



Seven Pillars

WHAT REALLY CAUSES INSTABILITY IN THE MIDDLE EAST?

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What Will It Take to Repair Middle Eastern Economies?

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The Middle East is among the world's richest regions in natural resources, but despite the Persian Gulf's ostentatious oil wealth, as a whole, the region teeters on the economic precipice. East Asia, South Asia, and even Latin America—once peers in business and development—have left the Middle East in the dust. Rather than embark on slow and steady growth, Middle Eastern economies remain trapped by boom-and-bust cycles of economic development, often a case of two steps forward, two steps back. Environmental concerns, such as desertification and fresh water shortages, add another layer of complexity. But other regions have overcome similar obstacles to thrive. Why has the Middle East failed so spectacularly to do so?

It is easy to blame the Middle East's democratic deficit, but that is not enough to explain the entire problem. After all, China and Singapore have seen exponential economic growth in the past half century without embracing democracy. And South Korea's and Taiwan's economic engines developed long before either completed their democratic transitions.

What then has stymied the Middle East's economic development? There is no single answer. Oil-rich countries have fallen prey to rentier state dynamics, but corruption ravages rich and poor states alike. Decades of socialism and command economies have taken their toll. So too has the Arab-Israeli conflict and myriad others. The business climate in many countries repels rather than attracts investment, but even when investors dip their toes into the Middle East market, the lack of a stable, developed middle class and indigenous capacity exacerbated by decades of labor importation continue to impede growth.

The Problem of Oil

In 2013, University of California, Los Angeles, political scientist Michael Ross published his seminal book *The Oil Curse: How Petroleum Wealth Shapes the Development of Nations*.¹ He showed that petro-states are 50 percent more likely to be ruled by autocrats than resource-poor countries and twice as likely to experience civil wars. Because oil-rich states spend significant shares of their national wealth on armaments, the use of force is too often the default response to political conflict. In Algeria, Bahrain, Saddam Hussein-era Iraq, and Sudan, the state has crushed social and political unrest with brute force. Syrian oil funded not only Bashar al-Assad's post-2011 crackdown but also the Islamic State's short-lived caliphate.

Subsequent events have only affirmed Ross' thesis. Democracy has expanded across the globe since 1980. Despite recent backsliding, democracy has made great gains in Eastern Europe, Latin America, Sub-Saharan Africa, and even East Asian countries, such as South Korea and Taiwan. Broadly speaking, however, oil-dependent countries have been the outliers.

Vast petroleum resources in the Middle East have enabled many states to resist reform. States such as Algeria, Iraq, and the oil-rich Persian Gulf emirates have grown dependent on oil or gas income, which in turn has created a dynamic nourishing patronage over economic growth.² Foreign aid has created a similar dynamic in states such as Egypt, Lebanon, and the Palestinian Authority. In each case, the result ossifies autocratic but brittle governance.

Not only do such dynamics stymie democracy (admittedly not a concern for the Gulf monarchies), but, when elections do occur, they also unleash patronage politics and competition over public resources and become a test of, as the University of Oxford's Paul Collier quips, "survival of the fittest."³ That is why when autocracies find oil, democratization becomes less likely.

The nationalization of oil industries, especially in the 1970s, has only augmented the resource curse in the Middle East. Oil revenues, which economists call rent, flowed into government coffers. Studies assert that large resource rents from oil and gas lead government officials to take the easier short-term path of seeking even more revenue from natural

resources rather than embarking on pro-growth policies that would provide longer-term stability.⁴

Rent also breeds inefficiency. As a fraction of their economies, petro-state governments are on average 50 percent larger than oil-poor ones.⁵ Compared to governments that rely on a solid tax base, petroleum rents create top-down flows of wealth and power. Moreover, the government sector benefits disproportionately more from oil rents and grows more quickly than the rest of the economy.

Although, on average, the oil sector constitutes only 19 percent of the economy, oil rents fund 54 percent of state budgets.⁶ Against low extraction costs that averaged below \$10 per barrel in the Middle East, no other industry can rival the return on investment. That is why, on autopilot, the petroleum industry tends to crowd out other industries and deepens not only the government's but also the whole economy's dependence on oil.

The danger of overdependence, of course, is that the price of oil is notoriously volatile. Crude was \$10 per barrel in June 1999, \$145 in June 2008, and \$45 in June 2017. In June 2014 alone, oil prices fell 40 percent.⁷ The Organization of the Petroleum Exporting Countries (OPEC) seeks to set prices, but political differences among members, cheating, and the growing number of non-OPEC producers erodes its ability to do so.

There are other dangers as well. Oil-rich, low-population states can be tempting targets for indebted states, which seek an easy way to fill their coffers without undertaking hard reforms. Saddam Hussein ordered Iraqi forces into Kuwait ostensibly over an oil drilling dispute, but, in reality, the aim was to loot Iraq's tiny neighbor to replenish Baghdad's treasury and patronage networks.⁸

Governments have been slow to adjust their oil-dependent economies. Four decades ago, Saudi Minister of Oil and Mineral Resources Ahmed Zaki Yamani warned, "The Stone Age did not end for lack of stone, and the Oil Age will end long before the world runs out of oil."⁹ And yet, it took Saudi Arabia decades more to begin serious efforts to diversify its economy, and even then, the success of diversification remains unclear.

Plans for building a broad-based economy are undermined by complacency during fat years and the need to increase spending at the expense of investment in low years. The problem is not just political inertia. Due to

the influx of foreign currency, exchange rates inflate in favor of national denominations. This in turn makes goods easier to import than produce.

The problem is that the energy industry is capital- and technology-rather than labor-intensive. Oil accounts for more than 80 percent of Saudi Arabia's revenues,¹⁰ but the industry employs only 1.6 percent of the workforce.¹¹ Governments then hire excess employees only to provide jobs, even if they are not productive.

When oil prices crash, ability to absorb the shock is limited. Saudi Arabia and the United Arab Emirates (UAE) cushion the blow with sovereign wealth funds, which they can tap to fill budget gaps, but they still have implemented some unpopular austerity measures. The Iraqi government managed to muddle through the perfect storm of low oil prices and the Islamic State challenge by slashing expenditures, deficit spending, and borrowing, but Iraq's Kurdistan Regional Government remains months behind in salary payments due to its bloated civil servant class and foreign creditors. However, simply cutting payrolls can be risky. The International Monetary Fund curbed its pressure on the Iraqi government to slash subsidies and reduce the size of government before the 2018 elections, which risks a populist backlash that could upend reform.

The Problem of Corruption

Corruption blights the Middle East and North Africa (MENA) from Morocco to Iran and from Turkey to Yemen. In 2015, 50 million people in the MENA region—nearly one in three—had to pay a bribe to access public services.¹² While terrorist attacks that dominate headlines may affect dozens or hundreds, corruption affects millions. Corruption fuels patronage networks, which in turn help ruling groups maintain power and resist reforms.

One of the problems hampering the fight against corruption is that legislative definitions of corruption are far more permissive of practices ordinary people would find corrupt. Many state legal codes lag behind the complexity of corruption in modern governments and state-business relations. For instance, while clear on bribery and embezzlement, Iraq's penal code is ambivalent toward more damaging practices such as conflict of

interest and nepotism, both of which have exacerbated the patronage networks that blight the country.¹³ No longer culturally sanctioned, the public is revolting against such corrupt practices.

Of the 21 Middle East states measured, 19 scored very low on Transparency International's 2017 Corruption Perceptions Index, which captures levels of corruption in the public sector. Transparency International concluded, "In the absence of separation of powers, and without strong and transparent public institutions and accountability mechanisms, the introduction of anti-corruption laws and regulations becomes more lip service than real and much needed political and institutional reform."¹⁴

Some improvements and new legislation curbing corruption have been introduced. Algeria and Tunisia, for instance, approved comprehensive anti-corruption frameworks, including greater transparency, a code of conduct for public workers, and protections for whistleblowers. Palestinian civil society campaigned against *wasta*, the ubiquitous practice of nepotism and intermediation in the Middle East.¹⁵ To attract business and reduce opportunities for bribery, Egypt cut down the number of procedures to register a business from 19 to three.¹⁶ The majority of Middle Eastern states have either signed or ratified the United Nations Convention Against Corruption and developed legal frameworks about bribery, money laundering, and public procurement. To support the UN Convention, the Arab Region Parliamentarians Against Corruption was formed in 2004.¹⁷ Nevertheless, complex and confusing legal codes continue to enable loopholes for evasion.

Oil, of course, exacerbates corruption. Oil industries are notoriously opaque. It is often easier to learn about the private dalliances and extravagance of oil princes and the *nouveau riche* than about the true reserves of various oil fields. Oil and gas contracts are prone to loopholes and kickbacks.

Moreover, since the sector is often highly centralized in an oil ministry or national company, revenues are easier to hide from the public. By turning national oil companies into personal banks and off-budget accounts, the dictators of Iraq and Libya used national wealth for self-enrichment at their people's expense. Even when the wealth does trickle down, it often does so in a fashion that nurtures patronage networks based on nepotism and cronyism, as in Algeria, Azerbaijan, or Iraq.

The Problem with Foreign Aid

Just as oil can grease corruption, so too can foreign aid. Traditionally, the United States gives military and economic aid to foster alliances, promote democracy, and address humanitarian concerns.¹⁸ But since 1946, the United States has given Middle Eastern countries nearly \$300 billion with little to show in either democracy or stability.¹⁹

This should not be surprising. The dilemma of foreign aid is not the amount of money given but how it is dispersed. In effect, foreign aid passes through a pork-barrel buffet of loyalist rewards before reaching its intended organizations, many of which are government-operated non-governmental organizations. Likewise, private-sector aid will often go to a dedicated regime ally who controls a disproportionate amount of enterprises to ensure regime loyalty.

The United States normally gives aid directly to foreign governments, which in turn promise to distribute it in mutually agreed on ways. Often, opaque governments divert aid. But, even when they do not, money is fungible, and aid can cover for other funds that top officials embezzle.

Hilton Root outlines his case against current foreign aid practices in his insightful book *Alliance Curse: How America Lost the Third World*.²⁰ He argues that authoritarian regimes are more concerned with the security of their regimes than with the well-being of civil society or the people. Therefore, instead of dispersing funds among civil society or independent firms, Middle Eastern governments are more likely to give funds to cronies and regime loyalists. Civil society atrophies when underfunded and neglected. Rather than strengthen civil society, then, foreign aid can actually strengthen its opponents.²¹

But despite its shortcomings, foreign aid remains a significant foreign policy tool, one that is evolving. To improve aid's effectiveness, the US Congress in 2004 created the Millennium Challenge Corporation (MCC), an independent aid agency. The MCC forced countries—those in the MENA region such as Algeria, Jordan, Morocco, and Tunisia—to compete across 17 policy performance indicators to qualify for assistance ensuring greater progress in good governance, human resource investments, and economic freedom. Each recipient country identified its growth priorities and lead in implementation.²² Nevertheless, the traditional model of

foreign assistance persists, not only from the United States but also more broadly from wealthier countries and the United Nations, and it continues to distort the economies of certain countries, much as oil does.

The Problem of Labor Importation

Many Middle Eastern states, especially the oil-rich Persian Gulf emirates, depend on imported labor. Qatar, Saudi Arabia, and the UAE consistently rank among the countries with the highest proportion of immigrant laborers as a percentage of the total population. Some of these workers are Arabs from poorer countries such as Egypt and Jordan, but a significant portion come from Asian countries such as Bangladesh, India, and Pakistan.²³ The International Labour Organization estimated that as of 2015 there were as many as 32 million immigrant workers in Arab states.²⁴

In many Persian Gulf countries, an unspoken social contract exists in which citizens receive a strong social welfare program in exchange for political quiescence. Part of this contract is the expectation that the state will provide jobs for locals regardless of skill set or capabilities.²⁵ Often, the burden of providing jobs falls on the public sector, which produces overloaded bureaucracies where governments pay employees to stare at stacks of paper. Failure to provide these jobs can have disastrous effects, as the Arab Spring demonstrated.

Immigrant laborers pose a theoretical threat to low-skilled, low-motivated natives. The UAE's private sector is 90 percent immigrant workers, leaving the bulk of UAE natives' roles in the public sector.²⁶ Certain countries have learned work-arounds for the burden of low-skilled workers by turning passports into commodities. In Kuwait and Saudi Arabia, only citizens are allowed to own land, so retail stores must have local stakeholders to operate.²⁷ Simply put, this shifts the burden of unemployed locals to another country's private sector.

The most significant effect of immigrant labor on local economies is remittances. Most immigrant workers, knowing their stay is temporary, send back as much of their salaries as possible to family members in their home countries. In 2014, these workers remitted an estimated \$95.8 billion from Kuwait, Oman, Qatar, Saudi Arabia, and the UAE.²⁸ That

year, in individual rankings, Saudi Arabia was second globally for total remitted dollars, and the UAE was sixth, with the United States in first place and the Russian Federation, Switzerland, and Germany occupying the third, fourth, and fifth positions respectively.²⁹

Remittances account for 14.6 percent of West Bank and Gaza gross domestic product (GDP) and 12.3 percent of Yemen's GDP. Across the Arab world, remittances still account for a significant 2.2 percent of GDP.³⁰ While in theory, outward cash flows should harm the host country, the reality is murkier. In 2017, the \$13.7 billion of remittances sent by Bangladeshi workers primarily in Saudi Arabia had a minimal effect on the kingdom's \$646 billion GDP.³¹ While they inject necessary cash into the local economy, remittances impede female participation in the workforce in countries such as Egypt, which sends male workers abroad to send back remittances.³²

That said, while host countries seek to remain homogenous and prevent an underclass of permanent immigrants, they arguably miss untapped potential. If managerial-class workers could move their families to host countries and settle more permanently, they would be more likely to invest in property or local industry, a benefit that might offset some obvious social challenges. The question then for Gulf economies is whether any mechanism can encourage local investment so that immigrant workers can have a more beneficial, rather than neutral, effect on the economy.

The Problem with Reliance on Subsidies

Subsidies, a government intervention ostensibly meant to benefit the poor or specific industries by suppressing prices, are corrosive to Middle Eastern economies. They serve political or social, as compared to economic, objectives. And while Arabs, Iranians, and Turks like cheap bread, gasoline, or electricity, such subsidies are counterproductive as they drain government budgets and perpetuate poverty and unemployment. While populations quickly come to view subsidies as entitlements, subsidies create deadweight loss whereby their costs surpass their benefits.

In Egypt, bread subsidies alone accounted for 10 percent of GDP in 2014. Coupled with those for fuel, spending on subsidies accounted for

90 percent of the country's deficit spending in the 2011–12 budget.³³ In comparison, Egypt spent a mere 3.75 percent of its GDP on education in 2008 and similar amounts in 2011 and 2013, down from an all-time high of 5.6 percent in 1983.³⁴ As a percentage of government spending, subsidies, grants, and other nonrepayable social transfers accounted for 41.7 percent in 2014, a sharp increase from 6.3 percent in 1994.³⁵ Such trends extend to the Middle East writ large, where subsidies and transfers accounted for 32 percent of government expenses in 2010, according to the World Bank.³⁶

According to Michael Ross, fuel subsidies are a hallmark of autocratic regimes, which spend more on suppressing fuel prices than do democracies.³⁷ In Saudi Arabia, gasoline is cheaper than bottled water. Fuel subsidies account for most of the unproductive government spending. According to the International Monetary Fund, energy subsidies cost Arab countries in 2015 an estimated \$117 billion, 5.5 percent of their GDP and more than a quarter of global energy subsidies.³⁸ In Iran, fuel and electricity subsidies amounted to 20 percent of Iran's 2007–08 GDP, equivalent to \$3,275 of revenue per family of four.³⁹

Fuel subsidies, however, can reverberate in negative ways. They primarily benefit the wealthy—one needs a car, if not many, to benefit—and they can also fuel corruption. Iran's Islamic Revolutionary Guard Corps makes billions of dollars each year selling subsidized fuel at marked-up prices. Rather than benefit ordinary Iranians, therefore, the fuel subsidies become a mechanism to transfer money from the central bank to the military.

To appease their populations during the 2011 Arab Spring, almost all Middle Eastern governments extended new subsidies to their citizenry.⁴⁰ But while subsidies are popular and easy to set up, eliminating them is trickier. In April 2010, demonstrations in Kyrgyzstan against high gasoline prices escalated into mass protests that toppled the country's president.⁴¹

Not even Saudi Arabia has been immune. Against the backdrop of oil price crashes in the 1980s, the Saudi government experimented with raising taxes and cutting subsidies. The result was extensive public protests that forced the government to revoke both measures.⁴² This phenomenon was similar to Egypt's experience with cutting subsidies in 1977, which also provoked bread riots throughout the country.⁴³ Even today, the Saudi government has struggled to raise fuel prices to international levels as part of

its plan to reduce dependence on oil. To augment public discord, the Saudi government is planning a benefit program to pay low- and middle-income Saudis to help their adjustment before price hikes come into effect.⁴⁴

Middle Eastern governments mainly spend oil revenues and foreign aid to finance subsidies. Such revenues are almost the antithesis of taxes. If taxation promotes accountable governance, subsidies support co-optation of the public and its acquiescence to the government. Subsidies also drain money that might otherwise be used to invest and develop.

Low oil prices have created incentives for subsidy reforms simply because Middle Eastern governments no longer have the cash to delay much-needed reforms. For example, as part of Egypt's 2016–17 budget, energy subsidies were cut from 61 billion Egyptian pounds to 35 billion (\$3.94 billion).⁴⁵

There is no magic formula about how to extricate economies from decades of subsidies. Transparency and timing matter.⁴⁶ To blunt the poor's pain, governments often extend targeted benefits, such as cash transfers, to those most in need as they cut broader subsidy programs.⁴⁷

Universal cash transfers are one popular policy prescription to wean populations off subsidies.⁴⁸ Coupled with other reform steps, such as communication campaigns and raising prices gradually, cash transfers have helped Iran, Jordan, and Morocco tackle the disruptive task of cutting energy subsidies.⁴⁹ Such measures, however, require effective governance to identify, for example, the most vulnerable who need cash transfers. Cutting food subsidies hurts inflation rates in a country such as Egypt, where food products account for 40 percent of its consumer price index. Hence, gradual phasing, accompanied with welfare spending and income redistribution measures, would be necessary.⁵⁰

The Problem of Business Climate and Job Creation

Singapore shows democracy is not always necessary to thrive economically. While Middle Eastern leaders believe they too can follow that model, they often miss two important steps: maintaining relatively even playing fields for business and upholding contract law. Hence, when Egypt, Turkey, and the Iraqi Kurdistan region sought economic development absent commitment to a level business playing field, the result was crony capitalism.

The state-business relationship tightened, and real or perceived corruption worsened. Cracks quickly developed, and promised outside investment dried up. The simple fact is this: When a robust and entrepreneurial private sector operates on a level playing field, it provides the services that society demands, but when a narrow, unaccountable elite rigs the rules, the result is concentration of wealth absent the goods and services the public desires.

The dichotomy between inclusive and exclusive institutions is important.⁵¹ Inclusive economic institutions—for example, labor unions and civil society organizations—promote sustainable economic development, while extractive institutions fester on rent-seeking and cronyism.⁵²

The Arab world continues to suffer from a cocktail of destabilizing factors; the region is burdened with the world's highest youth unemployment rate (30 percent of people age 15–24 are unemployed) while having one of the world's fastest population growth rates.⁵³ Government job creation has been unable to keep up with rising labor demand. Private-sector job creation has remained anemic; meanwhile, cronyism suppresses outside investment.

The way forward for job creation is to increase productivity through diversification and adopt modern technologies and organizational structures.⁵⁴ In addition to promoting small- and medium-sized enterprises, these countries should attract multinational corporations given their positive ripple effect on local economies; they create demand for local businesses and offer more training and upward mobility than family-owned enterprises can. Larger US and UK companies are also bound by national anti-corruption laws, such as the US Foreign Corrupt Practices Act, and so are less likely to indulge in practices that hinder the broader economy.

Enabling privatization remains a challenge. Socialism ravaged the Middle East in the latter half of the 20th century. Arab economies have historically been state-centered and hostile to foreign direct investment. Being the only familiar economic system, the elite and public often default to fixing the state-centric economy rather than tolerate the pains of transitioning to free markets. Protectionism shielded bloated state-owned industries from real competition. So long as political elites maintained their own local monopolies and could grow wealthy, they did not care that their national economies had grown increasingly moribund.

While necessary, privatization can catalyze corruption if it is mishandled. Politically connected elites use their inside track to acquire state-owned enterprises at fire-sale prices. In Russia, President Vladimir Putin's "associates" oversee state corporations. As Russia transitioned toward a market economy, privatization at the hands of well-connected insiders of state-owned assets gave rise to a new class of oligarchs. Similarly, real estate market privatization in the Iraqi Kurdistan region and preferential access granted to the politically connected resulted in a real estate bubble.⁵⁵ The US government has long expressed concern about the linkage between political leaders and private family businesses in the region.⁵⁶ Such a nexus between privatization and corruption feeds into an existing reticence toward the much-needed market reforms in the Middle East.⁵⁷

The Problem of the Middle Class

The middle class is a notoriously nebulous concept, but, generally, it relates to the economic security that prevents one from falling below the poverty line, which, of course, is different from state to state. In the Middle East, the middle class is a conundrum. Throughout the 1960s, 1970s, and 1980s, it was part of the ruling coalition among authoritarians and monarchies alike.⁵⁸ The middle class provided a large regime support base and was an integral part in stabilizing the economy. It was often disproportionately comprised of state employees rather than members of the private sector.

For the purposes of regime security, controlling the middle class made sense because it was most likely to organize and petition for political change. However, state control of the middle class stagnated economic growth by limiting the middle class to state structures and revenues and not allowing it the freedom to provide services where the state was not the most efficient provider. In petro-states, government-controlled middle classes are at the mercy of oil markets and may find that their salaries and subsidies need to be cut to continue funding other projects such as national defense.

In the 1990s, the middle class began to dissolve, and inequality rose, since growth was not accompanied by income distribution policies that would generate jobs.⁵⁹ Citizens disillusioned by the promise of public-sector employment and unable to advance in society without

necessary prerequisites, such as *wasta*, were forced to protest against the government for more jobs and economic opportunities.⁶⁰ Cries of “bread and social justice” underlined the people’s economic hardship. The erosion of the middle class and its quality of life was the real driving factor behind the Arab Spring uprisings, rather than slow growth or inequality.⁶¹

To bolster the middle class, governments must reduce the job market’s reliance on the public sector. Chronic unemployment was one of the most cited concerns by protesters during the Arab Spring partly due to the lack of private-sector firms that could hire workers in an overextended public sector.⁶² Allowing the private sector to grow will compromise the state’s stifling grip on enterprises, but if events like the Arab Spring are likely without reforms, then the safer bet for regimes is to reform and allow more workers to be employed outside government control.

Ending subsidies and monopolies will also benefit the middle class by forcing industries to become more efficient and hire educated, upwardly mobile workers. Reducing state inefficiency will also bring the economic benefit of freeing the state to fund development projects within their own countries, such as the King Abdullah Economic City in Saudi Arabia.⁶³ Funding development projects instead of subsidies could still placate the population through projects that grow the economy, raise standards of living, and provide jobs, even without lowering bread or cooking oil prices.

Easier social mobility could increase the speed of middle-class creation, although this requires modification of several social practices, most notably *wasta*. The use of family connections almost always guarantees that jobs do not go to the most qualified and permanently disenfranchises those who might otherwise join the middle class. Unlike *wasta*, inclusive and impersonal institutions drive economic growth and state stability.

The Problems of Women in the Middle East

Corollary to middle-class empowerment are prospects for women’s employment. The Middle East has a mixed record on female employment. Female education and literacy has increased along with the world average,

but translating education into employment and economic productivity has not proved easy.

Female education has increased in recent years. The number of women on campuses has increased and now surpasses the amount of men in secondary education in more prosperous Middle Eastern countries. Female literacy has also reached approximately 80 percent, matching the 2015 UN human development goal.

Economic theory dictates that higher education will logically lead to more economic opportunity and empowerment, but this is not the first time the Middle East has flown in the face of economic or political theory. A 2012 Gallup poll showed that two-thirds of Arab women were out of the workforce.⁶⁴ Although the gender gap is shrinking in sectors such as access to health care and education, it stays largely unchanged in the economic sphere. Average unemployment for women with postsecondary education in the region remains over 50 percent after one year of job search.⁶⁵ Similarly, and regardless of education level, the gap between women and men with a full-time job as a percentage of the population is 23 percent, the highest in the world.⁶⁶ The World Bank refers to this puzzling phenomenon as “the Arab Paradox.”⁶⁷

The World Economic Forum’s Global Gender Gap Report ranks the Middle East above only South Asia on economic opportunities for women. Moreover, progress toward parity remains extremely slow; at current rates it would take 153 years to close the overall gender gap. Less than 7 percent of women hold managerial positions in Egypt, Pakistan, Saudi Arabia, and Yemen.⁶⁸ Such gender gaps aggravate the issue of reservation wages and partially explain why women choose not to look for work. In instances when the opportunity cost of low-wage employment is not raising a family, women often prefer to stay home and raise families if their husbands have high enough wages to support a family. Moreover, no Arab country has legislated the prohibition of sexual harassment in the workplace.⁶⁹

States with no or insignificant oil, such as Lebanon, Morocco, and Tunisia, have greater female participation in their workforces, elections, and parliaments than their oil-rich neighbors Libya, Qatar, and Saudi Arabia. This is in part because of large government spending, which fosters patriarchy and reduces the need for women to enter the workforce. And those

who work tend to do it for the government, as in Jordan, where 82 percent of women's jobs are in the public sector.⁷⁰

Moreover, through Dutch Disease, oil wealth crowds out export-oriented industries such as textiles, which are more prone to hiring women. Consider Algeria and Morocco. The neighboring former French colonies have similar Muslim populations (35 million). Both granted women suffrage after their independence in the mid-20th century. However, Algeria's oil income per capita in 2002 was \$1,037 versus none in Morocco. The latter's clothing export per capita was \$94, compared to only \$9 in Algeria. Female labor force participation in Morocco was 26 percent (non-agriculture sector for 2000) compared to 12 percent in Algeria. By many accounts, Algeria should have performed better on women's rights since it is a socialist republic; Morocco is a conservative monarchy.⁷¹ Morocco's industry-based economy attracts greater women participation than oil-rich Algeria.

For those women who do work, cultural norms specify the professions acceptable to women: nurses, teachers, clerical workers, and other similar jobs. Employment theoretically competes with women's ability to bear and raise children, and the previously mentioned careers have short hours, high respectability, and plenty of leave to raise children. The UAE's public sector is 60 percent female due to its short hours, long vacation time, and forced retirement at age 49.⁷²

If women want to become self-employed and start their own businesses, acquiring loans is difficult as women do not usually have the required collateral to receive bank loans. A September 2017 World Bank report on Jordan noted that, due to discriminatory hiring practices and lack of access to capital, women often start home businesses, which provide more income without competing with child-rearing expectations.⁷³ Unfortunately, this has a deleterious effect on the economy as these informal businesses are not taxable because they are not reported. In other words, female discrimination in the Middle East not only limits economic growth but also actively removes money from the formal economy.

Several simple changes could be made that not only allow women to be more employed and employable but also maximize the economic benefits of allowing women to work. The first proposal is opening more profitable careers to women. Voluntary unemployment due to lower reservation wages is one of the major impediments to increased female employment.

Rather than simply mandating raised wages for female employees, allowing women to contribute to fields that are more profitable will solve the problem without creating further government involvement in the private sector. This suggestion may run counter to the societal limits on female employment, but economic data on the benefits of female employment will absolutely validate compromising cultural practices.

Second, raising retirement ages in public-sector jobs would allow women to have longer careers and contribute more to the economy and their personal careers. This suggestion has already been followed to a certain degree. The UAE proposed a law in February 2017 that increased the required retirement age by one year. Obviously, more drastic measures than a one-year increase are required to significantly expand economic benefits, but progress is already being made in the proper direction.

Third, lowering capital requirements on loans for female businesses could increase female business ownership, which in turn allows the state to tax income from these businesses. Formalizing aspects of the informal economy that are economically beneficial empowers employed women and allows the state to benefit.

Finally, imposing affirmative action-style requirements for company employees and university STEM programs would lend the might of the law to enhance female economic participation. While this might be the most economically viable move, higher numbers of female secondary-educated degree holders would increase the likelihood that more employees would become college educated. More females in STEM fields is not specifically a Middle Eastern issue but nonetheless could contribute to women filling more technical jobs and earning higher wages.

During a 2007 visit to Saudi Arabia, Microsoft founder Bill Gates was asked if the kingdom could become one of the top 10 economies in the world by 2010. Gates responded by saying that the kingdom would not get anywhere close when half its talent cannot work.⁷⁴ Female economic participation is not difficult to increase and could provide massive benefits to Middle Eastern countries. The question is not whether Middle Eastern countries should increase female participation, but whether they can stomach it.

That said, while a strong economy absent democracy is possible, it can be difficult to have democracy without economic liberalization. Modernization theorists, such as Seymour Lipset and Samuel Huntington, argue

that a linear relationship exists between economic modernization and democratization. They suggest that the industrialization, urbanization, literacy, transportation, and communication inherent in a strong economy creates enough complexity in the system to impede the central command inherent to autocracy.⁷⁵ Economic development, typically measured by increases in GDP, could be misleading, they argue, since not all economic growth is equal as far as political impact goes.

Not that the economic data shared by closed or opaque autocratic governments are necessarily accurate. GDP growth stemming from petroleum exports, for example, is qualitatively different than growth arising from a more diversified economy, as it does not require or result in the emergence of a middle-class characteristic of democracy. Diversification is necessary even absent democracy, as the sustained development of the resource-poor Asian Tigers and economic comparison to their former Middle Eastern and African peers demonstrates.

The Problem of Trade Unions

Trade unions represent a cornerstone of suffrage and lobbying the government for better working conditions. In the Middle East, trade unions have a mixed history in their function and relations to the state. Trade unions represent a tool of social control and worker coercion in many single-party republics. Often, Middle East states will recognize only one union, and the state will expect union leaders to keep workers under control, as was the situation in Egypt until the Arab Spring.

In promoting a middle class, trade unions offer the opportunity to demand better wages, working hours, and conditions. These rights are integral in helping produce a laboring middle class and fostering the development of industry outside government control. Middle Eastern trade unions rarely operate free from the central government. Governments that use unions to control the populace do not allow such promotion and, therefore, are less likely to promote middle-class-friendly policies. Many Gulf Cooperation Council (GCC) countries banned trade unions outright until the past decade because they feared workers lobbying for better work conditions or powerful trade unions agitating against governments.⁷⁶

Whether trade unions have actually improved circumstances in Gulf countries is questionable. Here, Qatar is a compelling example. The number of migrant worker deaths could reach 4,000 before completion of the World Cup stadium and infrastructure projects in 2022.⁷⁷ Other countries have more tolerant approaches to labor unions, such as Tunisia, where the government expects cooperation from union leadership, but leadership ultimately has a degree of freedom from the government.

However, change may be coming. In Egypt, for years, the government allowed only the Egyptian Trade Federation Union (ETFU) to exist, and all other unions were illegal. Union leadership did not allow workers to attend protests and rallies, so a new union was formed. The Egyptian Federation of Independent Trade Unions was created in 2011 from the members of the ETFU and allowed its members to take part in protests, substantially increasing the amount of people present during protests.

In Tunisia, the Tunisian General Labor Union (UGTT) was under control of the Ben Ali government despite its independent status. After Mohammed Bouazizi's death, the union cut all ties with the government and organized its members to protest the government. The UGTT was part of the Tunisian National Dialogue Quartet, which won the Nobel Peace Prize in 2015 for "its decisive contribution to the building of a pluralistic democracy in Tunisia in the wake of the Jasmine Revolution of 2011."⁷⁸ These two examples showcase that despite significant government constraints, labor unions can break limitations to promote workers' prosperity.

Iraq has a long history of trade unions, although Saddam Hussein banned them in 1987.⁷⁹ While Article 22 of the 2005 Iraqi constitution guarantees "the right to form and join unions and professional associations," the parliament has yet to modernize and update the legal codes that govern such unions, so the cabinet still regulates them.⁸⁰

In Iraq and the Iraqi Kurdistan region, such unions and syndicates are politicized and co-opted by ruling political parties. Party-controlled unions and nongovernmental organizations are always better funded than truly independent organizations. These party-dominated unions are among the loudest voices against privatization, as manifested by the strikes and protests of Basra oil workers and unions against the return of international oil companies.⁸¹ Too often, the government avoids the headache of dealing with workers by deferring the modernization of state-owned enterprises.⁸²

The Problem of Disruptive Technology

The region is facing technological penetration and disruption that present potential opportunities for closing the skills and employment gaps. The Middle East is catching up with the world in the realm of information and communications technology. A slew of technological companies—software development, e-commerce, and online and mobile phone services—have mushroomed in the region. A tech-savvy demographic, dubbed “the Arab Digital Generation,” accounts for 40 percent of the region’s population.⁸³ Between 2006 and 2016, data flows between the Middle East and the world increased more than 150-fold, according to a report by McKinsey & Company.⁸⁴ But digitization among countries in the region remains uneven: high in GCC countries and low in conflict states, such as Syria and Yemen.

There is a prize to consider. Research by McKinsey & Company estimates that if the region’s potential 160 million digital users by 2025 were to form a unified digital market across the Middle East, they could contribute 3.8 percent in GDP annually, a sizable \$95 billion. Digital adoption and growth are mutually reinforcing.⁸⁵

Unlike social reticence toward some measures such as privatization, the Arab attitude toward internet access is quite positive. One survey indicated that 90 percent of young citizens with internet access think such connectivity would help them find jobs and create business.⁸⁶ Enabling the younger generation to tap into the digital marketplace might make governments see the youth bulge less as a liability and more as an asset.

Coupled with and feeding into tech-enabled entrepreneurship is improving and updating the region’s education system.⁸⁷ In recent decades, the Arab world has made significant progress in education. For example, universal primary access has increased by 10 percent and youth and adult literacy by 22 percent, true for both genders.⁸⁸

The gap lies in the quality of education and its mismatch with skills the market needs. Rote learning, standardized tests, and university degrees designed for the public sector do not match the private sector’s ever-changing skill needs. Literacy and numeracy alone are no longer adequate; to meet market needs, youth need to “demonstrate adaptability, creativity, and above all aptitude for learning to learn—autonomously and continuously.”⁸⁹

Governments and businesses, too, lag behind this fast-paced technological trend and have yet to embrace full digital adoption. Despite ambitious plans, only 6 percent of the public lives under a “digitized, smart government.”⁹⁰ Likewise, business digitization faces inadequate funding available to startups and the workforce. Alignment of the region’s governance structures and ease of market entry, skilled and talented labor, and access to capital is needed. For example, a 2013 survey of the challenges facing startups in the MENA region showed that technology companies have greater access to angel investors, incubators, and venture capitals than funding from commercial banks.⁹¹

Conclusions

One way to circumvent the loyalist reward program is to invest directly in businesses and cut out the government middleman. Directly investing in nongovernmental enterprise and giving international approval to private competition can change the dynamic in Middle Eastern countries and actually promote liberal economies.

Within the World Bank Group, the International Finance Corporation acts as a private investor to create markets “where they are needed most.”⁹² If governments could act as private investors like the International Finance Corporation, skip the handouts integral to authoritarian regimes’ support networks, and finance firms directly, then investing in a variety of projects to create economic competition could noticeably affect market creation in the Middle East. On the other hand, once governments invest in a specific company or enterprise, they become responsible for ensuring that company succeeds and for staving off any attempts by local regimes to flounder it.

For real change to occur in the Middle East and to foster freer economies, support must come from the international community for private-sector creation and the promotion of businesses outside government control. True competition and the emergence of a private sector are no longer luxuries but necessary to create jobs for an evermore connected and worldly youth. Economic and financial literacy should be integrated into primary education. In turn, the return of the middle class depends on these countries’ ability to meet the rising demand for honorable work.

In addition to the invisible hand, there is the state. Limiting extensive state intrusion in the economy need not mean no state involvement. Effective, transparent, and law-bound state institutions can drive growth. Saudi Arabia's Ma'aden and Sabic are good examples of state-owned enterprises that have evolved into successful multinational corporations. In the UAE, state ownership through diverse investment vehicles has not stifled competition.⁹³

Outside of external intervention and support, Arab countries have already begun to initiate internal reforms. The UAE has already undertaken some of these measures by promoting a burgeoning tech finance industry that encourages companies such as Jamaloon, a Jordan-based bookselling website, to link up with Dubai operations offices to promote business.⁹⁴

Technology is now more accessible than ever to lower echelons of society, allowing some degree of economic mobility where social mobility is lacking. For instance, Ala' Alsallal, the founder of Jamaloon, was born in a Palestinian refugee camp and recently oversaw a \$4 million company expansion.⁹⁵

One move the Emirati government made to increase the potential for middle-class growth is passing a bankruptcy law. By allowing businesses to fail, the UAE is averting the possibility that businessmen would face jail time for penalties evoked surrounding debt and obligations. Due to this law and the capital available in Dubai, the UAE is spurring new growth in a middle class that might otherwise be floundering.

The economic performance of Middle East countries is all but uniform. The region juxtaposes Qatar, with the highest GDP per capita, and Yemen, one of the world's poorest countries. It is also prone to violent conflicts and vicious economic swings. Given such instability coupled with democratic deficit, economic prosperity of the citizenry is seldom the state's top priority.

Although many of the constraints on economic progress outlined above contributed to the Arab Spring uprisings, the urgent need to fix their economic policy remains lost on many Arab leaders. Regional cooperation remains elusive, even among the GCC countries. Country-specific economic reforms—such as tackling corruption, fixing the business climate to promote entrepreneurship, and closing the gender gap—make for more attainable goals that would also facilitate greater regional economic

synergy. Moreover, the public would have greater agency if their demands were anchored on cleaner government and a level playing field rather than greater shares of government handouts, subsidies, and unproductive jobs.

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