

Expert Group meeting on the priority theme of the 57<sup>th</sup>  
session of the Commission for Social Development

# ***Addressing social inequalities in Arab States: Competing narratives and role of fiscal policies***

Economic and Social Commission for Western Asia



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Khalid Abu Ismail and Niranjana Sarangi

Economic Development and Integration Division

# Outline

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**A- Conventional wisdom**

**B- Competing narrative**

**C- Fiscal policy considerations**

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# 1. Conventional wisdom



## Contextualizing inequality: Development stylized facts (1990-2010)

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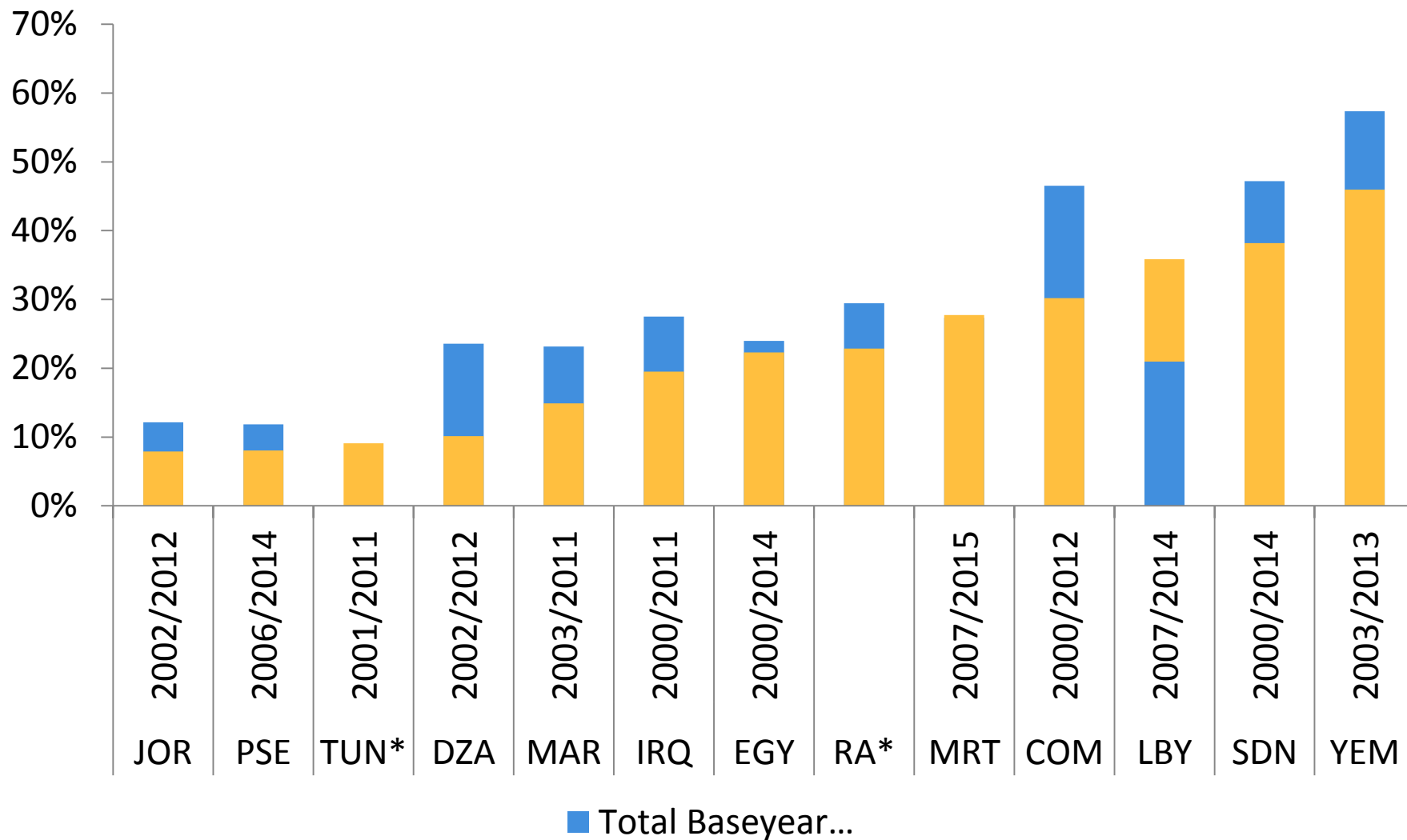
1. Relatively high GDP and growth was decent for most countries (4-5% in 2000s) before the spring
2. Fiscal and monetary indicators were stable and outlook positive in 2010 (IMF/WB regional outlook, 2010)
3. Most countries above medium HDI level with significant progress since 1970, especially in LE and education.

## Contextualizing inequality: Development stylized facts (1990-2010)

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4. Low and declining poverty according to international definitions (less than 10% using \$1.9 or global MPI) and Middle class using ESCWA definition is largest economic group in 2010.

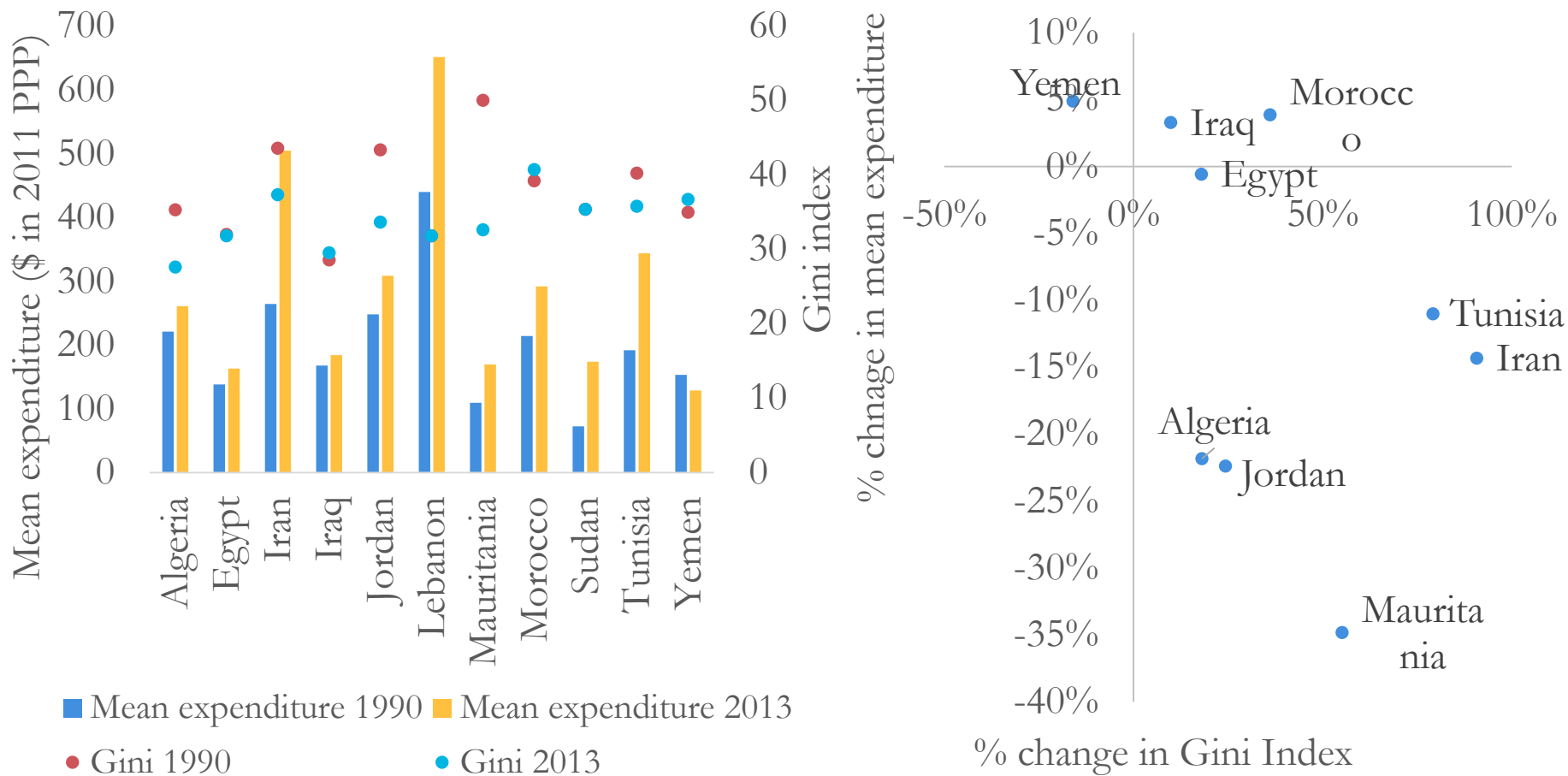
## 5. Complimenting decline in extreme poverty stunting declined in most countries





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## 6. Low and declining inequality along with rising household expenditure



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Finally, governance deficits are acknowledged but why worry about them if the development model that has prioritized economic growth and human development has delivered so much to so many on so many fronts?

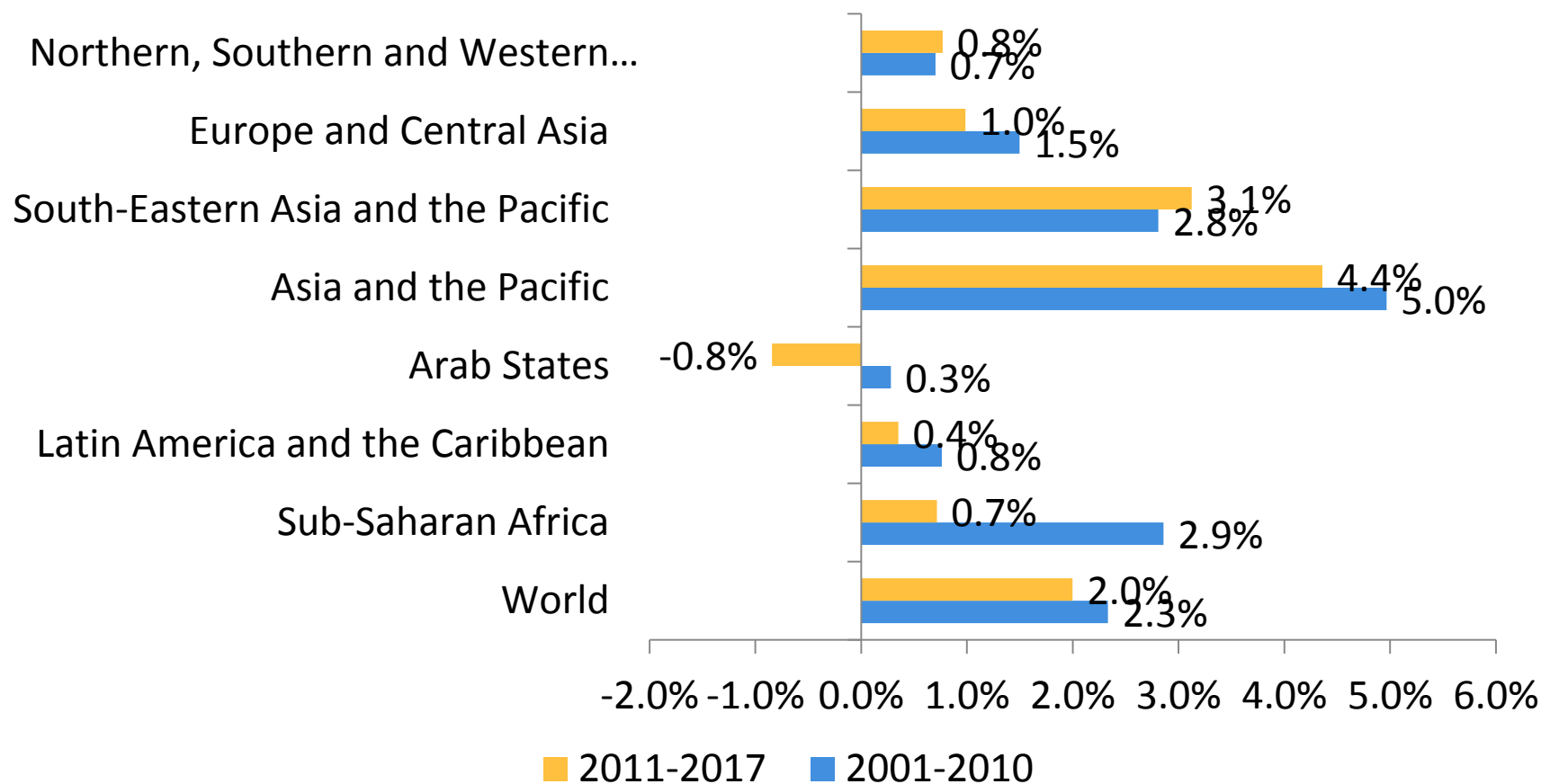


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## 2. But has it?

*Elements of a counter narrative*

# 1. Growth much lower on per capita basis and without structural transformation or productivity

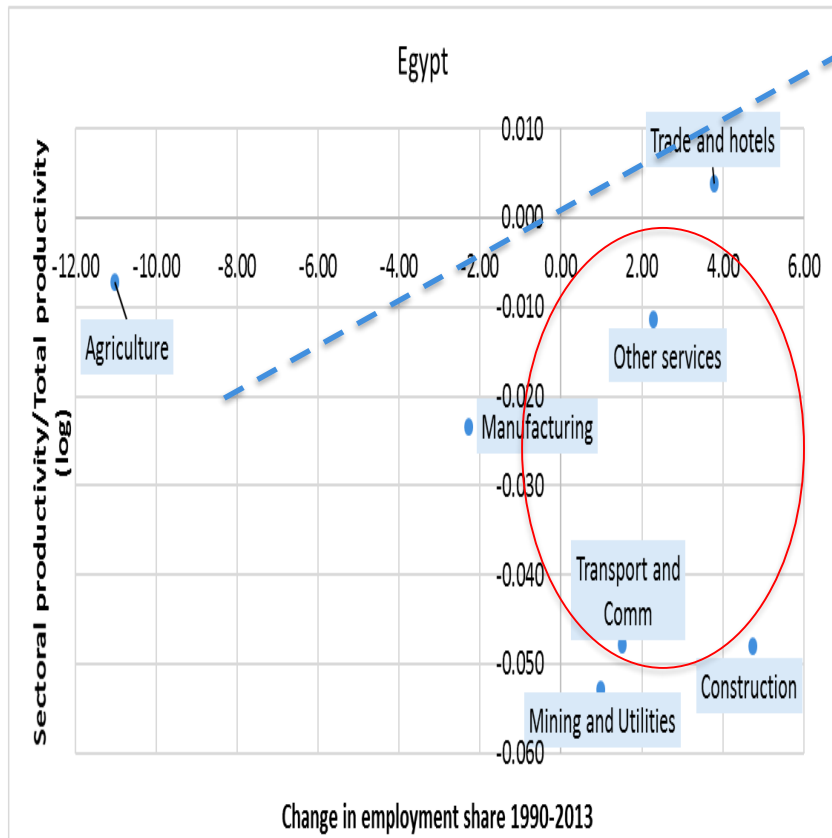


Source: ILO estimates and projections

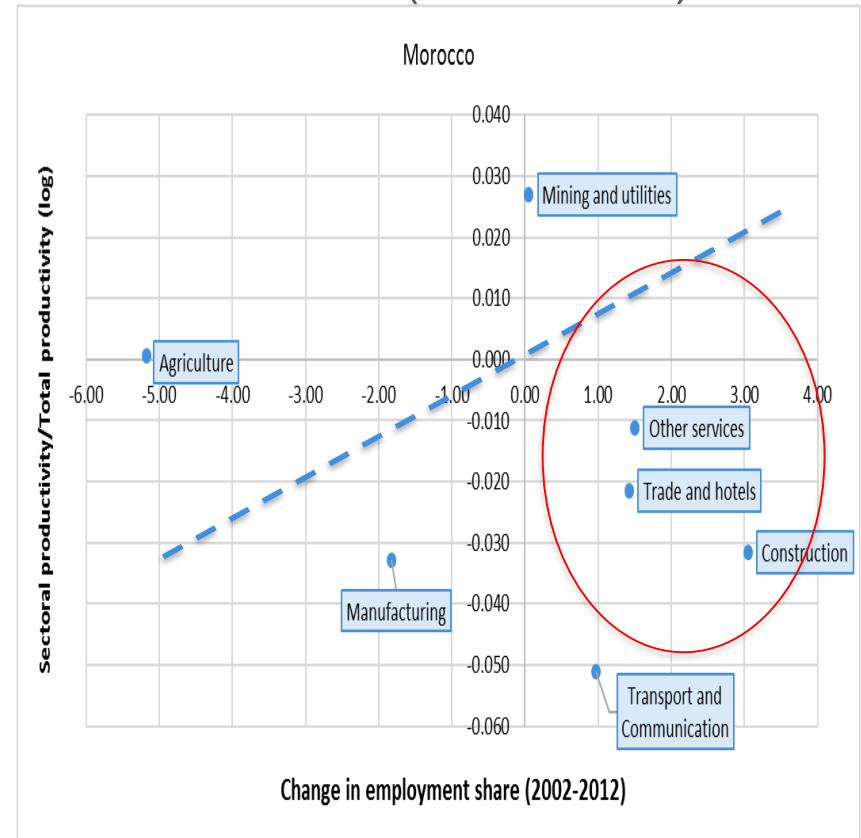
## 2. Employment with high and increasing informality

Labour moved from agriculture and even manufacturing to other service sectors with negative growth in productivity

Egypt (1990-2013)



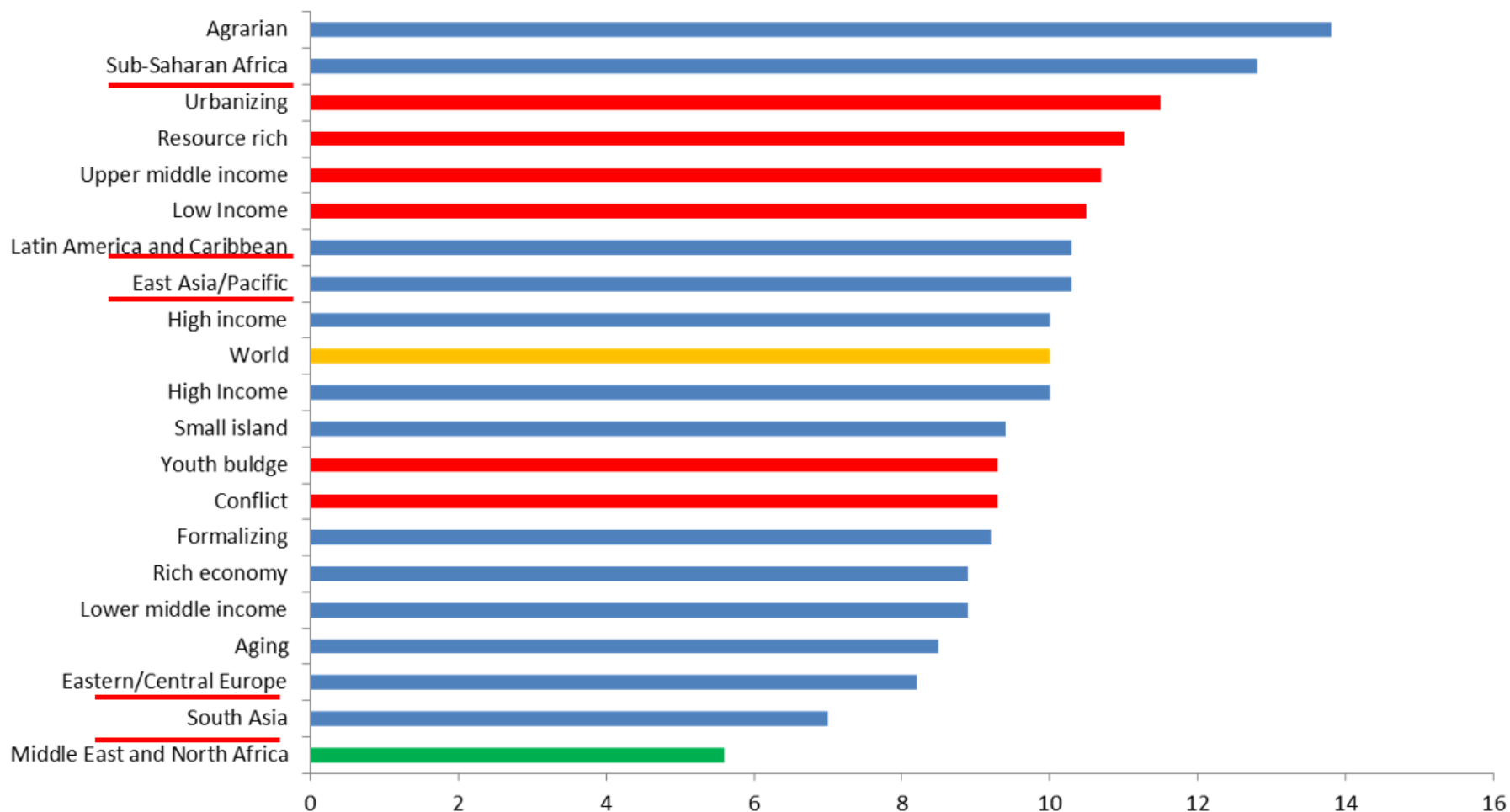
Morocco (2002-2012)



Source: N. Sarangi, K. Abu-Ismael and V. Gantner (2017). Fiscal Policy and Structural Transformation in the Arab Region: What are the Pathways? ESCWA Working Paper. E/ESCWA/EDID/ 2017/WP.7.

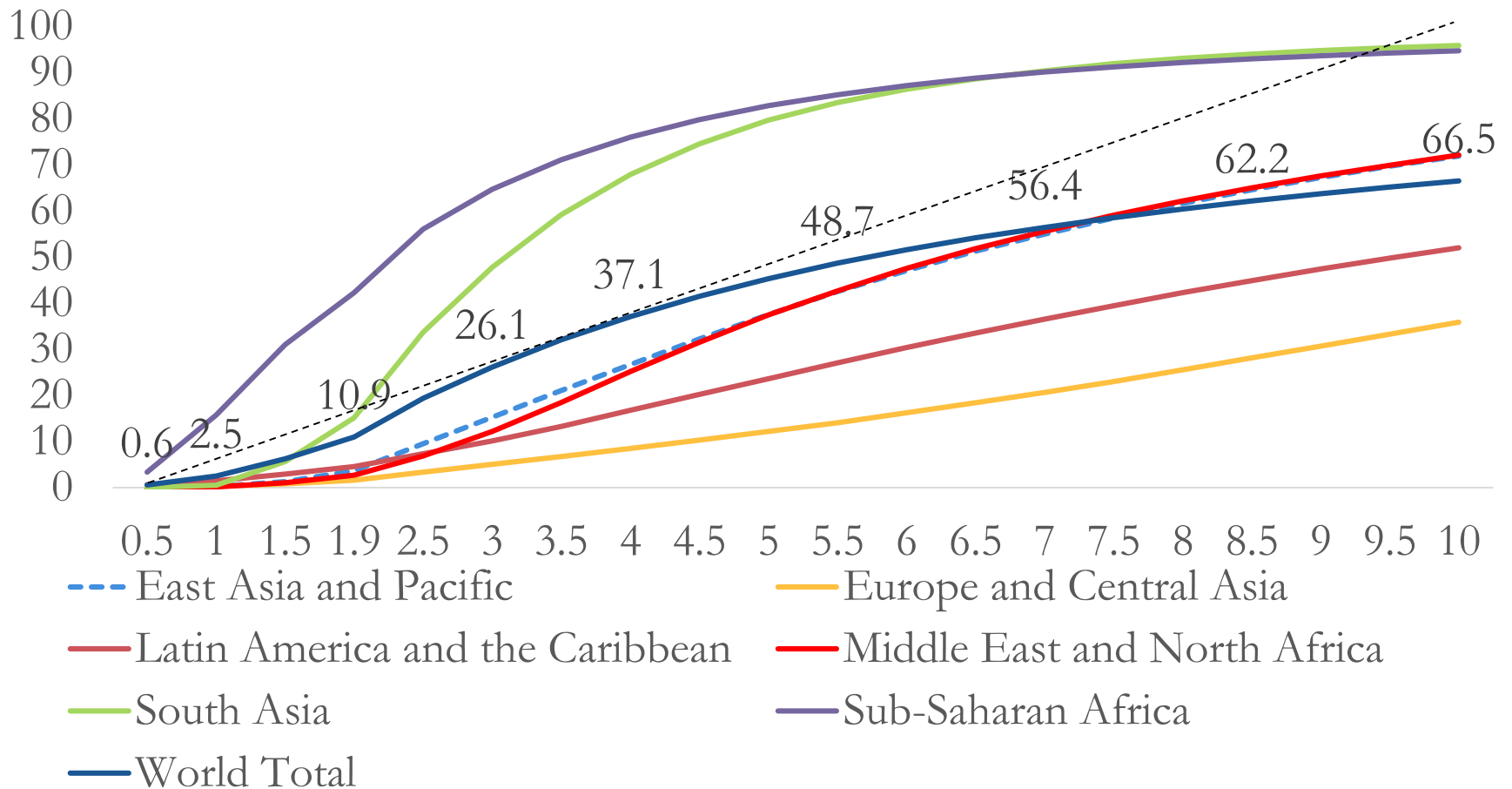
### 3. As a result, Arab Countries have lowest return to schooling with implications for social mobility

*almost half of the average for 120 countries*

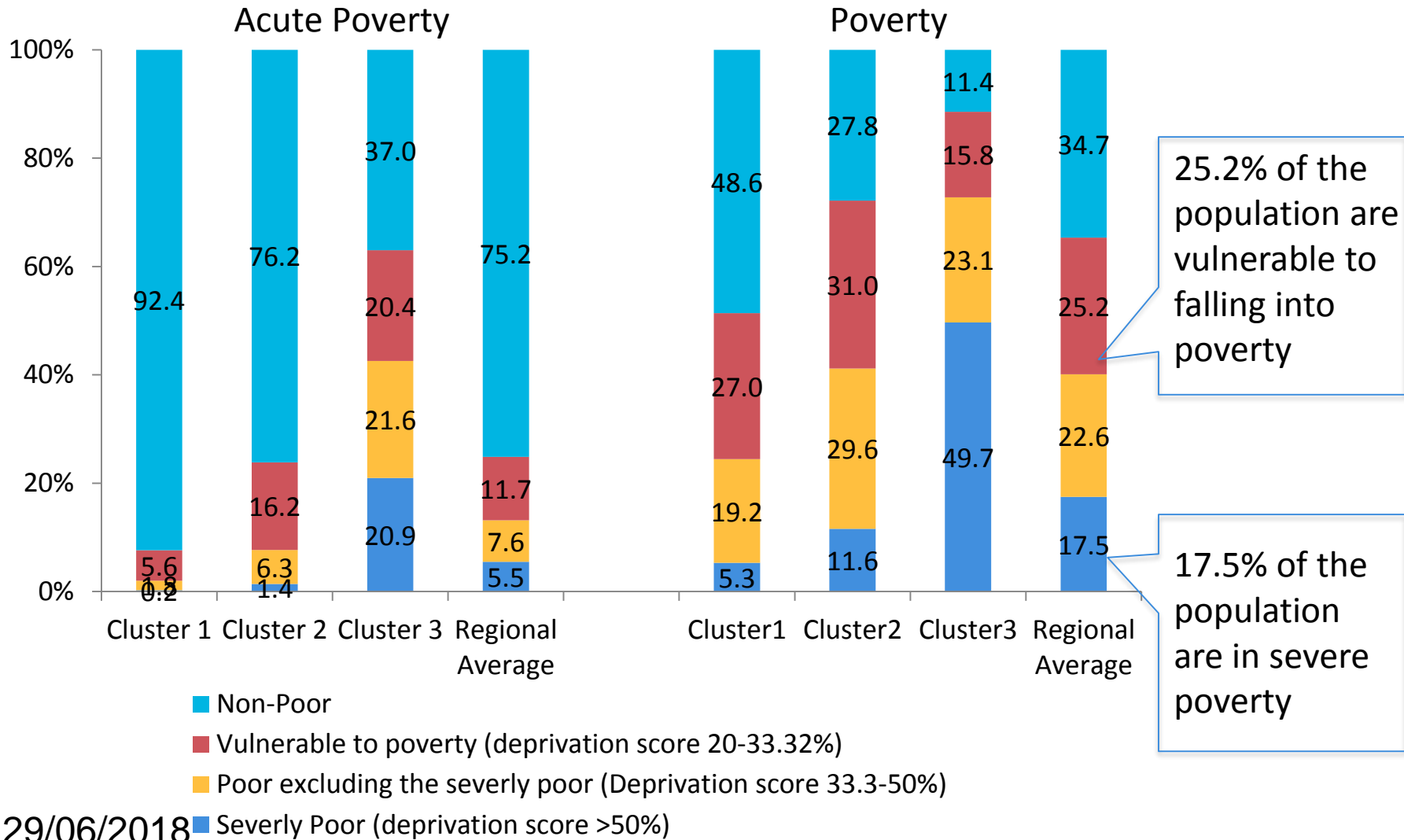


Source: Montenegro and Patrinos, 2013

## 4. Region is not as poor as SSA or SA but poorer than we think with higher PLs

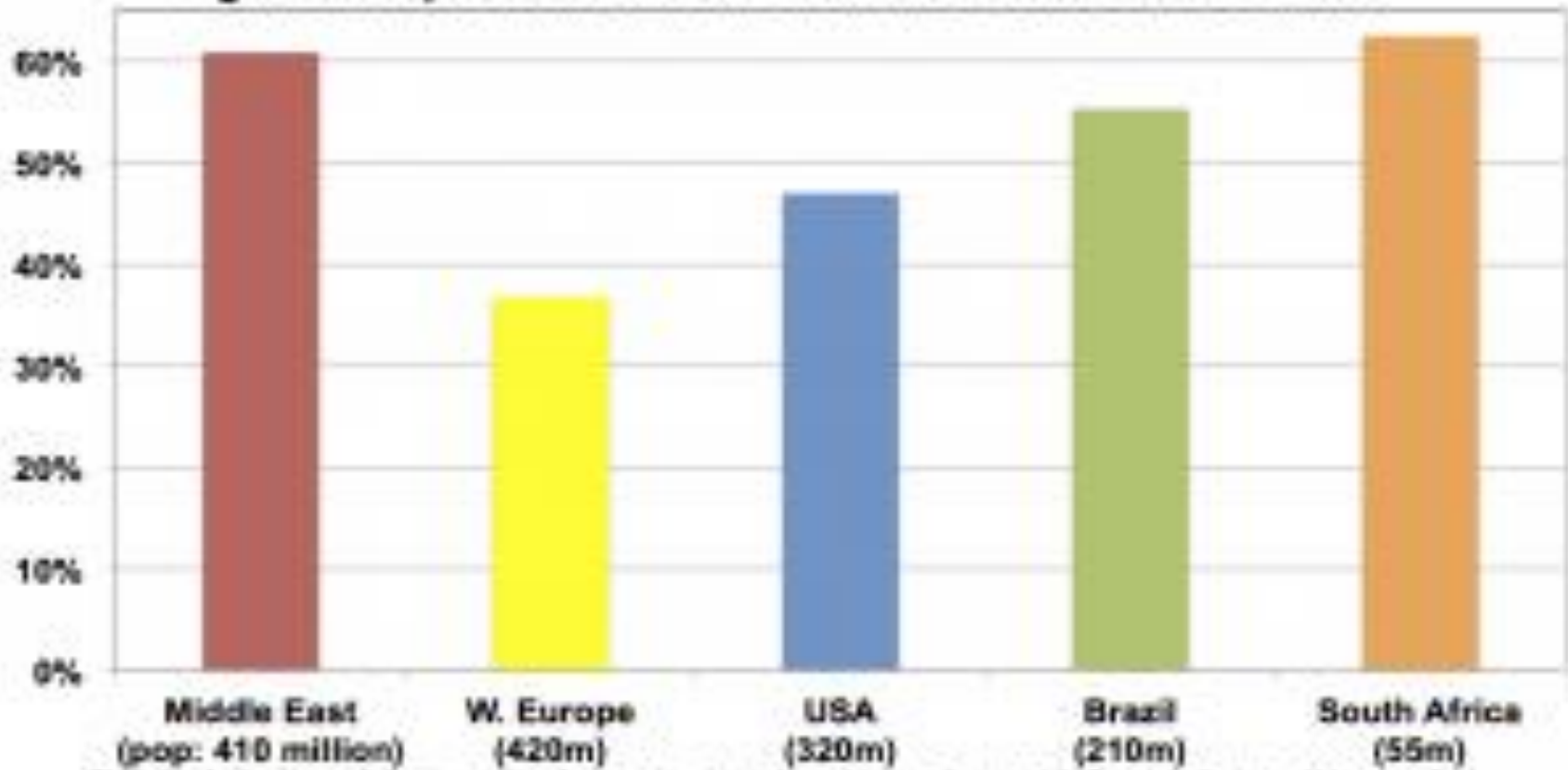


# 5. Multidimensional poverty and vulnerability is also much higher with a tailored regional definition, affecting 6.5 in 10 HHs



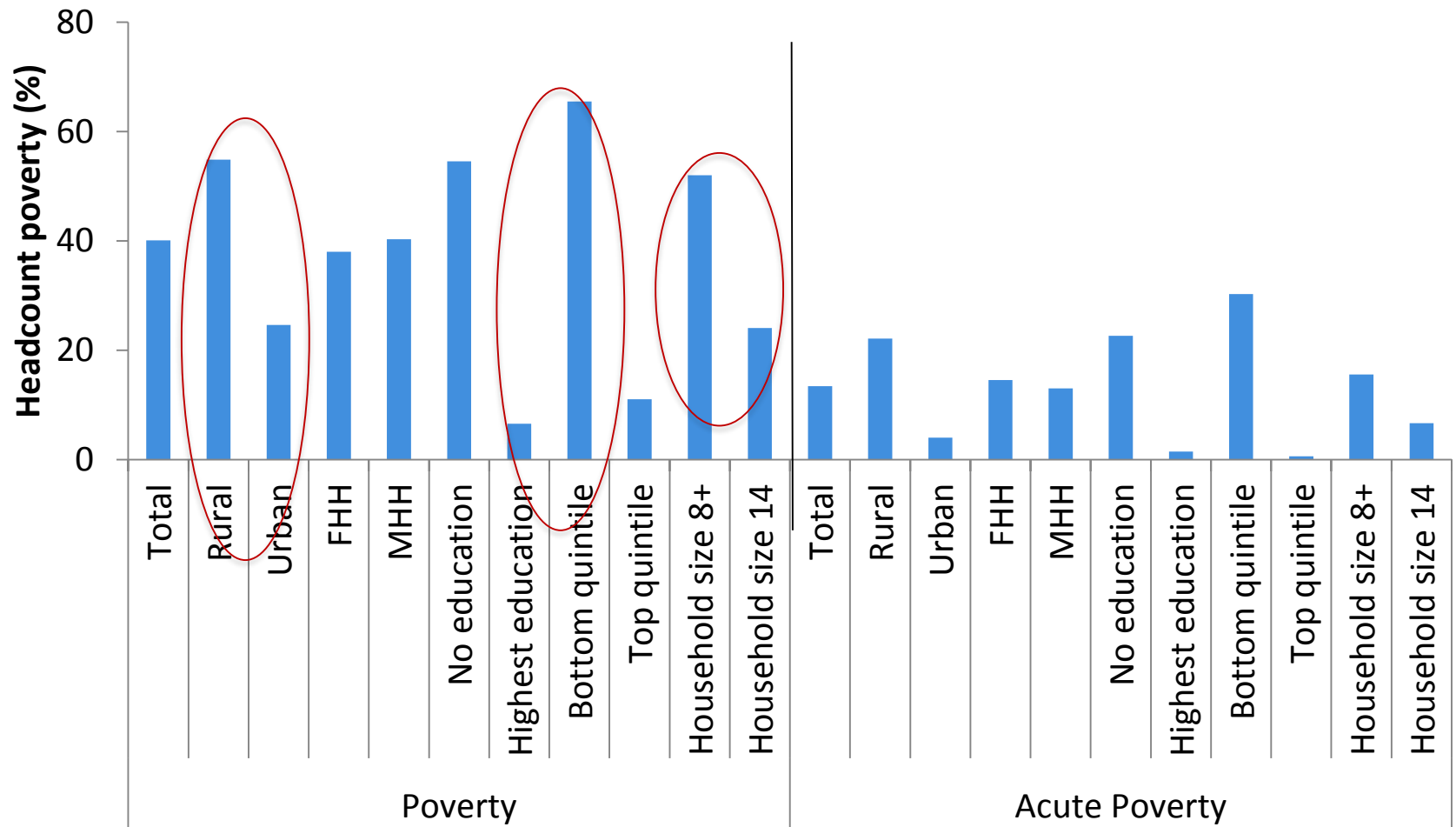
## 6. Expenditure Inequality is higher than Gini suggests when top spenders are factored in

Figure 5b. Top 10% income share: Middle East vs other countries



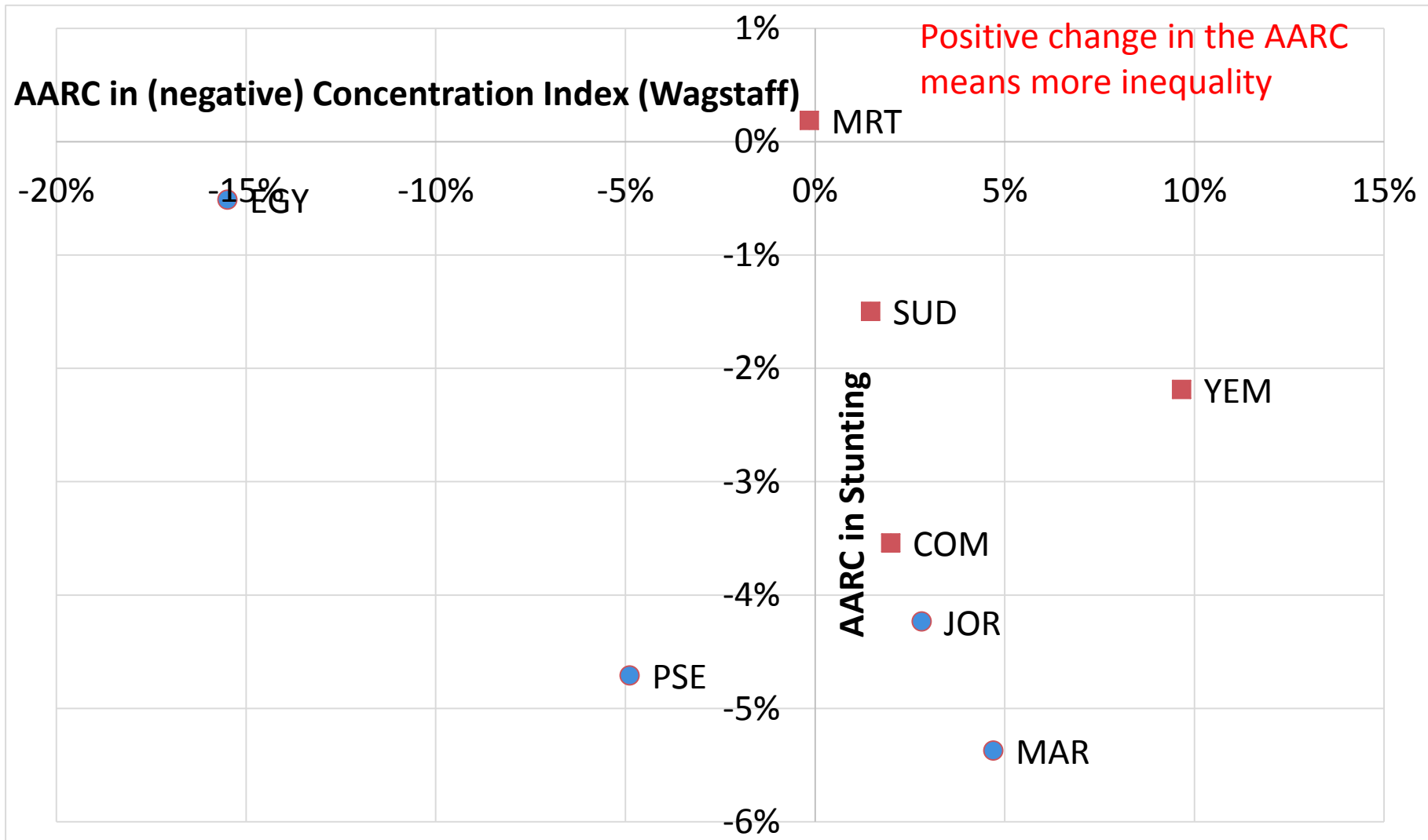
Distribution of national income (before taxes and transfers, except pensions and unempl. insurance) among adults. Corrected estimates combining survey, fiscal, wealth and national accounts data. Equal-split series (income of married couples divided by two). Latest years available (2010-2016). Source: WID.world.

# 7. High inequality in multidimensional poverty





## 8. Declining deprivation yes but in some cases with an increase in inequality as in the case of stunting



# Conclusion: We have two competing narratives and policy visions

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- (1) Arab development model was working- broken social contract on employment, not poverty and inequality, the cause of the AS. **Policy conclusion: some governance fine tuning to improve private sector by better doing business indicators, less state intervention (smaller public sectors, subsidies and social transfers) and better education quality (IMF-WB)**
- (2) Arab development model is fundamentally flawed. **Policy conclusion: Governance is key but through strong institutions that can manage complex development programs. But this will require different social and economic policies with different targets. Stabilisation needs to give way to structural transformation, long term unemployment and inequality reduction policies.**

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## 3. What to do?

# Fiscal Policy for social inclusion

This section draws heavily on the ESCWA report on “Rethinking Fiscal Policy for the Arab Region” (2017)

<https://www.unescwa.org/publications/rethinking-fiscal-policy-arab-region>

# 1. Design fiscal policies to promote economic transformation and decent work to raise return on education and promote social mobility

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(a) increased public investment/fiscal incentives into strategic sectors;

- ✓ *the strategic sectors (higher value-added and relatively high labour-intensive sectors)*

(b) increased investment in building infrastructure, innovations and improving human capital

- ✓ *Investing in knowledge assets, quality of education*
- ✓ *Investing in infrastructure*

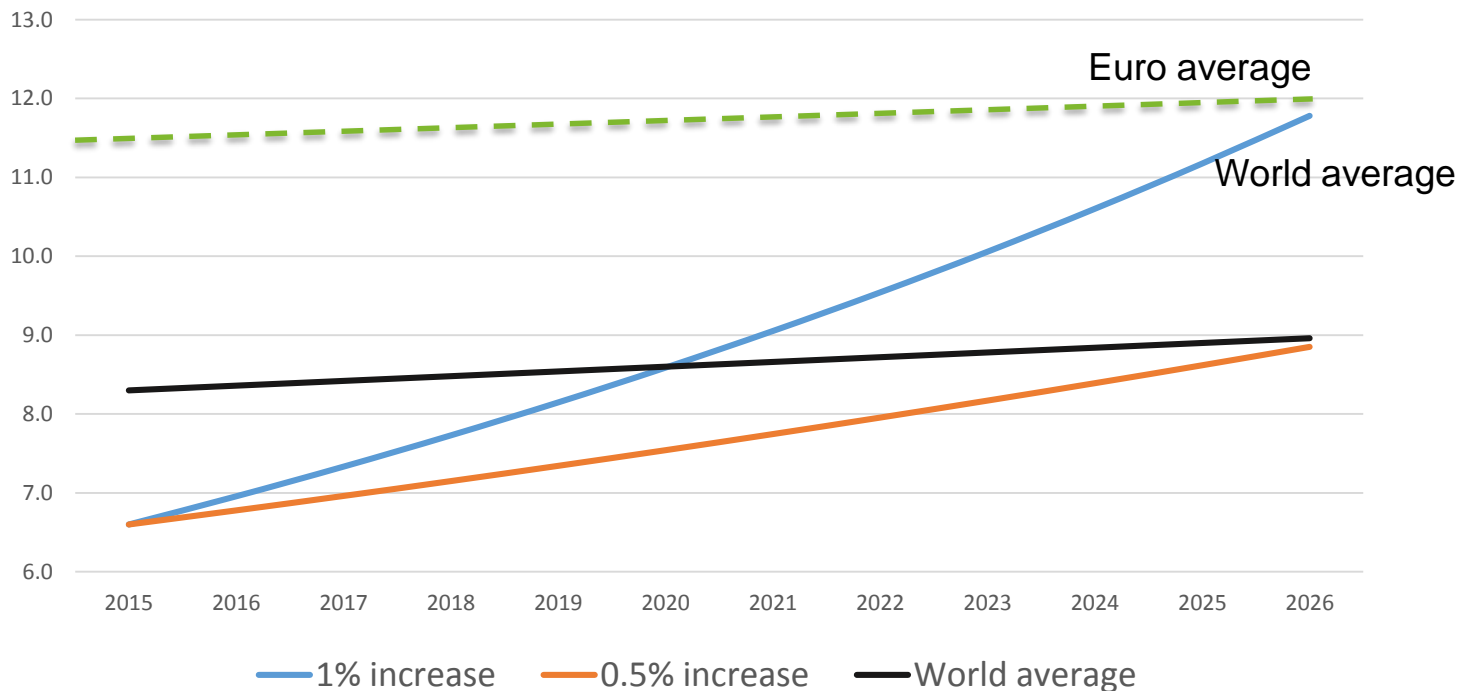
*As a direct intervention to boost sectoral investments, fiscal policy is crucial. Complementarities with monetary, trade and industrial policy can accelerate the process of structural transformation.*

Source: ESCWA (2017). Rethinking Fiscal Policy for the Arab Region. E/ESCWA/EDID/2017/4.

## 2. Make budget choices to reduce poverty and inequality, and close health, housing and education deficits

*Enhance spending on education and health*

*Long Term Effects of Increasing Education Expenditure on Mean Years of Schooling*



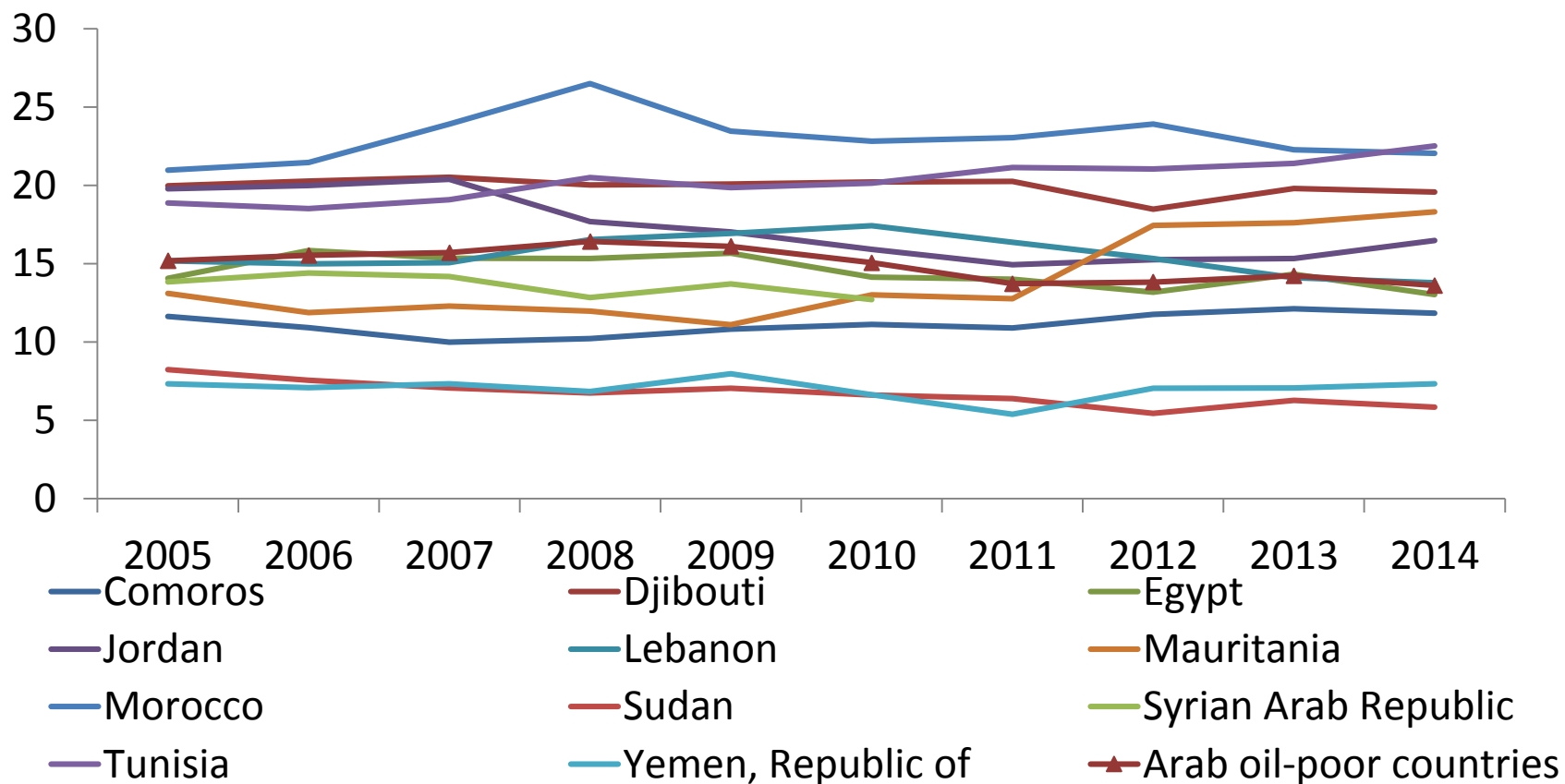
Source: N. Sarangi and J. von Bonin (2017). Fiscal Policy on Public Social Spending and Human Development in Arab Countries. ESCWA Working Paper. E/ESCWA/EDID/2017.WP.13.

### 3. Expand and sustain fiscal space by raising revenues

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- Oil-poor countries: Greater focus on mobilizing revenues rather than cutting productive expenditure
  - *Improve tax fairness, increase progressivity, identify potential tax base (property tax), rationalise exemptions (income tax, VAT, excise), Compulsory filing of tax (at residents'/businesses' end)*
  - *Administrative reforms to control tax evasion, tax avoidance and illicit financial flows*
- Oil-rich countries: Diversify revenue sources to cope with managing volatility and sustaining growth
- Better quality governance: Adoption of rule-based fiscal policy (short-term, medium term, long-term objectives)
- Better data and monitoring (improving transparency)

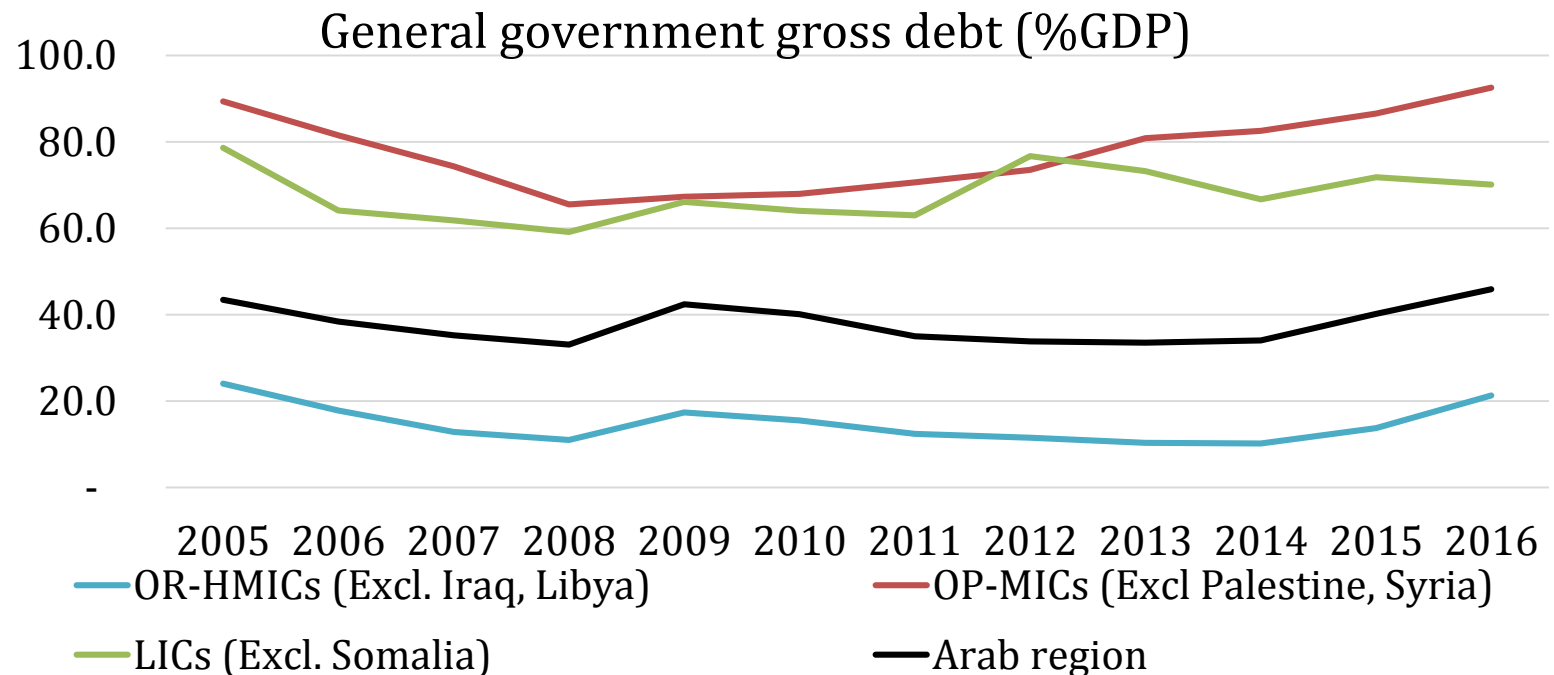
## So in a nut shell, this picture of low tax revenue to GDP ratios in oil poor countries needs to change



Source: N. Sarangi (2016). Domestic Public Resources in the Arab Region: Where Do We Stand?. ESCWA Working Paper. E/ESCWA/EDID/2017/WP.1.

# And this needs to happen soon

## Rising debt and debt servicing payments– A major concern



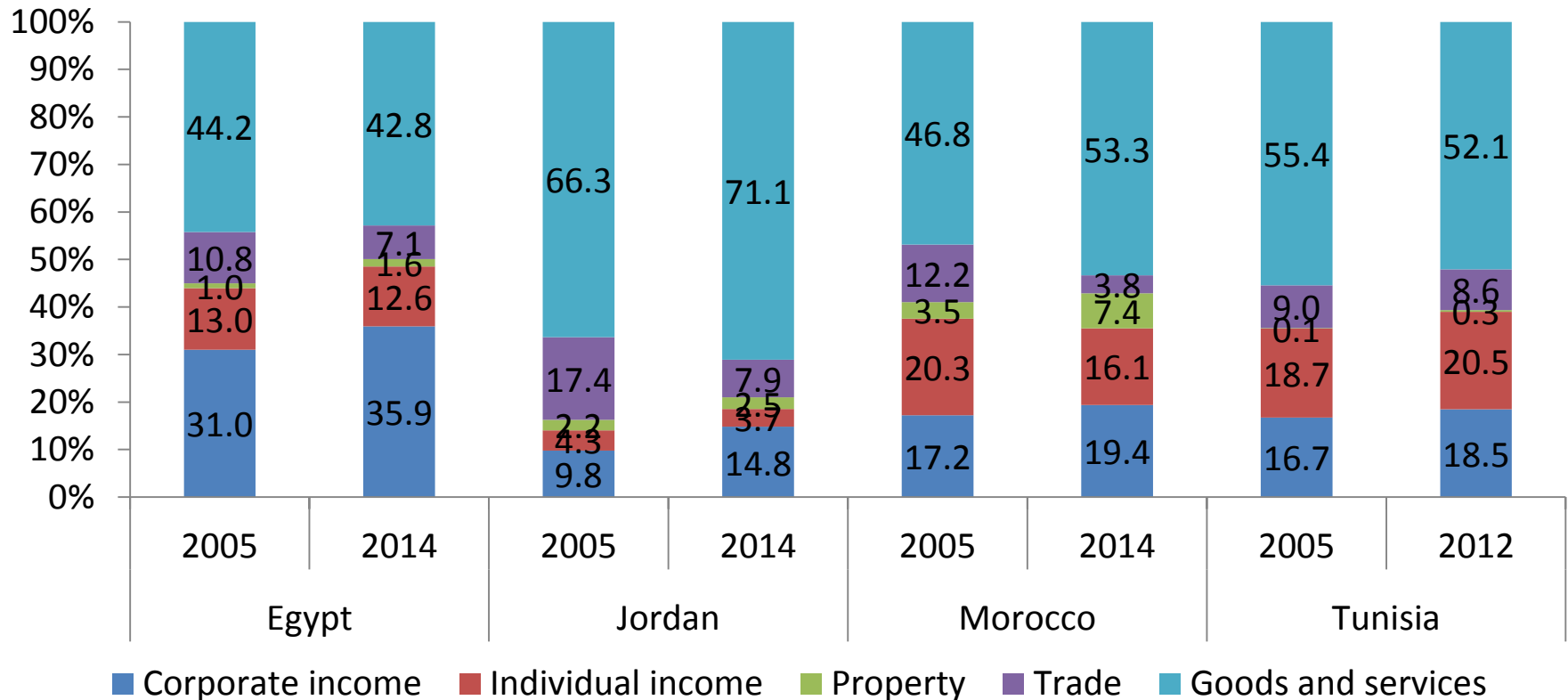
Source: N. Sarangi and L. El-Ahmadieh (2017). Fiscal Policy Response to Public Debt in the Arab Region. ESCWA Working Paper. E/ESCWA/EDID/2017/WP.6.



# And it can't be based on VAT only.

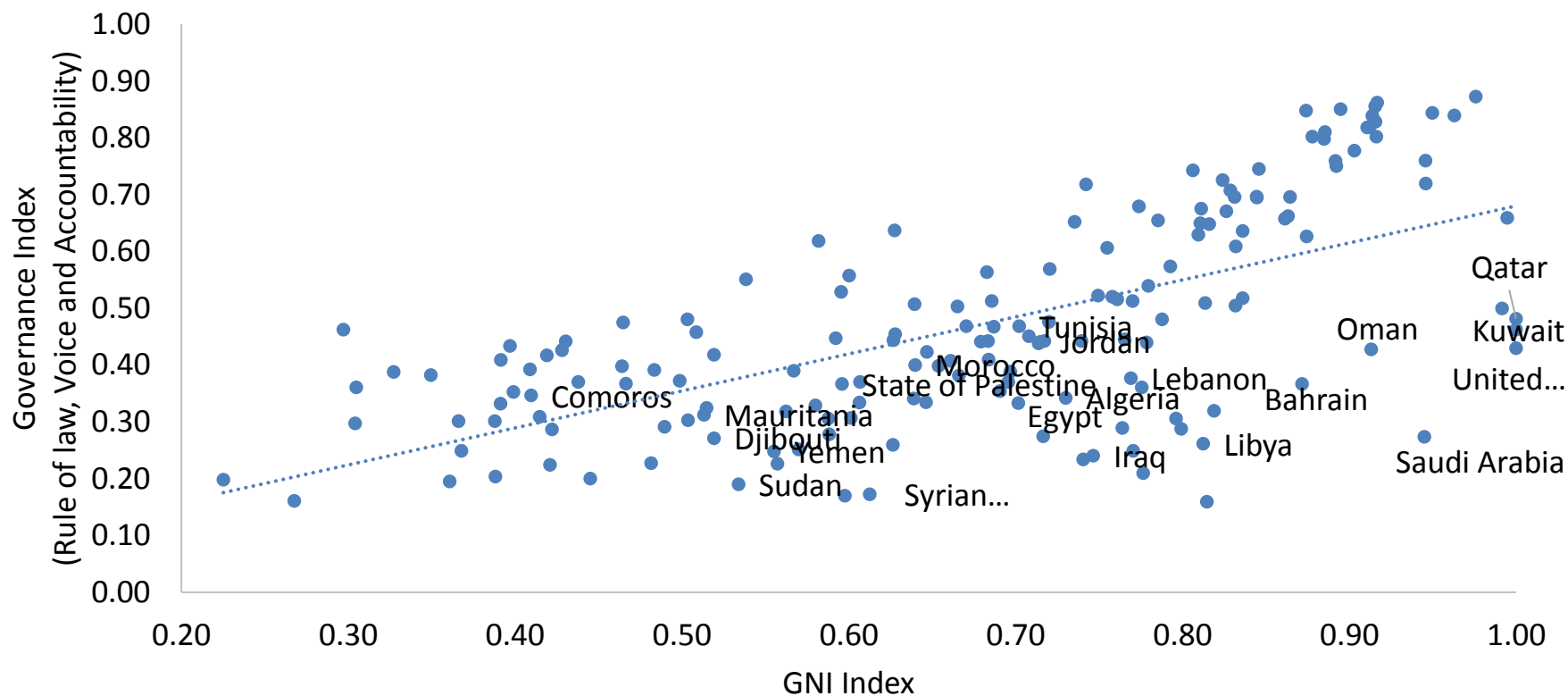
Taxation in oil-poor countries is predominantly on goods and services, imposing a greater burden on the poor and middle-class, exacerbating inequalities

**Composition of tax revenue (percentage share)**



Source: N. Sarangi (2016). Domestic Public Resources in the Arab Region: Where Do We Stand?. ESCWA Working Paper. E/ESCWA/EDID/2017/WP.1.

Finally, these fiscal policy changes will have limited effect in the absence of stronger institutions and political stability, which (many believe) are created and determined by voice and accountability and rule of law



Note: Data pertain to year 2013

Source: K. Abu-Ismaïl, A. Kuncic and N. Sarangi (2016), based on data from Worldwide Governance Indicators and World Development Indicators

# Thank you

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