Rethinking Inequality in Arab Countries

Overview

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Economic and Social Commission for Western Asia

Rethinking Inequality in Arab Countries

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Foreword

Policy makers in the Arab region are confronted with a significant knowledge deficit on inequality issues, which is paradoxical, given that social and economic equality concerns have received considerable attention in constitutions and development policies of Arab countries.

Realising importance of addressing this knowledge gap, the Economic and Social Commission for Western Asia (ESCWA) and the Economic Research Forum (ERF) partnered to “rethink” the stylised “facts” of inequality in Arab countries, with the aim of presenting a holistic narrative of its main determinants and consequent policy considerations.

Using a multidimensional approach that focuses chiefly on the non-income dimensions of health, education and living conditions, the report shows that the Arab region has achieved significant human capital gains, accompanied, generally, with decreasing outcome inequalities. However, unfortunately, these gains were not closely matched with a decline in inequality of opportunity. Furthermore, the human-capital pool remains a largely untapped economic resource, resulting in stagnating per-capita incomes and rising income inequality.

The report argues further that these socioeconomic inequalities ensue from structural and institutional deficits. Arab economies tend to be disproportionately concentrated in low-value-added unproductive sectors. This is manifested in labour market informalisation, low productivity and poor growth outcomes. Moreover, the rentier nature of Arab economies has also resulted in socioeconomic arrangements that systematically favour the interests of those with more influence.

Furthermore, the report underlines the escalating fragility of rent-based growth and development models, in view, particularly, of the evolving global patterns in oil markets; patterns that should impel adopting a new enabling political-economy framework for reducing poverty and inequality.

In effect, Arab countries need to go beyond temporary fixes to address the root causes of endemic development challenges. This, in turn, depends, crucially, on achieving two strategic objectives; namely, capitalising on the youth bulge through structural transformation and reforming institutions, which in itself is also a prerequisite for structural transformation. Additionally, good governance would make for prudent policy design that effectively targets the disadvantaged and reduces poverty and inequality, while simultaneously ensuring a competitive thriving economy capable of absorbing the young and capitalising on the abundant human capital; all of which would foster political stability and enhance human development and economic growth.

It is our hope that this report would stimulate public policy discussions of inequality issues in the Arab region and lead to concrete measures that rise to the mounting challenges.

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Background Papers

Khalid Abu-Ismail *Inequality in Arab States* (later published as Abu-Ismail (2019b), see Bibliography)

Khalid Abu-Ismail and Manuella Nehme *Political Economy of Rents in the Arab Region*

Bilal Al-Kiswani *Socioeconomic Determinants of Inequality*

Valentina Calderón-Mejía and Belkacem Ayachi *Violent Conflict and Multidimensional Inequality in the Arab Region*

Mesbah Fathy Sharaf and Ahmed Shoukry Rashad *Inequality of Opportunities in Child and Maternal Health in the Arab World: What New Can We Learn?*

Verena Gantner and Khalid Abu-Ismail *Inequality in Health Outcomes*

Verena Gatner and Manuella Nehme *Inequality in Education Outcomes*

Zahraa Langhi *Gender inequality in Deprivation in Conflict Torn Libya*

Rana Hendy and Nejla Ben Mimoune *Inequality of Opportunity in Education*

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Arab country codes

Country	Alpha-3 code
Algeria	DZA
Bahrain	BHR
Comoros	COM
Egypt	EGY
Iraq	IRQ
Jordan	JOR
Kuwait	KWT
Lebanon	LBN
Libya	LBY
Mauritania	MRT
Morocco	MAR
Oman	OMN
Qatar	QAT
Saudi Arabia	SAU
State of Palestine	PSE
Sudan	SDN
Syrian Arab Republic	SYR
Tunisia	TUN
United Arab Emirates	ARE
Yemen	YEM

Alpha-3 country code is based on the ISO 3166 international standard.
Available at https://www.iso.org/obp/ui/#searc.

1. An Integrated Multidimensional Approach

Arab policy makers face a significant knowledge deficit on inequality issues. Addressing this gap requires an approach that is at once integrated and multidimensional. An integrated approach adopts a holistic interpretation of both empirical results and how economic, social and institutional determinants interact to yield inequality outcomes, while multidimensionality embraces a conceptual framework and employs measurement tools that address the multiple overlapping facets of inequality, such as of outcome, opportunity, gender and wealth stratification. Fortunately, availability of harmonised data for twelve Arab countries enables undertaking an integrated multidimensional analyses for the first time, with the ultimate aim of "rethinking" the inequality narrative in Arab countries and building a case for inequality-focused inclusive development policy.

A. The case for rethinking inequality in Arab countries

Generally, inequality, particularly in income, is thought to be relatively low in the Arab region, with conventional wisdom attributing this to the statist development policies that, from the 1950s to the 1990s, addressed equity concerns through mechanisms such as social transfers, public employment and large investments in infrastructure. Indeed, since the 1960s, the Arab region has experienced consistent improvements in human development levels. Yet, inequality is perceived as a major underlying factor of the 2011 uprisings. The World Bank calls this the 'Arab inequality puzzle'.

However, the mystery is unraveled when inequality is examined from a wider perspective. When data on income, taxes and wealth from a variety of sources are combined, pieces of the puzzle fall in place to give a bigger picture, revealing that income inequality in the region is significantly higher (indeed, the largest world-wide, as reported by the World Inequality Report 2018). The real mystery, however, is how little we know about this issue, despite its centrality to socioeconomic and political economy outcomes of Arab development over the past few decades. The main question, therefore, is: what is the status of inequality in its multiple forms, and how did it evolve over the past few decades? A second and more challenging task is to interpret inequality trends and relate them to socioeconomic policies and institutional dynamics. As argued below, answering these questions requires an integrated multidimensional approach to inequality.

B. A multidimensional view

Income provides only a partial unidimensional view of inequality, and is, therefore, insufficient for addressing the multiple overlapping deprivations caused by inequality in other fundamental spheres of social capability and political participation; a task that requires a multidimensional approach, after Sen's capability approach, with enhancing human capabilities as a primary objective.

According to Sen, the debate is not only on the desirability of equality but also on the dimension along which equality is required or sought. In such a context, the real question is "*equality of what*". By extending analysis beyond the dimension of income and looking at the distribution of other key aspects of human development, including education, nutrition, health and living conditions, this report is largely compatible with Sen's capability approach. Another position adopted in this report is to consider, where possible, inequality of opportunity as equally important as outcome inequality.

This attention is well justified. Inequality of outcome does not account for individual responsibility for outcomes. Moreover, there has been recently a growing consensus that societies seeking social and economic justice, or equity in living standards, should promote equality of opportunity by compensating inequalities arising from 'circumstances' beyond the control of the individual, while simultaneously letting individuals bear the consequences of actions or "efforts" for which they can be held responsible. Nonetheless, the best way to reduce inequality of opportunity is to address inequality of outcome, since both are correlated with living standards where the individual is born affecting their future outcomes.

Using household demographic and health surveys for twelve Arab countries, the report assesses inequality, in both opportunity and outcome, among selected social, economic, spatial and demographic groups (rich and poor, men and women, rural and urban, educated and non-educated, etc.). In order to identify the most vulnerable population groups, the analysis also considers combinations of various characteristics, such as wealth ranking of household in combination with education of household head, or location of household in combination with family size. Finally, no discussion on inequality in the Arab region can be complete without addressing intercountry inequalities.

C. An integrated conceptual framework

Understanding inequality dynamics calls for not only a multidimensional empirical lens, but also a wider conceptual framework. When inequalities ensue from structural and institutional deficits reinforcing social and economic arrangements that systematically favour the interests of those with more influence, the outcome may be rigid poverty and inequality trends; i.e., an inequality trap. Connecting the dots provided by the multidimensional inequality lens could provide a basis for a coherent narrative on inequality determinants, thus paving the way for remedial policy conclusions.

To reach this goal, we rely on an integrated human development centred political economy approach. The cycle would thus begin with human capital improvements resulting from gains in health and education, as reflected in the non-income HDI. Capitalising on these human capital improvements, an inclusive development process would necessarily entail a sustained economic growth process with decent employment and structural transformation at its core, as witnessed, for example, in successful post-World War II Asian development experiences. This endogenous and employment friendly growth process would automatically translate into reduction in income inequality and poverty and thus an expansion of the economic middle class. The latter would allow the State to enhance its fiscal space for social and development expenditure which would feedback into sustained improvements in human capital with further gains and reductions in inequality in human capital, thereby necessarily expanding the social middle class. Finally, the successful operation of this inclusive development process assumes a minimum level of institutional strength and good governance that would systematically improve along with the transition from low to medium to high levels of human development. Institutional strength is, therefore, cross-cutting, in the sense that it allows all other elements of the model to function properly.

In this report, we work within this analytical conceptual framework, asking whether this cycle functions properly or whether there are impaired links in one or more of the causal chains, with implications for inequality results. For example, in many Arab countries some inequalities tend to be rigid notwithstanding impressive average growth and human capital achievements. This implies the existence of structural inequalities requiring shifts in development policy.

The dataset used covers four conflict-afflicted countries: Iraq (2011), Libya (2014), the State of Palestine (2014) and Yemen (2013), which are the latest surveys available at the time of writing. Particularly, for Yemen, we acknowledge that the figures do not reflect current conditions, for eruption of civil war in 2015 and its rapid escalation since have had a detrimental impact on human life and socioeconomic infrastructure.

2. Human Capital: Gains and Declining Inequalities of Outcomes but Less Equal Opportunities

Generally, the Arab region has experienced considerable human capital gains over the last two decades, coupled with decreasing outcome inequality, but these improvements were not matched by commensurate reduction in inequality of opportunity. Wealth and education of household head are increasingly critical determinants of the health and education opportunities of the individual, despite a decline in outcome inequality in both, which indicates that efforts are not rewarded by upward social mobility rewards. Closing gender inequality gaps have also not translated into economic and political participation gains for women.

A. Inequality of outcome and inequality of opportunity are not moving in tandem

Inequality in health and education outcomes is a mixed bag of results, depending on the indicator and type of inequality considered. The Arab region had significant improvement in health and education, as reflected in the positive average annual growth rates of the corresponding indicators (figure 2.1). With few exceptions in conflict afflicted countries, these improvements were coupled with decreasing outcome inequalities (figure 2.2). Nonetheless, gaps between the richest and the poorest wealth quintiles, as well as among other socioeconomic groups, remain wide.
In contrast, inequality of opportunity, measured by the dissimilarity index, reveals some incongruence, with more incidences of increasing inequality in human capital over time, particularly with respect to higher educational attainment (figure 2.2). For both inequality of outcome and inequality of opportunity, more progress has been realised in reducing health gaps than in education. The highest average annual reduction in both forms of inequality was achieved by Morocco in skilled birth attendance, while the highest increase in inequality was recorded for Yemen in stunting.

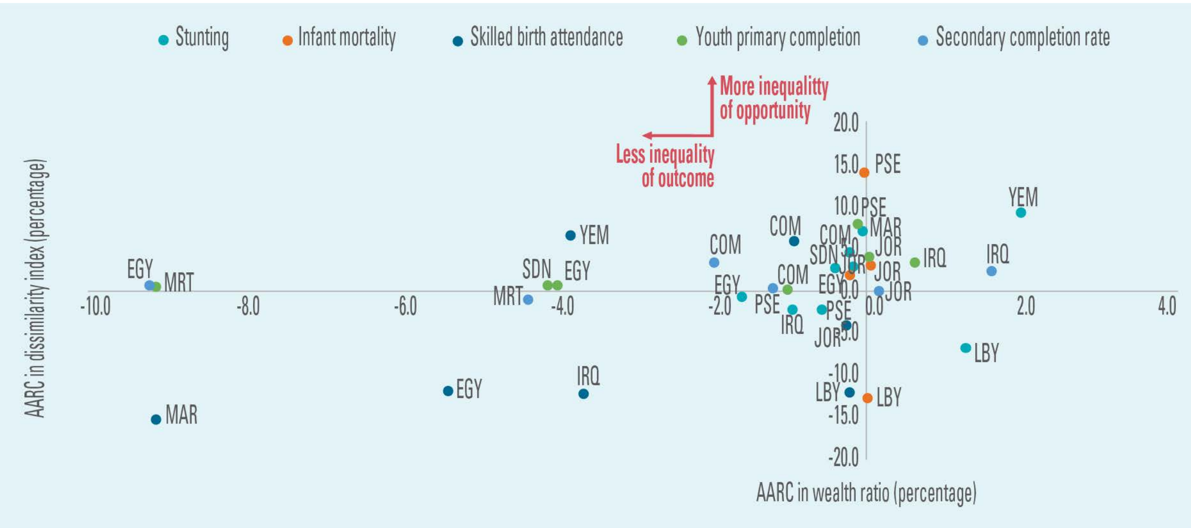
B. Poorest countries incurring highest inequality burdens

In practice, it is often difficult to disassociate poverty from inequality. The Arab multidimensional poverty index (MPI) developed by ESCWA (2017) indicates that, generally, Arab countries with a higher level of multidimensional poverty, particularly the LDCs, tend to also have higher levels of inequality in both outcome and opportunity (figure 2.3). This association is conspicuous for certain health indicators, such as full immunisation of children and skilled birth attendance (SBA). For instance, levels of inequality in outcome and inequality of opportunity in child immunisation in the Sudan, for which MPI exceeds 44 per cent, are almost twice and 9 times, respectively, those of a middle-income country, like Jordan that has an MPI below 5 per cent. Such variation is even more evident in SBA. While Jordan has reduced inequality of opportunity in SBA to near zero, the dissimilarity index of the Sudan is more than 50 times that of Jordan. Similar observations apply to educational outcomes and opportunities, especially when considering indicators for attending school and average years of schooling. Such observations suggest that multidimensional poverty and multidimensional inequality should be addressed simultaneously.

Figure 2.1 Average annual rate of change (AARC) in selected indicators

Source: Authors' calculations.
Note that all indicators are reported as achievements; hence, the wealth ratio measures richest to poorest quintile.

Figure 2.2 Average annual rate of change (AARC) in dissimilarity index and wealth ratio for selected indicators



Source: Authors' calculations.
Note that all indicators are reported as achievements; hence, the wealth ratio measures richest to poorest quintile.

Figure 2.3 Multidimensional poverty and inequalities in health and education

Source: Authors' calculations.
Note: MPI values are taken from Arab Multidimensional Poverty report E/ESCWA/EDID/2017/2.

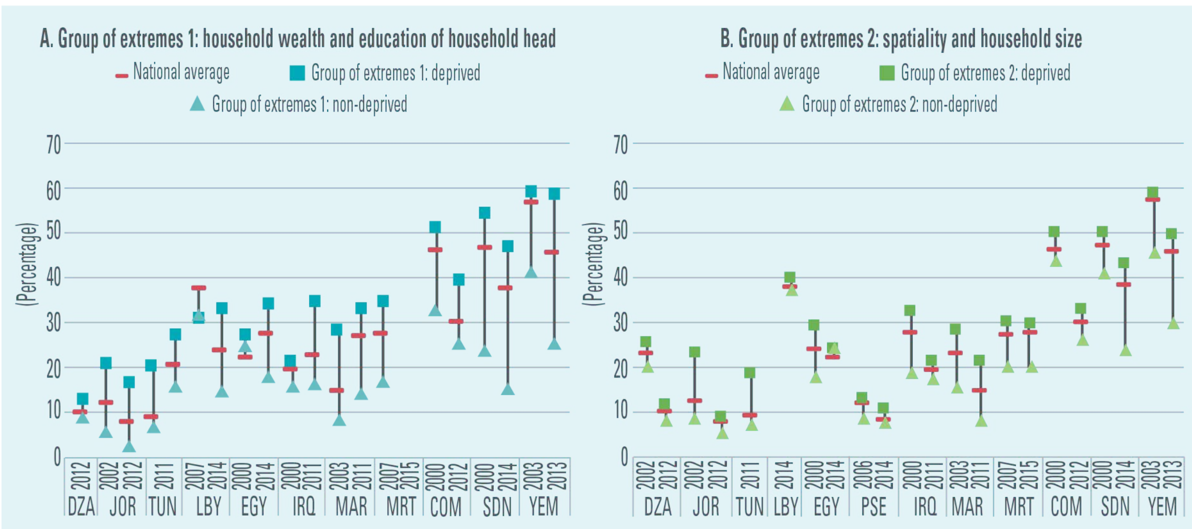
C. Inequalities in health

1. Significant progress in basic health indicators coupled with a downward trend in inequality of outcome

Analysis of two important determinants of health outcomes; namely, improved water supply and sanitation, show that access has improved in the Arab region, yet still varies across the countries. While some middle-income countries nearly achieved universal access to improved water supply and sanitation, the least developed countries (LDCs) still lag. In terms of inequality, most countries generally show declining trends between different socioeconomic groups. Despite a closing rural-urban gap, low coverage of water and sanitation still affects more rural areas and inequalities are persistent, particularly in the LDCs. Moreover, overall, progress is lower and inequalities are higher in access to improved sanitation relative to access to improved water supply. In access to maternal healthcare, Arab countries have had improvements in skilled birth attendance rates, accompanied with decreasing inequalities. Middle-income countries show nearly universal coverage of maternity care and little variation across different subgroups. The LDCs, most noticeably Yemen, however, still lag, with persistent inequality gaps between different sub-groups. This is particularly evident for groups of extremes, with wide gaps for the group combining wealth and education of household head.

Consideration of inequalities in child health outcomes; namely, mortality and malnutrition, also provides key insights. Arab countries have seen an appreciable decline in infant mortality rates (IMR) coupled with decreasing inequalities, yet spatial and wealth gaps persist. Gaps with respect to educational level of household head are rather moderate in countries with higher IMR, while countries with lower IMRs have larger gaps. In terms of malnutrition, prevalence of stunting has also declined over time for most countries. Rate of stunting in Yemen reached about 46 per cent in 2013, as numbers had been declining over time, yet the current conflict in the country must have subverted these positive trends and the rate is likely to have worsened. In terms of inequality, most middle-income countries have little disparities between subgroups, while the LDCs have larger and persistent gaps. Inequality gaps between groups of extremes have also widened considerably, indicating that progress is not reaching the most vulnerable groups adequately (figure 2.4).

Figure 2.4 Prevalence of stunting by group of extremes



Source: Authors' calculations.

While stunting is more pressing in the LDCs, results for child overweight are mixed, for its prevalence seems to affect both middle-income countries and LDCs. Incidence of overweight decreased in most countries; yet its prevalence is approximately 15 per cent in many middle-income countries, such as Egypt and Tunisia, and is nearly 30 per cent in Libya. Additionally, several Arab countries, including LDCs such as Comoros and non-LDCs such as Libya, were affected by the double burden of malnutrition, defined as the coexistence of high stunting and overweight rates. Overweight shows no clear pattern in term of inequalities; it seems generally higher in households with educated heads, but the link between education and child overweight is ambiguous. Data for groups having combined characteristics also show that, in many countries, rates of child overweight in rich households with educated heads are higher.

In terms of gender, health outcomes for children under five show minor gaps generally favouring girls, which may be partly due to biological factors. For instance, boys tend to have higher stunting levels than girls, as boys are more vulnerable to malnutrition. Nonetheless, girls are more affected when cultural factors exist. During conflict times, for example, malnutrition is likely to surge due to food insecurity and deterioration of access to improved water and sanitation. In this setting, favouritism towards boys may increase, which, in turn, may lead to more food resources allocated to the boys in the family. In Iraq, for instance, exposure to conflict appears to be associated with a higher likelihood of stunting and severe stunting, as well as with reinforced gender inequalities. Although boys appear more prone to stunting in baseline data, exposure to both low- and high-intensity conflict increases vulnerability of girls significantly, while vulnerability of boys increases only in times of high-intensity conflict.

Girls are also more vulnerable to cultural factors as they grow up. For instance, child marriage (before the age of 18) may have devastating impact on a girl's mental and physical health including pregnancy complications that may, in some cases, lead to death. Child marriage decreased significantly over time for most Arab countries; nonetheless, its incidence remained very high in conflict-afflicted areas and the LDCs. Additionally, sociocultural norms and perceptions may affect women's lifestyle and result in long-term health issues, such as obesity. Female obesity incidence in the MENA region is the highest in the world, with a regional average of 26 per cent, compared with 15.7 per cent for men. Referred to as the "Middle Eastern gender health inequality paradox" (Costa-i-Font and Gyori, 2018), this phenomenon may be linked to prevalent family roles: men are active in the labour market and generally outside the house, while the main role of women is within the house.

2. Mixed evidence on inequality of opportunity in health

While outcome analysis generally shows downward trends in inequalities, inequality of opportunity shows higher incidence of increasing inequality, suggesting that the two inequality measures are not necessarily moving in tandem in the region. Health opportunity and its main driver vary widely among countries. Yet, in general, inequality of opportunity persists in the Arab region, and in many countries, inequality of opportunity in infant mortality, stunting and child immunisation increased over time. Skilled birth attendance shows most consistency among the selected indicators, with both types of inequality declining, except in few LDCs and conflict-affected countries. Moreover, Shapley decomposition shows that socioeconomic background, especially wealth and education of household head, remains key in determining health opportunities, while contribution of child sex to inequality in health opportunity is generally minimal in the Arab region (figure 2.5). Further, re-computation of the inequality of opportunity while disaggregating education of household head by gender shows that in recent years, education of the mother is gaining more importance than that of the father in affecting positively the health and well-being of their children.

Figure 2.5 Shapley decomposition for infant mortality and stunting (Percentage)

Source: Authors' calculations.

D. Inequalities in education

1. Highest improvements in achievement and inequality reduction in education are markedly at the primary level (population aged 6-25)

Primary attendance and completion rates for youth have generally witnessed substantial progress and inequality reductions between different socioeconomic groups, reflecting Arab countries' commitment to attaining universal primary education. Nonetheless, primary completion rates show considerable reduction in progress relative to attendance rates. Countries that have a high primary net attendance ratio do not necessarily have a high primary completion rate. Lower primary completion rates can thus indicate low or delayed entry into a level, high drop-out or repetition rates, late completion, or a combination of these. Similarly, while progress in completion was accompanied with decreasing inequalities, present gaps between different socioeconomic groups are wider than in attendance rates. Both primary attendance and completion show a reduction in progress for children deprived in multiple socioeconomic dimensions in several countries.

Examining the secondary education cycle leads to three conspicuous findings. First, across all countries, attendance and completion rates are reduced at the secondary schooling relative to primary schooling. Secondary completion rates for youth are characterised by very low achievements in most countries. This may raise a concern, since at least a lower secondary education is needed in the Arab region to have the foundational skills necessary for finding work with decent wage (UNESCO, 2013). Secondly, as in the case of primary education, secondary completion rates are much lower relative to attendance rates. Thirdly, large gaps persist between different socioeconomic groups across both the LDCs and others. The wide persistent gaps in the Arab LDCs, along with the higher deprivation rates, reflect the double burden these countries face.

The gender gap is fairly low in the above-mentioned indicators. However, youth completion rates show a wider gender gap relative to attendance rates, with girls generally having lower completion rates. This differential between attendance and completion rates may signal a dropout incidence that is common for both boys and girls, though reasons may sometimes differ. For instance, boys' school dropout is commonly associated with having to work and earn income to support their families, whereas though economic reasons are also relevant for girls, they may also be vulnerable to sociocultural factors, such as persistence of child marriage, as well as social favouritism towards investing in boys' education.
In addition, conflict environments have impaired the safe-learning environment and exacerbated economic conditions, particularly for poor and lower-middle income households, leading to increased risks of dropping out of school among children. Moreover, conflicts have created unique challenges in terms of gender. Refugee policies in certain host countries translate into gender disparities that discourage school enrolment of adolescent girls. Yemen had been making great strides towards achieving universal education. However, due to conflict, there has been a substantial decline in overall enrolment rates, especially for girls, reflecting to a certain extent exacerbation of child marriage rates and favouritism towards boys during conflict.

Figure 2.6 Shapley decomposition for primary and secondary completion, age group 6-25 (Percentage)

Source: Authors' calculations.

2. In contrast to declining outcome inequalities, inequality in education opportunities is rising at both primary and secondary education levels (population aged 6-25)

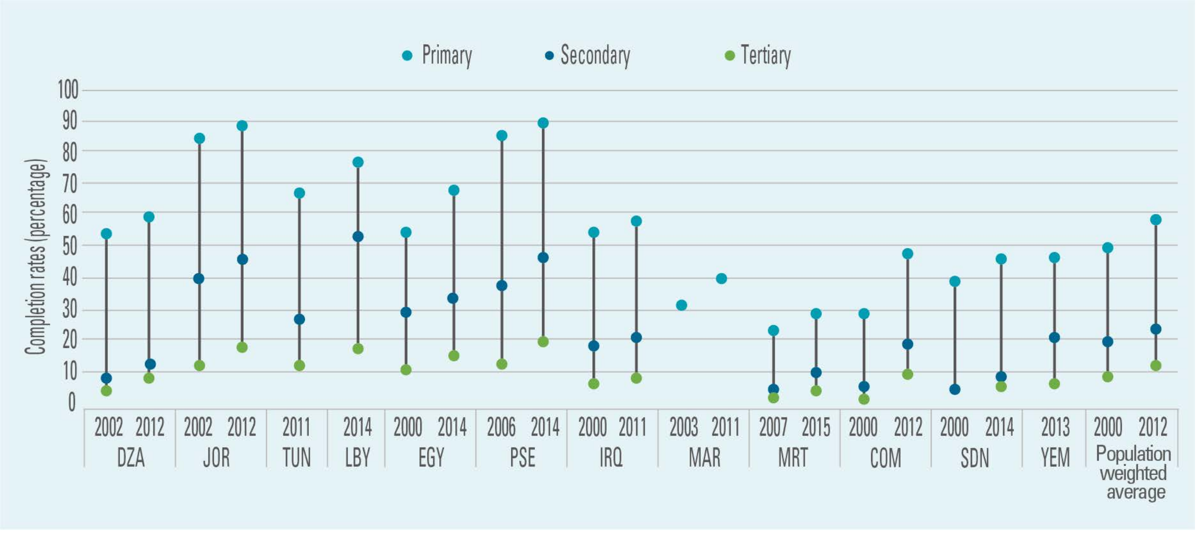
As in the case of health, incidence of inequality of opportunity in education is higher than that of inequality in outcome. Inequality of opportunity in ever attending school is fairly low across all countries and has decreased over time. However, the LDCs still have slightly higher degrees of inequality. Although individuals from different backgrounds stand equally in terms of entering school, inequality of opportunity soars when considering completion rates, especially at higher education levels. This trend is homogenous across the countries examined. Even in middle-income countries such, as Jordan and Algeria, that achieved nearly complete parity in ever attending school, the dissimilarity index (D-index) at primary completion exceeds 40 per cent. Moreover, inequality of opportunity grows larger at secondary completion, with the D-index surpassing 60 per cent in most countries. In addition, all these countries, including middle income countries, had worsening dissimilarity indices for primary and secondary completion rates over time. For instance, in Egypt and Tunisia, the government provides free higher education, yet scholars such as Assaad (2010) and Krafft and Alawode (2018) argue that public spending on higher education is regressive and has in effect subsidised the education of the better off at the expense of the disadvantaged. In essence, the contrast between the low inequality of opportunity in ever attending school and the increasingly high inequality of opportunity in completing primary and secondary education may signal the high drop-out incidence in the Arab countries. The Shapley decomposition further shows that wealth and education of household head continue to be the primary determinants for opportunity of academic progression (figure 2.6). Further disaggregation of household head education by gender of household head reveals that an educated mother plays a more important role in school attendance by children, and, particularly, in completion of primary and secondary education. Additionally, contribution of gender to inequality of opportunity in education is was fairly moderate in the region, indicating that females are largely on a par with males in education.

3. Progress in achievements and inequality reduction are lower at higher education for population aged 25 and above relative to primary education

A comparable picture emerges when educational attainments for the adult population are assessed. Primary completion rates increased significantly in nearly all countries, but have been persistently modest in the LDCs, falling below 50 per cent and even below 30 per cent in Mauritania (figure 2.7). Completion rates at the secondary and tertiary levels are significantly lower. Notwithstanding a positive trend, secondary completion rates are quite heterogeneous across countries, ranging from as low as 9 per cent in the Sudan to 47 per cent in the State of Palestine and Jordan and 54 per cent in Libya. The tertiary cycle underwent minor developments, yet its outlook remains the least favourable. Low tertiary completion rates in the Arab region may signal inadequate educational quality that may have prompted a brain drain effect, as students seek higher education abroad. As for inequality, at the primary level, most countries have closed gaps between the various socioeconomic groups, but at the secondary and tertiary levels, gaps either remained stable, or, in more cases, increased.

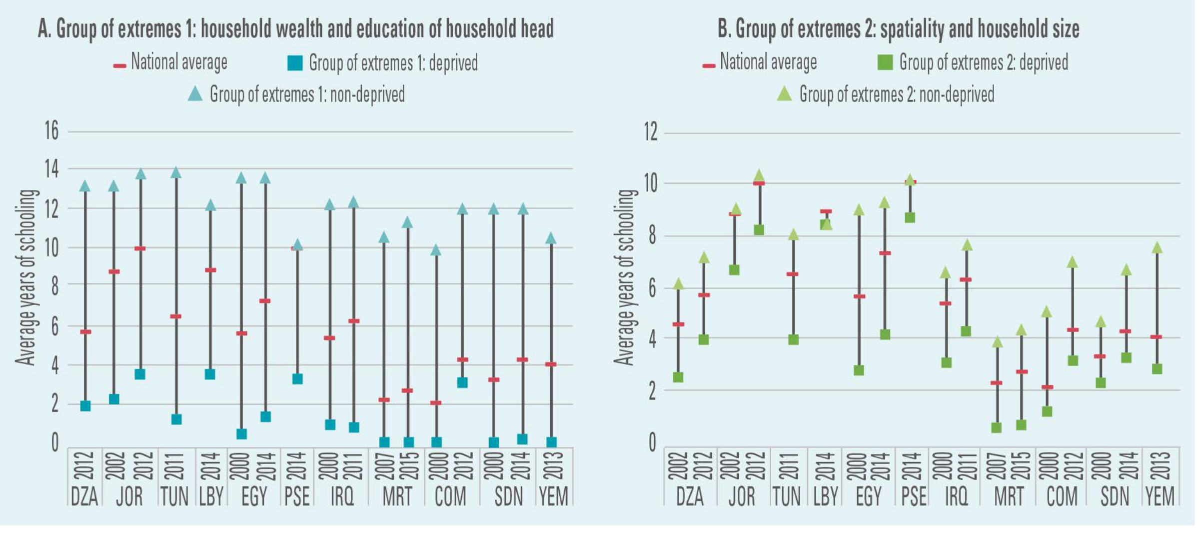
Generally, completion rates are regarded as inputs to human capital accumulation in society, while average years of education can be regarded as their proxy outcome. Average years of education in the Arab region has increased steadily to reach approximately seven, yet this regional average is still inadequate for securing a prosperous and equitable future for the youth, especially relative to their peers in developed countries. Moreover, while all the countries examined made progress in average years of education, intraregional heterogeneity is still wide, with the LDCs faring worst.

Figure 2.7 Completion rates



Source: Authors' calculations.
Note that in the case of Morocco in 2011, the data did not allow the construction of secondary and tertiary completion. For these indicators, the figures in the earliest year (2003) are not reported in the graph. The completion rates in 2003 are: 13.58 for secondary level and 3.54 for tertiary level.
The reported population weighted average includes only the countries with data across the 2 points in time.

Figure 2.8 Average years of schooling by group of extremes



Source: Authors' calculations.

Inequality patterns are very similar to completion rates. While inequalities are generally reducing, wide gaps persist, especially between wealth quintiles and with respect to education of household head. Composite data on groups of extremes substantiate these findings, as they show lingering large gaps, especially for group of extremes 1 that combines wealth and education of household head (figure 2.8). Interestingly, assessing inequality by wealth reveals that in some middle-income countries and the LDCs, average years of education for the middle quintiles falls below the national average, which suggests that wealth may impact educational achievement.

4. Deficits in education achievements are conspicuous when quality challenges are factored in

The substantial improvements in access to education over the past decades in Arab countries have not been matched with improvements in quality of education. TIMSS 2015 data show that average math and science scores for 8th graders in the Arab region generally fell below minimum proficiency standards, even in the oil-rich countries. However, there are intra-regional disparities in educational quality. While some countries, such as the United Arab Emirates, Bahrain, and Qatar, experienced improvements in test scores, several others, such as Saudi Arabia, Kuwait and Egypt, had declining test scores over the past years. Using TIMSS 2015 data for 8th graders, World Bank (2018a) shows that, on average, Arab countries lose between 2 to 4 years of schooling when quality and learning are factored in. Using the same dataset, ESCWA (2018c) assesses the inequality in accessing quality education in Arab region and finds that Arab countries, including oil-rich countries, have higher inequalities than their counterparts. In fact, Egypt has the highest inequality levels in the world sample. However, higher inequality of scores in the Arab region are not necessarily related to inequality of opportunity. Two plausible explanations are suggested by the study. First, given the fairly moderate circumstantial inequality in the region, luck and effort play a larger role in test score differentials. Secondly, and more compellingly, although better financial means allow children to enrol in private institutions, they do not necessarily guarantee an enabling-learning environment. This underlines deficiency in the overall educational systems that may lead to poor labour market prospects and the need for promoting inclusive quality education, as articulated in SDG 4, rather than mere educational access.

5. The educated female cohort remains an untapped human capital in the Arab region

Analyses of inequality of outcome and inequality of opportunity show that females are largely on a par with males in terms of human capital. Yet, these gains are not reflected in labour market outcomes, with women in Arab countries lagging extremely behind their male counterparts and behind women in the rest of the world. Female labour force participation rates (LFPR) in Arab region have been generally stagnant since the 2000s, with the rate of approximately 21 per cent in 2018 being one of the lowest worldwide. In that year, 18.7 per cent of females in the labour force were unemployed, compared with 6 per cent for females globally and around 7.7 per cent for males in Arab countries. In addition, female employment in the Arab region is characterised by high levels of informality and vulnerability, with many women engaged in unpaid domestic or even agricultural work. Around 80 per cent to

90 per cent of unpaid care work in Arab countries is undertaken by women, yet this remains largely overlooked in standard measures, such as LFPR. This uneven distribution of domestic work between men and women may create a barrier to participation of women in the labour force, since working women may face the “double-burden” of household and work responsibilities. Further, despite some declining trends, with 32.3 per cent of all working women in the region being in agriculture, the sector remains a primary source of female employment. Such informalities render women vulnerable, with low wages and inadequate social protection. Moreover, in the region, the public sector remains the primary source of formal employment, particularly for women who have less chances of finding decent jobs in the formal private sector. Indeed, the female share in full-time employment in the formal private sector is only around 15.4 per cent, which is almost half of that of the world average. In countries with high labour market informality, fiscal capacity constraints limit the ability of the public sector to absorb new labour market entrants; thus increasing incentives for job informality, especially for women, leading to widening the gender wage gap. Coupled with low economic participation, females in the region suffer low political participation, with women making only around 19 per cent of members of parliament on average, which is significantly below the global average of 24 per cent.

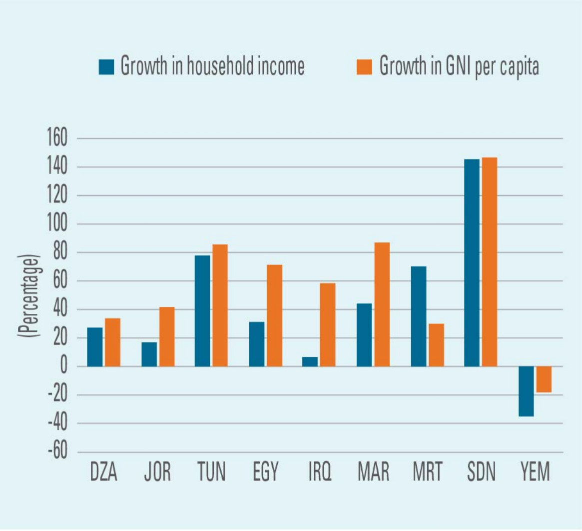
3. **Income:** Low Growth, High Inequality and Rising Poverty Risk

Improvements in health and education did not translate into major improvements in growth of per capita income at the national level, which was modest by global comparison. Quite the opposite, evidence suggests a trend of stagnating household income, along with high- and rising-income inequality, regardless of how the latter is measured. The implication is that the growth process over the past two decades, accentuated by armed conflicts in some countries and their regional spillover effects, has been associated with rising poverty risk, vulnerability and a shrinking middle class. This conclusion, however, is highly sensitive to selection of measurement tool.

A. Growth in national income not trickling down to households

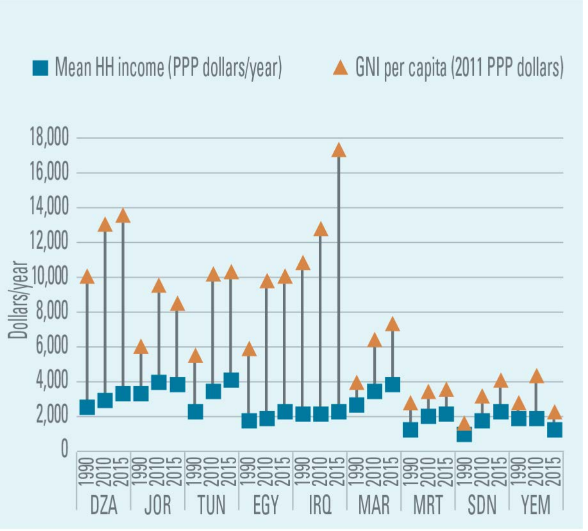
Although per capita income (2011 PPP dollars) for Arab countries grew by 50 per cent over the period from 1990 to 2017 to reach $15,700, most of the growth took place in the decade from 1990 to 2000. Over the period from 2000 to 2017, per capita GNI rose by only 30 per cent, the second lowest growth rate after Latin America and the Caribbean. Moreover, Arab countries did not grow evenly. Per capita income more than doubled (from $4,893 to $11,217) for the most populous group of medium human-development countries but only slightly increased for the (mainly oil rich and GCC) very high and high human-development groups that had by 2000 already reached comparatively high levels of per capita income worldwide. Interestingly, growth was fastest in the low human-development group, which more than doubled per capita income from 1990 to 2010. However, since then, mainly due to conflicts, growth in this group has deteriorated significantly.

Figure 3.1 Growth in GNI per capita (2011 PPP dollars) and household income, 1990-2015



Source: Household income levels are based on World Bank PovcalNet database. Available at http://iresearch.worldbank.org/PovcalNet/povOnDemand.aspx (accessed on 23 September 2019) and GNI per capita levels are based on UNDP, Human Development Data (1990-2017). Available at http://hdr.undp.org/en/data (accessed on 23 September 2019).

Figure 3.2 GNI per capita levels versus household income (Annual)



Source: Household income levels are based on World Bank PovcalNet database. Available at http://iresearch.worldbank.org/PovcalNet/povOnDemand.aspx (accessed on 23 September 2019) and GNI per capita levels are based on UNDP, Human Development Data (1990-2017). Available at http://hdr.undp.org/en/data (accessed on 23 September 2019).

The growth story for household income is less rosy. Figure 3.1 clearly shows that its growth rate fell below the growth rate of GNI in most countries. The growth narrative also changes completely when the size of the growth gap between national income and household income is considered, since it is largest for the medium human-development group of countries, such as Iraq and Egypt. For the latter, the data reveal a growth of household income over the period of 25 years of nearly 30 per cent in real terms, while the economy as a whole grew by more than 70 per cent.

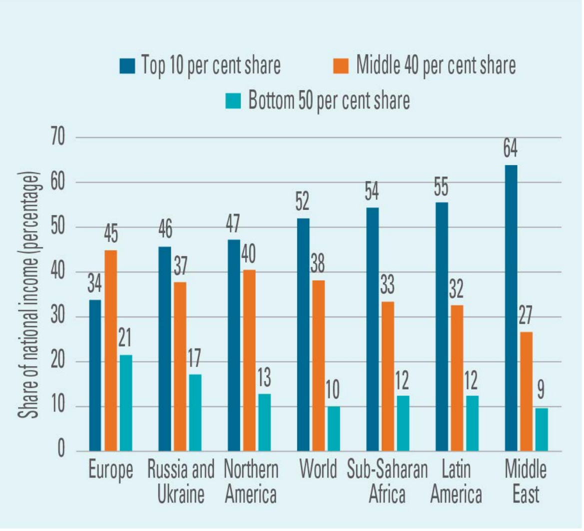
Low human-development countries, such as the Sudan and Mauritania, had minor gaps between GNI per capita and household income. Generally, household income has been stagnant in Arab countries and the already wide gaps with per capita GNI has persistently widened over time (figure 3.2). The policy relevant conclusion is that increases in the national income are not systematically transmitted to higher household income, thus delinking the growth process from its social impact and producing two contradictory inequality narratives.

B. Income inequality is a challenge, whichever way considered

To whom is the growth in national income, modest as it may be, allocated? This is a deceptively simple question for which there is no straightforward answer. As argued earlier, conventional measures of inequality such as the Gini coefficient derived from household surveys largely fail to capture total income distribution, in particular to those of the top decile. An alternative measure corrects for this omission by combining data from household expenditure surveys with other sources, such as national income, wealth accounts and fiscal data from taxes on income. Using this approach, the World Inequality Database estimates that 64 per cent of pre-tax national income in the region is captured by the top 10 per cent earners, while the middle 40 per cent and bottom 50 per cent of population capture less than 30 per cent and 10 per cent, respectively (figure 3.3). In addition, as shown in figure 3.4, this regional inequality average, which is the highest worldwide, is not confined to oil-rich countries.

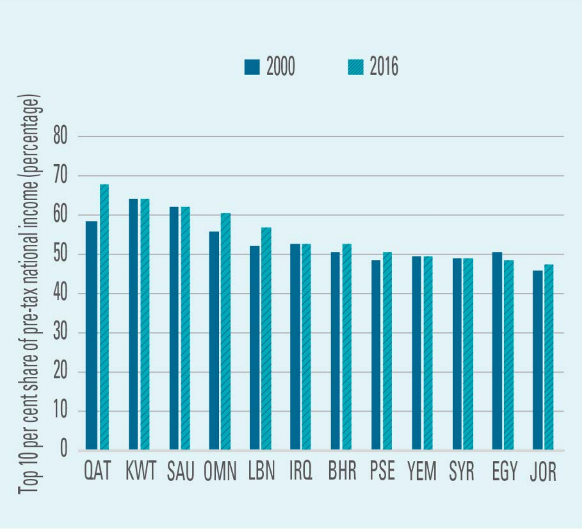
This findings runs directly contrary to the conventional wisdom on income inequality,

Figure 3.3 Top 10 per cent, middle 40 per cent and bottom 50 per cent shares of national income in 2016 by region



Source: Data based on World Inequality database. Available at https://wid.world/data/ (accessed on 10 January 2019).

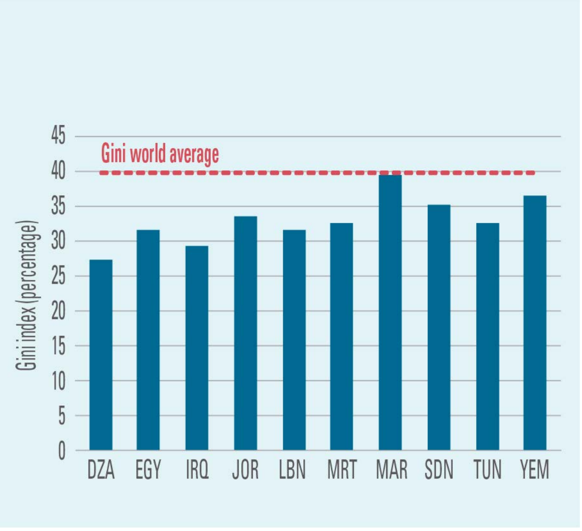
Figure 3.4 Trends in top 10 per cent shares, 2000-2016



Source: Data based on World Inequality database. Available at https://wid.world/data/ (accessed on 10 January 2019).

based on Gini estimates drawn from surveyed households, by which most countries in the region have comparatively low to moderate levels of income inequality (figure 3.5). However, there is a glitch. Many of the countries with a reported moderate level of Gini recorded the largest rising discrepancies between household expenditure surveys and household final consumption expenditures from national accounts, suggesting, as argued earlier, that it is in these countries where the order of magnitude of the inequality problem is most underestimated. Moreover, inequality among the surveyed households (using the Atkinson measure of inequality, which gives more weight to the lower tail of the income distribution) appears to have been fast rising since 2010 (figure 3.6). Hence, even if we disregard considerations arising from income of top earners being uncaptured, inequality still poses a major policy challenge.

Figure 3.5 Arab countries' Gini coefficient versus that of world



Source: World Bank, 2019.
Note: The reported Gini index for each country is the latest available between 2010-2015. For the Sudan, the latest available Gini index is for 2009.

Figure 3.6 Average annual rate of change (AARC) in income index (i.e. normalized GNI per capita, 2011 PPP dollars) and its Atkinson measures, 2010-2017

Source: Based on Abu-Ismail, 2019b. Data from UNDP, 2018.
Note: For Iraq, Lebanon and the State of Palestine, the baseline years are 2011 and 2013 respectively due to data unavailability in 2010. For Morocco and the Syrian Arab Republic, the end-line year is 2015 and 2016 due to data unavailability in 2017.

It is important to highlight that these within-country income inequality trends do not take into account the impact of large refugee movements, such as the influx of Syrians to Jordan and Lebanon. These displaced populations will have had an impact on the overall level of inequality in the host countries, since the vast majority of refugees are much poorer than their host communities. With the region having several ongoing conflicts, the role of these population movements on inequality needs to receive far more attention at both the national and regional levels.

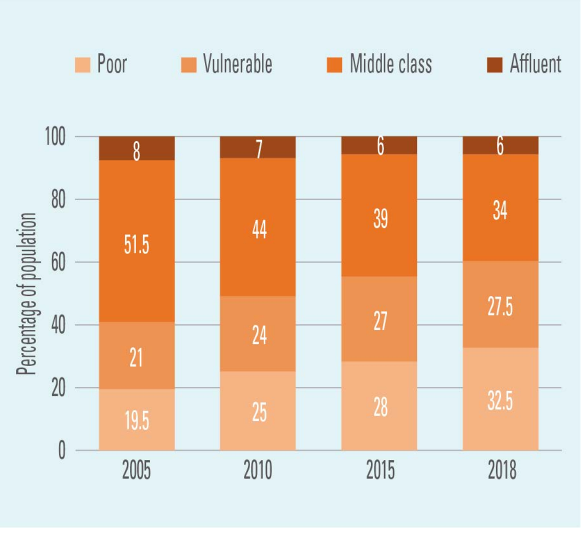
Inter-country inequalities are another important aspect of intra-regional inequality. Viewed from this angle, inequality is fast rising. Qatar, which has the highest HDI ranking among Arab countries, has a per capita GNI of around $117,000 (2011 PPP dollars), nearly 80 times that of Comoros. Moreover, the gap between the very high and low human-development groups has increased dramatically. In 2010 the average per capita GNI of the former was 13 times the latter, but in 2017 it reached a multiple of 20. Corroborating evidence of the enormously large intra-regional inequalities can also be found in the fact that the total wealth of the 42 richest Arabs (which according to Forbes 2017 list is 123.4 billion dollars) exceeds the GDP of the Sudan, Yemen, Mauritania and Comoros.

C. Impact on the poor and the middle class

Low real growth in household expenditure is not expected to produce significant income poverty reduction. According to the $1.9 per day poverty line, a global measure of extreme poverty, the headcount poverty ratio in the Arab region in 2015 was 5 per cent, which is half of the global average. However, the region achieved only 19 per cent poverty reduction since 1990, the lowest among developing regions. A snapshot of headcount poverty rates in 1990 and 2015 across a wide range of poverty lines starting from $0.5 per day and ending at $10 per day also suggests that poverty declined at a much slower pace in the region, relative to the global average, regardless of choice of poverty line. Moreover, although a small share of the population in the Arab region lives below the $1.9 line, a significantly higher share is clustered between the $1.9 and $3.5 lines. In other words, extreme poverty is low in Arab countries, but vulnerability to it is high. The policy implication is that negative (or positive) poverty impact of any social and economic policy will be comparatively higher in the region.

Given the large disparity in per capita income and the conflict situations within the region, regional averages conceal important country-level variations. Thus, the highest poverty reduction rates have been achieved by Jordan, Tunisia, Morocco, Egypt and Algeria, and the lowest by Iraq. Three countries, the Syrian Arab Republic, Yemen and Djibouti, experienced significant increases in poverty, mainly due to the impact of conflict. In Yemen, extreme poverty increased by 272 per cent from 1990 and an estimated 40 per cent of the population were living under $1.9 per day in 2015. In the Syrian Arab Republic, the corresponding rate of increase was 170 per cent. Still, the regional picture remains quite rosy, with a very low incidence of extreme poverty.

Figure 3.7 Population distribution across poor to affluent economic groups in Egypt using national definitions, 2005-2018



Source: Estimated based on Abu-Ismail and Sarangi, 2015; and Egypt Independent, "CAPMAS: 32.5 percent of Egyptians live below poverty line", 30 July 2019.

However, the story from a national perspective on poverty is somewhat different. As they build on household specific characteristics to estimate basic needs, national poverty lines have many advantages over fixed international poverty lines. Their main limitation, however, is lack of comparability across countries, due to differences in poverty definitions. To minimise these comparability problems, in 2015, the ESCWA led a research effort with a common measurement approach to examine the distribution of population across four economically distinct household categories (poor, vulnerable, middle class and affluent), using household income and expenditure surveys in nine Arab countries comprising over two-thirds of the Arab population.

The results confirm that, up to 2010, the middle class constituted nearly half of the population of the nine Arab countries (47.3 per cent). The (population weighted) regional average for poverty was 21 per cent. An additional 20 per cent of the population were vulnerable. This left an average of 12 per cent of the population in the affluent category. However, much has changed in the region since 2010. Conflicts in the Syrian Arab Republic, Iraq and Yemen are projected to have increased poverty. Egypt, the largest Arab country, has also recorded a rise in national poverty and vulnerability rates from 2010 to 2018, as a result of economic pressures on household income (figure 3.7). As a consequence, there may have been a significant decline in the region-wide size of the middle class to below 40 per cent in these countries. Likewise, poverty rates are likely to have exceeded 25 per cent.

4. Inequality Drivers

Socioeconomic inequalities are propelled by poor economic policy choices. Arab economies are mainly driven by services in oil importing countries (with a high proportion of low value-added services) and by the energy sectors in oil exporting countries, which results in labour market informalisation, as well as poor growth and productivity outcomes. At the same time, the rentier nature of Arab economies, weak governance and institutional frameworks, crony capitalism, restrictions on freedoms and low political participation have also resulted in socioeconomic arrangements that systematically favour the interests of those with more influence. Together, rentierism and mismanaged liberalisation economic policies have deepened existing socioeconomic and political inequalities.

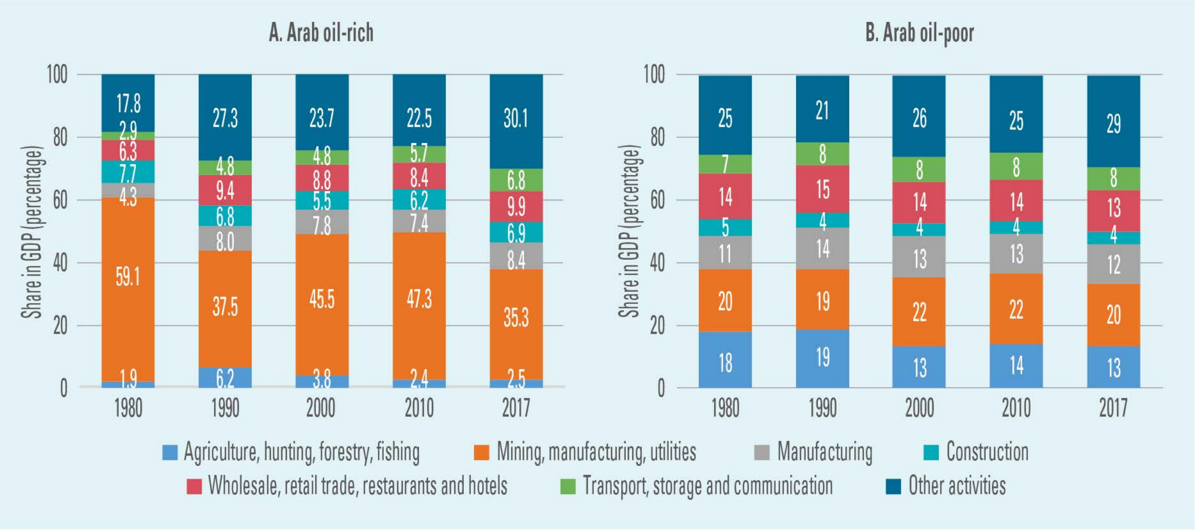
A. Economic policy drivers

1. Poor labour market and productivity outcomes

The Arab region appears to have a comparably high employment-output elasticity, indicating that growth was not jobless. This can be contextualised in the rentier economic structure that the region has long relied upon and which has paved the way for inflated public-sector employment. Nonetheless, since the late 1980s, and even more so over recent years, repeatedly low and fluctuating growth episodes, in both oil-exporters and non-exporters, significantly limited public sector capacity to absorb excess labour supply. At the same time, the role of the formal private sector in employment was limited and did not rise to the challenge of absorbing the growing influx of labour market entrants. Instead, most employment opportunities arose in low value-added and low paying informal service sector activities. In short, many of the jobs created were largely far from being decent.

This outcome is not easy to discern in figure 4.1, which depicts shares of sectors in GDP in Arab economies over the period from 1980 to 2017. Comparing evolution of sectoral growth over this period shows significant volatility in the share of the hydrocarbons sector in GDP for oil-rich countries (which declined from 59.1 per cent to 37.5 per cent over the period 1980-1990, then rose to 47.3 per cent in 2010, after which it declined to a low of 35.3 per cent in 2017). However, these trends are in line with movements in oil prices, while the structure for Arab oil-rich countries in 2017 remained very similar to that in 1990 prior to the era of rising oil prices from 2000-2010. In addition, since 1990, services and the other activity categories continued to be the primary growing sector in both oil-rich and oil-poor countries, at the expense of agriculture. Employment shares moved in the same direction, from agriculture mainly to services (figure 4.2). In this regard, workers moving into services from agriculture are likely to be engaged in low value-added work. The fastest rate of employment growth was recorded in construction and internal trade in oil-poor countries, while shares of employment in other activities also grew slightly in oil-rich economies.

Figure 4.1 Sectors shares' in GDP in Arab oil-rich and oil-poor countries (Percentage)



Source: Authors' calculations based on United Nations Statistical Division, 2017.

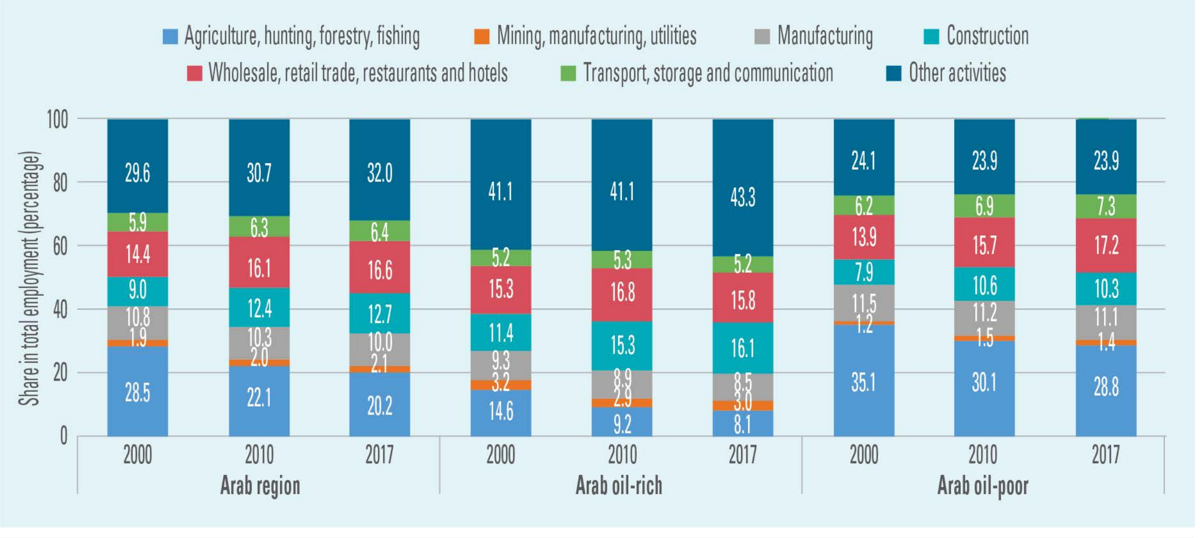
When the above trends are combined with outcomes, such as high informality, low labour force participation and productivity rates and high unemployment, especially among youth and women, it becomes clear that the growth process was neither productive nor inclusive. Based on ILO (2018), average informality levels in the five non-GCC Arab countries (Syrian Arab Republic, Yemen, Jordan, Iraq and State of Palestine) exceed the world average, with 68.6 per cent of total employment, including agriculture, being informal. The agricultural sector typically drives informality levels upwards. While excluding agriculture leads to considerable reductions in informality levels for the world average (from 61.2 per cent to 50.5 per cent) and for other regions, including developing countries (from 69.6 per cent to 59.5 per cent), in these five non-GCC Arab countries, average informality levels only decline to near 64 per cent, which, as noted elsewhere, suggests that informal employment may be high across other sectors.

High informality can also be traced by examining contributory pension schemes. Only 31.4 per cent of the labour force in the Arab region are active contributors and are covered effectively by old-age pension schemes, which leaves more than two thirds of the labour force without future social protection. Effective coverage is halved to 15.3 per cent if the total working-age population is considered instead.

These stylised facts and high levels of informal employment, along with concentration of economic activity in sectors with relatively medium to low value-added, may curtail GDP growth and affect labour and overall productivity growth. While labour productivity measured by output per worker in the Arab region may be higher than that of the world, growth of labour productivity has been generally below that of the world. Indeed, the region's labour productivity growth was largely negative over the 2014-2017 period, partly due to the decrease in aggregate output following the drop in oil prices and to recurrent conflicts, and remains close to zero in 2018. In this regard, continuous sluggish growth may have an adverse impacts on labour productivity growth and output per worker levels in the long term, which in turn may impact real wages, well-being and inequality. However, it is crucial to note that productivity and wage shares of the manufacturing formal private sector (which has low informal employment) have been largely consistent with global averages (with the exception of low-income Yemen and Mauritania, where they are distinctly lower) (figure 4.3). The lesson to draw is that low productivity growth in Arab economies is not an economy-wide feature.

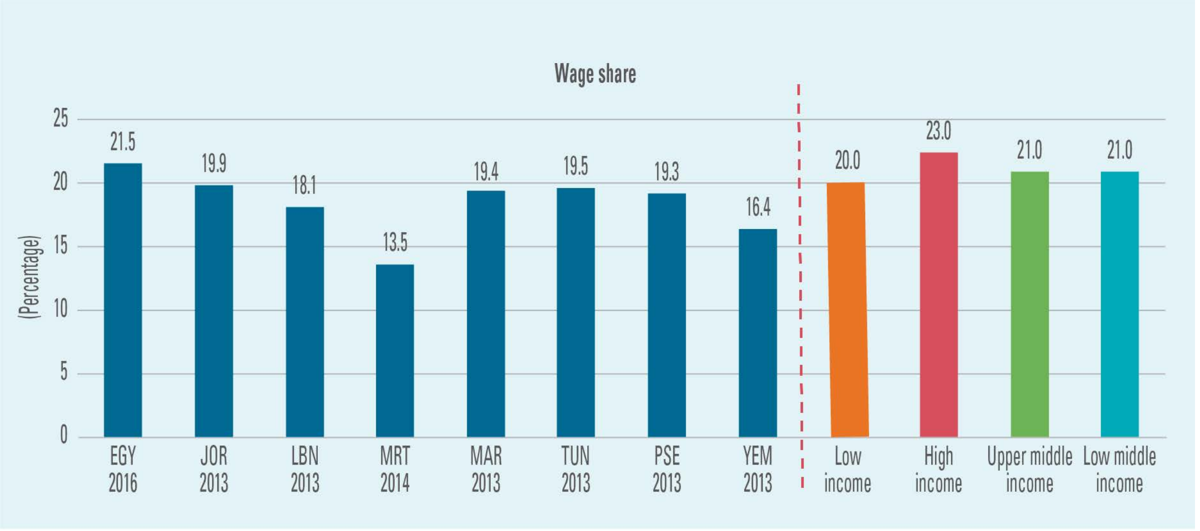
Nonetheless, Arab manufacturing enterprises tend to be more capital intensive than in other countries at similar levels of income and human capital as found from the enterprise surveys results. The higher capital shares relative to labour income shares in total firm revenues partly signal capital-to-labour substitution and low employment demand, notwithstanding abundance in educated labour force and high unemployment, especially among youth and females. Not only does this contribute to distorted employment incentives and increased unemployment in the near term, but may also, over the time, negatively impact average wages, job quality, and inequality, i.e., increases in the shares of capital may increase incomes of those at the top of the income distribution, acting as a driver of income inequality.

Figure 4.2 Sectors' shares in total employment in Arab oil-rich and oil-poor countries (Percentage)



Source: Authors' calculations based on ILO, 2018c.

Figure 4.3 Wage's share in manufacturing sector as a percentage of total sales for selected Arab countries in comparison with world averages by income group



Source: Authors' calculations based on the World Bank, Enterprise Surveys database. Available at https://www.enterprisesurveys.org/en/survey-datasets (accessed on 10 August 2019).

2. Stabilisation-focused macroeconomic policies

These structural features are an expected outcome of economic growth (and, consequently, continued rapid progress on key social indicators) being reliant on fluctuating external flows (oil exports, remittances, tourism, etc.). Other related aspects of this economic development model include Dutch Disease symptoms, such as overvalued and uncompetitive exchange rates, combined with poor non-oil export performance, large subsidy bills, rising debt and limited space for non-subsidy related social expenditures. Regional and internal conflicts also play a fundamental role in accentuating these macroeconomic weaknesses, through channels such as rising military expenditures, and declining remittances, ODA and foreign investments.

The end result is an unsustainable regional economic model, especially for resource-poor labour-abundant countries that have less room to manoeuvre, leading to frequent macroeconomic crises driven by balance of payments constraints. The negotiated economic reform programmes that follow these crises would lead to further constrains on macroeconomic policies that produce more pressure on the poor and middle class, while rarely addressing lack of structural transformation and decent work, the root cause of macroeconomic fragility.

One major channel through which a stabilisation-focused economic reform agenda affects poverty and inequality outcomes is through regressive fiscal policies. In the Arab region, taxes are comparably low, particularly in the resource-rich countries where oil proceeds provide an alternative income source for social expenditures. At the heart of the fiscal policy challenge is the fact that countries that are reliant on direct taxation as a major source of revenue are witnessing a pattern in which the share of income tax in total tax revenue remained either stagnant or declined over the years between 2005 and 2014. Thus, although tax levels vary across Arab countries, their tax structure is largely alike: most, including the GCC, have relied primarily and increasingly on indirect taxes (e.g., VAT). In addition to the low significance of income tax, wealth taxes have a negligible share of total tax revenue in most countries in the region. In short, the tax system that resulted from economic reform programmes in the Arab region led to two core problems: regressive features and high evasion incidence.

More generally, fiscal capacities for development expenditures are further constrained by high debt obligations. Caner, Grennes and Koehler-Geib (2010) established a public debt-to-GDP threshold of 77 per cent, after which accumulated debt would slow growth down. Many Arab countries have passed this threshold, with the Sudan and Lebanon having dire debt-to-GDP ratios, which raises concerns over unsustainability of debt trajectories and their repercussions on growth and development. While oil-rich countries tend to have moderate debt-to-GDP ratios, their social expenditures based on oil returns have also been consistently pressured over the past few years due to low oil prices. On the other hand, the structure of public expenditure in the Arab region is such that out-of-pocket spending on both health and education consumes up to 8 per cent of the disposable income of the poor and 11 per cent of that of the middle class; significantly higher than the global average. The constrained fiscal space across the region, therefore, struggles with meeting the greater need for enhancing social expenditure to achieve the SDGs.

The key policy lesson is that these macroeconomic constraints did not arise in a vacuum, but, as persuasively argued in Lance Taylor's Variety of Stabilization Experiences (Taylor, 1988), are directly related to the design and logic of liberalisation economic reforms. Stabilisation, it is crucial to keep in mind, kicks in after macroeconomic imbalances. It, therefore, primarily aims to reduce inflation, deficits (budget and balance of payments) and correct “wrong” prices, such as overvalued official exchange rate and undervalued or heavily subsidised fuel or commodity prices. If accompanied by complementary medium- and long-term structural adjustment policies that ensure specialisation, boost competitiveness and domestic production, the end result, according to economic liberalisation advocates, is high export-led growth and inflows of foreign investment that ultimately reduce balance of payment (BOP) deficit. Employment generation and productivity growth enhancements that would accompany this process would ensure structural transformation and positive social impacts, such as poverty reduction and an expanding middle class.

Evidence for these theoretical causal links is mixed. Experiences of several Arab country show that austerity measures can deliver lower inflation. Restrictive monetary and fiscal policies (raising interest rates, imposing taxes and decreasing subsidies) can thus restore macroeconomic stability in the short-term and possibly even resume aggregate growth. Yet, the second longer term part, where more productive and employment friendly growth is assumed to trickle down to households and reduce poverty and inequality is very problematic, as our earlier review of stylised facts suggests. As argued in the following section, economic reforms had another negative impact to which their protagonist were quite oblivious: rising cronyism.

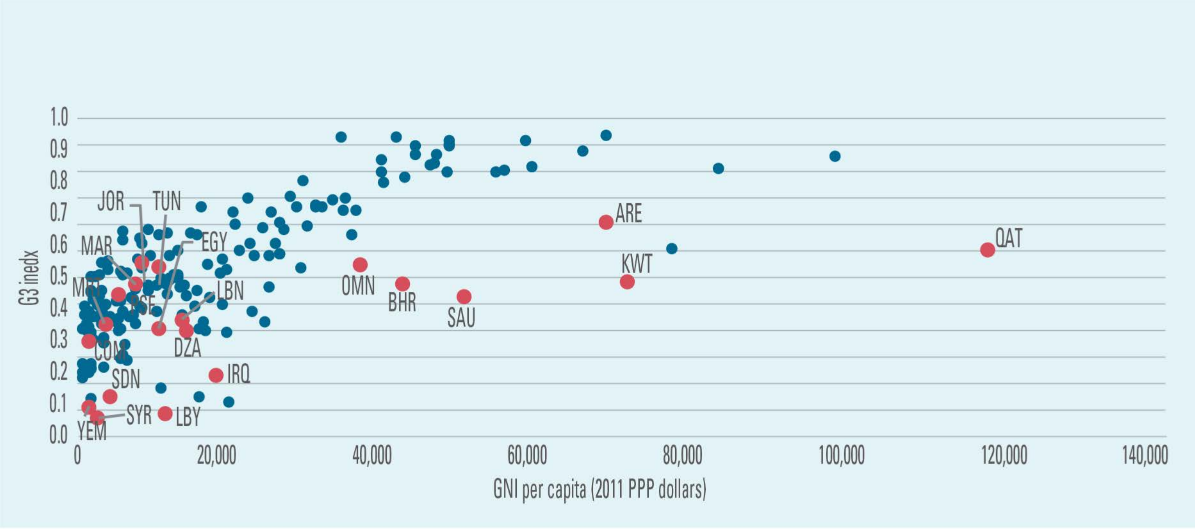
B. Institutional drivers

A major contributor to wage and income inequality is the existing schism between a small formal sector and the bloated informal sector, caused largely by prevalence of crony capitalism as an outgrowth of the policies of stabilisation and structural adjustment of the late twentieth century. As part of the bargaining rentier deal, the crony capitalist class that emerged from liberalisation led to the cementing of patron-client models of doling out services to the privileged few at the expense of those with no political connections.

Growth of the narrowed network of privileges and prevalent cronyism not only hampered growth and job creation and aggravated inequality, it also made for onerous opportunity costs. Inequality was further aggravated as these developments were accompanied by a retreat in public investment. Essentially, these reforms were devoid of the requisite political liberalisation and governance modes, hence sowing the seeds of inequality.

These developments were also accompanied by severe restrictions on freedoms that adversely impacted autonomy, such as the freedom and ability to form coalitions and increase the possibility of social change. Key findings of the ESCWA (2018c) report on “Inequality, Autonomy and Change in the Arab Region” suggest that, on average, personal autonomy tends to be relatively low in the region compared with the rest of the world, particularly in terms of self-expression, and there is unequal distribution of autonomy among the population in the region.

Figure 4.4 GNI per capita (2011 PPP dollars) and Governance index (G3) in 2017



Source: World Bank, World Governance Indicators database. Available at https://info.worldbank.org/governance/wgi/ (accessed on 10 January 2019); and UNDP, Human Development data. Available at http://hdr.undp.org/en/data (accessed on 15 August 2019).
Note: G3 is the geometric mean of 5 indicators from World Governance Indicators namely rule of law, voice and accountability, governance effectiveness, regulatory quality and control of corruption. We normalise the index using min-max criteria and it ranges from 0 to 1, with higher values indicating better governance.

Manifestations of these restrictions on autonomy are already well documented. Following the Arab uprisings, except for Tunisia, the region did not experience improvements in either human rights or political rights, nor did overall governance improve. Education has been used as an instrument of indoctrination to ensure obedience and sustain conservative values, rather than promoting critical thinking. Deep entrenchment of the patriarchal system is also a reason for low autonomy, especially among youth and women. This is evident along many dimensions, such as gender equality, commitment to democracy and religious tolerance, where the region is more conservative than elsewhere with the same level of development.

This low personal autonomy is intrinsically linked to inequality, as the rentier social contract is, in essence, based on an exchange of high per capita rents for low accountability and transparency, low political participation and regime legitimacy. This is evident in the location of oil-rich countries as outliers in the lower right side of figure 4.4, which plots a good governance index, developed by ESCWA based on the WGIs, against GNI per capita. Low self-expression and autonomy are thus inherently built into the social and institutional arrangements of the rentier state, including its educational systems. Not surprisingly, ESCWA (2018c) finds that, on average, the Arab region seems to be more accepting of inequality than the global trend. As argued in the next chapter, sustainability of this bargaining deal is of course questionable, as rents decline and as the youth increasingly call for more political participation, autonomy and democracy, and, certainly, for decent economic opportunities.

5. The Case for Inclusive Development Policy

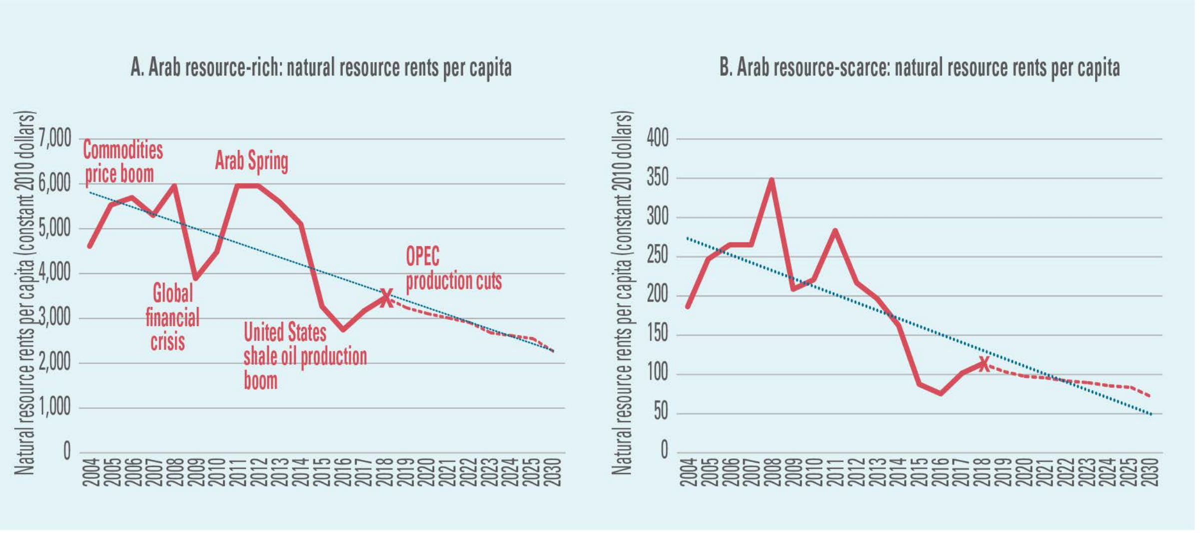
Arab countries need an inclusive economic development model that break the vicious cycle of low economy-wide productivity, slow growth in household income, sluggish poverty reduction and rising informality, along with inequality of income and opportunity. Reaching these goals, especially with projected decline in future rents, requires taking institutional reforms and structural transformation as existential development challenges. Institutional reforms, beginning with social dialogue, would target improvements in voice and accountability and rule of law. New social contracts that would emerge from such a social dialogue would reinvigorate commitment to public services, employment and social protection with improved conditional cash transfers and employment guaranteed schemes. Structural transformation requires a reorientation of macroeconomic and sectoral policies, with regional integration as a major enabler. A reorientation of macroeconomic policies, based on interventions such as ESCWA's proposed Social Expenditure Monitor (SEM) for Arab countries, would rationalise the fiscal space available for supporting social protection and structural transformation.

A. Dwindling rents as an opportunity for institutional reform

Natural-resource endowments have been shaping Arab economies for decades, especially in the nine resource-rich net oil-exporters (i.e., GCC countries and the three other OPEC members), where high per capita rents in the form of government provision of subsidies, low tax rates and public sector employment have been a pillar of development policy since the 1950s. Natural-resource riches have also influenced Arab oil-poor and non-oil exporting economies through capital flows from the resource-rich countries, especially investment, and remittance and tourism inflows. These rents and their spillover effects have thus played the lead role in promoting social and economic development over the past four decades across most Arab countries. But they have also cemented authoritarianism. The need to delink development prospects of the region from resource rents is increasing, as these seem to have poor medium- to long-term prospects.

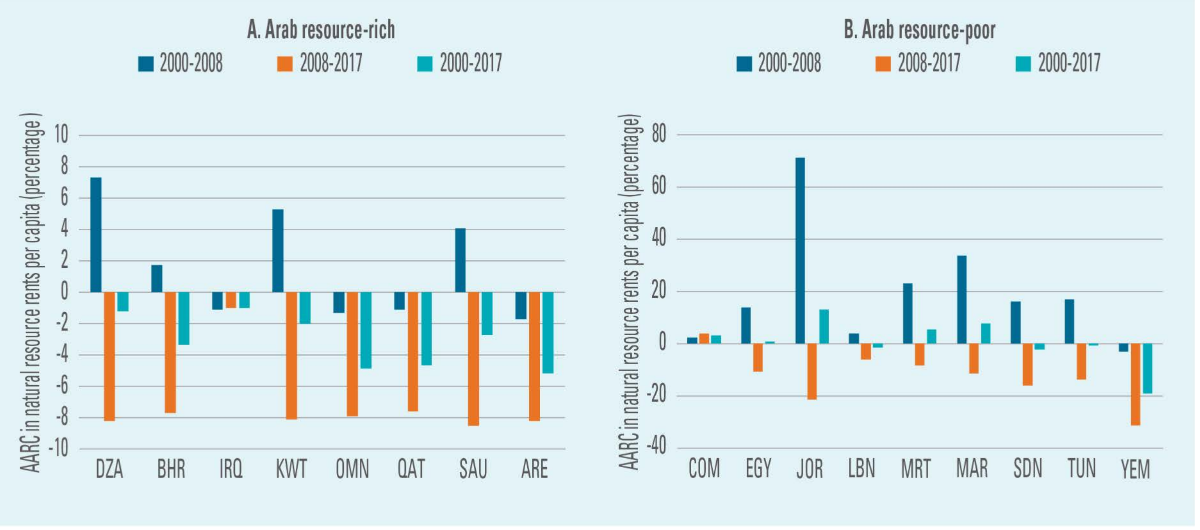
Figure 5.1A and figure 5.1B plot average real natural-resource rents per capita (constant 2010 dollars) over the period 2000-2017. As shown, oil price drops after the global financial crisis and particularly in 2014-2015 following the growth in the United States shale oil production suggest a post 2008 structural break in rents per capita, which plunged to their lowest level since 2004. This post 2008 break is also revealed by the negative average annual rates of change in per capita natural-resource rents for almost all countries (figure 5.2). Building on these trends, projected rents per capita in 2030 (the dotted line in figure 5.1) could drop to $2,240, less than half of their 2008 value in oil-rich countries, while the corresponding ratio for oil-poor countries is less than one third.

Figure 5.1 Group average: real natural resource rents per capita across Arab resource-rich and resource-poor countries, 2000-2017 and their projections, 2018-2030 (Dashed part)



Source: Authors' calculations based on WDI and UN DESA population data. The Arab resource-rich countries include: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates, Iraq and Algeria. The Arab resource-poor countries include: Comoros, Egypt, Jordan, Lebanon, Mauritania, Morocco, Tunisia, Yemen and the Sudan.
Note that for the projections in figure 5.1 2018 are estimates, while 2019 onwards are forecasts based on the World Bank forecasted commodity prices published in April 2019.

Figure 5.2 Average annual rate of change (AARC) in natural resource rents per capita



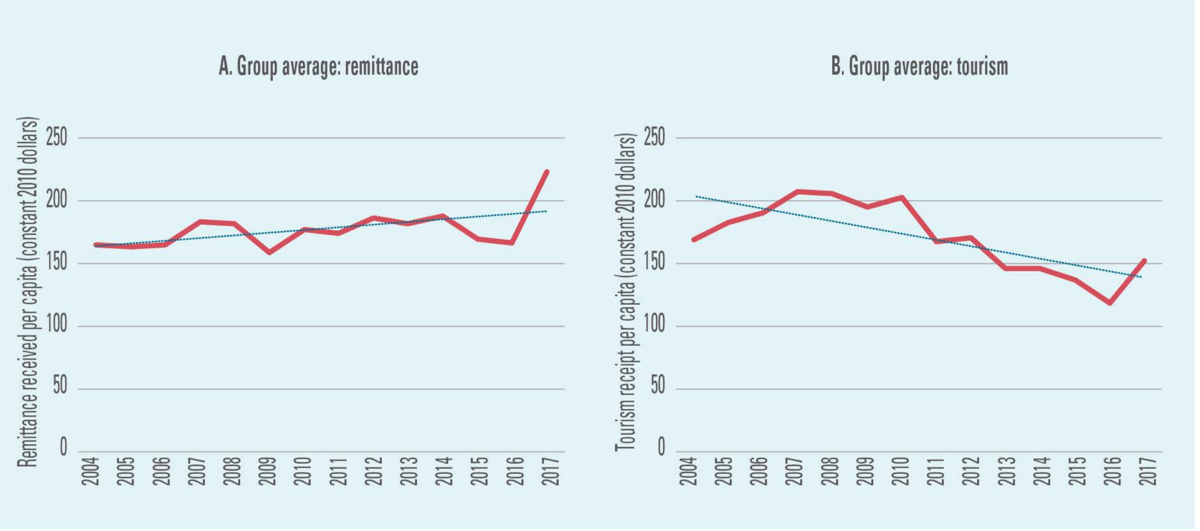
Source: Authors' calculations based on World Bank, 2019 and UN DESA, Population Division, 2019.
Note that in Iraq the data starts as of 2004. Hence the first period reflects 2004-2008 and the total period reflects 2004-2017.

These results should ring an alarm bell for all countries in the region, but especially for oil-rich countries with low rents per capita (such as Algeria and Bahrain, where rents per capita were already below $1,000 in 2017, compared with nearly $12,000 for Kuwait and Qatar). Also of concern is that these crude projections are quite conservative in that they do not factor in the worse-case scenario, in which effects of rapidly rising rates of own natural resource consumption or declining oil reserves (as in the case of Algeria) are taken into account.

Although resource-poor economies have low levels of rents per capita, they are highly reliant on remittance and tourism inflows that are closely tied to natural resource returns, with other factors, such as recent conflicts across the region, also negatively impact these inflows. Indeed, trends in remittance and tourism inflows per capita across Arab non-oil exporter are expected to coincide with those for natural resource rents per capita (figure 5.3). Post 2010, Arab resource-poor countries on average had stagnant per capita remittance receipts and declining per capita tourism receipts. Countries that are more reliant on remittances and tourism, as in the case of Lebanon, had sharper declines, leaving their economies more vulnerable. While 2017 shows some increases in tourism and remittance receipts, they are not expected to shoot up, given the expected rise in fiscal pressures in oil-rich economies, nationalisation of employment initiatives and regional conflicts.

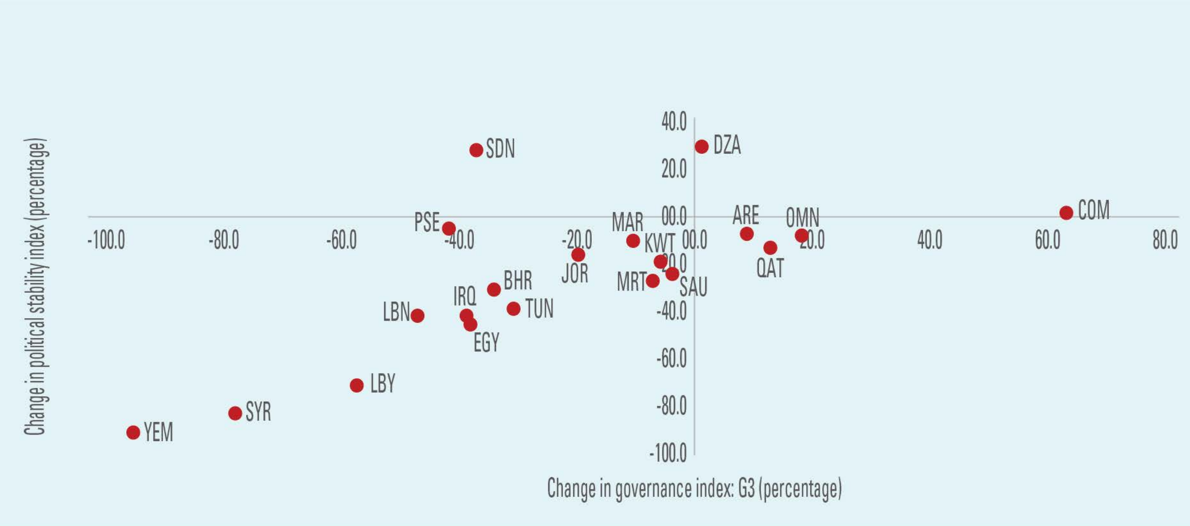
Although trends in oil prices underlying these projections are notoriously unreliable, the order of magnitude of numbers shows that lavish social contracts that have been a main pillar of regional development policies for the past four decades may very well be on their way to being a historical past-fact. This should raise concern, especially given reconstruction demands in some countries (Yemen, Syrian Arab Republic, Iraq, and Libya), high debt to GDP and debt service ratios (most resource-poor middle-income countries) and high and rising military expenditure (most Arab countries, especially resource rich). All this is expected to add to more pressure on rents and fiscal space for social expenditure.

Figure 5.3 Remittance and tourism receipts per capita across Arab resource-poor countries, 2000-2017



Source: Authors' calculations based on World Bank, 2019; UNDESA, Population Division, 2019.

Figure 5.4 Percentage change in governance and political stability indices, 2000-2017



Source: Authors calculations based on World Bank Governance indicators.
Note: Governance Index calculated following Abu-Ismail et al (2016). We normalize the governance (G3) and political stability (PSI) indices using min-max criteria.

The Arab rentier state, with its current institutional capacity and governance framework, is ill-equipped for addressing these multiple challenges. Policy responses since 2010 have offered either additional rents (GCC in 2011 till 2013) and/or less space for real voice and accountability and other governance reforms (resource poor). These responses are an extension of the same policies that led to the uprisings. Without fundamental economic policy, institutional and governance reforms, Arab countries will remain trapped in another vicious cycle of low and deteriorating governance and rising political instability (figure 5.4).

What can policy makers in Arab countries do to address these governance challenges? This requires profound stock-taking and systemic change at various political, economic and social levels. As argued in our conceptual framework, only an integrated approach that takes a long-term view would be effective in inducing real change. Such an approach would include questioning the pillars of the patriarchal society, religious teachings, and prevalent economic models and political decision-making.
In political economy terms, it would require a shift from rentier states to developmental states, where institutions rather than individuals play the lead role.

The first objective of change, therefore, is to restore credibility of state institutions by reinventing public services and incentivising public participation as crucial aspect for stakeholder involvement in new policies to ensure their relevance and applicability. Any serious reforms would have to begin by deconstructing the patron-client networks by relying more on institutions for services, treating citizens equally, cementing the rule of law and promoting good governance.
In the Arab region, such a transition requires a cultural transformation, by discouraging

oligarchic practices that prevail in a number of Arab economies; opening up the private sector to new entrants to transform it into a real 'private' sector, rather than a 'family' private sector, and fostering a healthy competition.

To these ends, promoting social dialogue is necessary, particularly in transition economies or seemingly stable regimes that have low voice and accountability (ILO and UNDP, 2012). Indeed, lessons from the region have taught us that social dialogue is the central apparatus for enhancing communication channels between government and people, and provides an institutionalised mechanism for conflict resolution.

B. Social contracts with reinvigorated commitment to better public services, employment and social protection

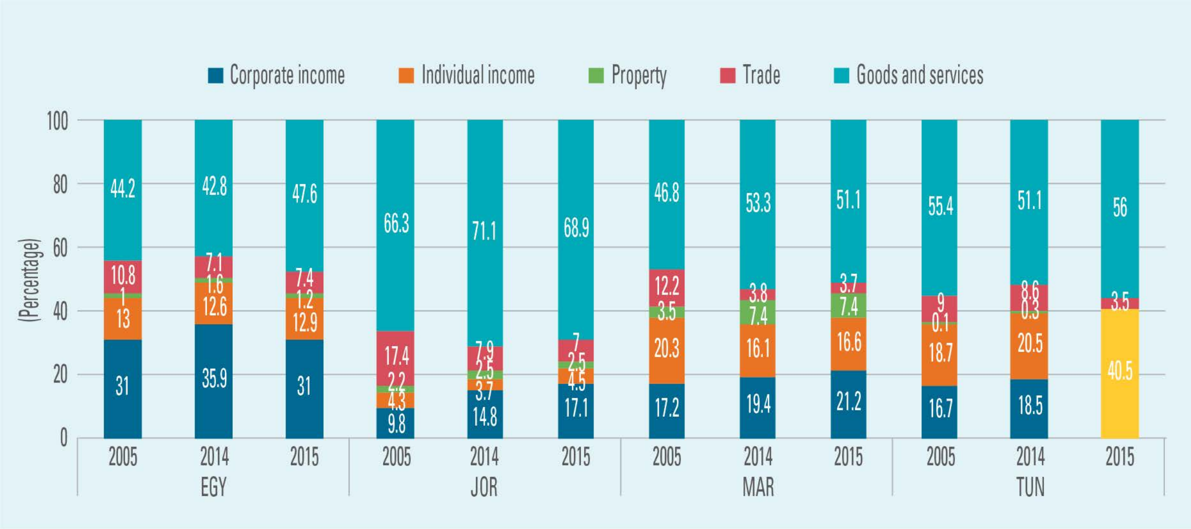
There is an urgent need for reinvigorating commitment to public services in Arab countries, most importantly by revisiting the role of education in social contracts, leading to higher quality systems conducive to achievement of national social and economic goals. Although Arab countries have in the post-colonial era succeeded in raising educational attainments, there are persistent issues with education quality. In addition to strategic alignment, education quality can be improved through more efficient resource allocation. More transparent budgets will likely identify a slew of areas where cost savings can be made and reallocated towards strategic reform, curricular development and teacher training. Budgeting procedures themselves should be reconsidered, for centralised budgeting tends to be rigid and unresponsive to local needs. Furthermore, some degree of administrative and financial decentralisation for education may enhance efficiency of resource allocation. In many Arab countries, the potential for revenue generation and cost savings among universities is relatively untapped. Thus, tertiary education is a potential area where resources can be allocated more efficiently. Above and beyond resource allocation, the region needs to rethink and eventually overhaul the overarching goal of the education system from one of indoctrination (ESCWA, 2018c) into one of emancipation, and, hence, greater autonomy and freedoms for individuals. Moreover, beyond education, renewed public commitment across basic services, notably health and housing, is needed.

Social welfare programmes can be designed to boost access to education and health services. In their most basic form, means-tested cash transfer programmes guarantee basic incomes. However, generally, conditional cash transfer programmes (CCTs) vary in design, but typically include an educational and/or a health behavioural requirement as a condition for receipt of transfers. Such programmes have the limitation of not addressing structural weaknesses, such as quality and supply of services. In terms of primary programme goals, CCTs do significantly increase uptake of health and/or education services, and in some cases boost outcomes by reemphasising the point that quality of services is critical in reaching desired outcomes. Indeed, it was found that they do conclusively increase school attendance, are effective in poverty reduction, and increase long-term wellbeing of children from poor households. Moreover, beyond individual benefits, CCTs address and alleviate multiple dimensions of inequality. Not unlike traditional cash transfers, they contribute to lowering gaps by raising post-transfer income and consumption levels of vulnerable groups. Among Arab countries, the Ministry of Social Solidarity in Egypt, with support from the World Bank, launched the country's first CCT programme in 2015: Takaful and Karama Programme (TKP).

Finally, social safety net programmes, in their most basic form, are critical for ensuring poverty protection. While extensive safety net programmes exist in several Arab countries, certain groups tend to be overlooked. For example, while public sector employees are protected, private sector employees receive partial or not protection in some cases. In 2009, under the banner of ensuring 'social protection for all', the United Nations System Chief Executives Board for Coordination (UNCEB) proposed the Social Protection Floor (SPF) Initiative, which identifies four essential and universal guarantees relevant to cases of: (a) lack of work-related income, caused by sickness, maternity, unemployment, etc.; (b) lack of access to affordable health care; (c) insufficient family support; and (d) general poverty and social exclusion. The Initiative calls upon countries to consider more centralised, coherent national social security systems to maximise effectiveness and cost efficiency and ensure that all relevant groups are reached. Arab countries should review existing social safety-net programmes to enhance protection from poverty and shocks, while avoiding undermining work incentives.

Addressing informality and generating employment for the young entrants to the labour force is also essential for addressing inequality. Reforms setting a minimum wage would help close the wage gap between the formal and the informal sectors and pave the way to formalising the latter. Employment guarantee schemes (EGS) are public work programmes that have been used to provide households with additional income during drought and other natural disasters, especially in rural areas. Their main purpose is to provide guaranteed employment at a certain wage level adequate for securing a desirable level of income for poor households. India was the pioneer of EGSs in an attempt to fight both poverty in rural areas and female unemployment. The Indian programme increased the bargaining power of employees and social protection in general, with a positive impact on the economy. However, there were also some risks and drawbacks. Ranjan (2015) point out the inflationary pressure caused by the increase in food prices. Moreover, such programmes may lead to a shift in economic activity from heavy manufacturing and services to agriculture and light manufacturing. Li and Sekhri (2013) also highlighted that such schemes could push more young children to substitute in home production and withdraw from schools to provide child-care when parents are at work. In the Arab region, jobs provided by employment-guarantee schemes may not match available skills, yet they could temporarily provide households with sufficient income to reduce susceptibility to poverty. Since Goal 5 of the SDGs is a priority for the region, well targeted EGS could also reduce the gender gap in income.

Figure 5.5 Composition of tax revenue in selected oil-poor countries (Shares in percentage)



Source: Authors' calculations based on data from IMF, "Tax revenues". Available at http://data.imf.org/?sk=77413F1D-1525-450A-A23A-47AEED40FE78&sId=1390030341854 (accessed on 15 June 2019).
Note: For Tunisia, the yellow section reflects both corporate and individual income.

Is there fiscal space to allow for these expenditures? Yes, but with fiscal policy reforms. Fiscal policies need to examine across-the-board subsidies, i.e., to maximise their impact on the most underprivileged, subsidies need to be rationalised and better targeted. On the other hand, in order to widen the fiscal space for social expenditure, adopting progressive income tax and wealth and property taxes is likely to improve revenues, while enhancing fairness. Tax resources in several countries depend highly on taxes on goods and services (figure 5.5), which are regressive in nature, since they put more burden on the middle class and the poor who constitute the consumer base. Tax reforms need to consider progressivity, including in taxes on goods and services, and rationalise exemptions. As a prerequisite, tax policies need to be coupled with reforms to tax administration systems. Reforms in public finance management can improve efficiency and effectiveness of expenditures, leading to improved social justice. *ESCWA's Social Expenditure Monitor (SEM)* for Arab countries is an enabling tool that can be tailored to national contexts to monitor and analyse gaps in public social expenditure data and social policy in responding to social development priorities and reducing overall inequalities (ESCWA, 2019b, 2019c). Should this social expenditure monitor be dynamically connected to a poverty observatory, then the ingredients for an evidence-based socioeconomic decision-making process would become available.

C. Regional Integration for decent work and structural transformation

Arab economies are in dire need of a structural transformation that takes into consideration the social impact of economic policy, so that economic growth becomes equitable, inclusive and sustainable. In order to further diversify the economy, increase productivity and generate employment, a shift away from the capital-intensive natural-resource sector must take place. Promoting small and medium enterprises is an entry point to boosting personal initiative, promoting entrepreneurship, and generating employment. In addition, support for micro enterprises serves to decrease inequalities, since it targets the most financially disadvantaged. Public investments, both in human development and infrastructure, need to prioritise areas that are deprived or lagging. Investments in infrastructure would ensure better access to services and incentivise private sector development. In conflict areas, alongside increasing public investments, enforcement of the rule of law is necessary for ensuring equitable distribution through structural transformation. Effective fiscal policies would pave the way for targeted investments and provide an environment conducive to addressing socio-economic inequality challenges. However, for any structural transformation to be successful, good governance practices need to be embedded in all public policies.

Pursuing Arab regional integration offers an opportunity for driving economic growth, and would contribute to poverty eradication, support job creation and help close inequality gaps in income, health, education and employment. Moreover, by allowing free movement of labour, goods and capital, it would enhance intra-regional trade and investment. Arab development funds can play a significant role in promoting regional integration and in supporting socioeconomic development. Finally, enhancing intra-regional investments calls for: (a) adoption of uniform policies for achieving food, energy and water security; (b) promotion of free movement of labour to close skill gaps; (c) removal of trade and institutional barriers to Arab investment; (d) investment in infrastructure development to boost fiscal space for social expenditure finance; and (e) allocation of more financial resources to Arab development funds to support local, national or regional projects aimed at improving access by the most disadvantaged.

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Conventional wisdom, based mainly on surveyed household income distribution statistics, suggests inequality is generally low in Arab countries. However, little attention has been devoted to social inequalities, whether in outcomes or opportunities. The present ESCWA-ERF report entitled Rethinking Inequality in Arab Countries offers a different narrative. Based on the largest research project on the subject to date covering 12 Arab countries, the report argues that the Arab region is caught in an inequality trap. Regarding economic policy, trends such as low growth in household income, stagnating poverty, a squeezed middle class, low productivity and high informal employment suggest much higher levels of income inequality than reported by expenditure-based Gini coefficients. Social inequalities, though declining in outcomes owing to rapid progress in basic education and health indicators, are rising in many indicators related to opportunities.

These trends imply improved social outcomes, especially for young people, but without commensurate progress in their economic welfare or in the equality of opportunities they face, which fosters a sense of economic and social injustice. When combined with high levels of inequality in personal autonomy and restricted voice and accountability, the final result, as argued by the authors, is an inequality trap where governance frameworks and their ensuing economic and social policies lead to socioeconomic arrangements that systematically favour the interests of those with more influence. Policy measures to address this trap cannot be short term or unidimensional. A new long-term development model is required, with economic and social justice and core governance reforms at its heart.

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