

# The BY MARCUS NOLAND Looming Arab Employment Crisis

*Idle hands are  
the Devil's workshop.*

**F**or two generations, the economic performance of the Arab countries of the Middle East has been middling: worse than East Asia, better than sub-Saharan Africa—the other region most profoundly marked by arbitrary borders and weak states—and about the same as Latin America and South Asia. Not the worst, not the best, falling behind the West. Yet while there has been no crisis in the past—indeed, on some social indicators progress has been spectacular—the region now faces an imminent challenge: how to create jobs for the large cohort of young people reaching working age. The task is immense and the stakes are high: over the next decade or so, the region may experience population growth of 150 million people—the equivalent of adding two Egypts. Only in a few small Gulf oil producers is the median age projected to reach thirty. Rising labor force participation by women only increases the pressure. The region is a demographic time-bomb.

The picture is not entirely bleak: growth has accelerated in recent years, and some countries in the region are benefiting enormously from

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relatively high oil prices. Whether this growth acceleration or the recent level of oil prices will be sustained is an open question. In any event, the impact of this windfall is felt unevenly across the Arab world.

Merely maintaining past performance will be insufficient to generate the necessary jobs. One method of rapidly creating a sustainable increase in employment is through an expansion of labor-intensive manufacturing or services exports. But outside the petroleum sector, the region's track record is inauspicious. Forget China and India: in one recent year the Philippines generated more manufactured exports than the entire Arab world. And until the recent oil-fueled expansion of intraregional foreign direct investment, the region typically attracted less foreign direct investment than Sweden. The Arab world risks being left behind at precisely the moment it needs to accelerate job growth.

Achieving that goal is inhibited by two factors, one institutional, the other political. The Arab countries score poorly on a nexus of indicators relating to cross-border economic integration and the transfer, dissemination, and application of technological knowledge and innovation. Outside of the special cases of the extractive industries such as oil and tourism, where geology or special attractions like the Pyramids confer unique and irreproducible advantages, as a group the Arab countries appear to have weak linkages to the outside world, whether measured in terms of merchandise trade, import of capital goods (which embody technological advances from abroad), cross-border investment, integration into trans-border supply networks, technology licensing, and internationally recognized intellectual achievements. In short, the neural synapses that would link the latent productive possibilities of the Arab people with the goods and services demanded in the global market appear to be weak or nonexistent.

Building such links presents a formidable challenge. Unlike issues of macroeconomic policy management—where policy change can be implemented by a relatively small number of centrally placed tech-

nocrats and is subject to relatively straightforward feedback mechanisms to facilitate benchmarking progress—addressing the institutional weaknesses requires a much more prolonged and uncertain slog.

The hesitancy to reform stems from concerns more fundamental than mere special-interest politics. While the region's contemporary economic performance may not be distinctive, its enduring political authoritarianism is. This lack of political dynamism in the face of underlying social change together with the increasingly religious orientation of the political opposition paradoxically raises the possibility of abrupt transitions or regime changes. Intermittent terrorist incidents further elevate the risk premium. Such deep political uncertainty discourages behavior that involves irreversibility—from investment to a reversal of the brain drain—and creates the possibility of a self-reinforcing downward spiral.

Yet substantial intraregional variation in achievement along many of the relevant benchmarks suggests that these outcomes are not determined by intrinsic cultural factors. The influence of Islam or the anthropology of Arab culture may have many effects on local institutions and practices, but they cannot explain why it takes fifteen times as long to enforce a contract in Egypt as it does in Tunisia. Significant improvements in economic outcomes could be achieved by simply matching the best practice standard established by others within the region. Egypt need not turn into Norway.

Whether reforms succeed primarily will be determined by developments within the region. But the international community has an enormous stake in the outcome and no real alternative but to engage in an attempt to support the reform process—and it is over this external dimension that we exert the most influence. The United States bears special responsibility for the situation in Iraq and secondarily for developments in Palestine. It is hard to overstate the depths to which America's image within the region has fallen. In one recent poll, 85 percent of Jordanians—a “moderate”

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| Population projections for the Arab world |                             |            |            |            |   |      |  |             |
|---|-----------------------------|------------|------------|------------|---|------|--|-------------|
|   | Total population (millions) |            |            |            | Dependency ratio<br>(percent, based on<br>scenario 2) |      | Median age (years,<br>based on scenario 2) |             |
|   | Scenario 1                  |            | Scenario 2 |            |   |      |  |             |
| Country                                   | 2000                        | 2020       | 2000       | 2020       | 2000  | 2020 | 2000                                       | 2020        |
| Algeria                                   | 30                          | 43         | 30         | 41         | 0.76  | 0.44 | 20   | 29          |
| Bahrain                                   | 1                           | 1          | 1          | 1          | 0.50  | 0.36 | 26   | 33          |
| Djibouti                                  | 1                           | 1          | 1          | 1          | 1.01  | 0.57 | 18   | 22          |
| Egypt                                     | 68                          | 102        | 68         | 91         | 0.73  | 0.46 | 20   | 29          |
| Iraq                                      | 23                          | 41         | 23         | 35         | 0.92  | 0.51 | 17   | 24          |
| Jordan                                    | 5                           | 9          | 5          | 7          | 0.78  | 0.50 | 19   | 25          |
| Kuwait                                    | 2                           | 3          | 2          | 2          | 0.45  | 0.37 | 27   | 34          |
| Lebanon                                   | 4                           | 5          | 4          | 5          | 0.88  | 0.47 | 18   | 28          |
| Libya                                     | 5                           | 8          | 5          | 8          | 1.09  | 0.45 | 15   | 25          |
| Morocco                                   | 30                          | 43         | 30         | 41         | 0.69  | 0.45 | 21   | 29          |
| Oman                                      | 3                           | 5          | 3          | 4          | 0.51  | 0.51 | 26   | 24          |
| Qatar                                     | 1                           | 1          | 1          | 1          | 0.41  | 0.33 | 27   | 36          |
| Saudi Arabia                              | 20                          | 39         | 20         | 33         | 0.51  | 0.49 | 26   | 25          |
| Syria                                     | 16                          | 27         | 16         | 24         | 0.91  | 0.50 | 17   | 26          |
| Tunisia                                   | 9                           | 12         | 9          | 12         | 0.67  | 0.46 | 22   | 30          |
| UAE                                       | 3                           | 3          | 3          | 3          | 0.29  | 0.38 | 30   | 41          |
| Yemen                                     | 18                          | 43         | 18         | 37         | 0.99  | 0.79 | 16   | 18          |
| <b>Arab Region</b>                        | <b>238</b>                  | <b>388</b> | <b>238</b> | <b>346</b> |   |      | <b>20.0</b>                                | <b>26.7</b> |

Scenario 1: Under the assumption that total fertility rate and life expectancy at birth remain constant at their estimates in the year 2000.  
 Scenario 2: Using the total fertility rate and life expectancy at birth as estimated by the United Nations for every year during the period (2000–20).  
 Source: United Nations Development Programme (2002, 144). Figures may not add due to rounding.

Arab country with which the United States has a free trade agreement—expressed unfavorable sentiments toward the United States. One might be tempted to discount this response as reflecting Jordan’s unenviable geographic position, wedged between the conflicts in Iraq and Palestine. But 69 percent of Egyptians, the other Arab country polled, recipient of billions of dollars in U.S. aid, also had an unfavorable assessment of the United States. Huge majorities in Arab countries are aware of the abuses at Abu Ghraib and

Guantanamo Bay. The Dubai Ports World debacle exposed U.S. hypocrisy. In counterpoint to the complex, difficult, and uncertain tasks that the Arab governments face in strengthening their local institutions, the United States faces a difficult path in repairing its standing in the Arab world.

Such an initiative would have four parts. The first component is regulatory and macroeconomic. As long as the United States runs current account deficits, it will require counterpart capital inflows from abroad. The U.S.

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deficits are mirrored by oil-fueled surpluses in the Gulf, and quite naturally Arabs will be prominent among investors in U.S. assets. One way of attenuating investment disputes would be to reduce U.S. reliance on foreign finance. Serendipitously, the first step would involve fiscal policy adjustment, which requires no diplomacy and can be undertaken unilaterally. Regulatory reform is also in order.

The second component would be public diplomacy aimed at both improving the image of the United States and strengthening progressive democratic political forces in the Arab world. One possibility would be to redirect resources from the U.S. government-sponsored satellite television channel al-Hurra, which has failed to attract a significant audience, and apply these resources to increasing the availability of Western news sources in the Arab world. Evidence suggests that there are not only profound divergences in opinion between Arabs and the West but also deep differences regarding the underlying facts linked to sources of news and information.

A complementary approach would be to expand two-way exchanges of opinion leaders to facilitate Arab exposure to nonofficial American opinion leaders. The United States also needs to reconsider Department of Homeland Security policies that significantly impede the issuance of visas to legitimate Arab scholars and opinion-makers, discouraging precisely the sort of contact that should be encouraged, and generally conveying a poor image of the United States. To be clear, mere familiarity will not engender love—but what is being communicated today is so negative that almost any kind of sincere and serious engagement would represent an improvement over the status quo. Pop music radio stations are not the answer.

The third component could be preferential trade agreements, though obviously the impact of any specific agreement will depend on its particulars as well as complementary policy changes undertaken by the partner country. However, the way that the United States has been negotiating these agreements is effectively creat-

ing a “hub-and-spoke” system in which individual Arab governments have strong bilateral agreements with the United States but weak or nonexistent agreements among themselves. In part this reflects differences in both capacity and orientation across the Arab governments, and in the specific cases of the militarily vulnerable Gulf oil exporters, a particular interest in deepening ties with a strategic partner. If it were just an issue of variable speed geometry to borrow a European phrase, that would be one thing. The bilateral agreements themselves contain mutual inconsistencies, however, which make incorporating them into a single region-wide accord difficult. The problem is exacerbated by the fact that the rules in the agreements the United States and the European Union reach with the Arab countries are inconsistent. It would be desirable to increase the internal consistency of these arrangements to facilitate integrating them in the future.

A renewed emphasis on multilateral coordination should be the fourth component of U.S. policy toward the region. Much of what is needed in the Arab world amounts to institutional reform and capacity building. The United States as a national government obviously has a role to play in providing technical assistance and support—its U.S. Agency for International Development mission in Cairo is the largest in the world. But the United States should not limit itself to unilateral measures, however, and ought to make use of the whole panoply of international institutions, including the World Trade Organization, International Monetary Fund, and World Bank, which are well-suited for a patient process of engagement with the countries of the region. In essence one is buying an option on reform: maintaining contact and a local knowledge base in anticipation of the day when the host government will be ready to move forward.

The Middle East has long been a politically contested region of global significance. The demographic pressures the region faces to productively employ its young people entering the labor force raise the stakes even higher. It is not difficult to envision the region caught in a downward spiral where impoverishment, discontent, militancy, and repression feed upon one another. Yet this is not the only possible future path. If the region’s daunting employment challenge can be successfully addressed, the region’s demographics could turn from a potential liability to a valuable asset. Growing prosperity, confidence, and optimism about the future could underpin movement toward greater political openness and social tolerance. The recognition that neither of these alternatives can be excluded is both an antidote to despair and a call to action. ♦