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SUMMARY OF THE SURVEY OF ECONOMIC AND SOCIAL DEVELOPMENTS IN THE ECONOMIC AND SOCIAL COMMISSION FOR WESTERN ASIA REGION, 2010-2011

Summary

The slowdown in the recovery of the global economy is expected to have an unfavourable impact on the economies of the member countries of the Economic and Social Commission for Western Asia (ESCWA) in 2011. However, a relative improvement in public finances and current account balances, particularly in the member countries of the Gulf Cooperation Council (GCC), which has also had some positive spillover effects in the more diversified economies (MDEs) in the region, coupled with the recent increase in oil prices, will go some way towards offsetting the potential impact of the global slowdown. The ESCWA region has also recently witnessed an unprecedented wave of social movements, which have spread across a number of member countries. The response to these movements has varied, ranging from an expansion in social spending to peaceful regime change and, in certain cases, to violence. In the very short term, the uncertainty brought about by change may undermine the economic and social outlook, but once conditions of greater stability and normality return, prospects should brighten. In 2010, average real gross domestic product (GDP) growth across the ESCWA region is estimated to have been 4.3 per cent, up from 1.7 per cent in 2009, with an increase to 5.1 per cent forecast for 2011.

To date, the monetary and fiscal authorities in ESCWA member countries have, in general, managed to weather the macroeconomic effects of the global crises. These achievements, however, need to be extended to cover other socio-economic areas which so far have prevented the relatively adequate growth rates from being translated into lower unemployment rates and poverty alleviation.

The socio-political events which have taken place in a number of ESCWA member countries since January 2011 have been unprecedented, both in their dynamics and in their potential for bringing about change in the region. These social movements, coupled with the series of economic crises which predated them, have exposed the weaknesses of the development models adopted to date by member countries. It is clear that a new development model is needed for the region and it is critical that that model should respond to the aspirations of the people who have led those movements. The new model should be more holistic, integrating the economic and social spheres, providing strong institutions and full democratization, ensuring the active participation of all in the decision-making process.

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A. GLOBAL CONTEXT

1. The recovery of the global economy from the financial crisis continued in 2010, albeit at a slower pace, with renewed increases in the prices of oil, commodities and, in particular, food. More recently, the repercussions of the Japanese crisis have placed an additional burden on the global economy, and the financial turbulence that emerged in the periphery of the eurozone towards the end of 2010 also had a negative impact on global conditions. There are fears of further macroeconomic imbalances in 2011, resulting principally from widening fiscal deficits and rising public debt, and several Governments have introduced fiscal austerity measures in their 2011 budgets. The stagnating GDP growth rates in the developed economies, coupled with potential currency wars and balance of payments imbalances, also bode ill for the economic outlook. It is predicted that the emerging economies in general will continue to suffer from volatile capital flows, weak global demand for their exports, and less fiscal and monetary space to deal with further potential macroeconomic imbalances.

2. The impact of these developments on ESCWA member countries varies from country to country, depending on the structure of each economy and its level of integration with the eurozone and the rest of the world. Overall, however, the region is still expected to benefit from rising international oil prices, which will attenuate the unfavourable impact of the global economic situation.

3. On the social front, the repercussions of the slowdown in global economic recovery on developed and less developed countries remain strong and are most evident in terms of rising unemployment rates. According to the International Labour Organization (ILO), the global unemployment rate in 2010 was estimated at 6.2 per cent, almost unchanged from 6.3 per cent in 2009. Developed countries saw a continued increase in global unemployment, while developing countries experienced unemployment rates ranging from steady to slightly improving.[1] Overall, employment in many ESCWA member countries and other developing countries continues to face serious stagnation.

4. The social pressures on developing ESCWA member countries have increased with the recent rises in food prices, given the high dependency on food imports across the region. The food price index maintained by the Food and Agriculture Organization of the United Nations (FAO) increased by some 24 per cent in 2010 and registered a further 6.0 per cent increase in the first two months of 2011, reaching its highest level since the index was initiated in January 1990. The unfavourable international economic conditions set the stage for the social discontent that spread across the ESCWA region in early 2011 and, in certain cases, developed into fully-fledged social movements. While the region had managed to minimize the damage from the financial crisis in terms of lost output, it had failed to address its socio-economic and political problems, which had been masked by generally adequate growth performance. However, international developments and the clear warning messages sent by the recent social movements have highlighted the importance of addressing external vulnerability and managing domestic economies in order to deal with future economic shocks more effectively. It is vital that ESCWA member countries not only maintain macroeconomic stability and growth rates throughout 2011, but also reconsider macroeconomic and social policies in combination, in order to shield their people from socio-economic insecurity and creating a political environment which allows citizens to voice concerns freely and influence the decision-making process.

B. OIL SECTOR DEVELOPMENT

5. According to estimates by the Organization of the Petroleum Exporting Countries (OPEC), total world demand for 2010 averaged 86.4 million barrels per day, while total supply of crude oil averaged 86.2 million

[1] See ILO, *Global Employment Trends*, January 2010.

barrels per day.[2] Demand for crude oil is estimated to have increased by 1.8 million barrels per day compared with 2009. Demand in the countries of the Organisation of Economic Co-operation and Development (OECD) was moderate, while demand from developing countries was resilient. The oil-producing countries of the ESCWA region which are also members of OPEC have increased their production levels moderately since January 2009, following an earlier decrease of 4.2 million barrels per day in response to the global recession, while crude oil production in non-OPEC ESCWA member countries remained relatively stable, given their limited capacity to expand exploration and production. For 2011, the recent social movements in North Africa and Western Asia, coupled with the current crisis in Japan, constitute a serious risk to the growth prospects of the world economy. Given this global context, demand and supply of crude oil is expected to balance out at approximately 87.8 million barrels per day in 2011, a 1.6 per cent increase on 2010.

6. The OPEC Reference Basket (ORB) price exceeded US$100 in February 2011 for the first time since September 2008 and in March 2011 averaged US$110. This constitutes a 50 per cent increase since mid-2010, the bulk of the increase being observed since December. Demand factors associated with the depreciation of the US dollar accounted for the price increases until the spread of the social movements in North Africa and Western Asia raised supply concerns at the production and transportation levels, leading to strong financial speculation in the oil futures market. In this context, heightened political risk premiums associated with security developments in the region were priced-in, while the developments in Japan and their repercussions on global demand and supply conditions are yet to be factored in. The moderate global economic recovery observed in 2010 and the beginning of 2011 supported refining margins as measured by the spread between WTI crude oil prices and reformulated blendstock for oxygenate blending gasoline prices. This upward trend is expected to ease in 2011, given sufficient spare capacity in production and refining globally, and a moderate slowdown in global recovery. However, political risks weigh heavily on these forecasts, particularly following the social movements in Bahrain, Egypt, the Libyan Arab Jamahiriya, the Syrian Arab Republic, the Sudan, Tunisia and Yemen. In this context, the average crude oil price of the OPEC reference basket is forecast to range between US$90 and US$115, with a median anticipated at US$95 (see table 1).

7. Given the moderate global recovery seen in 2010, the total crude oil production of ESCWA member countries was estimated at 18.7 million barrels per day, a 2.5 per cent increase on 2009. The production of the GCC countries was estimated at 14.6 million barrels per day, while that of other crude oil-producing countries in the ESCWA region (Egypt, Iraq, the Sudan, the Syrian Arab Republic and Yemen) was estimated at 4.1 million barrels per day. OPEC production ceilings have been maintained at an average of 24.8 million barrels per day since January 2009 following the expectation of the global economic recession. As of March 2011, it is not clear whether those quotas will be increased to meet the anticipated increase in oil demand from Japan, the third largest oil consumer globally, as a result of the disruption currently affecting its nuclear industry. Nevertheless, recent security developments in the Libyan Arab Jamahiriya, which produces some 1.6 million barrels per day (2 per cent of global crude oil production), will undoubtedly lead to an informal reallocation of production between OPEC member countries in line with their spare capacity. Saudi Arabia has already officially offered its large spare capacity. Consequently, the total crude oil production of ESCWA member countries is projected to increase by approximately 6.0 per cent in 2011, to 19.9 million barrels per day. The total production of the GCC countries is expected to stand at 15.6 million barrels per day in 2011, on the back of intensive previous investment by some member countries to lift their capacity constraints, that of the MDEs is projected to increase by 3.2 per cent to 4.3 million barrels per day. The normalization of the security situation in Egypt should allow oil production to stabilize at previous levels, and the Syrian Arab Republic and Yemen are expected to halt, at least temporarily, their recently-observed declining trend. Moreover, Egypt, the Syrian Arab Republic, the Sudan and Yemen have engaged in the development of their gas sectors, a field which is led by Qatar, the largest global exporter of liquefied natural gas (LNG). In this respect, the Japanese crisis is expected to affect energy

[2] See OPEC, *Monthly Oil Market Report*, March 2011.

markets for the remainder of 2011, triggering the substitution of crude oil, LNG and coal for nuclear energy sources in proportions yet to be determined. Consequently, the LNG market is expected to come under significant strain, which will be partly to the benefit of Qatar and other member countries diversifying away from oil. The total gross oil export revenues of the ESCWA region in 2010 were estimated at US$477 billion, against the average OPEC reference basket forecast of US$77.45 per barrel. These revenues are forecast to increase by 30 per cent in 2011 to US$620 billion against the median forecast average ORB price of US$95, with a slightly lower growth rate of 25 per cent for the MDEs, on the combined increase of production and price levels. It should be noted, however, that these global figures mask downside risks to the projections at the country level, notably the security situation in Bahrain and Yemen, as normalization appears to have been re-established elsewhere in the region.

TABLE 1. CRUDE OIL PRICE ESTIMATION AND FORECAST, 2008-2011
(*OPEC reference basket: US$/barrel*)

	Minimum	Maximum	Annual average	Forecast annual average for 2011		
				Lower	Median	Higher
2008	33.36	140.73	94.45			
2009	38.14	78.0	61.06			
2010	68.21	90.73	77.45			
2011				90.0	95.0	110.0

Source: OPEC for 2008-2010. Figures for 2011 are ESCWA forecasts as at March 2011.

C. ECONOMIC TRENDS AND DEVELOPMENTS

8. After the pessimism which prevailed in 2008-2009, the economic outlook in the ESCWA region has been continuously improving on the back of domestic and external demand recovery. Average real GDP growth is estimated at 4.3 per cent for 2010, compared with 1.7 per cent in 2009, with 5.1 per cent forecast for 2011 (see table 2). Crude oil prices, which tend to determine income and wealth in the region, increased steadily in 2010, with the ORB averaging more than US$77 per barrel in 2010, compared with an average of US$60 per barrel in 2009, representing an increase of 27 per cent. The region successfully averted the main risks posed by the financial crisis on the real, monetary, financial and external fronts, but, following recent social movements, now faces a set of new, region-specific challenges. For 2011, recovery in the ESCWA region is expected to continue at a steady pace, based on healthy domestic demand growth, backed by a continued fiscal stimulus and a strong net exports contribution. Favourable oil price developments are expected to have a positive impact on general business and consumer confidence. The main oil producers in the GCC countries will reap important benefits through sustained higher oil prices and increased production levels. This will allow GCC fiscal authorities to maintain an active fiscal stance amid the nascent social movements, supporting household incomes and private consumption, and meeting their main targets in terms of infrastructure investment, health, education and social provisions, while maintaining comfortable fiscal surpluses and lowering their debt levels. The MDEs are expected to benefit from the intraregional spillover effects of oil revenues, which will continue to relieve balance of payments pressures. At the domestic level, notwithstanding the deteriorating macroeconomic conditions in certain MDEs, Government consumption and general investment will support private demand amid moderate increases in bank lending, labour market reforms and a better business environment, with a relative return to normalization in Bahrain and Yemen. Development plans to tackle infrastructure projects are being launched and budget expenditure has been increased since the beginning of 2011 to support higher social transfers, private housing, and public sector employment and wage levels. On the external side, positive developments are expected to continue, as increases in the price of crude oil have been sustained to date in 2011. Neither financial market sentiment nor security developments appear to signal a reversal in oil market trends at this stage, as most crude oil price forecasts for 2011 have been reviewed significantly upwards.

9. Despite such relatively favourable performance, human development growth in the region has not moved forward in line with the aspirations of its population; indeed, it has failed to advance the human rights agenda or to reform politics and institutions to deliver in that respect. The rewards from growth have remained limited and subject to discretionary Government interventions, revealing the limitations of the economic development models adopted. This has been a major driver behind the recent social movements in certain countries. Economic growth continues to face a number of risks, resulting from domestic political uncertainty, social unrest and the global developments discussed above. However, as stability returns, the prospects for the ESCWA region should improve, allowing for fresh consideration of social and economic policy choices in the search for a new development model.

10. Consumer price inflation in the region has been subdued since the peaks observed in the second quarter of 2008 and the figures for 2010 indicate diversity in inflation developments across the region. Average consumer price inflation was estimated at 4.5 per cent in 2010, compared with 3.9 per cent in 2009. In the GCC countries, average inflation was estimated at 3.1 per cent, dominated by the deflationary pressures in Qatar and the United Arab Emirates, while double-digit inflation figures in Egypt and the Sudan resulting from structural supply bottlenecks led to estimated average inflation in the MDEs of 8.1 per cent. In 2011, average inflation in the ESCWA region is forecast at 5.4 per cent. Costs and consumer price developments will be affected by both recent and anticipated increases in food, international commodity prices, wage increases and other social measures. However, inflationary pressures are expected to be relatively subdued by a variety of factors, including extensive food and energy subsidies, the outlook for the US dollar, cautious and relatively weak credit growth, and lower regional liquidity in comparison with the period 2005-2008. It is anticipated that the deflationary trend observed in Qatar in 2009 and 2010 will be reversed, while in Saudi Arabia, inflation is set to increase as a result of higher food prices and housing shortages, although inflationary pressures should be relieved in the medium term with the expected enactment of new mortgage legislation. The deflationary trends observed in Jordan and Iraq during the first half of 2010 have been replaced by inflationary pressures. It should be noted, however, that these overall inflationary trends mask deflationary pressures in the real estate sector, with property rents declining in almost all ESCWA member countries, with the notable exception of Lebanon and Saudi Arabia.

11. The MDEs experienced another year of resilience in 2010, with average real GDP growth estimated at 4.1 per cent. With the rally in the eurozone and GCC economies, the MDE subregion benefited from a positive external environment in terms of remittances, higher levels of tourism and intraregional investment. Oil exporters among the MDEs (Egypt, Iraq, the Syrian Arab Republic, the Sudan and Yemen) benefited from higher oil prices and stable gross oil export revenues. Jordan experienced a recovery in exports, which improved its current account position and, despite limited fiscal policy space, the Jordanian Government achieved an estimated growth of 3.1 per cent in demand management. In Lebanon, construction and tourism led the growth, resulting in significant balance of payments surpluses and an estimated growth rate of 7 per cent. In Yemen, the initiation and expansion of LNG exports since November 2009 has helped to alleviate foreign exchange constraints, but the Yemeni riyal has come under severe devaluation pressures against the US dollar and the Central Bank of Yemen has been forced to intervene heavily in defence of the currency. The growth rate for Yemen in 2010 is estimated at 3.5 per cent, while in Palestine, it is forecast at 4.2 per cent on expectations of a resumption of development aid to the Gaza Strip and the relative stability in the West Bank. In Egypt, growth was estimated to have exceeded 5 per cent in real terms in the first two quarters of the fiscal year 2009-2010, but is forecast to slow down to 3.5 per cent for the fiscal year 2010-2011 as a result of recent developments.

12. Growth prospects for the MDEs vary from country to country and are expected to be affected by the wave of social movements which have spread across the region. In Egypt, the very short-term stance appears unfavourable, with political uncertainty weighing on the economy, yet the long-term outlook is more promising, as stability returns to the country. In the countries in which social movements turned violent, prospects remain unclear and are likely to be less promising, affecting economic forecasts for 2011. This is the case for Yemen, for example, where growth is forecast to reduce to 2.5 per cent in 2011, from an

estimated rate of 3.5 per cent in 2010. In the Syrian Arab Republic, the forecast is for growth of 4.5 per cent in 2011 with the launch of the 2011-2015 five-year plan. The main downside risk in the Syrian Arab Republic are the recent demonstrations, but sizeable infrastructure projects and Government subsidies will support growth. In contrast, forecasts for the Sudan in 2011 hinge on the peaceful implementation of the Comprehensive Peace Agreement following the referendum in January 2011, the effective management of the oil production and refining industries between the two new Governments, and the outcome of debt relief discussions with the Paris Club of Industrial Country Creditors and the international financial institutions. Real GDP growth in the MDEs for 2011 is forecast at an average of 4.8 per cent, led by the two largest economies in the subregion: Egypt, where a healthy recovery is expected, and Iraq, where an increase in growth is also forecast.

13. In the GCC countries, real GDP growth was estimated at 4.3 per cent on average in 2010, following average growth of 0.4 per cent in 2009. Healthy increases in oil revenues and sustained growth in domestic demand were the main drivers of growth in 2010. The GCC countries continued their efforts to diversify their hydrocarbon-based economies through major reforms targeting foreign direct investment (FDI) in the non-oil business and manufacturing sectors. Saudi Arabia led the recovery in the subregion, with an estimated 3.8 per cent GDP growth rate in 2010, a considerable achievement given the size of its economy. Domestic demand growth in Saudi Arabia was stable and the real estate sector recorded healthy growth. In Kuwait, real GDP growth was supported by net exports against a backdrop of lukewarm domestic demand and weak financial sector recovery. In the United Arab Emirates, a rapid recovery in energy-related net exports and sustained domestic demand contributed to growth, while the real estate sector remained weak, marked by continued decreases in commercial and residential rents.

14. In 2011, average real GDP growth in the GCC countries is forecast at 5.2 per cent, almost matching healthy pre-crisis levels. Domestic demand will continue to be supported by active fiscal policies with a modest rally in private spending. Growth in Kuwait is forecast at 3.6 per cent and the country is expected to continue to register the highest budget and current account surpluses in the region. Higher oil revenues will allow the Government to support domestic demand through heavy infrastructure projects and wealth redistribution. In the case of non-OPEC member countries in the subregion, namely Bahrain and Oman, the recent social movements cloud growth prospects. Bahrain is projected to grow at 2.5 per cent as a result of slower tourism and financial sector activity, while domestic demand is expected to be supported by increased regional transfers and investments. In Oman, relative stability has been re-established through higher social transfers and public sector employment. Real GDP growth is forecast at 3.5 per cent on the back of relatively weak domestic demand, despite active fiscal intervention. However, with the risk of a “debt-deflation” trap still looming, significant balance sheet adjustments in business and finance entities remain underway in the subregion amid volatile local capital markets. Monetary authorities and financial sector supervisors and regulators will have to continue to monitor internal and external liquidity conditions to allow smooth completion of balance sheet deleveraging and reorganization. The wave of social movements in the region, coupled with international financial developments, put an end to stock market recovery from the financial crisis troughs experienced in 2008. Stock markets in the United Arab Emirates, Kuwait and Saudi Arabia have proved highly volatile since the start of the social movements in the region in early 2011 and have plunged, partly reversing the gains observed since 2009.

15. Growth prospects will also be boosted by heavy social spending. Governments in the region have attempted to contain popular discontent and respond to a number of social demands. The GCC countries launched a US$20 billion fund for Oman and Bahrain (US$10 billion each), with a view to generating jobs, and upgrading housing and infrastructure. In Bahrain, the Government has identified the problem of low-income housing as the most pressing issue and, in response, plans to build 50,000 housing units. It has also made grants of approximately US$2,650 for every family and boosted housing allowances. Likewise, Oman has raised its minimum wage by 40 per cent. The largest package has been in Saudi Arabia, where a SR500 billion package has been announced, including a minimum wage and a cost-of-living bonus for Government workers, unemployment benefits, and increases in housing loans and health spending. Non-GCC countries

have seen similar interventions, with Jordan, for example, revising its budget to include around JD460 million in additional social spending. It has also increased public sector salaries and employment. In the Syrian Arab Republic, public sector wages have been raised as part of wider reform pledges promised following popular demonstrations. However, notwithstanding the importance of such direct social measures, they remain short-sighted in the way in which they deal with socio-economic problems, resolving only the symptoms, rather than dealing with the structural root causes.

TABLE 2. REAL GDP GROWTH RATE AND CONSUMER INFLATION RATE, 2007-2011

Country/Area	Real GDP growth rate (percentage)					Consumer inflation rate (percentage)				
	2007	2008	2009[a/]	2010[b/]	2011[c/]	2007	2008	2009	2010[b/]	2011[c/]
Bahrain	8.4	6.3	3.1	4.5	2.5	3.3	3.5	2.8	2.0	2.5
Kuwait	4.5	5.5	-4.6	2.0	3.6	5.5	10.6	4.0	4.0	5.5
Oman	6.8	12.8	3.6	4.3	3.5	5.9	12.6	3.5	3.4	4.2
Qatar	26.8	25.4	8.6	13.4	16.0	13.8	15.2	-4.7	-2.4	2.0
Saudi Arabia	2.0	4.2	0.6	3.8	4.5	4.1	9.9	5.1	5.3	5.5
United Arab Emirates	6.2	7.4	-1.9	2.7	3.2	11.1	12.3	1.6	0.9	2.0
Gulf Cooperation Council countries[d/]	**6.1**	**7.9**	**0.4**	**4.3**	**5.2**	**7.0**	**11.1**	**2.9**	**3.1**	**4.2**
Egypt[e/]	7.2	4.7	5.1	3.0	5.0	9.5	17.1	11.8	11.3	11.5
Iraq	1.5	9.5	4.2	4.0	5.5	30.8	2.7	-2.8	2.4	4.0
Jordan	8.5	7.6	2.3	3.1	3.5	4.7	13.9	-0.7	5.0	5.4
Lebanon	7.5	9.3	8.5	7.0	5.6	6.7	10.0	1.2	4.0	4.5
Palestine	5.4	5.9	6.8	4.2	4.5	1.9	9.9	2.8	2.8	3.5
The Sudan	10.2	6.0	4.5	5.5	5.0	8.1	14.9	11.2	13.2	11.5
Syrian Arab Republic	5.7	4.3	5.9	5.5	4.5	4.5	15.2	2.8	4.4	4.7
Yemen	4.7	4.5	4.7	3.5	2.5	7.9	19.0	5.4	8.5	11.0
More diversified economies[d/]	**6.4**	**6.1**	**5.1**	**4.1**	**4.8**	**11.2**	**13.5**	**6.2**	**8.1**	**8.4**
Total, ESCWA region[d/]	**6.2**	**7.4**	**1.7**	**4.3**	**5.1**	**8.2**	**11.8**	**3.9**	**4.5**	**5.4**

Source: National sources unless otherwise stated.

a/ Estimates for Kuwait, the Sudan and the United Arab Emirates as at March 2011.
b/ Estimates as at March 2011.
c/ Forecasts as at March 2011.
d/ Figures for country groups are weighted averages, where weights for each year are based on GDP at 2005 exchange rates.
e/ The GDP growth rates for Egypt are calculated for the country’s fiscal year, which starts in July and ends the following June.

16. Following a significant deterioration in 2009, the current account balances of ESCWA member countries improved in 2010 as crude oil prices and other commodities boosted export revenues, outpacing the import bill amid a moderate expansion in domestic demand. The current account witnessed a moderate recovery in workers’ remittances to the labour-exporting economies of the region. The total current account surplus of the GCC countries is estimated at US$144 billion in 2010, up from US$56 billion in 2009. The total current account deficit of the MDEs is estimated at US$12 billion for 2010, a significant improvement from the deficit of US$18 billion in 2009. Overall, the previously-accumulated international reserves of ESCWA member countries helped the authorities to avoid significant balance of payments difficulties during the financial crisis, and favourable external developments in 2010 further strengthened the net external position of the region. The level of current account deficits of non-surplus economies (Egypt, Jordan, Lebanon, the Sudan and Yemen) remained at manageable levels. In the cases of Egypt, Jordan and Lebanon, current account deficits were more than offset by the continuing inflows of capital, while the balance of payments in the Sudan and Yemen showed significant weakness.

17. In 2011, sustained high crude oil price levels are expected to lead to healthy current account surpluses in the GCC countries due to increased hydrocarbon export revenues and higher credit income positions. Near

record surpluses are forecast for Kuwait and the United Arab Emirates, while the current account surplus for Saudi Arabia is projected at close to 10 per cent of GDP. In Bahrain, GCC support will help to ease the balance of payments pressures triggered by the recent political and security developments. In the MDEs, rapidly rising food and energy-related import bills and lower external demand from their main trading partners, combined with an expected slowdown in global recovery, are projected to widen current account deficits. In Egypt, after the significant capital outflows observed during the social movements in the third quarter of the fiscal year, inflows of portfolio investments and FDI, coupled with reduced tourism receipts, will negatively affect balance of payments developments, and the Central Bank is expected to continue to manage the Egyptian pound at the current multi-year depreciated level of approximately EP6/US$ until stability returns. In Lebanon, a moderate deterioration in the current account is expected on the back of a higher import bill and decreases in services surpluses resulting from the uncertain political situation. In Iraq, the current account will benefit from higher gross oil export revenues on higher prices and production capacity, broadly balancing the high food and import-related bill.

18. For the first time since 2001, FDI inflows in the ESCWA region dropped in 2009, and the picture for 2010 is ambiguous. In 2009, FDI inflows were estimated at US$70.5 billion, compared with US$84.2 billion in 2008, representing a decrease of 16.4 per cent.[3] Bahrain, Egypt, Iraq, Jordan, Oman, Palestine, Saudi Arabia, the Syrian Arab Republic, the United Arab Emirates and Yemen all saw declines in FDI inflow. These falls are attributable to a number of factors, including the recent social movements, falling oil prices, a sharp correction in the real estate sector, a slowdown in economic activity, and financial problems experienced by multinational corporations, which represent the major source of FDI inflows in the region. Preliminary data for 2010, which is currently only available for a small number of countries, suggests a further slowdown in FDI in several member countries, despite earlier expectations of a speedy recovery. Saudi Arabia experienced a sharp decline in FDI in the first quarter of 2010, compared with the fourth quarter of 2009,[4] while data for Jordan indicate that FDI inflows saw a steady decrease throughout 2009 and the first half of 2010.[5] Conversely, FDI in Egypt was estimated to have picked up in 2010, compared with its 2009 level. Even with sporadic good performance in attracting FDI in 2009 and the progress achieved by ESCWA member countries towards improving the business environment, many challenges remain to be tackled if long-term changes are to be made. The wave of social movements that has recently swept the region will slow down economic growth in the short term, but the ability of the countries affected to perform well in attracting investment and promoting development in the longer term, particularly in the face of competition from other regions, will undoubtedly depend on them undergoing a constructive transitional process coupled with the synchronization of economic and social policies with institutional and political reform. In the short term, this political and social upheaval is expected to lead to lower FDI inflows, and expectations for FDI performance for both 2010 and 2011 should consequently be moderate. However, in the medium and long term, the ESCWA region is expected to continue to attract even higher levels of foreign investment, boosted by an improved investment environment, lower levels of corruption, a modern infrastructure and enhanced overall economic competitiveness.

D. ECONOMIC POLICY DEVELOPMENTS

19. In the light of recent economic developments, policymakers in the ESCWA region have been faced with a number of macroeconomic challenges, yet they currently have recourse to only limited policy instruments. As most countries in the region manage their own exchange rates, the effectiveness and role of monetary policy has been increasingly restricted. Fiscal policy thus remains, relatively, a more effective tool, notwithstanding the constraints facing the non-oil-exporting countries of the region.

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[3] United Nations Conference on Trade and Development, *World Investment Report 2010: Investing in a Low-carbon Economy*.

[4] Saudi Arabian Monetary Agency, *Quarterly Statistical Bulletin, Third Quarter, 2010*.

[5] Central Bank of Jordan, *Monthly Statistical Bulletins 2009-2010*.

20. Following the successful fiscal measures introduced by ESCWA member countries to counter the recessionary effects of the global financial crisis, high crude oil prices in 2010 allowed GCC countries to maintain expansionary fiscal policies, keeping them out of the global trend of fiscal austerity measures. Fiscal authorities in GCC countries had been prudent in using conservative oil price projections in their budget planning and implementation, and actual budget surpluses overshot planned budget figures on higher crude oil prices than had been assumed in their budget legislation, resulting in greater fiscal stimulus in 2011.

21. The fiscal stance of the GCC countries will remain active in 2011, with the usual major targets of fiscal policies emphasized in their budget legislation. The investment in infrastructure, health, education and social expenses provided for in their budget legislation are being bolstered by discretionary social measures. These include an ambitious social plan in Saudi Arabia, making provision for higher wages and increases in funds to support housing loans; social transfers and food distribution in Kuwait; food subsidies in the United Arab Emirates; and monthly allowances for job seekers and an increase in public sector employment in Oman. Moreover, the GCC countries have stepped in to support Bahrain and Oman following the recent social movements in those countries, providing an aid package targeting their housing and infrastructure sectors. Saudi Arabia, Kuwait and Qatar have all launched major development programmes and the positive developments in crude oil prices will allow the financing requirements of such programmes to be met comfortably, while maintaining significant budget surpluses and further lowering their debt levels.

22. The GCC countries clearly have the luxury of relatively easier fiscal manoeuvring and can effectively use this policy instrument counter-cyclically to influence aggregate demand. In the medium to long term, fiscal policy can play an even more active role in resource allocation and income distribution. Fiscal policy has the potential to be a cornerstone of a new socio-economic model that would move oil-exporting countries further away from their current dependency on oil and towards greater diversification, bringing about long-term economic structural transformation. Linking this type of policy with the desired social policy and social outcomes under a strong institutional framework would ensure significant progress in human development.

23. In the MDEs, the situation is more difficult. Limited fiscal space continues to constrain public finance management, even though healthy real GDP growth rates have partially relieved pressures on public budgets through higher tax revenues. Fiscal austerity measures have been implemented, notably in Iraq, Jordan, the Sudan and Yemen, in an effort to ensure fiscal sustainability. The average budget deficit in this subregion is estimated to have exceeded six per cent of GDP in 2010, with an average budget surplus of nine per cent for the GCC countries. Public finance management in the MDEs will prove more difficult in these fiscally-constrained economies, with increased social expenditure expected to lead to a moderate deterioration in fiscal positions and an increase in public debt stocks. Oil exporters in this subregion, in particular the Syrian Arab Republic, are expected to benefit from higher oil receipts, which will go some way towards allowing them to manage their deficits despite increased social and development spending. In Lebanon, political uncertainty holds considerable risks for 2011 and the expected moderate slowdown in growth will affect the budget, while in Egypt, Palestine and Yemen more international support will be required. As a result of the recent social movements in several member countries, a number of international bond rating agencies have downgraded their sovereign ratings for Egypt and Bahrain. These measures are expected to reduce the limited fiscal space available in those countries even further and put additional pressure on interest rates and the ability of their respective Governments to service their outstanding public debt, which may in turn render their public debt unsustainable.

24. The limited fiscal space and the social movements together point to an accumulation of problems which have exposed the weakness of the economic model adopted over the last two decades. The countries affected had focused above all on liberalization and structural adjustment, aiming primarily to balance their twin deficits. However, in doing so, they missed the opportunity to make the economic transformation that would not only contain the imbalances, but also change the pattern of economic growth, rendering it more sustainable and inclusive.

25. Monetary policy in the ESCWA region remains constrained by exchange rate regimes. Pegged exchange rate regimes remain the rule, with the US dollar as the predominant reference currency, with the exception of Kuwait and the Syrian Arab Republic, which peg their currencies against a currency basket and the special drawing right respectively. Egypt, Iraq, the Sudan and Yemen continue to manage their currencies closely against the US dollar. In 2010, there were few changes in policy interest rates, although Jordan and Kuwait lowered their rates in February, followed by Qatar in August. Moreover, the Kuwait Interbank Offered Rate, Saudi Arabian Interbank Offered Rate and Emirates Interbank Offered Rate all remained above the three-month London Interbank Offered Rate (LIBOR) throughout the year. The spread was marginal until the start of 2008, then in the first half of 2008 it turned negative when the region was awash with liquidity. For 2011, monetary policy in the region is expected to closely follow the US Federal Reserve policy of quantitative monetary easing which is expected to continue throughout 2011, with no major shift in the monetary policy stance foreseen, and liquidity funding remaining tighter than the three-month LIBOR on inflationary concerns. Liquidity, nonetheless, should be feeding into markets and ultimately raising business and consumer confidence in the region. However, to channel this liquidity productively into the real sectors of the economy and to spread its benefits across society, other macroeconomic and social policies are required.

26. Despite the advantageous liquidity position of many ESCWA member countries, the hurdles associated with business and household financing are significant. Indeed, most financing in the ESCWA region is geared towards the service sector, in which employment is relatively volatile. The absence of a trickle-down effect may have been the result of a concentration of economic activity in the service sector, where workers are often laid off during a downturn. In turn, in the absence of adequate social protection mechanisms, laid-off workers tend to switch to the informal sector of the economy. Financial deepening is a development issue concerned with individual and enterprise finance. People and businesses require a range of financial services (savings, payments, insurance and, most importantly, credit), not only to meet their basic needs, but also to thrive. In the ESCWA region, serious barriers to financial depth prevail. These include, among others, lack of competition in the delivery of financial services, weak credit information systems and creditor rights, inefficient contract enforcement, and lack of reliable collateral. In this context, banks are reluctant to finance small and medium enterprises (SMEs), although they recognize the profit potential in developing banking relationships with this significant business segment. Indeed, banks perceive SMEs as posing a greater investment risk than corporations, despite the fact that they have the discretion of allocating a lower credit charge against SME financing following international capital adequacy guidelines. In sum, financial services alone cannot bring people out of poverty, but financial inclusion can significantly contribute to meeting social and development objectives.[6] The ESCWA region lags behind many other emerging regions in terms of financial infrastructure development, broadly defined as the underlying foundations of a financial system, which is vital to facilitating greater access to finance, enhancing transparency and governance, and ensuring overall financial stability.

E. Social dynamics

27. The ESCWA region has witnessed a wave of historical social movements which spread rapidly from one country to another. This has changed the world’s perception of social dynamics in the region, the potential of the region and the role that Arab people can assume. The social movements in Egypt and Tunisia, in particular, demonstrated that people in the Arab region can use non-violent power to voice their concerns, achieve ambitious targets and gain worldwide support. Notwithstanding such important successes, the challenges remain daunting. The road to tackling deep-rooted social problems requires much more concerted effort. Among the most critical socio-economic problems is unemployment, resulting mainly from shrinking job opportunities and high population growth rates. The latest statistics available place unemployment rates in the ESCWA countries among the highest in the world. The ILO reports estimated

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[6] United Nations Secretary-General’s Special Advocate for Inclusive Finance for Development, *Annual Report to the Secretary-General*, 2010.

unemployment rates in the Middle East at around 10 per cent in the last two years, with youth affected at four times the rate of adults.[7]

28. According to the ILO, regional trends in vulnerable employment, informalization of employment and working poverty have progressed only slowly. Vulnerable employment has reduced by three per cent over the last decade and now stands just below a third of all workers. Figures are not available to measure informalization, but most assessments consider that it accounts for between one third and one half of total employment in the Arab world. Working poverty, measured at US$2 per day, was around 19 per cent in 2009, almost unchanged in ten years.[8] Yet this is only one dimension of poverty in the region. In general, poverty rates, measured by national poverty lines, show higher levels of deprivation. Levels of income inequality also appear to have increased, although data measuring it are scarce in the region. The Gini coefficient, which is available only for certain member countries, indicates that over time the trend shows either no progress or, in certain cases, deterioration.[9]

29. Such problems are not recent; in the course of the last decade, however, they have become chronic. Political exclusion and ineffective social protection systems have magnified hardship in the aftermath of worldwide increases in the price of food and commodities, and the ensuing inflationary trends. The social movements and popular protests succeeded in bringing these issues to the forefront, but the prospects for countries which witnessed social movements remain unsettled. Economic growth rates have been revised downwards for these countries, with tourism, FDI, external financing and private consumption being affected to a greater or lesser extent. In a region where the tertiary sector and, more specifically, tourism ensure a large number of jobs,[10] such economic conditions are expected to translate into increased temporary unemployment, at least in the short term. Egypt, for example, has recently seen the return of some 150,000 workers from the Libyan Arab Jamahiriya. With the informal sector also accounting for a significant share of employment in the region, vulnerability is expected to increase and, in the short term at least, people who are currently living just above the poverty line may well fall below it before any economic readjustment takes place.

30. In the light of these developments and in an attempt to dampen the impetus of the social movements, many Governments have responded with sporadic social and political intervention. Measures have ranged from some level of increased political participation to augmenting subsidies and distributing one-off grants. While such measures may head off some of the popular discontent in the immediate term, what is required from decision makers – whether existing or future Governments – is far greater if the real problems are to be tackled. In the long run, as normality returns, it will be vital for policymakers to address the root causes that led to the social movements. Innovative employment creation strategies are necessary in many countries to move away from jobless growth and towards further diversification and industrialization. There is an urgent need for an integrated social policy in which social issues are not viewed as secondary to economic processes. Problems of inequality, poverty and unemployment must be tackled by synchronizing policymaking within a long term development vision. This can only be achieved through capable institutions,

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[7] ILO, *Global Employment Trends 2011: The Challenge of a Jobs Recovery*.

[8] Ibid.

[9] The Gini coefficient for the Syrian Arab Republic rose from 33.7 in 1997 to 39.2 in 2004; that of Yemen from 34.4 in 1998 to 37.7 in 2005; and that of Egypt from 28.7 in 1995 to 34.4 in 2007. (Figures from Ali, A., *The Political Economy of Inequality in the Arab Region and Relevant Development Policies*, Arab Planning Institute, 2009). The same trend is implied by a compilation of data from a variety of sources reported in *The Third Arab Report on the Millennium Development Goals 2010 and the Impact of the Global Economic Crises,* United Nations and League of Arab States, 2010.

[10] According to World Travel and Tourism Council (WTTC) statistics, the total contribution of travel and tourism to employment in 2010, including jobs indirectly supported by the industry, was estimated at some eight per cent of total employment. This regional WTTC classification covers the following ESCWA member countries: Bahrain, Jordan, Kuwait, Lebanon, Oman, Qatar, Saudi Arabia, the Syrian Arab Republic, the United Arab Emirates and Yemen, as well as two non-member countries.

backed by a political system and democratic practices that protect civic rights and ensure the participation of the most disadvantaged groups.

F. Conclusion

31. For 2011, a slow recovery in the more advanced economies and the emergence of several regional conflict areas, combined with limited scope for further countercyclical Government policy action, imply that the growth rate in the ESCWA region will hover around 5.1 per cent. Policymakers in the region need to focus more on supply-side reforms that will help to boost productive capacity in the industrial sector, bolster employment and enhance competitiveness. As a result of the rebound in crude oil prices, revenues and production, the oil-exporting countries – primarily the GCC countries – will see significant improvements in their fiscal and external balances in 2011, with positive spillover effects for the MDEs. Moving forward, further efforts in financial sector development and economic diversification should top the economic agenda of policymakers in the region. Social policy should aim for a more equitable and inclusive developmental process, and the socio-economic policy framework must reconnect with political dynamics to advance a human rights-based agenda.

II. RECENT EVENTS: AN OPPORTUNITY FOR EQUITABLE DEVELOPMENT

32. The ESCWA region stands at a crossroads in history, with changes sweeping many of its countries and creating an environment conducive to reform. Having missed a number of chances to introduce extensive economic and institutional reforms and make substantial progress in development, the current situation presents another golden opportunity. The social movements in the region and the earlier series of economic crises have exposed the weaknesses of the adopted development models and have raised questions as to how to reshape policies most effectively and create the space to address the needs of everyone in society, reaching even the most deprived. The neo-liberal economic model implemented in most ESCWA member countries, centred on fiscal and monetary stabilization and economic liberalization, has yielded a relatively acceptable level of economic growth and, in general, managed to meet the goals of economic and financial stability. Fiscal deficits have been contained. Monetary and inflationary pressures have, overall, been smoothed. Oil booms have kept the region upbeat, with oil-abundant countries delivering much more than those less developed. However, the impact of such economic policy choices has not led to the desired outcomes in terms of human development, human rights and political reforms. Indeed, in certain cases, liberalization has actually aggravated the divisions in society, with economic and political marginalization increasing. In the light of a critical reassessment of the achievements and failures of ESCWA member countries, a new development approach is being shaped, one which is more holistic, integrating the economic and social spheres in combination with strong institutions and democratization, ensuring full participation in the decision-making process. It is vital that policymaking should expand to accommodate these spheres and place them on an equal footing in the service of a long-term rights-based developmental vision.

33. The new model will reconsider macroeconomic policies that incorporate developmental priorities and would thus achieve structural change. Fiscal and monetary policies will be reshaped to achieve not only stabilization, adjustment and economic growth, but will also trigger the transformation required to generate growth that is broad-based, inclusive and sustainable. Within this context, such policy tools as taxation, financial inclusion, labour market legislation and sectoral diversification will be addressed. At the same time, macroeconomic policies should not shy away from meeting the same objectives as social policy under this new development paradigm, in which the interests and welfare of every person in society are the target. It is also of central importance to ensure that social policy goes hand-in-hand with economic policy to bring about the required transformation and ensure inclusive economic growth. This would involve a move away from the policies of the “minimalist” welfare State to a situation in which social policy is a pillar of the development model. Social policy needs to provide social security and basic services, ensuring that basic human rights are secured.

34. While the social and economic spheres interconnect to create synergies, this new development model will not achieve its goals if political and institutional reforms remain shallow changes. The objective is to reinstitute democratic values and have strong developmental political systems. Appropriate State capacities need to be built to ensure that politics are developmental and not anti-developmental. Experience from around the world has shown that some authoritarian regimes, notably the east Asian “tiger” States, have been successful in building capacity to modernize their economies, yet in the long run, they have still come under pressure to respond to the voice of their people. Most regimes aiming to develop their countries have needed to engage their citizens at some stage in order to successfully extend the development process.

35. Democratic institutions provide the opportunity for the most disadvantaged groups in society to participate, institutionalize their rights, make choices, challenge public policies and hold Governments accountable. This is not to say that democratization is a magic bullet for development, only that it incorporates elements that could buttress socio-economic advancement. In the ESCWA region at present, the building of such capacity and institutions faces two main challenges. The first is the challenge to break rent-seeking corruption networks that have managed over the years to survive and influence ruling regimes and policymaking, weakening the State apparatus and ensuring that only the interests of a limited number of people are met. The second challenge is to overcome the religious and ethnic divisions which have recently become further heightened. If these major obstacles can be successfully surmounted, the resulting democracy would boost human development in the region substantially.

36. In conclusion, sustainable human development requires an acknowledgement that politics, institutions and socio-economic policies are intertwined and have an impact on each other. To achieve optimal impact, outcomes should be planned from a multidisciplinary perspective. Synchronizing economic and social policies with institutional and political reforms would bring about positive, sustainable change under a clearly defined development vision. This year’s Survey investigates the nature and extent of the decoupling of the economic, institutional and social dimensions of development in the ESCWA region by revisiting previous socio-economic policies. Based on this analysis, it will suggest a new development paradigm which would reconcile policymaking on various fronts. While it remains abundantly clear that there is no one-size-fits-all model, the Survey will highlight those elements which are critical for the development process to be sustainable and equitable in the countries of the ESCWA region.