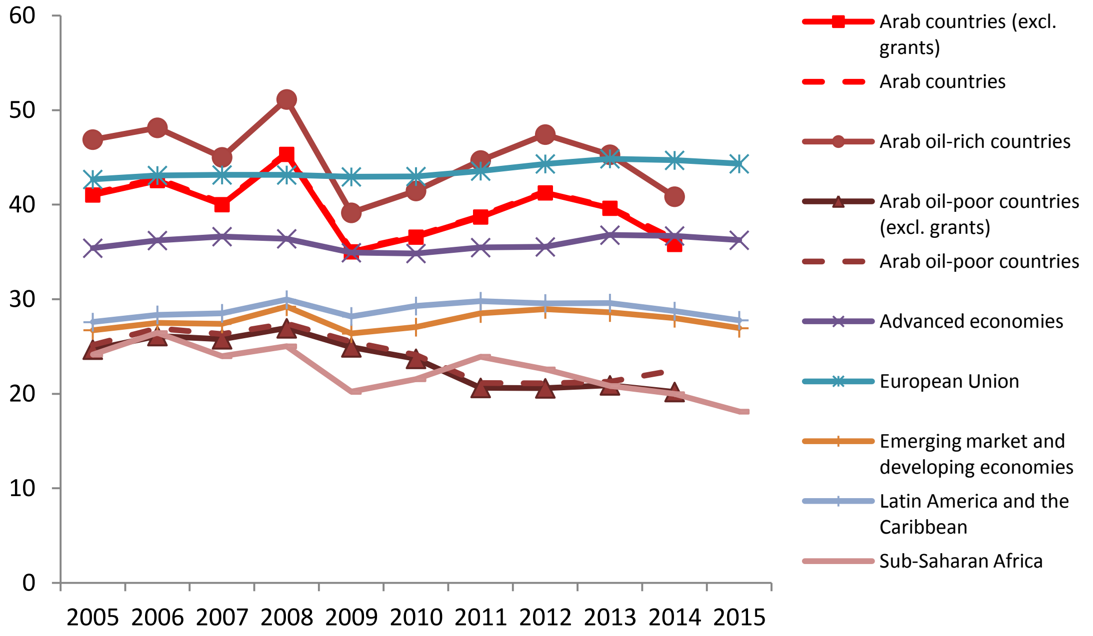
On average, the share of revenue (excluding grants) to GDP in the Arab region is 35.8 per cent in 2014, which is slightly lower than that of the average of the 'advanced economies' (Figure 1).[6] It was higher than that of the 'advanced economies' from 2010 to 2013. If we review the decade during 2005 and 2015, the trend of the average revenues (excluding grants) to GDP for the region shows large swings than that of the 'advanced economies' or any other region (Figure 1). In particular, the Arab regional average of the revenue to GDP share is influenced by the revenues in the 'oil-rich' countries that derive most of their revenues from oil and gas sectors. Depending on the swing in international oil prices, the revenues to GDP share goes up or down.[7] The recent plunge in oil prices and its stagnation since 2014 has led to reduction in oil-revenues, which is reflected in the decline in the revenue to GDP ratio for the 'oil-rich' countries as well as for the whole region. Therefore, the volatility in the revenues in the Arab region is quite apparent as compared to the other regions of the world.

[5] ESCWA, 2014b.

[6] The regional categorization in this graph follows that of the IMF World Economic Outlook regions. The Arab region and sub-regions are author's categorization as mentioned in the text.

[7] In fact, considering 20 observations from the period 1994 to 2014, the correlation coefficient between international oil price (Europe Brent Spot Price FOB US Dollars per Barrel) and the ratio of total revenue (excluding grants) to GDP is 0.82, showing high association between their movements.

Figure 1: Total revenue (% GDP) across regions in the world



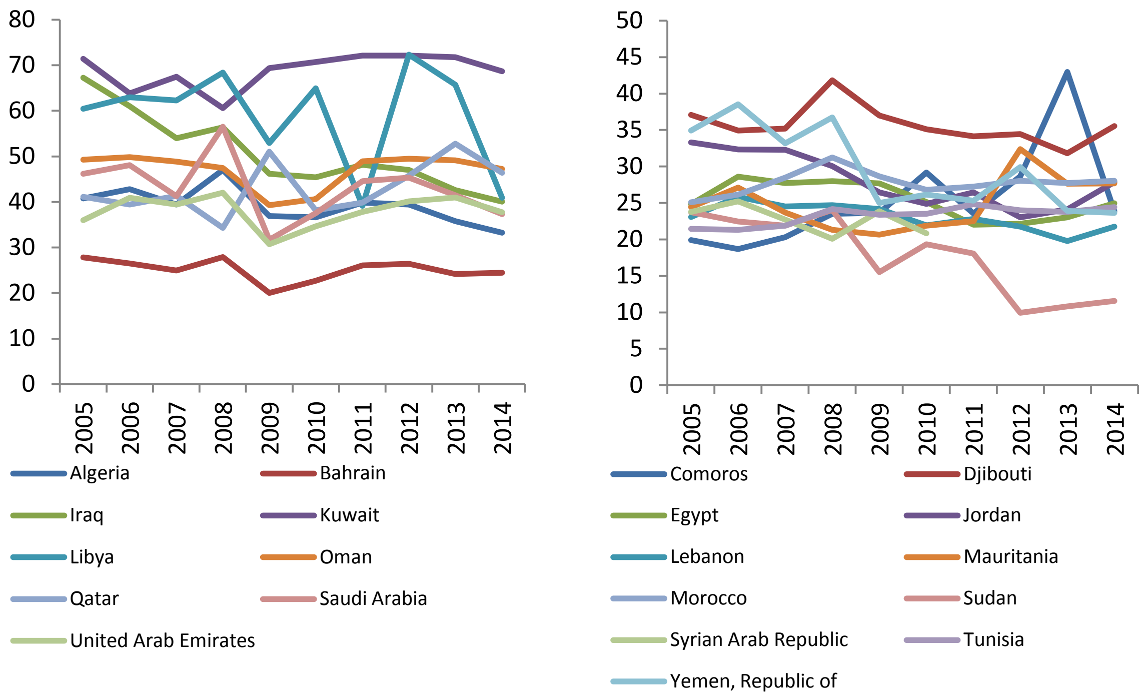
Source: Author's calculation based on IMF (2016a); IMF (2016b).
Note: Regional and sub-regional aggregates are weighted averages.

Another point is that the disparity in average revenue to GDP between 'oil-rich' and the 'oil-poor' countries is quite evident as the 'oil-poor' countries perform poorly in mobilising revenues. Their average revenue to GDP, which is about 22 per cent in 2014, is lower than most regions in the world, including that of the emerging market and developing economies (Figure 1). Excluding grants, their average revenue to GDP is further lower, only about 20 per cent in 2014 and it has witnessed a declining trend since 2008. There is however variation across the 'oil-poor' countries where their shares range between a quarter and 30 per cent in 2014 (Figure 2B). In most 'oil-rich' countries, the share of total revenue[8] to GDP is in the range between 40 and 70 percent in 2014 (Figure 2A). Considering the potential revenues from hydrocarbon resources, the 'oil-rich' countries tend to have larger fiscal space for meeting their development needs in near and medium terms. But that may not be sustainable in the long run, owing to the downward pressure on oil prices and the depletion of oil and gas resources, as discussed later in the paper. However, the revenue collection systems of the two clusters of countries differ significantly, which is discussed in the following sub-sections.

[8] The term revenue refers to total revenues including grants, unless specified as revenue excluding grants.

Figure 2: Total revenue (% of GDP) of Arab countries

A. 'oil-rich' countries B. 'oil-poor' countries

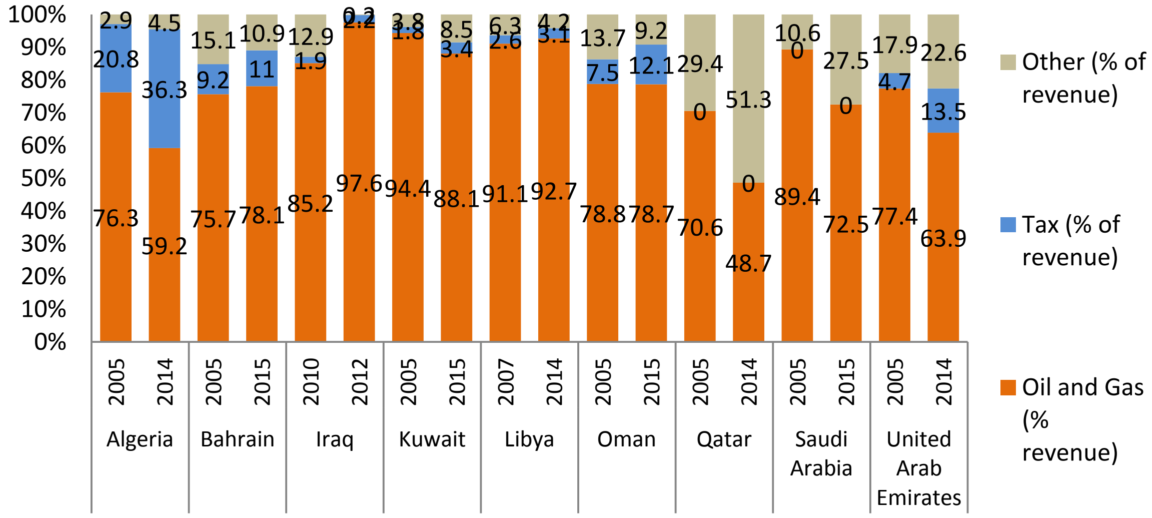


Source: IMF (2016b).

A. 'Oil-rich' countries: Diversification of revenue sources is a key priority

The IMF WoRLD doesn't provide any information on revenue composition by oil and gas sectors and others. To assess the composition of revenue systems, the paper relies on the national data sources, particularly the ministry of finance reports of respective countries. Figure 3 shows the shares of different types of revenues in 'oil-rich' countries. As expected, the 'oil-rich' countries rely heavily on oil and gas sector resources for mobilising revenue. For instance, Kuwait mobilised over 88 per cent of the total revenue from oil and gas sector in 2015 (Figure 3). Several countries such as Qatar, Oman and Libya have been able to mobilise majority of their revenues from oil and gas sectors as well. In Saudi Arabia, the share of revenue from oil sector was around 90 percent in 2005, which recently declined due to the low oil prices since 2014, but still it constitutes above 70 percent of the total revenue in 2015. A simple (unweighted) average of the share of oil and gas revenues out of total revenues in the oil-rich countries turns out to be 82 per cent in 2005 and 76 per cent in 2014. The GCC countries don't impose personal income tax on their citizens. The volume of direct tax collection is mainly from the corporate taxes, but that is negligible in most countries, except for Qatar.

Figure 3: Revenue sources in 'oil-rich' countries: Share of tax vs hydrocarbon-based revenues



Source: Author's calculation based on data compiled from Central Bank/Ministry of Finance of each country.

Note: For Qatar, "Other" revenues include investment income from public enterprises (33% of total) and the rest miscellaneous (18%). The investment income comprises the dividends paid by Qatar Petroleum and other state-owned enterprises, which may not be from the oil and gas sector. Given the limited information, the entire investment income cannot be added to the revenues from oil and gas sector although a large part may qualify for its inclusion.

Therefore, the tax component of total revenue as a per cent of GDP is too low in the 'oil-rich' countries. Among the 'oil-rich' countries, the share of tax to GDP is negligible for most countries, which varies from as little as 1 per cent in Kuwait to 5 per cent in Qatar in 2013 (Figure 4A). United Arab Emirates and Algeria are exceptions that show relatively high percentage of tax to GDP, 21 per cent and 34 per cent respectively in 2013, considering that their economies are relatively more diversified than others in the GCC. Since major source of revenue is oil and gas exports in the GCC countries, their total revenue is affected by fluctuations in international oil prices or sales affected by global demand situations at times of economic crises such as the global economic slowdown of 2008 or due to productions being affected by political conflicts and crises situations such as in Iraq and Libya since late 2000s. Recently, the low oil prices since 2014 has hit fiscal balance in all the oil-exporting countries negatively. The sharpest decline in the share of oil revenue to GDP was reported for Saudi Arabia: from 42 percent in 2012 to 18.8 percent in 2015.[9]

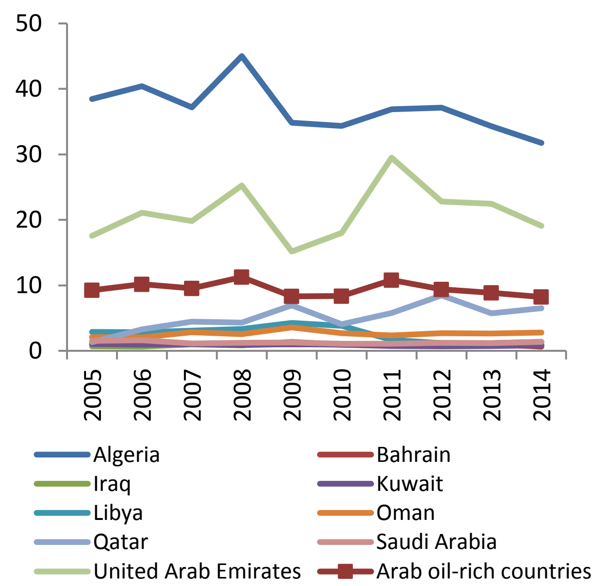
The 'oil-rich' countries have incurred high fiscal deficits as well as negative primary balances since 2014, as against the usual primary balance surpluses. Saudi Arabia and Oman

[9] SAMA, 2016.

reported negative primary balance since 2014, Kuwait and United Arab Emirates reported negative primary balance since 2015 (figure 4B). Qatar is the exception in the GCC countries to report primary balance surplus. In fact, a recent study projects worsening situation in 2016. In Bahrain, the estimated budget deficit of 11.5 per cent of GDP in 2015 is forecast to rise to 12.6 per cent in 2016. The respective figures for Kuwait, Qatar, Saudi Arabia and the United Arab Emirates are: 16.7 per cent (18.8 per cent in 2016); 21.8 per cent (19.8 per cent in 2016); 15 per cent (13.1 per cent in 2016) and 5.2 per cent (4.5 per cent in 2016).[10] These countries are increasingly considering borrowing by issuing sovereign bonds in international capital markets in order to meet the expenditure needs, in addition to introduction of new policy measures such as introduction of value-added tax (VAT), reduction of subsidies, cut in capital expenditures, Public-Private Partnership (PPP) to implement projects and Islamic finance options, such as sovereign *Sukuk*. A well strategized revenue diversifying framework is thus a priority for these countries in order to sustain fiscal spending levels in the medium and long term.

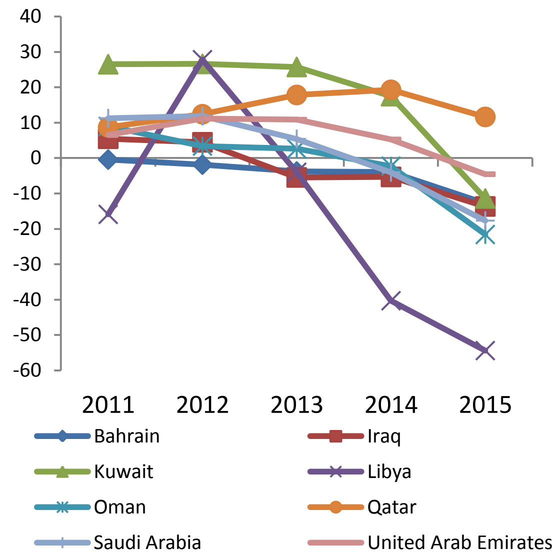
Figure 4: Tax revenue (Panel A) and Primary balance (Panel B) in Arab 'oil-rich' countries (% of GDP)

A. Tax revenue (% of GDP)



Source: IMF (2016b).

B. Primary balance (% of GDP)



Source: IMF (2016a).

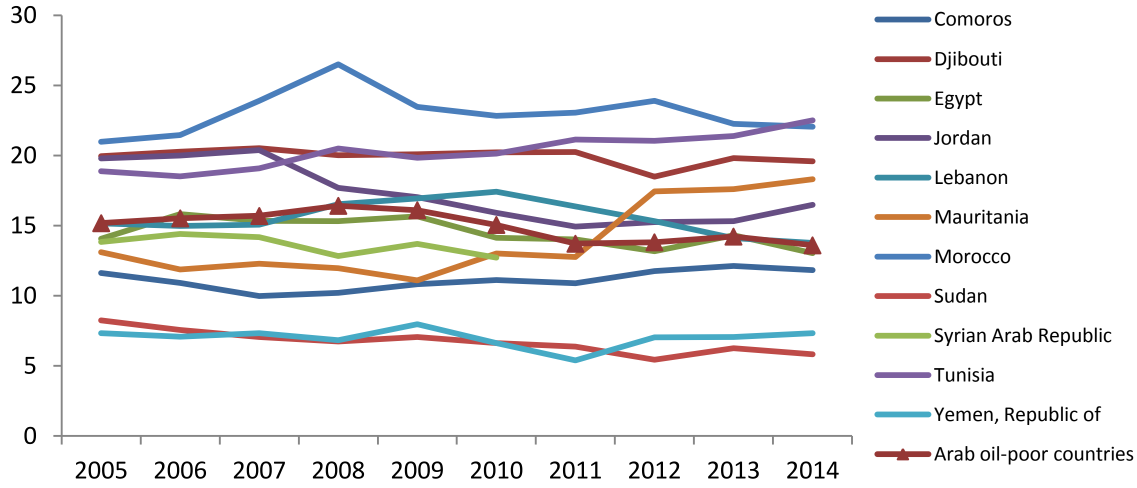
B. 'Oil-poor' countries: Tax reforms toward improving progressivity and tax fairness is a priority

The major source of revenue in the 'oil-poor' countries is taxes but its share to GDP is much lower in most of these countries than the world average of about 15 per cent. In Sudan and Yemen, the share of tax to GDP is significantly low at 6 per cent and 7 per cent respectively.

[10] ESCWA, 2016b.

The share varies between 10 to 20 per cent in other countries except for Morocco where the tax revenue as percent of GDP is the highest at 23 per cent (Figure 5). The trend of the share of tax to GDP has been largely stagnant in most countries over the past ten years or so, except for Mauritania, Morocco and Tunisia, which witnessed a slight increase in the trend during the same period. It may be noted that Morocco was experiencing a high increase in share of tax to GDP until 2008, but after that there has been a drop in the share. In general, Arab countries are below their potential in raising taxes and many Arab countries have the potential capacity to mobilize additional revenue through tax reforms, in particular through improving enforcement and increasing tax bases while taking into account equity.[11]

Figure 5: Tax revenue (% of GDP) in Arab 'oil-poor' countries

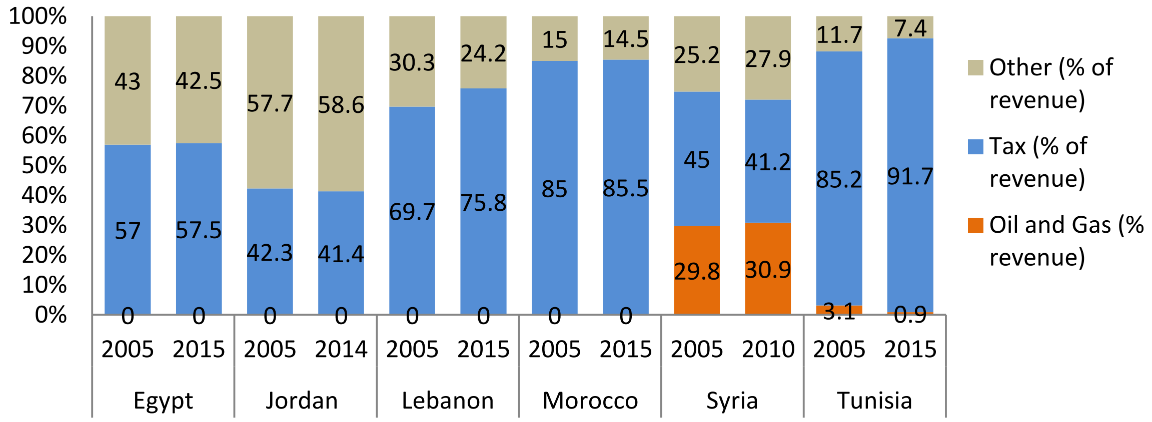


Source: IMF (2016b).

There is wide variation in the share of tax revenues in total revenues across the 'oil-poor' countries (Figure 6). The highest tax collections, at over 85 percent of total revenues, are recorded in the two Maghreb countries: Morocco and Tunisia during 2005 and 2015. Egypt and Lebanon also mobilize majority of their revenues from taxes. Mobilization of taxes in Jordan, however, is comparatively lower at about 42 percent of the total revenue in 2015.

[11] ESCWA 2014b.

Figure 6: 'Oil-poor' countries: Share of tax revenue and hydrocarbon-based revenue



Source: Author's calculation based on data compiled from Central Bank/Ministry of Finance of each country.
Note: "Other" revenues include all other revenues minus taxes and oil and gas revenues.[12]

Disaggregation of total taxes into its components indicates that indirect tax constituted the main source of tax in all the tax systems of 'oil-poor' countries. In some cases, such as in Jordan, indirect taxes constitute around 71 percent of total tax revenue in 2014 (Figure 8). Further, Jordan and Morocco show increasing share of indirect taxes in the total tax revenue during the same period. The issue is that in the major diversified economies of the 'oil-poor' countries, such as Egypt, Jordan and Morocco, the share of income tax in total tax revenue remained either stagnant or declined over the years between 2005 and 2014. In Tunisia, however, the share of income tax in total taxes showed some improvement during the same period. Nevertheless, major contribution to tax revenue has come from taxes on goods and services in all the four countries, which tend to be regressive in nature than that of direct taxes. For instance, a recent study on tax incidence analysis in Jordan shows that the lower 40 per cent of the population end up paying a larger share of budget in terms of indirect taxes as compared to the higher decile groups.[13] Further, evidence on implementation of value-added tax (VAT) across the countries suggests that multiple tax exemptions and rates often reduce equity in the administration of VAT and burdens the poor and the middle class more than the richest sections of population.[14]

In addition to low significance of income tax, wealth tax constitutes a negligible share of total tax revenue in most countries in the region. Among the four countries in the Figure 7, Morocco has relatively higher share of earnings from property tax, which increased from 3.5 percent of tax revenue in 2005 to 7.4 percent in 2014. In Egypt, the contribution of wealth tax

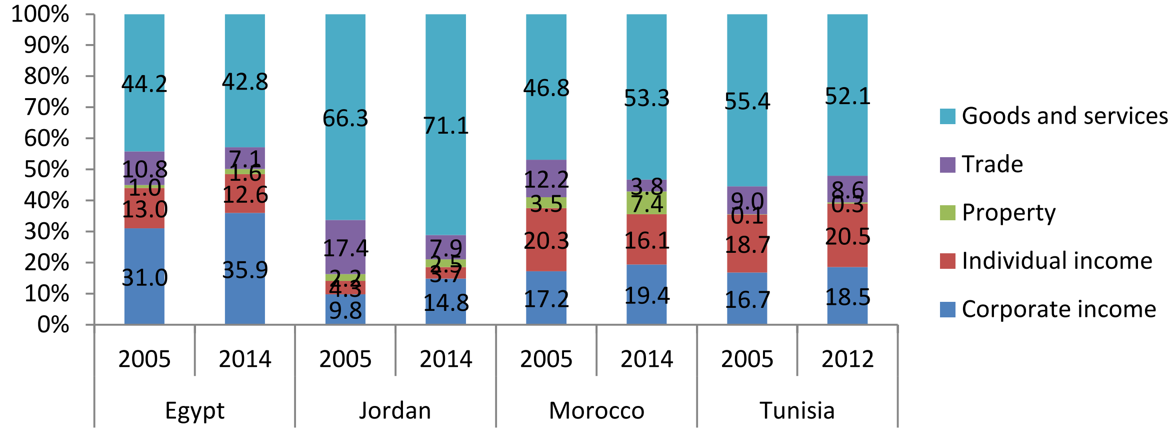
[12] For instance, in Jordan, "other" revenues include social contributions (11.8%), grants (12.4%), repayments (0.2%) and the rest (34.2%), such as "fees", "licenses", "capital revenues, interest and profits", "mining revenue" and the rest not specified.
[13] Sarangi et al 2015.
[14] IMF 2015.

in total tax revenue increased meagrely from 1.0 percent in 2005 to 1.6 percent in 2014. The share of property tax is negligible in Egypt, although there is evidence of increasing inequality within the country. A Credit Suisse (2014) report estimated that wealth Gini was 0.80 in Egypt in 2013, making Egypt among the countries which experienced the fastest rise in wealth inequality in recent years. A study by van der Weide, Lakner and Ianchovichina (2016) estimated the top tail of the income distribution in Egypt by a method of combing the top tail of the house price listing with that of the income distribution. They noted that the Gini coefficient for urban Egypt is found to increase from 0.36 to 0.47 after correcting for the missing top tail. Property tax can be considered as a useful tool of correcting imbalances in any society, improving tax fairness as well as it can be a major potential source of revenue. Globally, taxes on property form around 7 per cent of total tax revenue, which is much higher than the average in Arab countries.

Another important observation is that the share of trade tax has declined over time in the developing countries of the Arab world, as shown in the figure 7 and figure 8.[15] The region being highly reliant on imports, a large segment of trade tax is expected in the form of tariff revenues. The decline in the tariff revenues in these countries can be reasonably linked to the trade liberalisation policies adopted by the governments and their accession to WTO.[16] For instance, Jordan's accession to WTO since 2000 significantly lowered the share of tariff revenues, which decreased from 30 per cent in 1999 to 17 per cent in 2005, and then to 8 per cent in 2014.[17] Similarly, decline in tariff revenues can be noted for other countries accessing WTO, including Egypt, Morocco and Tunisia. In addition to accessing WTO, they have also joined several other trade liberalization agreements, such as Agadir Agreement, GAFTA, and Bilateral trade agreements in the recent past. In fact, the countries in the region that have not joined WTO, such as Lebanon and Algeria, have also reduced their customs duties as part of trade liberalisation policies. For instance, Lebanon reduced its dependence from customs duties by switching to introduction of VAT since 2002. The overall decline in the share of trade tax revenue (as % of GDP) across the countries in the region, as a proxy for tariff revenues, can be seen as reducing importance of a crucial domestic resource at the hands of governments, as these economies embrace trade liberalisation measures.

[15] The trade tax includes customs and other import duties, taxes on exports, profits of exports or import monopolies, exchange profits, and exchange taxes (IMF GFS).
[16] Egypt, Morocco and Tunisia accessed WTO in 1995; Jordan accessed WTO in 2000.
[17] ESCWA (2016a).

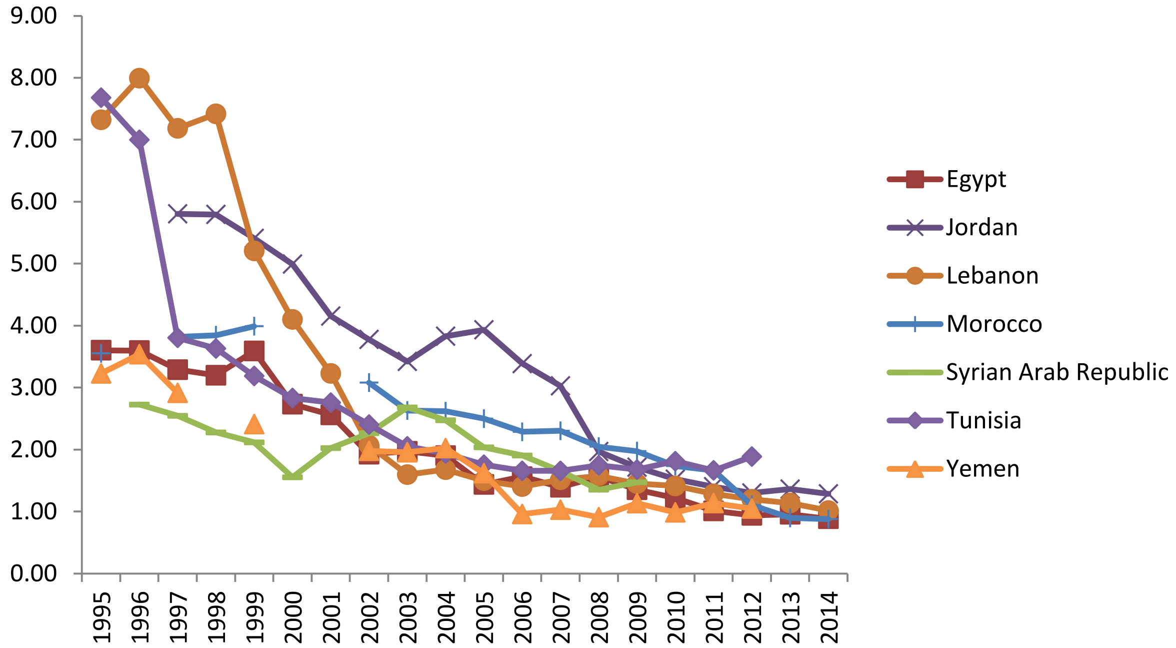
Figure 7: Composition of tax revenue in selected 'oil-poor' countries (percent share)



Source: Author's calculation based on IMF (2016b); Ministry of Finance of respective countries

Note: Property tax in Morocco belongs to closest year to 2014.

Figure 8. Declining trends in trade tax revenue (% of GDP) during 1995-2014



Source: Author's calculation based on IMF (2016b).

As noted above, the domestic fiscal stance of most 'oil-poor' countries is weak. On top of it, the development deficits widened in these countries particularly in recent years due to conflicts in several parts of the region. With insufficient international support to tackle the refugees, the rising debt in some of these countries is increasingly becoming a concern. Despite repeated requests from Jordan and Lebanon, international financial support for their spending on Syrian refugees has been slow in coming.[18] In Lebanon, Jordan and Egypt,

[18] ESCWA 2016b.

which have high debt to GDP ratio at 139%, 92% and 88% respectively in 2015, are experiencing fiscal deficits to GDP at a rate of -8.9%, -4.0% and -11.7% respectively (Figure 9A). Egypt's primary deficit to GDP is at -4.9% in 2015, and most 'oil-poor' countries except Comoros and Lebanon are facing negative primary balance in 2015 (Figure 9B).

In this situation, a typical solution by the IMF policy suggests fiscal consolidation with a focus on shrinking government expenditure in the short and medium term. Typically, during fiscal consolidation episodes, policymakers cannot reduce current expenditure, e.g. wages & salaries, so they turn to capital expenditure. Reducing public investment would drastically affect key public services in health, education and infrastructure. In addition, expenditure reduction policies may be adopted for tailoring social expenditure to more targeted category, including cutting subsidies and other public transfers. These policies may improve macroeconomic imbalances but such one sided measures will neither benefit growth nor will it benefit unemployment and poverty reduction.

The impact of fiscal consolidation on output growth has been studied extensively by several scholars in the recent years, prominent studies among those are by Alesina and Aldagna (2010), Alesina et al (2015) and Kleis and Moessinger (2016). Looking into a period between 1985-2014 in 16 OECD countries, Alesina et al (2015) concluded that the effects of fiscal consolidations depend on their design, whether those are tax-based or spending-based adjustments, with the former being more costly than the latter. According to the authors, the output losses associated with the latter are very small, on average close to zero. According to IMF (2010), fiscal consolidation policies typically reduce output and raises unemployment in the short term. It can be harmful to output growth subsequently if monetary policy is not positively responsive to offset the costs associated with spending cuts. A recent study by Kleis and Moessinger (2016) looked into the evolution of post-consolidation trajectories of economic growth in six case studies of OECD countries. They concluded that the results do not offer clear-cut evidence on the long-run effect of fiscal consolidation on economic growth. Half of the case studies point to a positive effect with the other half indicating a negative effect on economic growth trajectories. They also could not find any exact pattern with respect to the type of fiscal consolidation. Given this mixed results, it would be reasonable to conclude that country specific features need to be looked into in more detail in explaining the impact of fiscal consolidation measures on output and employment growth in conjunction with monetary policy.

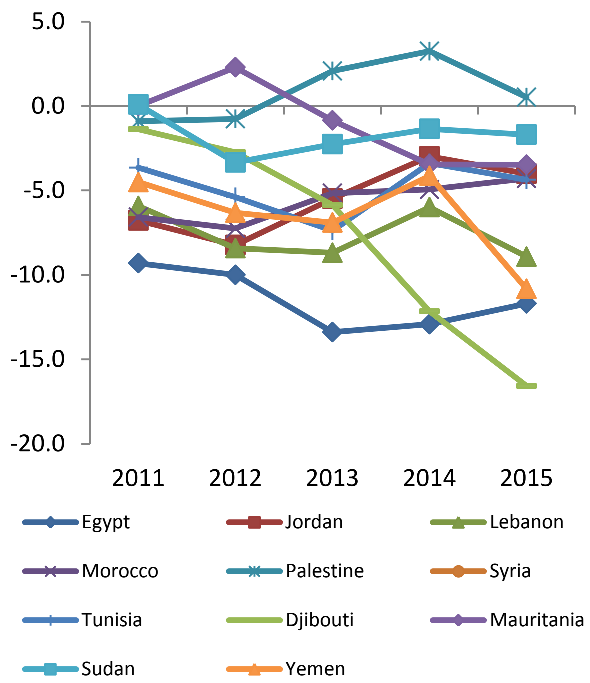
In Jordan, for example, the consequence of fiscal consolidation policy during 2014-15 confirms to reduction in growth and employment rate. Reducing expenditure on social sector spending (% of GDP) since 2013, Jordan's fiscal balances and debt to GDP ratio improved to some extent but economic growth and employment rate declined during 2014-

15.[19] As monetary policy is constrained due to pegged exchange rate in case of Jordan and in other Arab economies, except for Egypt that recently allowed exchange rate to float since November 2016, monetary policy response is likely to be zero.[20]

Therefore, a more comprehensive and well strategized macro-fiscal framework is needed, which takes into consideration both expenditure and tax reforms in a way that enhances fiscal space for meeting the public expenditure needs for spending on social protection or other development indicators related to the SDGs and for achieving potential growth rate in the Jordanian economy. Even with best of their efforts whether they can mobilize enough resources for financing the SDGs is another question. In this context, some of the key inherent constraints that affect growth and domestic resources sustainability are narrated in the next section.

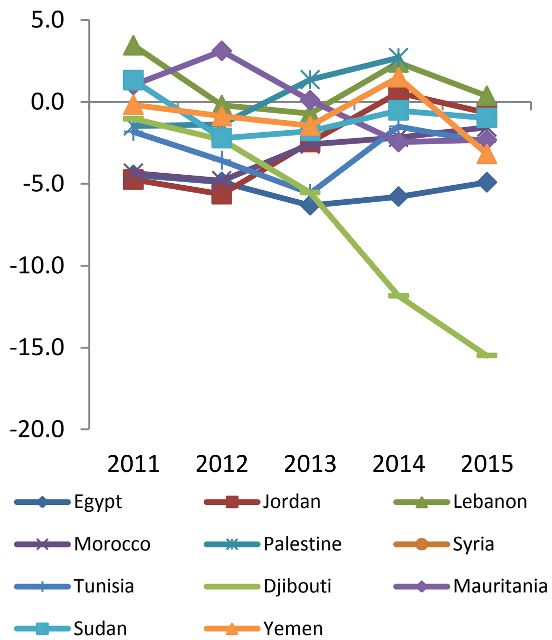
Figure 9: Fiscal and primary balances (% of GDP) in 'oil-poor' countries in recent years

A. Fiscal balances (% of GDP)



Source: IMF (2016a).

B. Primary balances (% of GDP)



Source: IMF (2016a).

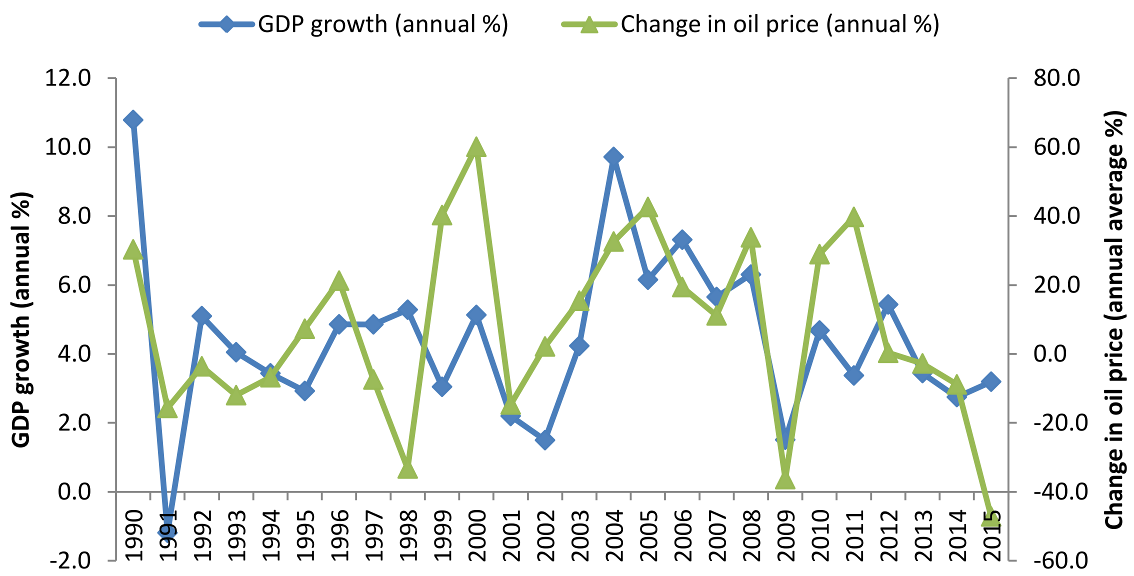
[19] The calculations on social expenditures are based on IMF GFS 2016 (See Sarangi 2016). For detail analysis, see Sarangi et al 2015.
[20] Alesina et al 2015.

3. Key challenges to growth and domestic resource sustainability

A. Volatile economic growth impacts sustainability of fiscal balances

Arab growth processes are characterized by relatively high volatility, particularly due to the reason that the growth is linked to the volatility in oil prices. While the 'oil-rich' countries are directly affected by the episodes of oil price fluctuations, they have a spill over effect through remittances and flow of intraregional development funds. The Figure 10 shows the association between economic growth and oil price changes during 1990 and 2015, which indicates significant co-movement between the two indicators.[21]

Figure 10: Correlation between growth of GDP of Arab World and change in international oil price



Source: Author's calculation based on WDI and EIA data.
Note: Oil price refers to Europe Brent Spot Price FOB Dollars per Barrel

Analysing a longer term period between 1970 and 2010, Von Arnim *et al* (2010) concluded that economic growth in both oil-rich and 'oil-poor' countries in the region is highly volatile. In the 1970s, the Arab region witnessed an impressive economic growth of 8.5% a year on average, mostly thanks to rising oil prices. Growth slowed down to an average of 1.6% in the 1980s and picked up again to 4.3% in the 1990s. It increased to nearly 5% in the 2000s, but slowed down to 3.8% over 2010-15.[22] The degree of volatility in economic growth varies across countries in the region. Only Egypt, Jordan, Libya, Morocco, Oman and Tunisia can be characterized by low volatility in growth: Egypt (with an average annual real GDP per

[21] The correlation coefficient between growth and changes in oil prices between 1990 and 2015 is high and significant statistically (around 0.5).
[22] Author's calculations based on WDI data. See also Von Arnim et al 2010.

capita growth rate of around 3.2 per cent and a coefficient of variation of 0.86), Jordan (2.5 per cent and 2.6), Libya (2.7 per cent and 1.8), Morocco (2.4 per cent and 1.7), Oman (2.6 per cent and 2.6), and Tunisia (3.0 per cent and 1.1). However, four of these six countries – Egypt, Jordan, Tunisia, and Libya -- are facing negative consequences of conflicts and political confrontation directly or indirectly, which have severely affected their economic and social achievements as well as negatively impacted their fiscal balances.

Furthermore, the fiscal constraints of the region recently suffered by the plunge in oil-prices since 2014. The sharp fall in oil-price led to a significant reduction in current account balances of the oil-exporting countries. These GCC countries that used to incur surpluses are registering negative primary balances as well as fiscal deficits in 2015, given that public expenditure is hard to respond to the sharp regression in oil revenues in the short run. Even the biggest player in OPEC – Saudi Arabia, could have only five years of financial assets remaining at the level of current spending.[23] Not only is oil wealth vital for oil-exporting Arab countries for their economic development and diversification strategies, but it is also the primary source of positive spillover to the oil-poor countries because of the intraregional flows of capital, remittances and aid from the region's major GCC oil producers. Amid intensifying geopolitical tensions in the Arab region, this pillar of regional economic stabilization and resources has started to wane. Overall, sustaining economic growth is the biggest priority of the Arab governments to ensure enhancement of fiscal space and domestic resource sustainability.

B. Lack of structural transformation impacts diversification in revenue sources

The figures 11a and 11b show the economic structure of 'oil-rich' and 'oil-poor' countries respectively since the 1990s. As expected, oil and gas and utilities dominated among all sectors and contributed more than half of the GDP of the 'oil-rich' countries in 1990. The share of oil and gas has reduced slightly by 2012, but it is still the dominant sector. The economic structure of non 'oil-rich' countries remained more diversified than the oil rich countries (figure 11b), but there as well the share of manufacturing in GDP remained low, and stagnant since the 1990s at around 12.5 per cent. There are of course variations among countries. Since 1990, in both groups, the share of the service sector has increased, while that of agriculture fell or remained negligible. The increasing share of "other services" largely indicates the share of low value-added sector activities that tend to be informal activities, which are outside of the tax net.

The lack of structural transformation also explains the nature of occupations across the region. In the absence of a developed industrial sector or modern high value-added service sector, jobs were created largely in the "other services" sectors that tend to be informal in

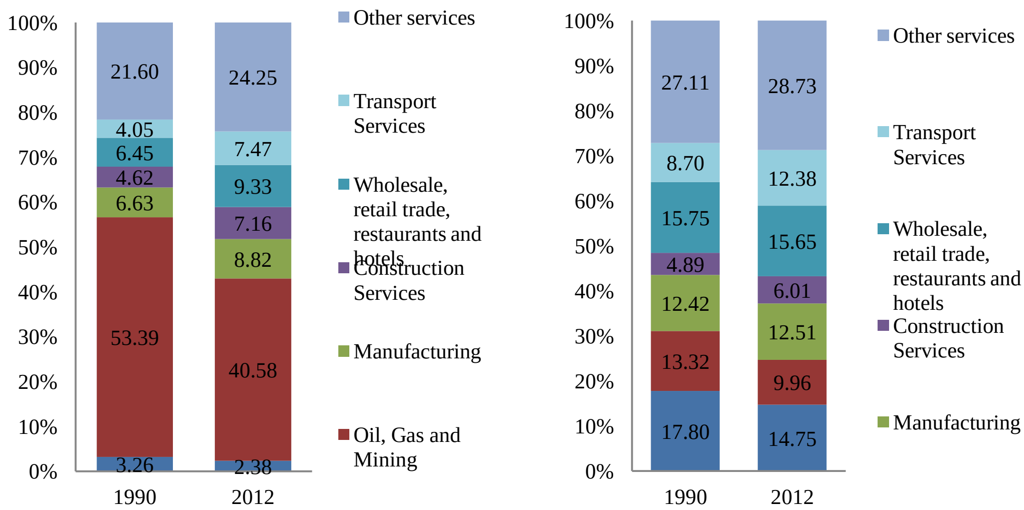
[23] Al-Darwish, et al, 2015..

nature. For instance, in 2011, 35.5 per cent of youth occupations in the middle class households in Egypt were in the "other services". The corresponding figure in Jordan was 58.2 per cent (in 2010) and 30.7 per cent in Tunisia (in 2010).[24] The presence of large informal labour markets and slow or negligible productivity gains in this region[25] are associated with lack of structural transformation.

The large prevalence of the informal sector in the region affects collection of tax revenues, in addition to negatively affecting productivity and sustainability of growth.[26] Ordonez (2014) analysed the distortions associated with presence of the large informal sector in case of Mexico and of the incomplete tax enforcement. The study summarised three main distortions. First, a misallocation of resources towards small and unproductive enterprises, as they engage in tax evasion; second, a distortion in occupational choices as unproductive entrepreneurs are attracted to the market; and third, a distortion in the capital use of informal establishments, as they reduce their scale to remain undetected. The study estimated that significant improvement in labor productivity and output growth is possible by improving tax enforcement. The conclusions of this study indicate that enforcing taxation and bringing the informal sector to the formal economy would benefit the Arab economies significantly in terms of improving growth and productivity as well as in increasing revenues of the governments.

Figure 11: Economic structure (sectoral shares in GDP)

A. Arab 'oil-rich' countries B. Arab 'oil-poor' countries



Source: Based on data from UNSD. See Sarangi, 2015.

[24] Sarangi, 2015.

[25] Between 1991 and 2012, the productivity growth rate barely exceeded 1 per cent, and was particularly low in 'oil-rich' countries (ESCWA, 2013).

[26] See a discussion on Arab region on this issue in Elbadewi and Loyeza, 2008.

C. Conflicts and political confrontation across the region cost high to economies and societies

Conflict and political confrontation in several parts of the region have exacerbated the economic growth trends, particularly since 2010. Today, Iraq, Libya, Palestine, Somalia, the Sudan, the Syrian Arab Republic and Yemen are in crises. The influx of refugees has had a negative impact on inflation, employment, the fiscal deficit and the overall economy in Egypt, Jordan, Lebanon and Tunisia, which are also facing domestic political difficulties.[27] Most 'oil-poor' countries are experiencing huge fiscal deficits since the 'Arab Spring' in 2011. Some countries increased public spending during the uprisings to satisfy protestors' demands for wage increases, subsidies and expanded social assistance. These commitments have become difficult to reverse for political reasons and added pressure on government budgets. Most recently, the ongoing crises in Syrian Arab Republic has not only resulted in huge loss of capital stock but also reversed the hard won development gains of decades (See Box 1).

The longer the conflicts in Iraq, Somalia, the Sudan, the Syrian Arab Republic and Yemen continue, the greater will be the devastation. Decades of development are being undone, adding greater misery to human insecurity. Ending conflict and occupation is a major development challenge of the region, as noted in the Arab Development Outlook: Vision 2030.[28] In addition, reforming public institutions and systems of governance and promoting economic diversification can generate widespread and decent employment and can provide a way forward toward meeting social justice and human development demands of Arab people. Development is an interdependent process with many feedback effects and loops. Therefore, enhancing fiscal space in isolation would be difficult to achieve unless the root causes of development challenges are addressed.

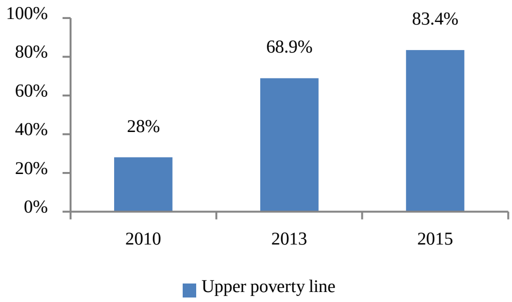
BOX 1. Poverty in Syrian Arab Republic

Falling income, widespread unemployment and diminished purchasing power mean rising poverty. Measuring poverty in Syria today is complex. It has been estimated that 83.4 per cent of Syrians now live below the upper (moderate) poverty line applied by the Government of Syria, up from 28 per cent in 2010 (figure A).A large share of the employed population may thus be considered as the working poor. This is largely because the cost of the standard food basket has risen more than threefold in nominal terms since 2010, and modest rises in nominal salaries have absorbed only 15-20 per cent of the price increases. Extreme poverty is also projected to have increased from approximately 14 per cent in 2010 to more than 50 per cent of the population in 2015.

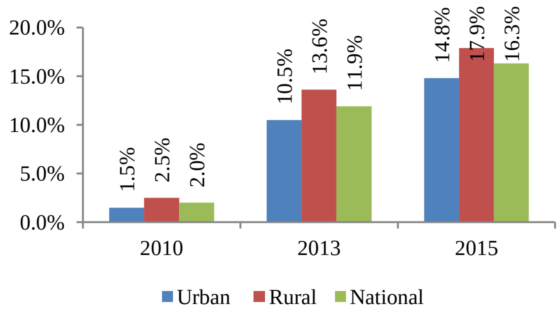
[27] ESCWA, 2015b.
[28] ESCWA, 2015b..

The poverty gap has deepened. In 2010, poverty in Syria was considered "shallow". In other words, most of the poor had expenditure that was close to the poverty line and thus relatively little effort was needed to lift them above that line. That is no longer the case. The poverty gap reached a new record in 2015 of 16.3 per cent, up from 11.9 per cent in 2013. The gap was worst in rural areas at 17.9 per cent, up from 13.6 per cent in 2013 (figure B).

(A) Population below the upper poverty line



(B) Poverty gap ratio, 2010-2015



Source: ESCWA and University of St Andrews, 2016.

Having discussed the above key development challenges in the region from the perspective of fiscal space analysis, the next section proposes key reforms that the region can consider for enhancing fiscal space through mobilising domestic resources.

4. Promoting ways for mobilizing domestic resources

Mobilizing domestic revenues is crucial to meeting the increased expenditure needs of the governments today and in the coming years in the Arab region. The analysis of revenue sources suggests that the Arab countries have significant potential to mobilize additional domestic revenues through tax reforms, in particular through improving enforcement and increasing tax bases while taking into account equity concerns. In addition, there are number of other corrective ways that can augment public resources significantly, such as reducing illicit financial flows, harnessing public-private partnerships and so on. The paper suggests some key areas of intervention in this direction, while keeping in view that implementing such measures require significant capacity development support to the countries by the international community. The paper also acknowledges that achieving peace and security in conflict-affected parts of the region is a pre-requisite to initiate any reform agenda.

A. Fair and progressive taxation

Public sector can be more efficient in resource mobilization and it can correct any major economic imbalances in the society through fair taxation. It is especially important at a time when the gap between rich and poor is rising and getting employment opportunities is hardened.[29] The Arab Middle Class Report, which was launched in 2014, showed the high and growing disparity between average expenditure of the rich and the poor as well as the middle class. Increasing wealth inequality in certain countries is also testimonial to widening economic imbalances in Arab societies. Unfortunately, property tax is low or absent in many countries.[30] Property tax in general, and taxing the top incomes in particular, can be an effective tool to improve equity in Arab societies.[31] The marginal effectiveness of property tax would be high as these taxes are low and largely evaded across all countries in the region. One of the important benefits of a well designed property tax or wealth tax in the region is to decrease rent seeking and speculative activities and hence channel funds to more productive investments. The design of it should ensure that burden of wealth tax doesn't not fall on the poor and middle class. Poor tax records and complex wealth tax procedures in certain countries make the challenge complicated to analyse tax fairness.

The tax systems across the region have so far relied largely on indirect taxes, including adoption of value-added tax (VAT) by several countries, to raise revenues. Indirect tax, by design, is regressive in nature and, therefore, the burden of taxes on middle class and the poor tend to be more than the rich, since the former constitute the largest sections of consumers in the Arab countries. It may be argued that the level of regressivity of VAT could be reduced by making basic food items and other products mainly consumed by the poor exempted from taxes. However, the regressivity cannot be eliminated. A simulation exercise of the impact of shifting the tax burden from labour to consumption (switching from direct to indirect tax) in five European countries concluded that indirect taxes are less progressive than the other components of the tax system, making the proposed measure a regressive one in any case.[32] Therefore, heavy reliance on flat VAT rate or indirect tax may contribute to increasing revenue mobilisation, as it is easy to enforce, but it would lead to aggravate the disparity between rich and poor. A study of VAT reforms in Lebanon argued that an increase in VAT rate will impact severely on the welfare of the middle class and households living just above the poverty line.[33] The estimate shows that an increase in VAT by 2 and 5 percentage points can lead to an increase in poverty by 5 and 20 percentage points. In addition, multiple rates and exemptions of luxury goods in application of VAT

[29] ESCWA, 2014a
[30] Jewel et al., 2015.
[31] Alvaredo and Picketty, 2014.
[32] Decoster et al., 2010.
[33] Salti and Chabban, 2009.

often reduce revenue efficiency and lead to poor targeting. The design of VAT and effective strategies to reduce cost of expenditure categories that bear heavily on the poor are therefore important policy considerations. Another important category of indirect tax is the excise tax. Currently, excise taxes are often poorly designed, which limits their revenue potential. More importantly, an optimal excise tax is also important for reducing negative externalities in the society.

Furthermore, the direct taxes *per se* do little to correct the increasing inequality within the countries especially if they are not progressive enough (Box 2). Jewel et al (2015) documented some of these distortionary practices in the tax systems. In the region, personal income taxes lack progressivity due to low top tier rates and exclusion of non-wage earnings. For instance, a study of top incomes in Lebanon shows that income is highly concentrated at the top end. The 0.01 per cent of the income distribution account for over 3 per cent of the total income.[34] The schedular form of the Lebanese personal income tax and the complexity of the tax laws tend to disproportionately benefit the rich, partly because they leave scope for tax evasion at the top. The study estimated that the difference between pre and post tax income narrows by moving up the income distribution, and the difference is almost non-existent at the top end.[35] The personal income tax does little to reduce the high income disparity in Lebanon.

Jewel et al (2015) also found that corporate income taxes across the region suffer from widespread exemptions, often provided in non-transparent ways and with a high degree of discretion. Exemptions and multiple tax rates often create complications in administering the tax and thus create opportunities for tax avoidance. The complex systems in taxing corporate not only erode revenues to the government but also damage the 'doing business' environment.

BOX 2: Tax incidence in Jordan

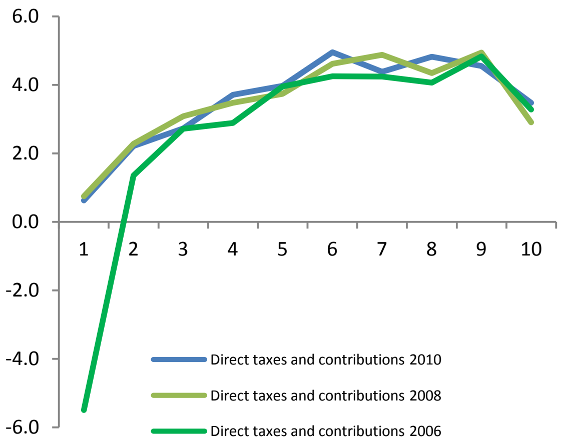
In Jordan, an incidence analysis shows that the direct taxes show mild progressivity, but only up to the 9th income decile. The highest income decile shows a decline in share of taxes to average income as compared to that of the lower income deciles (figure A). There is a need for more detail data on tax records to analyse the constraints but this finding implies that the burden of taxes on the richest decile in the income distribution tend to be less than that of the middle income deciles. In fact, many countries in the region have tax systems that

[34] Assouad 2015.
[35] Also see a critical review of tax systems in Lebanon by Nabil Abdo, Arab NGO Network for Development (Abdo 2017).

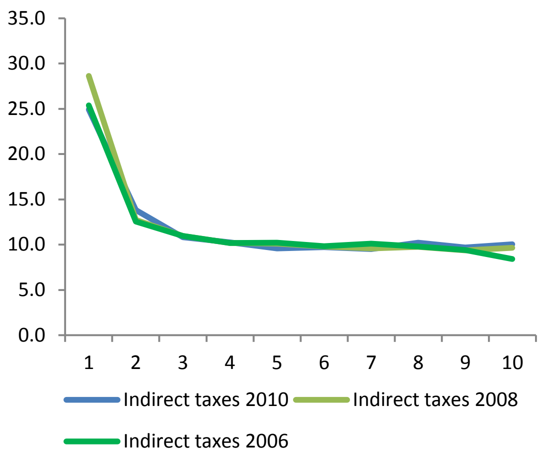
suffer from distortionary effects of either corruption or discretionary application of rules, which helps the upper-income bracket to avoid paying tax or understate their income.[36] The incidence of indirect tax shows a typical pattern where the burden lies more on the poor than that of the higher income deciles, and the pattern is consistent over the years.

Figure: Incidence of direct and indirect taxes across market income deciles

A) Incidence of direct tax across income deciles



B) Incidence of indirect tax across income deciles



Source: Sarangi et al 2015.

Given this background, there is a high potential to mobilise tax revenue through improving the fairness of tax systems by two critical policy directions: (1) increase progressivity, and (2) rationalise exemptions in all aspects of tax system (individual income tax, corporate income tax, value-added tax, excise). Experience from other countries show that direct tax progressivity can increase if there is a political will. Even among the lower-income countries, direct tax collection could increase by 2–4 percent of GDP. Similarly, in lower-income countries where VAT performance is weakest, base-broadening and improved compliance might raise something up to 2 percent of GDP.[37] What is an optimal income tax rate (or rates) and what is an optimal VAT rate (or rates) may vary from country to country and those are subjects of detail discussion and further research. There are good lessons to learn from countries that have improved their tax collection using progressivity within the overarching principles of equity. Overall, evidences from other countries suggest that fiscal policy that promotes progressive taxation and social benefits are consistently associated with lower inequality for disposable income.[38]

[36] Jewel et al 2015.
[37] IMF 2011.
[38] Woo et al 2013.

B. Taxation for incentivising economic diversification

Incentivising economic diversification and structural transformation toward high value added sectors can enhance growth and therefore it has potential to increase revenue mobilisation in the Arab region. The issue of structural transformation should be viewed from the perspective of sustainable development to ensure long-term stability of the economy as well as for sustaining the revenues.[39] Traditionally, structural transformation implies mobility from agriculture to manufacturing or services sector. In the context of Arab region, structural transformation needs to be viewed largely as mobility from low value added services to high value added services or manufacturing sectors. In most countries, there has been significant shift in labour force from agriculture to services, but most of them have ended up in "other services' that tend to be at the lower end of value added.[40] That is also implied from the evidence on large and growing informal sector activities. For the 'oil-poor' countries, promoting high value added sectors to encourage deeper structural transformation and increase productivity is critical for boosting growth and for improving formalisation of the informal sector activities. In addition, bringing the large informal sector to the formal economy is important for increasing revenues of the governments.

Structural transformation is a priority for the 'oil-rich' countries too. Creating non-oil and modern economic sectors is essential for these countries for sustaining growth and resource mobilisation in the long run. At a time of depletion of the oil and gas resources, and the economic crises due to global economic downturns, there is a need for transforming the growth process in the Arab region. Fiscal measures, including tax and non-tax incentives, can support such a transformation and economic diversification that can in turn help improving economic stability and revenue stability, as noted in case of other countries and regions. Therefore, the need to develop tax systems that support the diversification of these economies provides an opportunity to design them with emphasis on fairness, simplicity, and efficiency. This is important when global economic outlook indicates gloomy prospect for oil prices to move back to the pre-2014 level in the foreseeable futures.

C. Controlling tax evasion, tax avoidance and illicit financial flows

Corruption indicators are strongly associated with low revenue, as well as regressivity in tax collection.[41] Tackling tax evasion and illicit capital flows out of the region are important considerations in raising resources. Estimates indicate that the cumulative amount of illicit outflows for the Arab region over the period 2003-2012 account for $739.3 billion; more than

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[39] See a discussion on revenue diversification and economic diversification in Suyderhoud (1994) and Yan (2012).
[40] ESCWA, 2014a.
[41] Attila et al. 2008, cited in IMF 2011; Jewel et al., 2015.

the combined inflows of FDI and ODA to the region over the decade-long period, which was $714 billion.[42] Trade mis-invoicing constitutes a significant leakage, amounting to about 77 per cent of the total illicit flows.

Tax administration need to be simple and transparent, without complexities and exceptions that lead to tax evasion and tax avoidance. At the same time, a global standard for information exchange needs to be adopted in enforcing information exchange between different government entities to tackle illicit financial flows. In addition, there is need for improving fiscal records and their consistent reporting over time. It is not only important for monitoring tax revenues but also for tax analysis, including analysing top incomes and inequality related issues. Unfortunately, poor tax records and complex tax procedures across the region make tax compliance and tax fairness analysis more complicated.[43] Improving tax and customs administration, simplifying coding and regulation, and investing in technology and human resources can enhance tax compliance. It would certainly require upfront investment in administrative infrastructure. But over a period of time better tax administration would lead to a broader culture of tax compliance by improving formalisation of informational sector activities (Unsworth 2005).

D. Harnessing public-private partnerships (PPP)

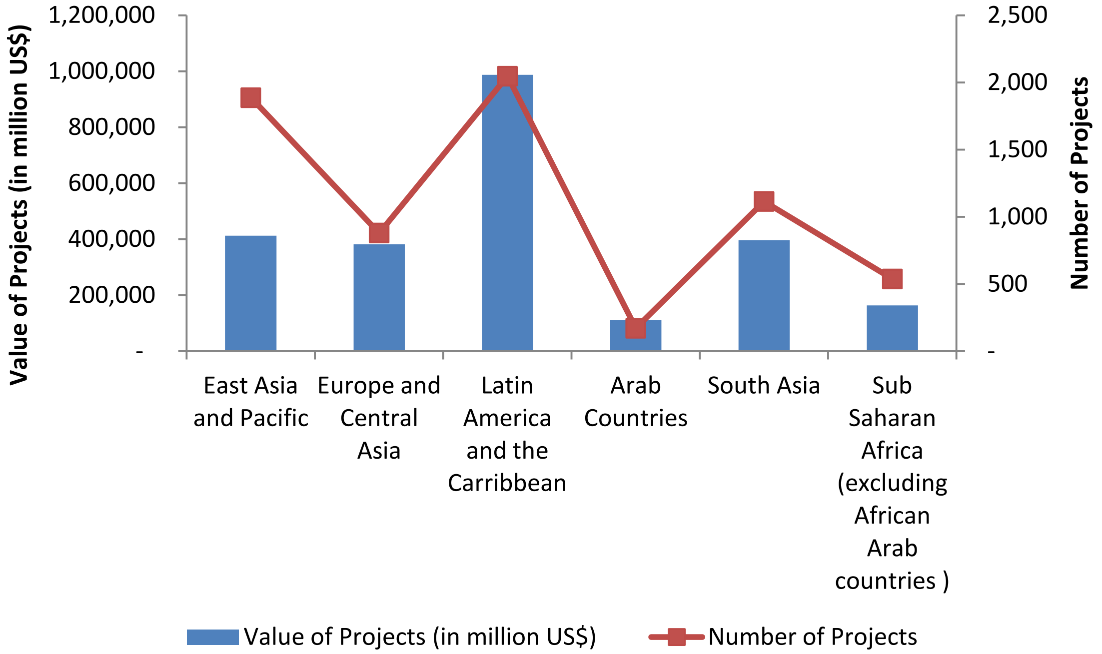
Relative to other parts of the world, the Arab region has shown a relatively poor performance in mobilizing private capital for financing larger infrastructure projects. Out of a world total of US$ 2.2 trillion, private participation in infrastructure in low and middle income Arab countries[44] reached only US$ 100 billion during 1990-2013 (Figure 12). As a percentage of GDP, the low and middle income Arab countries have one of the lowest levels for private participation in infrastructure, surpassing only East Asia and the Pacific, but their score is lower than the average of the developing countries.[45]

Most Arab countries are facing, to different extent, constraints such as: fragile political environment, lack of public consensus on the need for PPP, non existence of PPP regulatory framework, unclear division of authority among different ministries for the implementation of such projects, unclear dispute resolution mechanisms etc. National authorities can ensure to provide adequate protection to investors, for example through the right to appeal against a procurement decision to an independent judicial body. Also in order to attract investors, it is highly recommended to set up an independent monitoring authority/auditor to

[42] ESCWA, 2015d.
[43] See Alvaredo and Picketty 2014.
[44] Excludes high income countries such as Bahrain, United Arab Emirates, Saudi Arabia, Qatar, Kuwait and Oman.
[45] See ESCWA, 2015c.

investigate PPP procurement practices and help rule out any conflict of interest in the dealings of the contracting authority.

Figure 12: Private sector participation in infrastructure in low and middle income Arab countries



Source: World Bank (2016).

For the Arab region to make full use of PPPs, most countries require an intense overhaul of the regulatory framework. It is advisable that governments establish specific PPP laws with a clear definition of PPPs, the scope and type of arrangements they intend to pursue with the private sector. PPP laws should clearly identify terms and conditions under which public assets can be pooled with private funds, and provide financial security instruments suitable to external investors. PPP Units are vital for delimitating roles and responsibilities, yet in the Arab region only Egypt and Kuwait have established a PPP unit.

Other sources of private finances for public investments in the region include Islamic bonds (*sukuk*), and remittances. The *sukuks* are well-suited to channel the growing global pool of Shariah-compliant capital to fund infrastructure, clean and renewable energy and climate change projects. On attracting remittances and their utilization for public investment, three major challenges persist: the absence of national strategies and policies to channel remittances to development; the relatively weak financial and institutional infrastructure supporting remittances; and the lack of sufficient data/information on workers' remittances.

5. Conclusion

The Arab region comprises diverse countries on many counts. On average, the share of revenues (excluding grants) to GDP of the region is about 36 per cent, which is slightly lower than that of the average of the 'advanced economies' in 2014. Between 2005 and 2014, the average ratio has remained mostly above that of the 'advanced economies' but the volatility of the revenues in the Arab region is apparent as compared to that of the 'advanced region' or any other region of the world. Depending on the swing in international oil prices, the revenues to GDP share goes up or down. For instance, the recent plunge in oil prices since 2014 has led to decline in the revenue to GDP ratio of the region.

From the standpoint of sources of revenue mobilisation, the region can be referred as two clusters of countries: 'oil-rich' and 'oil-poor'. The 'oil-rich' countries primarily rely on oil and gas revenues and their reliance on tax and other non-oil revenues is negligible. For instance, Kuwait mobilised over 70 per cent of the total revenue from oil and gas sector in 2014. Several other 'oil-rich' countries mobilise above 50 per cent of total revenue from oil and gas. On the contrary, the 'oil-poor' countries rely on diverse source of revenues, but mainly around 50 percent of their revenue is collected from indirect taxes. There is high disparity between 'oil-rich' and the 'oil-poor' countries in terms of their average revenue to GDP ratio and its variation overtime. The average ratio for the 'oil-rich' countries is around 40 per cent in 2014, which is above that of the 'advanced economies' but the trend shows large swings, particularly due to fluctuations in oil prices. The 'oil-poor' countries perform poorly in mobilising revenues and the trend shows a decline over time since 2008 in particular. Excluding the grants, their average revenue to GDP hovers around 20 per cent in 2014, which is lower than most regions in the world, even that of the emerging market and developing economies.

Among the 'oil-rich' countries, United Arab Emirates and Algeria show high percentage of tax to GDP, 19 per cent and 32 per cent respectively in 2014, which indicates the diversification of their revenue sources although they are resource rich countries. Among others, tax revenue as a percentage of GDP varies from as little as less than 1 per cent in Bahrain to 6.5 per cent in Qatar in 2014. Among the 'oil-poor' countries, the tax revenue as percent of GDP is the highest at around 22 per cent in Morocco and Tunisia in 2014. In Sudan and Yemen, the share of tax to GDP is significantly low at 6 per cent and 7 per cent respectively. The share varies between 10 to 20 per cent in other countries. The low tax to GDP ratio in many Arab countries as compared to world average indicates significant potential to mobilize additional domestic revenue by improving tax fairness and tax enforcement.

There are several key constraints to growth and domestic resource sustainability in the Arab countries. The fast and foremost is the concentration on oil sector, which results in the high volatility in growth. Low productivity gains, lack of creation of modern non-oil sectors, and loss of revenues due to plunge in oil prices since 2014 have affected resource sustainability significantly. Above all, long years of conflicts and crises since 2010 in several parts of the region have not only resulted in loss of capital but also wiped out decades of development gains. The region stands at a situation where fiscal constraints are high and development challenges are many.

Rising to the challenges of mobilizing domestic public resources requires greater need to effectively use all sources of finance (public and private), as per commitment of governments in the AAAA. Among some of the key policy areas, the governments may consider reforming tax systems such as promoting fair and progressive taxation, incentivizing fiscal framework that promote economic diversification, controlling tax evasion, tax avoidance and illicit financial flows. Tax fairness and progressivity is also important for improving social justice and lowering the economic inequalities in society. Administrative reforms for greater tax compliance would certainly require upfront investment in infrastructure, but that would support a broader tax compliance culture and the long run prospects of enhancing fiscal space domestically. Innovative ways of harnessing public-private partnerships (PPP) is also essential for the Arab governments to address fiscal constraints in specific projects.

In addition to finding ways and means of raising revenues, expenditure reforms are important considerations for building fiscal space. The fiscal frameworks need to be well strategized in integrating revenues and expenditures – the two sides of the fiscal balance. The real challenge is to analyse the benefits or distortionary effects of tax and expenditure policy proposals in the process of developing any macro-fiscal framework. As noted in the previous sections, this paper has discussed some policy proposals with a focus on raising domestic revenue mobilization. A detail analysis of expenditure-based policy reforms require another study and therefore left beyond the scope of this paper.

Overall, the contemporary economic situation of the Arab countries calls for expansionary macroeconomic policies in order to progress toward achieving the SDGs. But many countries are facing increasing fiscal deficits in recent years, which forces them to adopt fiscal consolidation policies, particularly expenditure reducing policies, in order to improve macroeconomic balances. A caution is that such one-sided policy would have distortionary effects and it can cause more harm than good, as discussed in the previous section of the paper. Giving importance to the two sides of the fiscal balance in formulating policy, with a proper analysis of policy simulations, can minimize the distortions and benefit output as well as fiscal space. Increasing domestic revenue mobilization by all possible means is a priority for most countries in the region. Simultaneously, fiscal expenditures can be spent efficiently to promote the target of economic diversification and increase revenue mobilization in a long term perspective. Finally, any fiscal framework should consider long-term growth and stability of the economies in the region, not just temporary fixes, and address the root causes of fiscal and larger development challenges, which are not isolated from one another.

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Annex

Table 1: Tax and non-tax sources of revenues in 'oil-rich' countries

'oil-rich' countries		Oil and Gas (%GDP)	Total revenues: Oil and Gas (% revenue)	Total revenues: Tax (% of revenue)	Non-oil revenues: Tax (% of Non-oil revenue)	Non-oil revenues: Income and profits tax (% non-oil revenue)	Non-oil revenues: Indirect tax (% non-oil revenue)
Algeria	**2005**	31.1	76.3	20.8	87.7	23	23.7
	2010	24.2	66.1	29.5	87.2	37.8	17.6
	2014	19.7	59.2	36.3	89.2	37.6	13.9
Bahrain	**2005**	21.1	75.7	9.2	37.9	-	-
	2010	19.2	85.1	8.2	55.3	-	-
	2015	13.9	78.1	11.0	50.2	-	-
Iraq	**2005**	-	-	1.2	-	0.5	0.7
	2010	43.6	85.2	1.9	12.6	-	-
	2012	54.3	97.6	2.2	91.8	-	-
Kuwait	**2005**	54.9	94.4	1.8	32.0	7.6	-
	2010	60.3	92.8	1.5	20.6	5.6	-
	2015	29.8	88.1	3.4	28.4	7.1	-
Libya	**2007**	61.5	91.1	2.6	29.1	-	-
	2010	54.3	90.6	3.7	38.8	-	-
	2014	38.0	92.7	3.1	42.2	-	-
Oman	**2005**	29.8	78.8	7.5	35.3	8.3	-
	2010	28.4	80.8	8.9	46.7	18	-
	2015	26.4	78.7	12.1	57.0	23.4	-
Qatar	**2005**	40.5	70.6	-	-	-	-
	2010	34.3	62.1	-	-	-	-
	2014	43.7	48.7	-	-	-	-

Saudi Arabia	**2005**	41.0	89.4	-	-	-	-
	2010	33.9	90.4	-	-	-	-
	2015	18.8	72.5	-	-	-	-
UAE	**2005**	16.8	77.4	4.7	20.9		-
	2010	16.2	60.2	9.3	23.5		
	2014	18.6	63.9	13.5	37.3		

Note: * The 2015 figures for Kuwait and Oman are provisional data; - implies NA
UNSTAT GDP data is used for all countries up to year 2014. The 2015 GDP data are taken from IMF-WEO.
Source: Compiled from Central Bank/Ministry of Finance of each country.
Iraq was compiled from ESCWA DATA.

Table 2: Tax and non-tax sources of revenues in 'oil-poor' countries

'oil-poor' countries		**Oil and Gas (%GDP)**	**Total revenues**			
			Oil and Gas (% revenue)	**Tax (% of revenue)**	**Income and profits tax (% revenue)**	**Indirect tax (% revenue)**
Comoros	**2005**	-	-	58.3	-	-
	2010	-	-	38.1	-	-
	2014	-	-	49.5	-	-
Djibouti	**2006**	-	-	58.0	27.4	27.8
	2010	-	-	57.1	26.3	27.9
	2015	-	-	58.0	23.6	27.7
Egypt	**2005**	-	-	57.0	23.8	23.6
	2010	-	-	56.2	25.3	22.1
	2015	-	-	57.5	24.4	23.1
Jordan	**2005**	-	-	42.3	6.6	23.7
	2010	-	-	45.7	9.3	29.6
	2014	-	-	41.4	7.7	28.1
Lebanon	**2005**	-	-	69.7	15	27.1

	2010	-	-	83.0	17.1	29.8
	2015	-	-	75.8	21.2	27.3
Mauritania	**2006**	7.4	13.0	20.8	5.7	9.6
	2010	1.1	5.3	57.4	17.1	31.2
	2015	0.9	2.9	59.0	-	-
Morocco	**2005**	-	-	85.0	35.7	32.4
	2010	-	-	88.4	35.6	38.3
	2015	-	-	85.5	36.7	37.4
Palestine	**2010**	-	-	51.4	3.8	32.4
	2015	-	-	68.6	3.0	41.4
Somalia	**2013**	-	-	58.8	0.6	5.1
	2014	-	-	50.8	0.7	5.8
	2015	-	-	43.1	2.4	5.4
Sudan	**2007**	10.9	54.4	35.4	5.0	30.4
	2010	5.7	41.6	48.3	5.5	42.8
	2013	2.0	18.6	70.3	5.0	65.3
Syria	**2005**	7.0	29.8	45.0	16.6	1.3
	2009	5.1	21.3	48.3	21.0	1.4
	2010	7.0	30.9	41.2	12.8	1.6
Tunisia	**2005**	0.7	3.1	85.2	31.1	54.1
	2010	0.7	2.8	85.7	34.0	51.7
	2015	0.2	0.9	91.7	38.8	52.9
Yemen	**2005**	20.6	67.8	25.6	14.7	10.9
	2010	16.1	60.3	25.1	12.1	13.0
	2012	15.4	44.0	22.7	11.0	11.8

* The 2015 figures for Morocco and Tunisia are provisional data; - implies NA

UNSTAT GDP data is used for all countries up to the year 2014. The 2015 GDP data are taken from IMF-WEO. For Somalia, GDP data is taken from 2015 ARTICLE IV CONSULTATION-Somalia. For Palestine, GDP for year 2015 is taken from PMA.

Source: Compiled from Central Bank/Ministry of Finance of each country.