ECONOMIC AND SOCIAL COMMISSION FOR WESTERN ASIA (ESCWA)

SURVEY OF ECONOMIC AND SOCIAL DEVELOPMENTS IN THE ARAB REGION 2012-2013

SUMMARY

United Nations

Distr.
GENERAL
E/ESCWA/EDGD/2013/2
10 April 2013
ORIGINAL: ENGLISH

ECONOMIC AND SOCIAL COMMISSION FOR WESTERN ASIA (ESCWA)

SURVEY OF ECONOMIC AND SOCIAL DEVELOPMENTS IN THE ARAB REGION[*] 2012-2013

SUMMARY

United Nations
New York, 2013

[*] Following the accession of Libya, Morocco and Tunisia to the Commission in July 2012, it was decided that the territorial coverage of the Survey of Economic and Social Developments would be expanded to include all the countries of the Arab region. Subregional groupings are used in this paper, reflecting a combination of per capita income level, geographical proximity and similarities in economic and social characteristics and conditions. The subregional groups are as follows: Gulf Cooperation Council (GCC) (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates); Arab Mashreq (Egypt, Iraq, Jordan, Lebanon, Palestine and the Syrian Arab Republic); Maghreb (Algeria, Libya, Morocco and Tunisia); Arab least developed countries (LDCs) (Comoros, Djibouti, Mauritania, Somalia, the Sudan and Yemen).

13-0070

Summary

The average growth rate of gross domestic product (GDP) in real term of the Arab region is estimated to be 4.8 per cent for 2012, compared to 2.2 per cent in 2011. The recovery in the Maghreb subregion, particularly of Libya, and the consistent economic growth in Gulf Cooperation Council (GCC) countries were significant contributing factors. For 2013, the average real GDP growth rate of the region is projected at 4.4 per cent. The GDP growth rate on average is likely to taper off due to the decline in energy export revenues which marked a historic high in 2012.

However, the polarization of economic and social developments in the region deepened in 2012. Major energy exporters in the region, namely GCC countries, are on a stable recovery path which was enabled by an expansionary fiscal and monetary policy mix. At the same time, net energy importing countries in the region are struggling to stabilize their economies amid worsening foreign exchange constraint. The polarization resulted in part from political instability and social unrest, but also from the diminished flow of intraregional trade, tourism and investments. The lack of confidence in intraregional business transactions resulted in the segmentation of regional economies and the loss of regional leverage, which amplified the seriousness of unemployment throughout the region, even in GCC countries.

Amid those economic and employment difficulties, social development in the region has continued gradually through policy reforms and institutional development. Most notably in 2012, Saudi Arabia took a series of active labour policies for nationals and emphasized the importance of female employment. Concurrently, the social dynamics of the region have been characterized by social unrest and political instability. The structural weakness of the economies in the Arab region, represented by high unemployment rates and income inequality, is the chronic undercurrent motivating social unrest and political instability. Reviving effective regional leverage through further cooperation and integration is crucial to compensate for failing market-based intraregional resource transfers.

CONTENTS

I. GLOBAL CONTEXT

1. Throughout 2012, the world economy continued to struggle to recover from the global financial crisis of 2008-2009. Central banks in developed economies took the stance of monetary easing to its maximum. A series of monetary policy coordination efforts of that line successfully contained the contagion of liquidity crisis. Moreover, a series of fiscal stimulus policies at the global level in 2008 and 2009 successfully averted the risk of an implosion in global demand growth and prevented the world economy from becoming trapped in a deflationary spiral. Nevertheless, despite those short-term successes, the struggle for a stable economic recovery became more apparent in 2012 as economic policy options for many Governments were further exhausted. The quickly shrinking fiscal space forced many Governments to maintain a stance of fiscal austerity. Meanwhile, the speed of balance sheet adjustments of the financial sector varied: while a smooth adjustment has been observed in the United States of America, the process has been slow in the euro area. The remaining uncertainty over financial risks, which still could be contagious, precluded the strong investment-led growth recovery of the world economy at this stage. The developed economies, particularly in Europe, are still prone to a double-dip recession.

2. Developing economies, including those of Arab countries, increased their presence in the world economy in 2012 by sustaining the demand growth of the world economy. However, it appeared that the economic performance of developing economies diverged according to their resource endowments. Global investment flows stagnated as investors remained cautious about risk. Therefore, developing economies with natural and financial resources were able to weather the uncertain situation of the world economy. The resilience on the part of developing economies sustained the world demand for natural resources and compensated for the moderately decreased demand of developed economies. However, developing economies without natural resource endowments have increasingly suffered from the rising foreign exchange constraint as the capital inflow became insufficient to finance the current account deficits. International prices of food and energy stayed relatively stable in 2012, but some developing economies experienced high inflation rates due to country-specific factors which are mainly related to foreign exchange constraint.

3. For the immediate prospects for 2013, the sustainability of sovereign debt, both in developed and developing countries, casts a shadow of vulnerability on the world economy related to two issues of concern. Firstly, the balance sheet adjustments of the financial sector have not been completed in many economies. The asset side of their balance sheets suffered during the global financial crisis of 2008-2009, and the recovery of asset prices has been slow. Most remain below the pre-crisis level. The fiscal intervention of Governments was intended to directly and indirectly support the balance sheet adjustments of the financial sector, but such intervention turned out to be unsustainable in several countries, particularly in southern Europe. The most recent case in point is the financial insolvency crisis in Cyprus for which the Government has been unable to sustain fiscal support. Stagnant asset prices and the slow adjustment of financial sector balance sheets indicate that the world economic situation is still fundamentally fragile. Secondly, with the exception of those countries with natural resources, Governments maintained a stance of fiscal austerity in the 2012-2013 fiscal years, and it is expected that more central banks are shifting to a tighter monetary stance in 2013. Fiscal prudence and the rising level of expected inflation have been offered as the justifications for the general trend of tightening the policy mix. However, policy tightening may negatively affect ongoing balance sheet adjustments in the financial sector in most developed economies.

4. The fragility of the world economic recovery was also reflected in extremely weak employment creation. In developed economies in 2012, weak employment creation resulted in multiple negative effects on employment opportunities in developing economies. Developing economies often suffer from chronic high unemployment, and jobseekers had fewer options for migration to cope with poor employment prospects in their home country. The employment situation has crucial financial implications for developing economies that increasingly rely on worker remittances to finance current account deficits. In sum, the main challenges that the world economy is facing consist of the following: 1) to adjust balance sheets smoothly in parallel with the recovery of asset prices at the global level; 2) to revive the financial sector through an appropriate growth-encouraging macro policy mix; and 3) to create sufficient employment, both in the developed and developing economies, which will be crucial for a solid economic recovery.

5. In the global context, Arab countries exhibited further polarization in their development paths in 2012. Major energy exporters in the region, namely Gulf Cooperation Council (GCC) countries, are on a stable recovery path which was enabled by an expansionary fiscal and monetary policy mix. At the same time, net energy importing countries in the region are struggling to stabilize their economies amid worsening foreign exchange constraint. The polarization was partly due to political instability and social unrest, and it further obstructed the flow of intraregional funds from the major energy exporters of the region. The lack of confidence in intraregional business transactions resulted in the segmentation of economies in the region and the loss of regional leverage, which amplified the seriousness of unemployment throughout the region, even in GCC countries. Amid those economic and employment difficulties, social development in the region has continued gradually through policy reforms and institutional development. However, the social dynamics in the region were characterized by social unrest in parallel with political instability.

II. OIL SECTOR DEVELOPMENT

6. According to the Organization of Petroleum Exporting Countries (OPEC), the total world demand in 2012 averaged 88.8 million barrels per day while total supply of crude oil averaged 89.8 million barrels per day.[1] The demand for crude oil in 2012 is estimated to have increased by 0.8 million barrels per day over the previous year. The trend of declining demand from developed economies continued while demand from developing economies continued to increase. The greatest oil demand growth came from China. Since August 2012, OPEC member countries have gradually reduced crude oil production from the near-maximum level. Meanwhile, the crude production of the United States and Canada has shown a notable increase through the development of shale oil, tight oil and tar sands extractions. Geopolitical risks in crude oil supply are expected to remain, but the world crude oil supply is expected to have sufficient spare capacity for 2013. If needed, OPEC may moderately reduce the production quota in 2013 to balance supply and demand.

7. Crude oil prices experienced a rapid decline in the first half of 2012 mainly due to concern over world demand growth. However, crude oil prices recovered throughout the second half of the year to mark a historic high annual average. The average OPEC Reference Basket Price was US$109.45 per barrel in 2012. During the year the price ranged between a high of US$124.64 per barrel on 8 March and a low of US$88.74 per barrel on 22 June (table 1). Speculations on commodity futures markets remained influential in both selling and buying. Financing for speculators remained available as a result of the prolonged easing of monetary policies in developed economies where nominal interbank interest rates stayed at a historic low. For 2013, the prices of crude oil and fuel products are increasingly dependent on the extent of potential supply glut in the global market. The weak recovery of the world economy continues to be the main concern. Moreover, refiners in North America have become more competitive, due to the increasing production of shale oil, which has reduced the profits of refiners in Asia and Europe. Overcapacity in the oil tanker market is another factor that may lower the price of crude oil and fuel products. As several other classes of assets have begun to show signs of recovery, speculations on oil are expected to be relatively less influential. Having taken those factors into consideration, the OPEC Reference Basket Price for 2013 is projected to range between US$85.00 and US$120.00 per barrel.

TABLE 1. CRUDE OIL PRICE ESTIMATION AND FORECAST, 2010-2013
(*United States dollars per barrel*)

	Minimum	Maximum	Annual average	Forecasted annual average for 2013		
				Lower	Median	Higher
2010	66.84	90.73	77.45			
2011	89.81	120.91	107.46			
2012	88.74	124.64	109.45			
2013				85.00	102.50	120.00

Source: OPEC data for 2010-2012 and forecasts for 2013.

[1] OPEC, February 2013, *Monthly Oil Market Report*, pp. 27 and 67.

8. The total crude oil production of the GCC countries, the major energy exporters of the region, is estimated to average 16.8 million barrels per day in 2012, 4.2 per cent higher than the previous year. Total production marked a record high, surpassing the level of 2008. Iraq continued to expand its production capacity, and crude oil production grew by 11 per cent to average 2.9 million barrels per day in 2012. The crude oil production of Libya saw a rapid recovery from a drastic production plunge in 2011. Its crude oil production has grown to average 1.3 million barrels per day, 89 per cent of the 2010 level. Transport difficulties related to the worsening security situations in the Sudan and the Syrian Arab Republic seriously reduced crude oil production and exports from those countries. In 2012, Yemen managed to maintain the export level of the previous year despite occasional disruptions of pipelines that transport crude oil.

III. REGIONAL ECONOMIC TRENDS

9. The real gross domestic product (GDP) growth on average in the Arab region is estimated at 4.8 per cent in 2012, compared to 2.2 per cent in 2011 (table 2). The recovery in Maghreb economies, particularly Libya, along with consistent growth in GCC economies contributed to the improvement in the average growth rate. However, the polarization of the economies of the region deepened in 2012 and was partly due to political instability, social unrest and armed conflicts. Those factors increasingly obstructed intraregional flow of funds from the major energy exporters of the region. While major energy exporting countries in the region recorded another year of high energy export revenues, energy importers in the region struggled to finance their current account deficits. The weak demand of European economies for non-energy exports from the region and hovering energy prices also contributed to the widening of the current account deficits of energy importing countries in the region. High oil prices combined with the near-maximum output level led to another historic high in energy export revenue for major energy exporters in the region. However, while positive spillovers have been observed in the markets of GCC countries, other Arab subregions have not benefited from the present oil boom, which has deepened the segmentation of the economies of the Arab region.

10. On average, GCC countries are estimated to have 5.7 per cent GDP growth in 2012, after registering 6.6 per cent growth in 2011. Despite the decelerating growth rate, GCC economies showed more robustness with consistent domestic demand growth. With the exception of Saudi Arabia, the most important concern that emerged from the global financial crisis of 2008-2009 was the possible implosion of domestic demand and debt deflation. Favourable external economic conditions such as the recovery in energy prices and international coordination of monetary easing favourably influenced economic sentiment and confidence in GCC countries. The balance sheet adjustment of the financial sector of GCC countries progressed smoothly despite the fact that prices of both financial and property assets have yet to recover to the pre-crisis level. Saudi Arabia led the economic recovery in the subregion. The Saudi Arabian economy continued to experience stable domestic demand-led growth, supported by an expansionary fiscal and monetary policy mix.

11. For 2013, stable economic growth is expected to continue in GCC countries, though the average GDP growth rate is likely to taper off, reflecting the expected decline of energy export revenue. Both crude oil production and prices are expected to decline moderately. However, strong domestic demand growth is expected throughout GCC countries with the recovery of the balance sheets of the financial sector. To diversify economies based on energy production, continuing efforts will include institutional reforms and targeted foreign direct investment, and will create further growth potential in the subregion. The average real GDP growth rate of the subregion is projected at 4.7 per cent for 2013. In general in GCC countries, the structural fragility of domestic demand is likely to be offset by active fiscal policies and projects implemented in the non-energy sector. In the case of Kuwait, however, projections indicate that domestic demand growth will remain relatively weak and non-energy sector growth will be slow. In 2013, the forecasted growth rates are 3.0 per cent for Bahrain, 3.2 per cent for Kuwait, 4.0 per cent for Oman, 5.2 per cent for Qatar, 5.5 per cent for Saudi Arabia, and 3.8 per cent for the United Arab Emirates.

TABLE 2. REAL GDP GROWTH RATE AND CONSUMER PRICE INFLATION, 2009-2013
(*Annual percentage change*)

	Real GDP growth					Consumer price inflation				
Country/Area	2009	2010	2011[a/]	2012[b/]	2013[c/]	2009	2010	2011	2012[b/]	2013[c/]
Bahrain	2.5	4.3	1.9	3.4	3.0	2.8	2.0	-0.4	2.8	3.2
Kuwait	-7.1	-2.4	6.3	4.7	3.2	4.0	4.0	4.8	2.9	3.2
Oman	3.3	5.6	0.3	6.5	4.0	3.2	3.2	4.1	2.9	3.2
Qatar	12.0	16.6	13.5	6.2	5.2	-4.9	-2.4	1.9	1.9	2.5
Saudi Arabia	0.1	5.1	7.1	6.8	5.5	4.1	3.8	3.7	2.9	3.0
United Arab Emirates	-4.8	1.3	4.2	4.0	3.8	1.6	0.9	0.9	0.7	2.0
GCC countries	-0.7	4.6	6.6	5.7	4.7	2.7	2.6	2.9	2.2	3.7
Egypt[d/]	4.7	5.1	1.9	2.2	3.2	11.8	11.3	10.1	7.2	11.0
Iraq	5.8	5.9	8.6	11.3	7.8	-2.8	2.4	5.6	6.1	6.0
Jordan	5.5	2.3	2.6	2.7	2.9	-0.7	5.0	4.4	4.8	5.0
Lebanon	8.5	7.0	1.5	1.2	1.8	1.2	4.0	4.9	6.6	5.2
Palestine	7.4	9.3	12.2	5.3	4.0	2.8	3.7	2.9	2.7	3.0
Syrian Arab Republic	5.9	3.4	-2.0	-31.4	-7.1	2.8	4.4	4.7	36.5	12.0
Arab Mashreq	5.6	5.1	2.2	-1.7	2.6	6.5	7.7	7.6	11.4	9.3
Algeria	2.4	3.3	2.9	2.8	2.9	5.7	3.9	4.5	8.6	4.8
Libya	-0.7	4.2	-61.3	100.7	15.0	2.5	2.5	15.0	5.0	3.5
Morocco	4.8	3.7	5.0	2.8	4.9	1.0	1.0	0.9	1.3	1.8
Tunisia	3.1	3.2	-1.9	2.6	3.6	3.5	4.4	3.6	5.6	5.2
Arab Maghreb	2.5	3.6	-9.3	10.6	5.3	3.6	3.0	5.5	5.7	3.9
Comoros	1.8	2.1	2.2	2.5	3.5	4.8	4.2	6.8	5.0	3.2
Djibouti	5.0	3.5	4.8	4.7	4.8	1.7	4.0	6.8	5.0	3.2
Mauritania	0.1	5.6	5.1	4.8	6.3	2.2	6.3	5.7	6.2	6.0
Somalia	--	--	--	--	--	--	--	--	--	--
Sudan	5.9	5.2	2.7	-7.0	2.5	11.2	13.0	18.1	35.1	22.0
Yemen	4.3	6.8	-15.3	-1.0	4.5	5.4	11.1	19.4	10.2	9.5
Arab LDCs[e/]	5.1	5.5	-2.3	-4.6	3.2	9.5	11.6	17.2	24.6	16.5
Total Arab region[f/]	1.3	4.5	2.2	4.8	4.4	3.9	3.9	4.9	5.5	4.8

Source: National sources and United Nations Statistics Division for Algeria, Comoros, Djibouti, Libya and Mauritania.

a/ Figures for 2011 are preliminary and are subject to revision. The figures for Lebanon, the Sudan, the Syrian Arab Republic and Yemen are estimates as of March 2013.

b/ March 2013 estimations.

c/ March 2013 forecasts.

d/ Annual GDP growth rates are for Egypt fiscal year, 1 July-30 June.

e/ Least developed countries.

f/ Figures for country groups are weighted averages, where weights for each year are based on GDP in 2005 constant prices.

12. The economies in the Arab Mashreq subregion are, on average, estimated to have contracted by 1.7 per cent in 2012, after registering 2.2 per cent growth in 2011. The devastation of the Syrian economy was the most significant factor in the economic contraction of the subregion. It was most affected by political instability, social unrest and economic repercussion of the Syrian crisis. The slump in non-energy exports and the higher cost of energy imports widened the account deficits. Moreover, weakened capital inflows into the subregion from GCC countries and Europe made it difficult to finance external deficits. Tourism, which had

been one of the main economic activities for the domestic demand growth of Arab Mashreq economies, was substantially affected by various security warnings which deterred tourists from visiting the subregion. Construction activities, another pivotal source for domestic demand expansion, have also slowed down. Meanwhile, industrial development of the subregion marked a significant set-back particularly in the Syrian Arab Republic. The production factories and facilities in Syrian industrial zones were severely damaged by the ongoing conflict. The real GDP growth of Iraq was mainly due to a special factor of crude oil production expansion, which did not correspond to the slow domestic income growth. The real GDP growth of Palestine was also based on a scaling-effect for the ongoing reconstruction of the economy in the Gaze Strip. The physical blockades and continuing insecurity, instability and hostility constrain the Palestinian economy.

13. For 2013, the Arab Mashreq subregion is projected to mark a moderate recovery at 2.6 per cent growth on average. The figure is highly influenced by the increasing crude oil production of Iraq and other energy-related activities in the subregion. As no resolution to deteriorating security situations is yet in sight, particularly in the Syrian Arab Republic, business confidence and consumer sentiment are expected to stay weak in 2013. Moreover, capital account position is expected to stay weak, and the risk remains that there will be further difficulties related to the balance of payments. The space for domestic demand growth remains limited by both supply and demand side factors. Fiscal austerity is expected to continue in Egypt, Jordan and Lebanon, and it is likely that Egypt and Jordan will adopt a tighter monetary policy stance in defence of their national currencies. The resource flows of official development aid are expected to be crucial for the subregion to reduce fiscal and foreign exchange constraints. In 2013, the forecasted growth rates are 3.2 per cent for Egypt, 7.8 per cent for Iraq, 2.9 per cent for Jordan, 1.8 per cent for Lebanon, 4.0 per cent for Palestine. The economy of the Syrian Arab Republic is projected to contract further by 7.1 per cent.

14. The economies in the Maghreb subregion are, on average, estimated to have grown by 10.6 per cent in 2012, after registering 9.3 per cent contraction in 2011. The major factor in subregional economic expansion is that energy production resumed in Libya in 2012 after it collapsed in the previous year. Despite the phenomenal rate of growth, the Libyan economy has not reached the pre-crisis level of 2010. Meanwhile, the economy of Morocco was affected by the underperforming agricultural sector due to poor weather conditions. Despite increasing social unrest and security incidents, the subregion exhibited resilience and moderate growth. For Algeria, stable energy export revenues were sufficient to cushion negative economic and non-economic impacts. The availability of international finance in Morocco and Tunisia filled the gap of external deficits and reduced the severity of foreign exchange constraint. Moderate domestic demand expansion was observed throughout the subregion. Nevertheless, growth was clearly insufficient to create enough decent employment opportunities, particularly for young jobseekers.

15. For 2013, the Maghreb subregion is projected to continue to grow by 5.3 per cent. With that rate of growth, the subregion is expected to surpass the pre-transition level of 2010. In spite of unsettling social unrest in several cities and neighbouring countries, the Maghreb countries are well situated to receive foreign direct investment and international aid and the business environment of the subregion is increasingly perceived to be less risky than that of Arab Mashreq. Uncertainty concerning the investment environment has gradually lifted, particularly in the energy-exporting countries of Algeria and Libya. The continuing sovereign debt crisis in the euro area may cause foreign investors to re-evaluate the potential of Morocco and Tunisia. However, the structural fragility of the economy of the subregion remains because of its weak export-oriented non-energy production base. More decent employment opportunities are urgently needed to resolve the fundamental cause of social unrest in the subregion. In 2013, the forecasted growth rates are 2.9 per cent for Algeria, 15.0 per cent for Libya, 4.9 per cent for Morocco and 3.6 per cent for Tunisia.

16. The economies of Arab least developed countries (LDCs) are, on average, estimated to have contracted by 4.6 per cent in 2012, following the contraction of 2.3 per cent the previous year. Economic contraction in the Sudan and Yemen accounted for much of trend in the subregion. The struggle of the Sudan for economic stability continued after the succession of South Sudan. A number of armed conflicts over the border area in early 2012 hindered a smooth adjustment to the new economic environment. However, the Sudan and South Sudan finally reached an agreement over the terms of oil production and transportation in

March 2013, and external economic and non-economic factors are expected to stabilize. Due to the loss of crude oil export revenue, the Sudan suffered from severe foreign exchange constraint which negatively affected domestic demand and income. The economy of Yemen was more stable toward the end of 2012. Although the security situation worsened, the country maintained a stable crude oil export level. The energy export revenue, both in crude oil and liquefied natural gas, prevented domestic demand from falling further. Furthermore, financial support for the transition in Yemen was actively pledged at the regional and international levels. Other Arab LDCs, Comoros, Djibouti and Mauritania, marked moderate GDP growth in 2012, which has made only a weak contribution to the income level of those countries. The economic outcome of political stabilization in Somalia was still uncertain during 2012.

17. For 2013, real GDP growth of Arab LDCs is projected to average 3.2 per cent. The stable growth in energy and natural resource exports is expected to buoy GDP in Mauritania and Yemen. The economic prospects of Comoros and Djibouti depend largely on that of neighbouring countries, which are expected to be stable. The Sudan is expected to mark positive growth after two years of economic decline. The severe foreign exchange constraint is to remain, but its extent is expected to be relaxed due to the consistent growth in non-energy exports. The growth prospects of Arab LDCs are, however, far too weak to reduce the prevailing poverty level. In 2013, the forecasted growth rates are 3.5 per cent for Comoros, 4.8 per cent for Djibouti, 6.3 per cent for Mauritania, 2.5 per cent for the Sudan and 4.5 per cent for Yemen.

18. The average consumer price inflation rate of the Arab region is estimated at 5.5 per cent in 2012, compared to 4.9 per cent in 2011 (table 2). Although international commodity prices of energy, metal and food items hovered at a higher level, no extreme price spikes were observed during 2012. While the pass-through from international commodity markets had less impact, the consumer inflation level of each country was determined by country-specific factors. Deflationary pressure remained on housing-related items in Bahrain, Qatar and the United Arab Emirates. Weak property rent and the oversupply of rental properties contributed to the trend, which became apparent after the global financial crisis of 2008-2009. By contrast, Saudi Arabia and Oman were under constant inflationary pressure, including housing-related items, owing to the sustained growth of real estate sector. Nevertheless, consumer inflation averaged 2.2 per cent in GCC countries in 2012, and with the exception of Morocco, other Arab countries experienced a higher consumer inflation rate. Structural supply bottlenecks resulted in hovering consumer prices in the Arab Mashreq, Maghreb and Arab LDCs, and inflation accelerated in the countries under foreign exchange constraint, namely Egypt, the Sudan and the Syrian Arab Republic. The upward shift of private sector wages in parallel with recent wage hikes in the public sector was observed in GCC countries, but the shift is not expected to influence the inflation rate of GCC countries.

19. The average consumer price inflation rate of the Arab region is forecasted to average 4.8 per cent in 2013. The low-inflation regime of GCC countries is expected to continue. Food prices have been observed to increase since 2012, but the price increase is expected to remain moderate. Moreover, the price of housing-related items, such as property rents, is projected to be depressed in Bahrain, Kuwait, Qatar and the United Arab Emirates. Although the exceptionally high inflation rates in the Syrian Arab Republic, the Sudan and Yemen of 2012 are expected to taper off in 2013, the severe foreign exchange constraint is anticipated to raise the price level of those countries. Egypt is also expected to experience an acceleration of inflation due to the foreign exchange constraint and the devaluation of its national currency. In 2013, GCC countries may implement another round of wage hikes in the public sector, but the impact on general price level is expected to be limited. With the exception of a few occupation categories in GCC countries, private sector wages in the region are expected to stay depressed. Wage-push inflation is not likely to take place in 2013 in the region. Surplus fiscal and external accounts of GCC countries will maintain sufficient supply capacity for domestic demand growth. In other subregions, the private sector wage level is expected to be depressed though the year, meaning that wage-push inflation could only result from public sector wages. Since 2012, public sector wage hikes have been proposed in a few countries, most notably in Lebanon, but the impact on projections of inflation remains uncertain.

20. The exchange rates of the Arab region stayed stable from 2012 to early 2013 with the exception of Egypt, the Sudan and the Syrian Arab Republic. Kuwait has continued to peg its national currency to the basket of foreign currencies, while other GCC countries have kept their national currencies pegged to the United States dollar. Djibouti, Jordan and Lebanon have also continued to peg their national currencies to the dollar. Central banks of Algeria, Comoros, Iraq, Libya, Mauritania, Morocco, Tunisia and Yemen maintained the managed float regime of foreign exchange rates. For the Sudan and the Syrian Arab Republic, the rapid decline in the value of the national currency widened the spread between the official exchange rate and the exchange rate of parallel markets. Foreign currencies were rationed. Economic sanctions and other non-economic events contributed in large measure to the national currency depreciation in the Sudan and the Syrian Arab Republic, whereas the depreciation of Egyptian pound was caused primarily by economic factors. In a space of three months beginning in December 2012, the Egyptian pound depreciated by 8 per cent to the level of 6.8 pounds per dollar in March 2013. As of April 2011, the Egyptian pound had been pegged to dollar as a nominal anchor for the Egyptian economy during unstable political and social transitions. Throughout 2010, Egyptian pound gradually depreciated by 7 per cent from 5.4 to 5.8 pounds per dollar. The currency peg regime was effective in maintaining the level of domestic demand during the highly turbulent period. However, it resulted in the rapid dwindling of foreign reserves from US$28 billion in April 2011 to around US$15 billion in February 2012. Egypt was wary of resuming the gradual depreciation policy because there was a risk that currency devaluation could cause an immediate fiscal crisis by increasing food and energy subsidies, while only modestly enhancing the competitiveness of Egyptian exports. A gradual depreciation of the Egyptian pound is expected to continue in 2013, but the key to the orderly resolution of the present balance of payment crisis in Egypt rests on the prospects of fiscal reform.

21. Armed violence in the Syrian Arab Republic, the destruction of commercial and residential properties, infrastructure and production facilities has already caused significant economic damage. It was estimated that GDP in real terms contracted by 31.4 per cent in 2012. The contraction of GDP arose neither from idle production capacity nor the suspension of economic activities. Rather it has been caused by damage to physical capital stock and the loss of human capital. Even under the most optimistic scenario, it would take at least a few years for Syrian economy to regain the level it had in 2010. Economic sanctions that have been imposed by the United States, the European Union and the League of Arab States caused severe foreign exchange constraint. After financial sanctions and the oil embargo were imposed in 2011, the Syrian economy lost a substantial amount of export revenue and difficulties in financing hampered its trade facilitation capacity. The official exchange rate of the national currency, the Syrian pound, gradually fell from 47.1 pounds per dollar in January 2011 to 87.09 pounds per dollar in March 2013, with a widening spread between the official rate and parallel market rate. The devaluation of the national currency and the destructions of domestic transport networks caused hyperinflation. The year-on-year consumer inflation rate surged from 5.8 per cent in November 2012 to 49.7 per cent in November 2013.

22. Despite the magnitude of the violence and destruction, the Syrian economy exhibited resilience and avoided falling to a complete halt. Financial institutions are still in operation and international trade with neighbouring countries continued though at a reduced level. For example, according to Lebanese customs data, Syrian exports to Lebanon in January 2013 stood at US$16.0 million which is 56 per cent of the pre-crisis monthly average in 2010. Neighbouring countries felt the impact of the crisis not only in reduced trade through the Syrian Arab Republic, but also through the spillover of geopolitical tensions. It adversely affected risk perception in the subregion of Arab Mashreq and the inflow of capital and tourists, which had been the main driver of recent economic expansion in Jordan and Lebanon. Moreover, the rapidly increasing number of Syrian refugees to Jordan and Lebanon has put an additional fiscal burden on both countries. At the end of March 2013, the Office of the United Nations High Commission for Refugees (UNHCR) estimated the number of Syrian refugees at 1.23 million, of which 396,000 refugees were in Lebanon and 394,000 refugees were in Jordan.[2] As of March 15, 2013, the only 31 per cent of the required funding for the UNHCR regional response plan had been provided.

---

[2] Updated figures are available from http://data.unhcr.org/syrianrefugees/regional.php. Figures are of “persons of concern”, the total number of registered refugees and those awaiting registration.

IV. POLICY DEVELOPMENTS

23. The economic environment that policymakers faced in 2012 diverged significantly between major energy exporters of GCC countries and other Arab subregions. To mitigate the risk of domestic demand stagnation and continuing deflationary pressures, Governments in GCC countries adopted a mix of expansionary fiscal and monetary policies. That expansionary policy path was sufficiently sustainable given the ample fiscal space created by growing energy export revenues and the continued monetary easing of the United States. The monetary policy of GCC countries mirrors that of the United States through the currency peg. By contrast, the Governments of other Arab countries were under pressure to implement further fiscal consolidation through austerity measures. Monetary policy has also tightened in energy importing countries in Arab Mashreq and Maghreb. In response to the rising inflationary pressure from worsening foreign exchange constraints, central banks in Egypt, Jordan and Tunisia tightened their monetary stances by early 2013. A clear policy dilemma existed in energy importing countries in the Arab Mashreq and Maghreb, as a much-needed pro-growth mix of fiscal and monetary policy became unaffordable.

24. Despite the limited latitude of monetary policy in GCC countries owing to the link to the United States dollar, the relatively stable general price level allowed central banks in GCC countries to comfortably stay an easing stance in parallel with the United States monetary authority. The funding cost of the three-month interbank money market has converged around 1.0 per cent among GCC countries, 70 basis points higher than three-month United States dollar London Interbank Offered Rate (LIBOR). A policy shift for monetary easing was seen in Yemen where the Central Bank lowered policy interest rates in October 2012 and February 2013 to 15 per cent. A neutral monetary stance was maintained in Algeria, Lebanon and Morocco. Monetary policy was tightened in Egypt, Jordan, the Sudan and Tunisia in order to cope with inflationary pressures from binding foreign exchange constraints. The Central Bank of Egypt raised policy interest rates in March 2013 for the first time since November 2011, which brought the overnight deposit rate to 9.75 per cent. The Central Bank of Jordan raised its policy rates in February, June and December of 2012, by which the overnight deposit rate reached 4.0 per cent. The Central Bank of Tunisia raised its policy interest rate in August 2012 and March 2013 to 4.0 per cent.

25. For the fiscal years 2012 and 2013, the stance of GCC countries remained expansionary. The emphasis on infrastructure investment, health and education, and social provision continued. The main challenge for GCC countries in the fiscal policy area was scope rather than size. It became increasingly important to implement budgeted projects effectively in order to attain long-term policy goals such as improvement in productivity. The boom in revenue could easily be used for income transfers or similar expenditures, rather than public investment for physical or human capital formation. Given chronic high unemployment among nationals, GCC countries are keen on strategizing fiscal policy with a comprehensive development plan in both the economic and social spheres. By contrast, energy importing countries of Arab Mashreq, Maghreb and Arab LDCs struggled to form and implement fiscal austerity measures in the fiscal years 2012 and 2013. In need of fiscal consolidation, the reform of food and energy subsidies has become the main policy focus of those Governments. Attaining consensus for reform while assuring a basic living standard for low income populations will be a challenging priority in forming fiscal policy measures in the years ahead.

26. Employment challenges worsened in the Arab region in 2012. In addition to chronically high unemployment among nationals, the prolonged economic slump in North America and Europe discouraged the immigration of jobseekers. A sizeable trend of return migration from Europe was observed in the Maghreb. The employment situation in GCC countries remained unbalanced, with foreign workers constituting the majority of the workforce in the private sector. In spite of its consistently expanding domestic economy, the labour markets in GCC countries continue to exhibit the combination of a high unemployment among nationals and a low unemployment among foreign workers. The policy to increase the share of the nationals in the private sector workforce has been in place more than a decade in GCC countries, and in 2012, there was more stringent application of that policy. The case in point was Saudi Arabia, where as of November 2012, firms that do not employ a legally-set proportion of Saudi nationals must pay a fine. Saudi Arabia also campaigned for the promotion of female employment. More occupational classes in the private sector were opened for female jobseekers and several Government ministries began employing

female workers. Moreover, 30 prominent female figures were appointed to the Shura Council for the first time in the history of the country. The gradual shift of labour policy in Saudi Arabia is expected to impact other GCC countries and countries of other Arab subregions.

V. CONCLUSION

27. On average, the GDP growth rate of the Arab region is likely to taper off in 2013 due to the decline in energy export revenues which marked a historic high in 2012. It should be noted, however, that it is increasingly difficult to project economic and social developments in the region for 2013. The polarization of the economic and social developments in the region is anticipated to deepen and several signs of further segmentations have already been observed. Moreover, the region is exposed to the downside risk of dependency on energy exports. In spite of the active policy efforts for economic diversification, major energy exporting countries are still far from diversification targets. It is considered unlikely that there will be another oil price plunge like the one that occurred in 2008, nevertheless the weakened non-energy sector in the Arab Mashreq and Maghreb indicates that the economy of the Arab region is more vulnerable to abrupt changes in the energy price. A strong recovery is not foreseen in confidence for intraregional business transactions, particularly in the Arab Mashreq. However, the structural weakness of the economies in the Arab region, represented by high unemployment and income inequality, is the chronic undercurrent that motivates social unrest and political instability. In turn, social unrest and political instability can lead to further economic underperformance and reinforce a vicious cycle. In order to break out of that cycle, the Arab region must leverage economic activities through further cooperation frameworks and the augmentation of integration efforts.