

THE INTERNATIONAL ECONOMIC ENVIRONMENT OF THE ARAB SPRING

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Since 2010 most of the developed economies of the Organisation for Economic Cooperation and Development (OECD) have been going through simultaneous economic and financial crises that are generating unemployment, loss of competitiveness and slow but steady loss of their international leverage in determining the international economic agenda.

Emerging economies from Asia, Latin America and, to a certain extent, Africa are starting to have a deeper impact on shaping the new economic scenarios of the mid- to long-term future. The strengthening of cooperation frameworks within non-OECD economic blocs (such as Association of Southeast Asian Nations (ASEAN), the Gulf Cooperation Council (GCC) or Mercosur) is giving them a bigger share of world GDP, trade and financial resources, thus challenging the traditional leading economic role of western economies.

This world trend of new emerging economies gaining relevance and a bigger role as economic partners also seems to be occurring in the Arab world. Emerging economies like China, certain Gulf countries, Turkey, South Korea and Brazil are increasingly aggressive in trying to seize the economic opportunities of the Arab revolts.

This increasing economic presence of these countries in the region had already started before the uprisings took place and coincided in historical terms with the economic uncertainties and deep crisis of the traditional economic partners of the Arab countries, the US and very particularly the EU economies.

These two realities – an economic setback of the western partners and the filling of the vacuum they have left by emerging economies – made the Arab Mediterranean countries pay more political and economic attention to them. These economies are more competitive, broadly specialised in medium technologies (the most needed in Arab economies) and have financial resources to offer them in a time of scarce liquidity at a national and international level.

EU: Reinforced Economic Role in the Emerging Scenario of the Region

Changing deeply-rooted trade patterns and international production value chain integration is a long-term process. Over the last few decades, the EU economies, especially those of the European Mediterranean such as Spain, France and Italy, have developed intense and complementary production and trade relations with the majority of the Mediterranean countries, mostly with the Maghreb economies. Textiles, tourism, agro-food, services or petrochemicals are among the sectors increasingly integrated into the Euro-Mediterranean region.

Globally, certain European economic sectors are increasingly redefining their international production strategies based on new logistical and production cost considerations, redeploying investments from distant countries to nearer markets, especially those in the Mediterranean, such

as Morocco, Tunisia and Turkey. This is making many companies in the sectors involved (many of them small- and medium-sized enterprises in textiles, automotive components and electricals and electronics, among others) develop active production strategies towards the region, thus strengthening economic relations between Europe and the main Mediterranean economies.

This integration of production between many Arab economies of the Mediterranean and the EU is still a strong reality for these economies, thus making it a structural factor that will continue shaping their international economic near future.

Moreover, the EU is still a key partner for these countries in other relevant factors that determine their socio-economic reality. It is the origin of most of the tourists visiting the Mediterranean countries, thus contributing to the development of this strategic sector for these economies and leaving much needed foreign currency.

Migration and remittances are other economic factors that strongly link the EU to Mediterranean countries, although new migration patterns might develop in the near future towards the Gulf, other southern Mediterranean countries like Libya or other emerging economies outside the region.

All these elements suggest that the EU will still play a significant and strong role in the economic future of the new regimes emerging after all the transformations in the Arab Mediterranean countries, whether governed by Islamic parties or not.

But Competition from Emerging Economies Will Increase Strongly

The economic and financial performance of the main emerging economies in the world, systematically seeking new markets and access to natural resources, is a growing variable that needs to be taken into account.

Some of these emerging economic blocs, such as the Gulf Cooperation Council, do already have a deep and intense involvement in the Arab Spring, having developed a comprehensive political, economic and financial agenda to try to shape the outcomes of the changes.

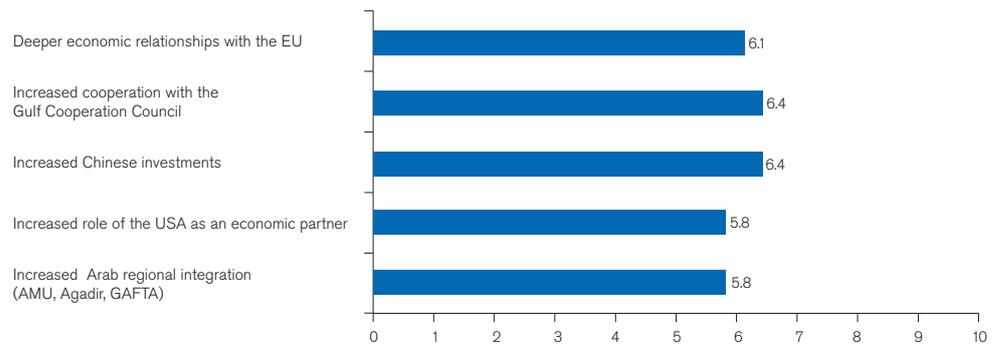
The relations between their political and economic elites with the new more Islamic leaders governing the region results in more intense trade, investment and financial involvement of the GCC economies in these countries. This trend is very likely to continue and gain strength in the near future, very especially in the Mashreq countries where their linkages have been developing further in recent years.

Another factor that is likely to have an economic impact in the region is the growing involvement of China. Currently in permanent need of access to natural and energy resources, China is actively seeking to develop good economic relations with these governments, whether resulting from changes or not.

Its “non-conditionality” approach has permitted China to have growing access to the economic opportunities of the region vis-à-vis western economies, more prone to pressure the governments on economic reforms and on democratisation and human rights issues.

This political factor, together with the financial and investment resources China can offer to these economies in today’s difficult economic context, makes the growing involvement of China in these economies in the future very likely.

Graph 1: New regional economic long-term strategic options of post “Arab Spring” governments
(average on a scale of 0-10, where 0 stands for no probability and 10 for very high probability)



Source: Compiled by the IEMed based on the results of the 4th Euromed Survey

Increase Arab Economic Integration in the Agenda?

There are several political frameworks in the Mediterranean that are expected to strengthen Arab economic integration but none of them has performed successfully so far. Political blockages or lack of economic complementarities have persuaded the Union for the Arab Maghreb (UMA), the Agadir Agreement or the more ambitious Greater Arab Free Trade Area (GAFTA) to reach any acceptable level of economic integration.

The new governments formed after the Arab Spring, whether through reforms or revolutions, seem to have more political will to pursue Arab regional economic integration. Changes might have opened a window of opportunity to approach this objective based on active policies. Examples are the implementation by the Tunisian government of visa-free movement of people for nationals of some North African countries or several agreements of the Libyan government to strengthen socio-economic and financial relations with Egypt. Nevertheless, daunting economic policy disparities persist among states in the region regarding key issues, such as their vision on the depth of economic reforms, the role of the state in the economies or the need for a financial sector reform.

Some interesting steps have been taken, such as the recent creation of a regional bank for development in the framework of the UMA, but Arab integration today is still an objective more than a process.

What the aftermaths of the Arab Spring seem to show is that the “business as usual” scenario of developing mainly bilateral relations with one main partner, basically the EU, and relying on the attractiveness of small- to medium-sized non-regionally integrated markets in today’s globalised world is an outdated approach.

It is very likely that there will be more active policies from these Arab countries in trying to diversify their international economic and financial partners. It is also foreseeable that the most important emerging economies’ role in the Arab countries will increase, both from a trade and investment point of view, in the coming years. And it might evolve towards playing a more sophisticated role by getting involved in new kinds of cooperation frameworks, such as management of key infrastructures under several Public-Private Partnership (PPP) forms, transferring technology or even training key professionals in several sectors.

What is the Islamist Governments' Capacity to Address Socio-economic Demands?

The political changes that have swept the Arab Mediterranean countries have been capitalised mostly by Islamic political movements. So far, these movements have been able to unite under their political umbrella the discontent of many of the people who went into the streets demanding changes.

The Islamic political parties have come to power through the democratic elections that have widely taken place in the region after the uprisings. Thus, these parties are leading governments in the countries where political changes have occurred, either through uprisings or reforms. In some cases, such as in Egypt, they have been able to gain control of most of the political institutions (Parliament, Presidency and Government), while in others, such as Morocco and Tunisia, they are the main partners of government coalitions of ideologically heterogeneous political parties.

In either of the cases, the Islamic parties have had to face the fact that they have become, suddenly to a certain extent, the main decision-makers responsible for the definition and implementation of the policies in their respective countries. This has meant that the Islamic parties have had to recruit cadres from their own ranks to cover all the government institutions the previous regime had left.

As parties without much or significant experience in managing institutions and power structures, they have had to rely on ideologically loyal and professionally inexperienced people from within their political circles.

The fact of having appointed unsuited, and sometimes unskilled, cadres for high and medium level management posts, together with the heterogeneity and in some cases divergence of the ideological political background of the other government partners, has led to difficult government situations.

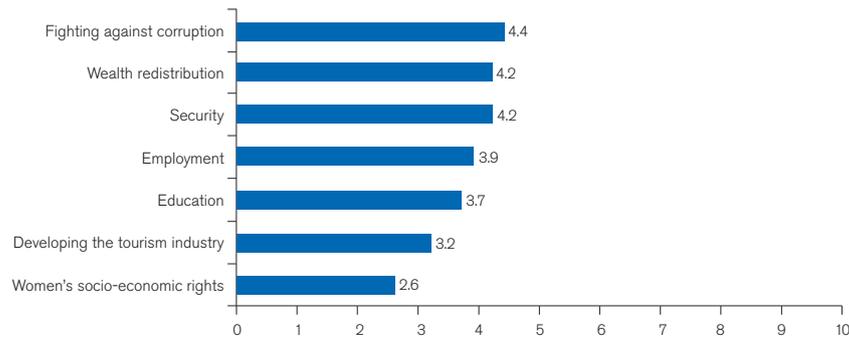
The mounting social tension in the streets and the economic uncertainty has created a very unstable and difficult socio-economic and political context, both at a national and regional level.

From Politics to Policies: an Urgent Need for *Real* Policies

This challenging environment, with increasing socio-economic demands from the people, requires coherent well-targeted sustainable policies that respond to it based on the real means and capabilities of the existing state resources in today's context of severe scarcity. There are fewer resources at a time of greater needs and demands. Resolving this equation requires experience in management and wise and inclusive political decisions.

Some of the most pressing social and economic demands, such as employment, modernisation of the education system, redistribution of wealth among the population and the fight against corruption, respond to deep-rooted structural factors and need comprehensive policies that can bring results in the medium rather than short term. But in today's context of urgent need for short-term positive results, the Islamic parties are widely seen as incapable of addressing these issues, due to their lack of experience in these fields, but also due to the belief that the *deep state* of the old regime is profoundly rooted in the institutions and that revisionist forces are still very powerful and well organised to resist possible changes.

Graph 2: Assessing the capacity of the new Islamist governments to address the socio-economic demands (average on a scale of 0-10, where 0 stands for no capacity and 10 for very high capacity)



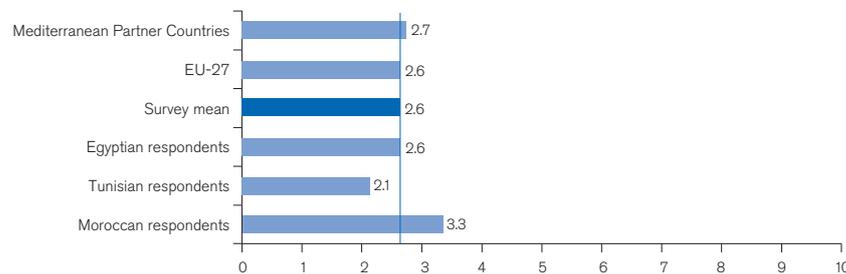
Source: Compiled by the IEMed based on the results of the 4th Euromed Survey

Although one of the main political strengths of the Islamist parties while campaigning for power was their deep commitment to fighting corruption in the public institutions, they are not seen as powerful and capable enough to address this critical issue in the short term. The instability of the governments, with frequent changes in high level posts and not enough human and economic resources to implement policies to fight corruption (as in the case of Mohamed Abbou, who resigned as Minister for the Administration Reform of the Tunisian Government in 2012 due to this issue), shows a short-term inability to commit to a comprehensive approach to this critical issue.

Many people in these countries, especially in Egypt and to a lesser extent in Tunisia and Morocco, do not see the Islamic-led governments committed to coping with key issues in their societies such as improving the socio-economic rights of women, who are critical emerging political actors in the uprisings against the old regimes. Islamists' view of the role of women in society collides with the collective and individual demands of women's rights organisations asking for egalitarian legal and social treatment.

Graph 3: Assessing the capacity of the new Islamist governments to address the socio-economic demands on: Women's socio-economic rights

(average on a scale of 0-10, where 0 stands for no capacity and 10 for very high capacity)



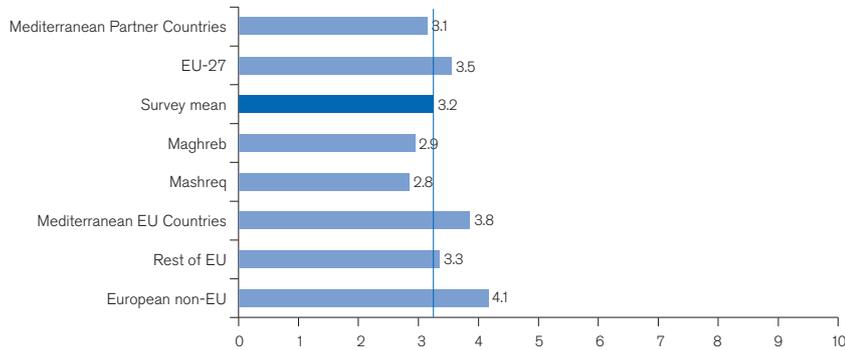
Source: Compiled by the IEMed based on the results of the 4th Euromed Survey

In today's context of uncertainty there is an urgency to restore security in the streets, due to the dramatic increase of all kinds of violence. In the main cities of Egypt, women are increasingly harassed, thefts and killings have grown dramatically and weapons are widely carried by civilians. Islamic-led governments have not so far been able to restore minimum security to the streets. In certain cases they have even been openly accused of passivity towards Salafist violence in demonstrations, their temporary occupation of some villages or the killing of opposition leaders, such as in the recent cases of Tunisia.

Regarding their policies to promote value added sectors, create jobs and attract foreign direct investment, there seem to be reasonable doubts about their willingness to develop such a critical sector as tourism. Their public debates on issues with a direct impact on the attractiveness of these countries as tourist destinations, such as the possibility of banning alcohol, restricting some beaches to nationals or the possibility of asking women to wear more conservative clothing, do not encourage confidence in the willingness of the Islamist parties to promote this important sector.

Graph 4: Assessing the capacity of the new Islamist governments to address the socio-economic demands on: Developing the tourism industry

(average on a scale of 0-10, where 0 stands for no capacity and 10 for very high capacity)



Source: Compiled by the IEMed based on the results of the 4th Euromed Survey

There is a general willingness by the new governments to promote added value sectors as well as to strengthen innovation in those that have been developed over recent years. But no clear, ambitious, comprehensive and systematic plan seems to have been developed thus far, bringing more doubts over their priorities and capabilities in these strategic issues.

Foreign Direct Investment (FDI): Has the Arab Spring Affected the Flows towards the Region?

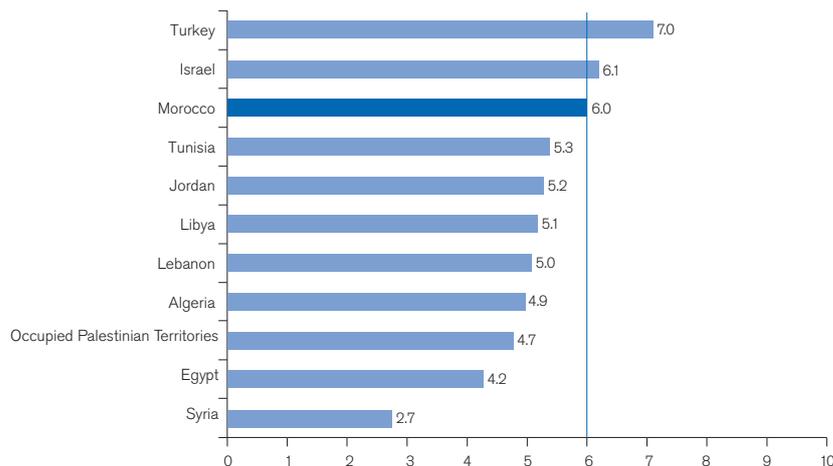
Investment flows always seek out profit but in a context of minimum stability, both political and legal. Today's situation of economic crisis in most of the developed economies is making SME investment in production abroad scarcer and demands more stable contexts, difficult to find in today's Arab Mediterranean economies.

Large-scale investments carried out by big multinationals have a more global approach and are ready to cope with more risk than SMEs. Nevertheless, legal and political uncertainties, retroactive revision of laws for political reasons and, in some cases, widespread insecurity (due to open conflict situations as in Libya or Syria) are increasingly making international investors reluctant to honour previous investment commitments or study new ones.

In this respect, it is likely that the countries reforming their economies and legal frameworks through inclusive policies, such as Morocco, will revalue their attractiveness in a turbulent neighbourhood.

Graph 5: Arab Spring impact on the level of Foreign Direct Investment in the region in the next two years (country risk)

(average on a scale of 0-10, where 0 stands for less FDI and 10 for more FDI)



Source: Compiled by the IEMed based on the results of the 4th Euromed Survey

The countries that seem to be going through mid-term instability, although they might have great economic potential such as in the case of Egypt, will face a serious decrease in foreign direct investment in the coming years. Policies adopted by the government revising the conditions of previous large-scale investments from abroad, especially from the Gulf economies, have scared some other potential investors from asking for more legal security for their projects.

Widespread disruptions in production and logistics as well as growing labour rights demands from the trade unions of recent years in Egypt are another factor that discourages potential industrial investors to step into the Egyptian market in the short term. Objectively, the size of the local market, the key logistical accessibility to many other relevant markets, especially the EU and the GCC, and the availability of skilled labour seem to be good factors to encourage entrance into the market. But as of today, national legal and economic uncertainty prevails in investors' decisions on Egypt.

The countries hit by war in the context of the Arab Spring, mainly Libya and Syria, might experience different scenarios. Libya, although still experiencing turbulent instability and even spontaneous open armed conflict, seems likely to attract foreign investment, mainly concentrated on the improvement of the energy sector. Most of the national reconstruction might be financed by the Libyan government itself through its own high revenues from this sector.

The case of Syria is different as a consequence of the size of the destruction, the uncertainty of the resolution of the conflict and the huge dimension of the civil cost. No private investors or multilaterals will invest in this country until the conflict is clearly over, which could take longer than expected due to the balance of forces. This scenario will persist as long as the different forces in the conflict and the international donors' community do not reach a satisfactory agreement that might stabilise the social and economic situation. In this case, significant international funds will be needed to be able to cope with the daunting challenges of reconstruction, thus attracting the international, and very especially regional, private sector to get involved in Syria.

In a context of regional instability, Turkey seems to emerge as the economic beneficiary but due rather to internal dynamics than economic consequences of the Arab Spring. Its internal economic dynamism, the size of its national market and the successful liberalisation and diversification policies implemented have made Turkey one of the most attractive emerging markets in the world. Turkey's private sector has developed an aggressive dynamism to internationalise and diversify its trade and investment partners in the last decade. This has made Turkish entrepreneurs regular visitors to the most important cities of the Middle East and North Africa (MENA) countries. The easy logistical accessibility of people, funds and goods from Turkey to the MENA markets has increasingly made it a hub for the region, thus adding to the growing size of its internal market in GDP and population terms.

Although one of the expected consequences of the Arab Spring is the improvement of socio-economic policies, more transparency and accountability and more attractive economies, it seems that delivering will take longer than expected, thus keeping potential investors waiting for better economic times in the region.