

## STRUCTURAL IMPEDIMENTS TO ECONOMIC GLOBALIZATION IN THE MIDDLE EAST

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There has been a basic tension between the stated objectives of Middle Eastern leaders to integrate their countries into the world economy, on the one hand, and the actual, tangible levels of this integration, on the other. Consequently, the non-democratic states of the Middle East have consistently lagged behind in such globalization indices as foreign direct investment (FDI), competitiveness, market growth and integration into international markets. Broadly, there are indigenous as well as exogenous factors responsible for the limited nature of economic globalization in the Middle East. While a number of recent studies have examined the outside factors prompting international investors to be leery of these states, the internal barriers to globalization have remained largely unexplored.<sup>1</sup> This article analyzes these internal impediments, arguing that the pervasiveness of authoritarian practices and political structures in the Middle East and North Africa significantly undermines prospects for greater levels of international economic integration.

These indigenous barriers to globalization, the article argues, go to the very heart of the political economy of the authoritarian holdouts in the Middle East. Most studies of globalization in the Middle East have, often accurately, linked the region's comparatively low levels of global economic integration to any combination of insufficiently developed local markets, an underdeveloped or non-existent local labor force (as in the small monarchies of the Persian Gulf), inadequate and inaccessible information technologies, and "moralizing" or other defensive reactions by local leaders to the perceived sociocultural and political threats of globalization.<sup>2</sup> In general terms, each of these causes can and often does indeed serve as a real impediment to higher levels of globalization in the Middle East. Nevertheless, this article introduces a slightly different conceptualization of these impediments. More specifically, the article argues that the main impediments to greater integration into the global economy on the part of non-democratic Middle Eastern states lie in three structurally related phenomena: the "ruling bargains"

that underlie these authoritarian systems, the resulting state trade policies, and the phenomenon of economic semiformality.

Authoritarian ruling bargains serve to severely curtail the potential for greater integration into the world economy. While the specific dynamics of these bargains often vary, in broad terms they feature provisions whereby the state provides for the needs of politically relevant social classes in return for their political quiescence in the face of lack of political accountability and representation. Besides manifold political consequences, there are two primary, and interrelated, economic side-effects resulting from authoritarian ruling bargains: *étatisme* and economic nationalism. Both, the article argues, serve as obstacles to greater integration into the global economy.

Directly related to the political economy of authoritarianism are state trade policies. Guided by the logic of authoritarianism, state trade policies in the Middle East have been highly focused on specific types of commercial interaction that are often quite narrow in range and, more important, do not easily foster a deepening of the domestic market or the creation of additional commercial links internationally. Therefore, instead of serving as the principal vehicle for greater economic participation globally, international trade policy has been pursued by most Middle Eastern states in a way that has hindered the integration of their economies into global markets.

Another prominent feature of Middle Eastern economies, as well as those in much of the developing world, is a highly pervasive and financially significant “semiformal” sector. Interestingly, this same semiformal sector holds equal or

even greater sway in those parts of the developing world that have higher levels of globalization as compared to the Middle East. By itself, economic semiformality is not a determinant of levels of global integration. But it does become a crucial element when placed in the larger context of Middle Eastern political economies.

Before exploring each of these structural impediments in greater detail, some conceptual clarifications are in order, beginning with the very region of the Middle East itself. The Middle East, of course, is far from monolithic and includes countries as diverse as Iran and Israel, Saudi Arabia and Turkey, and Bahrain and Morocco. Even the non-democratic states of the Middle East that are the focus of this article often differ profoundly regarding their politics and institutions. Nevertheless, in their political economies – macro- and micro-economic policies, trade practices and even patterns of political rule – they share significant similarities that warrant comparative analysis. The primary focus of analysis here is that group of countries from Iran in the east to Morocco in the west. I omit Turkey and Israel, whose ostensibly democratic polities and higher comparative levels of global economic interaction merit separate analysis.<sup>3</sup>

Equally important is the concept of “economic globalization” employed here.<sup>4</sup> In this article it has been interpreted in a narrow economic sense, referring to the levels of international trade and foreign direct investment involving the authoritarian states of the Middle East.

## THE MIDDLE EAST AND THE GLOBAL ECONOMY

It goes without saying that the Middle East region has economies with different

capacities and levels of performance. The gross national income per capita can range from about \$4,000 to \$8,500 in Lebanon and Saudi Arabia, respectively, classified as “upper middle income” by the World Bank, to approximately \$1,500 in “lower middle income” countries such as Algeria (\$1,720), Egypt (\$1,470), Iran (\$1,720), Morocco (\$1,170), and Tunisia (\$1,990). There are also a number of “high income” countries, most notably Bahrain (\$10,500) and Israel (\$16,020).<sup>5</sup> Moreover, there are concomitant variations in population (ranging from 698,000 in Bahrain to 65.5 million in Iran), gross domestic product and its annual growth, government revenues, and the availability of technology and infrastructure.

Taken as a whole, however, the Middle East and North Africa (MENA) has had consistently low shares of the world’s overall trade, technology exports and foreign direct investment (Table 1). Of total merchandise exports from the developing world, those from MENA account for only 8 percent, and only 16 percent of that is manufactured goods.<sup>6</sup> The percentage of FDI in developing countries going to the Middle East is even lower, 2.7 percent, well below that of Sub-Saharan Africa and South Asia, and far behind Latin America (44.77 percent) and East Asia and the

Pacific (54.8 percent).

Within MENA itself, a couple of countries have a disproportionately large share of high-technology exports and FDI (Table 2). For Israel, with its extensive and highly developed technological and infrastructural base, high-tech goods account for 20 percent of manufactured exports, compared to only 4 percent in Jordan, 2 percent in Turkey and Tunisia, and 1 percent in Algeria. Beginning in the late 1980s and the early 1990s, a number of MENA countries launched aggressive plans to attract FDI, and Egypt, Tunisia, Turkey and, to a lesser extent, Morocco have met with notable successes in this area. Egypt, for example, receives more than 21 percent of all FDI going to the Middle East, with Tunisia receiving another 12.9 percent. These FDI-recipient success stories tend to be the exception rather than the rule, however, and countries such as Algeria, Iran, Iraq, Lebanon and Syria – all ravaged by intense domestic or international conflicts – and even the oil monarchies of the Persian Gulf, have some distance to go in attracting foreign or even domestic investors.

As these figures indicate, when compared to the countries of East Asia and Latin America and the Caribbean, MENA countries have been very slow to integrate

**Table 1. Selected Trade and Finance Indicators in the Developing World, 2002**

	World	East Asia & Pacific	Latin America & Caribbean	Middle East & North Africa	South Asia	Subsaharan Africa
High-technology exports (% of manufactured exports)	21.4	31.9	15.5	2.0	4.0	---
Foreign Direct Investment (billion US\$)	630.8	54.8	44.7	2.7	4.2	7.8

Source: World Bank, *World Development Indicators, 2004* (World Bank, 2004).

**Table 2. Trade Indicators in Selected Middle Eastern Countries, 1998**

	Algeria	Egypt	Iran	Israel	Jordan	Lebanon	Morocco	Saudi Arabia	Syria	unisia	Turke
Trade as share of PPP GDP (%)	16.4	10.2	8.40	47.7	34.1	5.2	18.1	31.9	14.6	27.0	18.8
High-technology exports (% of manufactured exports)	('97) 1.0	0	---	20.0	('97) 4.0	---	('97) 0	---	---	2.0	2.0
Foreign Direct Investment (% of total for MENA)	0.1	21.3	0.47	---	6.1	3.9	6.4	---	1.6	12.9	---

Source: World Bank, *World Development Indicators, 2000* (Oxford University Press, 2000).

into the world economy, particularly in respect to attracting FDI or being able to engage in the export of manufactured goods.<sup>7</sup> The examples of Israel and Egypt demonstrate that not all countries integrate at the same rate, with MENA once again having a high proportion of “weak” and “slow” integrators (Table 3). Nearly 67 percent of the countries in East Asia are considered “fast integrators,” as are 23 percent of those in Latin America and the Caribbean. But only 15 percent of MENA countries can be classified as such. By contrast, the percentage of MENA countries that are “slow integrators,” 38.4

percent, is only marginally lower than similar ones in Sub-Saharan Africa (39 percent), but significantly higher than those in Latin America and the Caribbean. Intra-regional trade among MENA’s Arab countries has not been substantial either, accounting for only about 5 percent of their total trade volume.<sup>8</sup>

The integration attempts of developing countries are often hampered by a variety of “external” factors, the most notable of which are limited access to foreign markets, limited private and official capital inflows, fluctuations in interest rates on external debt, declines in primary commod-

**Table 3. Speed of Integration of Developing Countries, Early '80s to Early '90s**

	East Asia		South Asia		Latin America & Caribbean		Middle East & N. Africa		Subsaharan Africa		Europe & Central Asia	
	#	%	#	%	#	%	#	%	#	%	#	%
Fast integrators	6	66.7	3	60	5	23.0	2	15.4	2	5.4	5	55.6
Moderate integrators	---	---	2	40	5	23.0	4	30.8	10	12.8	2	22.2
Weak integrators	3	33.3	---	---	9	42.0	2	15.4	10	27.8	---	---
Slow integrators	---	---	---	---	2	9.5	5	38.4	14	39.0	2	22.2
<b>Total</b>	<b>9</b>	<b>100.0</b>	<b>5</b>	<b>100</b>	<b>21</b>	<b>97.5</b>	<b>13</b>	<b>100.0</b>	<b>36</b>	<b>100.0</b>	<b>9</b>	<b>100.0</b>

Source: World Trade Organization, *Participation of Developing Countries in World Trade*, p. 8.

ity prices, and cyclical changes in industrial-country demand for exports.<sup>9</sup> In specific relation to MENA countries, perceptions of the region as the dividing line of “clashing civilizations,” problems of political consensus and governability, and lack of competitiveness and human and capital resources are also important in keeping external integrative initiatives, such as foreign investments and trade, in check.<sup>10</sup>

Important as these may be, they only tell half the story, for there are even more fundamental dynamics at work within the political economy of the countries involved that undermine the prospects of globalization. This is especially the case in a majority of MENA countries, where the political economy has been specifically designed to prop up inherently fragile states and placate potentially rebellious societies, thus giving rise to a particular political formula – an unspoken *modus vivendi* between the state and society – whose alteration entails considerable risk for political leaders. At best, the dominant political economy, having been nurtured and enforced for generations, may be dismantled only slowly and with fear.

### THE RULING BARGAIN

One of the more significant impediments to the global economic integration of MENA countries is rooted in the larger nature of the region’s political economy. As mentioned earlier, two specific factors stand out in this respect: a still-resonant sense of economic nationalism among both policy makers and some of the elite literati, and the pervasiveness of corporatist, patron-client ties as supported by economic rents handed out by the state.

With the exception of Israel, post-

World War II MENA economies have embodied three organically linked, reinforcing features: corporatism, clientalism and rentierism. While rentierism financed the state, corporatism and clientalism tied various social classes to it. Over time, the political significance and clout of certain social classes grew compared to others – most notably the professional urban middle classes. In family monarchies, state largess resulted in the dependence on the ruling clans of wealthy merchants, industrialists, professionals and the aspiring middle classes.<sup>11</sup> These oil monarchies feature especially strong commercial, familial and institutional links between members of the ruling family, on the one hand, and wealthy merchant families, on the other.<sup>12</sup> In “presidential monarchies” – most notably Algeria, Tunisia, Egypt and Syria, as well as Turkey – labor was added to these dependent social groups, which was incorporated through a variety of official union organizations (e.g. Türk-İs in Turkey, the General Confederation of Tunisian Workers in Tunisia, the Egyptian Trade Union Federation and the like).<sup>13</sup> Corporatism, in one form or another, became the primary means through which the states of North Africa and the Middle East controlled the politically relevant social classes.<sup>14</sup>

Underlying corporatism in MENA have been the dual forces of rentierism and patron-client relations. Beginning in the 1960s and especially the early 1970s, virtually all MENA states embarked on aggressive rent-seeking initiatives of one form or another in order to strengthen their ties with various social classes, their clients.<sup>15</sup> In order to ensure the active participation of the urban middle classes in maintaining the political status quo, or at

least their passive compliance, the state has often engaged in rent-seeking activities and pumped the proceeds into the urban economy.<sup>16</sup> With varying degrees of success, depending on the larger context within which rent-seeking occurred and corporatist and patron-client relations were forged, a self-perpetuating, implicit understanding emerged between a politically and economically omnipresent state, on the one hand, and a deepening, increasingly dependent pool of

societal clients, on the other.<sup>17</sup>

These clients of the state were primarily composed of urban-based labor groups and unions, industrialists and civil servants and other public employees (bureaucrats, teachers, physicians working in

state-run hospitals, etc.). Stated simply, the essence of this ruling bargain was one of state provision of social goods and services through renting out access to natural resources (often hydrocarbon resources or, for those not endowed with oil, migrant labor) in return for general societal acquiescence to non-accountable, undemocratic government.<sup>18</sup>

By the early to mid-1980s, however, drastic shortfalls in oil revenues, compounded by mismanagement and corruption, threw established methods of rent-seeking and the supporting corporatist system of patron-client bonds into serious

crisis.<sup>19</sup> Oil output fell from a high of 31 million barrels per day in 1979 to 18 million in 1982, while the price fell by 50 percent. Reluctant to revise the political bargains that had served them so well in the 1960s and the early 1970s, MENA leaders initially borrowed heavily internationally, owing \$80 billion by 1985 and \$144 billion by the end of 1986, an increase of 21 percent in two years.<sup>20</sup> But, before long, the need for new survival strategies could no longer be

masked by borrowing, and entrenched corporatist arrangements had to be altered accordingly. In one form or another, MENA states responded by introducing austerity measures, on the one hand, and liberalizing their economies – again, of course, to vastly

differing degrees – on the other.<sup>21</sup> In confronting the crisis of rentierism, a vast majority of MENA states changed their *modus operandi* only slightly and silenced their opponents with heightened repression and reinvigorated authoritarianism. Only a handful – notably Iran and Morocco, and to a much lesser extent Jordan and Kuwait – instituted certain (mostly cosmetic) political reforms aimed at placating potential opponents.

The late 1990s and the early years of the new decade only brought new economic and political challenges for MENA states, threatening some to their very core.

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Declining standards of living and deepening cracks in ruling bargains fostered the desertion from the bargain of increasingly frustrated urban classes, particularly those in the lower and the middle strata, many of whom found comfort and shelter in extremist groups and ideologies. Deepening political tensions were met by heightened levels of political repression, the main protagonists being the state security forces on the one side, and the growing pool of disenchanting and disillusioned urban youth on the other. Nevertheless, the steady polarization of the body politic in non-democratic MENA states throughout the 1990s – especially in, though not exclusive to, Algeria, Tunisia, Egypt, Libya, Syria and Saudi Arabia – did not breach the ruling bargains. So far, even the U.S. invasion and occupation of Iraq following the 9/11 tragedy and the ensuing American “war on terrorism,” while seriously straining these bargains, have not brought them down.

The primary reason for this reliance appears to lie in the very manner in which these ruling bargains were constituted and have evolved. Although repression has been part of the political equation, particularly in recent years, clientelistic ties between the state and the politically relevant classes have steadily become an integral part of the political economy. This is a product of the processes of state-building in almost all of the Middle East and North Africa. As David Waldner has demonstrated, state-building in Turkey, Syria and almost all other parts of MENA occurred in the context of intense competition among the elites and the resulting mobilization and incorporation of popular groups by the different elite factions.<sup>22</sup> Gradually, the bonds that tied state elites to their client classes became unbreakable, in

essence making the former hostage to the latter. Thus corporatism and patron-client networks became an integral, indeed essential, feature of the political system. Today, some in the popular classes may no longer find any utility or hope in their continued incorporation into the state and may choose to abandon it or, as is often the case, to turn against it altogether. The state, however, is hardly in a similar position; it cannot totally abandon the groups on whose incorporation and supposed political acquiescence it relies. Of course, as any patron worth his salt would do, on occasion, the state metes out heavy punishment against wayward clients. In any event, the ruling bargain cannot be dismantled, nor can its linchpin of clientelism and patronage be abandoned.

For the state, therefore, maintaining the status quo in recent years has meant generating financial and economic creativity (especially in the form of World Bank loans and grants), tightening up the corporatist links between the state and its societal allies, and resorting to repression to remind opponents of the consequences of nonconformity.<sup>23</sup> To satisfy international creditors, a number of states also embarked on a highly selective privatization campaign, conspicuously absent from which have been most heavy industries, banks, insurance companies, the oil and phosphate sectors, airlines, railways and the like.<sup>24</sup>

The upshot of all this has been a gradual and reluctant recalibration, but not dismantling, of the rentier economy, tilting it ever so slightly in an international direction. This international focus has been driven by the need for investments to fill the void left by the retreating state. Limited domestic capital and the move toward greater

technological modernization have reinforced the appeal of international investors as well as inflows from banks and official creditors. Ironically, however, the very selective structural adjustments that have taken place have only strengthened the state by bringing it new sources of rent. Three North African examples illustrate the point. From 1990 to 1997, some \$5 billion in FDI went to the Egyptian state; Tunisia raised \$1 billion through international bonds between 1992 and 1997; and Morocco received \$3.7 billion in FDIs from 1990 to 1997 and another \$680 million from portfolio investments.<sup>25</sup>

The ruling bargain continues to be perpetuated, albeit with slightly new trappings. The old corporatist systems of patronage and clientelism have been maintained also, although, out of necessity, they have had to be adjusted. Instead of needing patrons to get domestic goods or services, or promotions within the bureaucracy, now more and more clients search for public and private patrons who would facilitate the next import-export license, act as liaison with foreign companies, or speed up customs clearance. However, the old network of clientelistic ties and support mechanisms – and with it the rentier economy that underpins the whole system – are too pervasive and entrenched to be easily sidestepped and made obsolete, resisting even a marginal degree of reorientation. After all, what is at stake is the very basis of the dominant political economy, the essence of political rule.

Rentierism, then, helps maintain corporatist systems of patronage and clientelism. Economic liberalization and the sudden discovery by the state of the benefits of globalization have forced both patrons and clients to adjust accordingly.

But articulating new state policies is easier than changing the modus operandi of the system, and patron-client ties have been slow to adjust themselves to an internationally more integrated environment. They have, in fact, undermined globalization.

As the brief arguments above have indicated, political economy in the Middle East has been much more political than economic. Corporatism, clientelism and rentierism – and for “progressive” regimes, populism – all have combined to dramatically augment the apparatus and functions of the state in the Middle East.<sup>26</sup> As Chaudhry has convincingly argued, the étatism of the 1950s to the 1970s blunted the emergence of a functioning market economy in the late-developing countries of MENA and elsewhere.<sup>27</sup> One of the legacies of this era has been the emergence of public dependence on government services.<sup>28</sup> At the same time, the private sector is structurally and politically fragmented and remains largely dependent on the state.<sup>29</sup> Moreover, the economic, financial, infrastructural and legal necessities for the emergence of a market remain mired in official indecisiveness, red tape and insufficient resources. Banks, whether private or state-owned, enjoy little monetary and financial autonomy and, despite promises of reform, often remain instruments of state policy and, ultimately, part of its patronage machinery.<sup>30</sup> Within this context, private enterprises also assume an ad hoc nature and often operate informally or, at best, semiformally.<sup>31</sup>

Despite the absence of widely accepted market rules and procedures and a general lack of financial and other institutions necessary for the successful operation of markets, since the 1980s, lesser-developed countries have been hurriedly

implementing programs of economic liberalization. However, as the cases of Saudi Arabia and Iraq suggest, after two decades of neoliberal reforms, it is still not clear how much of a functioning national market has emerged in these and in most other countries of MENA.<sup>32</sup> Similar problems are being encountered most extensively in Iran, Algeria, Syria and Libya, where for ideological reasons the state has only recently assented to the project of liberalization.<sup>33</sup>

Two of the ensuing economic developments stand out. On the one hand, informal, or at best semiformal, institutions and procedures have proliferated among private industrialists and entrepreneurs, often in cooperative forms and set up by entrepreneurs themselves, intended to protect their interests in the absence of similar safeguards sanctioned by the state. The consequences for globalization of this informality in the economy will be elaborated below. More immediately, in the context of the present discussion, immature markets have kept domestic entrepreneurs busy at home, leaving them unprepared in terms of skills and resources (and also without sufficient connections) to break into the international market.

Compounding the difficulties involved in undoing the ruling bargain is the rise in the last couple of decades of Islamist opposition throughout the region, not only in such bastions of secularism as Algeria, Tunisia, Egypt and Syria, but also in Iran and Saudi Arabia, where the banner of Islam is supposed to be the very *raison d'être* of the state.<sup>34</sup> Islamist activism, from reformist to violent, is largely a product of the manifold failures of the regimes in power. These failures span the gamut from economic to political, ethical

and military. Although the ideological message of Islamists may be universal or perhaps regional, their frame of reference and the specific issues to which they address themselves are more immediate. Rhetoric aside, Islamists are essentially nationalists, outraged not only at the moral turpitude of their political leaders but also the plunder of the country's resources, the auctioning of positions and privileges to the well-connected, and, of course, their own marginalization and lack of access to portions of the ever-shrinking pie.<sup>35</sup> The secret tracts circulated in high schools and universities, the graffiti on the walls of narrow streets, the slogans whispered by disenchanted youths often portray national leaders as lackeys of the West, stooges if not of multinational corporations or the CIA, certainly of the International Monetary Fund. The so-called "bread riots" that wracked Morocco, Algeria, Jordan and Egypt in the late 1980s were all specifically sparked by reaction to the imposition of IMF-mandated austerity plans.<sup>36</sup> In Egypt, as a result, the officially tolerated Muslim Brotherhood has repeatedly called for a return to the statist economic policies of the Nasser era, which featured the promotion of "social justice" as one of their central principles.<sup>37</sup>

To this day, the depth of resentment against the IMF and the World Bank, not only among Islamists but among average individuals in the street, is quite palpable. Ironically, in the yesteryears of ideological politics, it was the state itself in places like Algeria, Egypt, Libya, Syria, Iraq and Iran that sang the praises of economic nationalism and the evils of foreign presence in the domestic economy.<sup>38</sup> Today, faced with the necessities of divestment, its own ideological ghosts are coming back to haunt it. As

the mostly failed economic adjustment policies of Algeria,<sup>39</sup> Saudi Arabia, Saddam Hussein's Iraq,<sup>40</sup> and Iran<sup>41</sup> demonstrate, when MENA leaders are faced with tough choices in political economy, they often favor the political over the economic.

### STATE TRADE POLICIES

A related impediment to greater international economic integration is the particular set of policies being pursued by the various states of North Africa and the Middle East. In the absence of well-developed domestic markets and because of the lingering legacy of the étatism of the 1950s and the 1960s, much of the international trade in MENA has been conducted by and through the state. Despite significant increases in the volume of this trade in the last three decades or so, the state policies guiding it have been inimical to a deepening of integration into the world market. Developing countries generally have a difficult time integrating into the world economy if they do not already participate in WTO trade policies, have their exports concentrated in a limited number of goods, pursue inflationary macroeconomic policies, or suffer from real exchange-rate volatility.<sup>42</sup> As this section demonstrates, all MENA economies feature two or more of these characteristics.

Export concentration, protectionist barriers and international indebtedness are some of the most common consequences of bungled implementations of the import-substitution industrialization (ISI) strategy of development, a strategy that by the 1960s all MENA states had adopted. In order to protect new imported industries, the state kept the exchange rate artificially high and erected major trade barriers to keep out competing, often cheaper and

better, foreign goods.<sup>43</sup> For those with significant oil resources, financing the importation of industry was made possible through oil exports. Others, like Turkey, Jordan, Egypt and Morocco, borrowed heavily. But, after the "bust" of the late 1970s, even the oil economies had to resort to massive international borrowing in order to maintain ISI policies, thus keeping overpriced consumer goods available for the consumption of the middle classes. In addition to accumulating international debt, ISI prompted MENA leaders, like those elsewhere pursuing the same policy, to import industries with an eye to keeping the middle classes happy. This has often led to a concentration of imports in specific industries (automobiles or household appliances, for example), tying up available revenues that could otherwise be used to diversify the domestic economy and international trade.

Despite the glaring shortcomings of ISI, few MENA states have abandoned or significantly altered their pursuit and implementation of it. Nonaccountable states, after all, often persist in their economic mistakes.<sup>44</sup> Only begrudgingly have some of them finally recognized their failure and begun to diversify. Nevertheless, only Israel and Turkey appear to have made significant headway in adopting export-led strategies of growth.<sup>45</sup>

The original intent of ISI was to expand the domestic industrial base and, once internationally competitive, export the manufactured goods to international markets. But ISI never successfully matured in MENA in the same way that it did in Taiwan and South Korea, for a variety of reasons failing to move beyond its early "import" phase. In the meantime, to keep the strategy going in order to

**Table 4. Percentage of Exports of Manufactures by Region, 2002**

Western Europe	40.0
Asia	26.4
North America	16.9
Latin America	5.8
C./E. Europe, Baltic States, CIS	4.3
Middle East	4.3
Africa	2.3

Source: World Trade Organization, *International Trade Statistics, 2003* (World Trade Organization, 2004), p. 39.

satisfy domestic demand, foreign revenues and, therefore, continued reliance on the export of primary goods, have been required. And, despite attempts to the contrary, export diversification has largely been a failure.<sup>46</sup> As Table 4 demonstrates, MENA countries account for less than one percent of the world's trade in manufactured goods, again limiting the scope and markets for their international trade.

Equally detrimental to further integration into the global economy is the relentless pursuit of military purchases by all MENA states. Throughout the Middle East, the armed forces have played an indispensable role in the process of state-building, and they still remain powerful institutions decades after these states have made the transition to civilian rule.<sup>47</sup> In fact, many MENA militaries have carved out separate, powerful economic enclaves, controlling their own productive assets and financial institutions, and negotiating their own foreign and domestic loans and

contracts.<sup>48</sup> The region's history of wars and repeated military coups has only enhanced the entrenched interests of the military establishment. In the 1980s and 1990s, MENA countries spent an estimated \$600 billion on arms purchases.<sup>49</sup> From 1971 to 1994, on average, MENA governments spent an astounding 22.3 percent of their total expenditure on the military. That figure exceeded 40 percent for Syria, Oman and the United Arab Emirates, and 30 percent for Israel, Jordan, Kuwait, Saudi Arabia and Yemen (Table 5).

There is little consensus over whether high levels of military spending are harmful or beneficial to overall economic development.<sup>50</sup> But as far as globalization is concerned, the negative consequences of excessive military expenditure cannot be disputed. Although the purchase of arms and equipment may constitute a sizable portion of a country's international trade, it is a highly specialized, narrow form of trade that does little or nothing to integrate the various sectors of the domestic economy into international markets. International arms manufacturers, often with the permission of their governments, sell their hardware directly to MENA states. Whatever residual consequences that are spawned from the trade (e.g. infrastructural development, local training centers and schools) are domestically focused and have little or no interaction with the world economy at large. Moreover, this is a one-way form of trade, almost exclusively in the form of imports and, apart from some light-arms manufacturing in Egypt and Iran, mainly for internal use. There is really no arms manufacturing for export.

Lastly, less than half of all MENA states have joined the World Trade Organi-

zation, membership in which opens up domestic markets to outside investors and, theoretically at least, facilitates access to international markets.<sup>51</sup> WTO membership requirements – removing domestic subsidies, liberalizing trade regimes, making commitments in areas of services and intellectual property rights, among others – necessitate a steady dismantling of patronage and rent-seeking mechanisms. As discussed earlier, most MENA states are reluctant to risk implementing such systemic adjustments even if the benefits include more favorable treatment from the IMF and increased international prestige. The political costs outweigh the benefits. Not surprisingly, even the MENA states that have recently become WTO members, such as Morocco, Egypt and Jordan, still have some distance to go in satisfying the organization's rigid open-trade and non-protectionist requirements. Once again, however, Israel and Turkey have gone the furthest in implementing WTO dictates.<sup>52</sup>

#### SEMIFORMALITY AND THE PARALLEL ECONOMY

One of the more significant consequences of the stunted evolution of markets and the partial and incomplete retreat of the state from the economy has been the emergence of a vibrant parallel economy throughout the Middle East and North Africa.<sup>53</sup> MENA is not unique in this respect; virtually all developing countries have a sizable informal sector whose economic activities and capital fall outside of the regulatory purview of the state.<sup>54</sup> In both MENA and elsewhere, the distinction between the formal and informal sectors is not always clear cut, there being a considerable portion of the economically active population whose designation comes closer

to “semiformal.” The economic activities of this sector straddle institutional formality

**Table 5. Military Spending as Percent of Total Government Expenditure, 1971-94**

	971-94	199
lgeria	.5	12.
ahrain	0.2	18.
gypt	0.2	('97) 9.
ran	5.0	11.
raq	6.0	N/
srael	1.8	18.
ordan	2.0	27.
uwait	5.0	20.
ebanon	5.8	11.
ibya	.8	('95) 19.
orocco	5.6	13.
man	2.0	36.
atar	3.8	22.
audi Arabia	5.8	43.
udan	6.0	46.
yria	0.8	25.
unisia	.6	5.
urkey	9.8	13.
AE	0.3	39.
emen (North '71-'89)	0.9	18.
<b>otal average</b>	<b>2.3</b>	<b>21.</b>

Source: Data collected from U.S.-Arms Control and Disarmament Agency, *World Military Expenditures and Arms Transfers, 1971-1980, 1988, 1995, 1999-2000* (U.S. Government Printing Office, 1983, 1989, 1996, 2002).

and informality. Most often, these are entrepreneurs who operate out of established shops and other officially recognized business establishments (i.e., they have the necessary permits and licenses from the appropriate state agencies), but they abide by few if any of the laws and regulations of the state, including paying taxes. In essence, they appear to belong to the formal sector, but they operate largely as the informal sector does. At best, they only partially observe official procedures and regulations.

In the last couple of decades, especially since the liberalization campaigns of the 1980s, a growing number of semiformal entrepreneurs have expanded their economic activities abroad. This was particularly the case in a number of North African countries, especially Morocco and Egypt, whose migrant laborers abroad started using informal money changers in preference to banks to send home their remittances. For the Moroccan government, the problem was one of illegal immigration of its workers into European countries, notably France and Spain, and their use of personal connections in sending money back. In Egypt, semiformality manifested itself in a more institutionalized manner. Beginning in the 1980s, a number of investment companies emerged that, sometimes out of conviction and sometimes out of prudence, labeled themselves "Islamic." Gradually, these Islamic investment companies became one of the major venues through which Egyptians abroad sent home their remittances.<sup>55</sup> Being one of the country's major sources of foreign exchange – along with tourism and Suez Canal fees – the extensive network of unofficial Islamic financial institutions cut deeply into the state's potential revenues.

Although the Egyptian state subsequently cracked down on these and other similar companies, its authority over and knowledge of remittances is still far from certain. The collapse of the Soviet Union and the stalled nature of CIS economies has led to the emergence of a similar "suitcase" economy in Turkey, in which citizens from both sides of the Black Sea sell to each other's markets in trips that may last only a day or even a few hours.

Semiformality does not directly impede globalization per se. By circumventing the bureaucracy and its countless and at times arbitrary rules and procedures, semiformal entrepreneurs can conduct their business faster and, most probably, more profitably. But they also undermine standardization, the institutionalization of international trade, and the increasing equalization of tariffs. The transnational and informal nature of the trade also makes it difficult for governments to stop, regulate or, at times, even to get a handle on it. "International" as this trade may be, it is not what the proponents of economic globalization had hoped.

## CONCLUSION

Despite the excitement with which the international academic and economic policy communities have embraced globalization, data indicate that South Asia, Subsaharan Africa and the Middle East and North Africa have so far played marginal roles in the process. This article has highlighted three main domestic structural impediments to the greater integration of MENA into the world economy, especially insofar as FDI and the export of manufactured goods are concerned. Perhaps the most prominent is the larger nature of the region's political economy, more specifically the reluctance of state leaders to discard the ruling

bargains that have so far maintained them in office. The hallmarks of this ruling bargain have been rent-seeking, corporatism and patron-client relations, which, both in combination and on their own, have hampered the development of domestic markets and their expansion abroad. Semiformality and parallel economies also undermine the state's ability to regulate international financial transactions and impose standards and institutions for foreign trade. Equally important are the policy preferences of state leaders, who in MENA are reluctant, despite obvious economic failures, to abandon import-substitution industrialization strategies that are ultimately inflationary, protectionist and stagnant.

What the future holds for MENA's globalization prospects is far from certain. If one is to believe optimistic predictions by policy makers and academics, greater economic integration with the outside world is imminent. Certainly, the prediction goes, the initial indicators for intraregional integration are quite positive.<sup>56</sup> My own assessment of these prospects is tempered by the belief that meaningful integration into the world economy would be exceedingly difficult, given the region's present overall political economy. With the exception of Turkey and Israel, states in the Middle East and North Africa do not have the popular legitimacy and electoral mandates to be able to undertake significant structural adjustments to their political systems and their economies. Turkey and Israel have taken the largest strides toward globalization because of their uniqueness in

relation to the rest of the Middle East. Ostensibly democratic polities in Turkey and Israel, its limits in Turkey notwithstanding, have led to a dismantling of state patronage networks, in turn facilitating and indeed necessitating economic liberalization. Economic liberalization has brought with it greater integration into the international economy.

The relationship between political liberalization and globalization in the Middle East confirms the empirical and theoretical conclusions that Haggard and Kaufman drew in relation to other parts of the developing world.<sup>57</sup> As the preceding analysis of MENA political economies has demonstrated, economic liberalization is exceedingly difficult if not impossible without political liberalization. Partial or cosmetic political liberalization, designed to further a regime's survival rather than to reform it, results in equally distorted economic liberalization and integration into the international economy. In fact, desperate measures aimed at finding new sources of rent can deepen dependence on international suppliers, thereby heightening popular resentment to the perceived negatives of globalization. For the time being, even limited experiments with political liberalization have been halted or reversed in most parts of the Middle East and North Africa.

The region's many unelected leaders do not have the political wherewithal to make tough economic decisions. For the foreseeable future, the prospects of economic globalization in the Middle East and North Africa appear bleak.

<sup>1</sup> See, for example, Colin MacKinnon, "The Party's Over for Israel's Integration into the Middle East," *Washington Report on the Middle East*, January/February 1998, pp. 20-22; Miranda Beshara, "Globalization and the Middle East: Growing Together or Growing Apart?" *Middle East Institute Policy Brief* (Middle East Institute, 1999); and Cecilia Klein, Abdelali Jbili, Kevin R. Taecker, and Shafeeq Ghabra, "Joining the Global

Rules-Based Economy: Challenges and Opportunities for the GCC,” *Middle East Policy*, Vol. 7, No. 2, February 2000, pp. 1-19. An invaluable study that looks at Arab integration is Michael Hudson’s edited volume, *Middle East Dilemma: The Politics and Economics of Arab Integration* (Columbia University Press, 1999).

<sup>2</sup> Clement M. Henry and Robert Springborg, *Globalization and the Politics of Development in the Middle East* (Cambridge University Press, 2001).

<sup>3</sup> On the imperfect democracies of Turkey and Israel, see Mehran Kamrava, “Military Professionalization and Civil-Military Relations in the Middle East,” *Political Science Quarterly*, Vol. 115, No. 1, Spring 2000, pp. 67-92. On their differential rates of integration into the world economy as compared to the rest of the Middle East, see Springborg and Henry, *Globalization in the Middle East*, pp. 202-12.

<sup>4</sup> For various definitions of globalization, see Jan Aart Scholte, *Globalization: A Critical Introduction* (St. Martin’s, 2000), pp. 14-17.

<sup>5</sup> Data compiled from World Bank, *World Development Indicators, 2004* (Oxford University Press, 2000).

<sup>6</sup> World Bank, *World Development Report 1999/2000* (Oxford University Press, 2000), p. 269.

<sup>7</sup> See also Paul Sullivan, “Globalization: Trade and Investment in Egypt, Jordan, and Syria since 1980,” *Arab Studies Quarterly*, Vol. 21, No. 3, Summer 1999, pp. 35-73; and Enid Hill, “First World, Third World, Globalizing World: Where is the Middle East,” *Arab Studies Quarterly*, loc. cit., pp. 73-96.

<sup>8</sup> Kemal Dervis, Peter Boccock, and Julia Devlin, “Intraregional Trade among Arab Countries: Building a Competitive Economic Neighborhood,” Paper presented at the 52nd Middle East Institute annual conference, Washington, DC, October 17, 1998.

<sup>9</sup> World Trade Organization, *Participation of Developing Countries in World Trade: Overview of Major Trends and Underlying Factors* (Geneva: WTO, 1996), pp. 10-11.

<sup>10</sup> Beshara, “Globalization and the Middle East,” pp. 5-6.

<sup>11</sup> In the oil monarchies of the Arabian Peninsula, labor’s political significance has been muted by its expatriate nature and by tight government control and segregation. See Ian Seccombe, “Immigrant Workers in an Emigrant Economy: An Examination of Replacement Migration in the Middle East,” *International Migration*, Vol. 24, No. 2, June 1986, pp. 377-89. These controls were significantly tightened after the Gulf War.

<sup>12</sup> Michael Field, *The Merchant: The Big Business Families of Saudi Arabia and the Gulf States* (Overlook Press, 1985).

<sup>13</sup> Alan Richards and John Waterbury, *A Political Economy of the Middle East*, 2nd ed. (Westview, 1996), pp. 316-17.

<sup>14</sup> For studies of corporatism in MENA, see, among others, Marsha Pripstein Posusney, *Labor and the State in Egypt: Workers, Unions, and Economic Restructuring* (Columbia University Press, 1997); Robert Bianchi, *Interest Groups and Political Development in Turkey* (Princeton University Press, 1984); and Robert Bianchi, “The Corporatization of the Egyptian Labor Movement,” *Middle East Journal*, Vol. 40, No. 3, Summer 1986, pp. 429-44.

<sup>15</sup> Chaudhry rejects the argument that the state deliberately seeks to foster clientalism and patronage, instead maintaining that social outcomes can be best explained by examining “the interaction of laissez-faire distributive imperatives undertaken for growth alone, the lack of economic information, and the preexisting composition of the bureaucracy.” Kiren Aziz Chaudhry, *The Price of Wealth: Economies and Institutions in the Middle East* (Cornell University Press, 1997), p. 191 (emphasis added). Nevertheless, the outcome, namely the acquiescence of important economically active sectors of the population to state authoritarianism, remains the same.

<sup>16</sup> There is a rich body of literature on the phenomenon of rentierism. A sample of this literature includes Rex Brynen, “Economic Crisis and Post-Rentier Democratization in the Arab World,” *Canadian Journal of Political Science*, Vol. 25, No. 1, March 1992, pp. 69-97; Barnett Rubin, “Political Elites in Afghanistan: Rentier State Building, Rentier State Wrecking,” *International Journal of Middle East Studies*, Vol. 24, No. 1, 1992, pp. 77-99; Hootan Shambayati, “The Rentier State, Interest Groups, and the Paradox of Autonomy: State and Business in Turkey and Iran,” *Comparative Politics*, Vol. 26, No. 3, (April 1994), pp. 307-31; and Eva Bellin, “The Politics of Profit in Tunisia: Utility of the Rentier Paradigm?” *World Development*, Vol. 22, No. 3, 1994, pp. 427-36. Briefly, a rentier state can be defined as one that “depends on external sources for a large portion of its revenues. These revenues from abroad are called rent. Rent is not the only income, but it certainly predominates. In the past, rentier states have been based on international trade in gold or bat guano. Today, the term refers most often to the oil states whose income is derived from the international sale of petroleum.” Gwenn Okruhlik, “Rentier Wealth, Unruly Law, and the Rise of Opposition: The Political

Economy of Oil States,” *Comparative Politics*, Vol. 31, No. 3, April 1999, p. 295.

<sup>17</sup> This take on rentierism is shared by most but not all students of the phenomenon. Okruhlik, for example, maintains that in Saudi Arabia “rent did not buy the support or loyalty of different social groups even during the boom as the uneven distribution of its proceeds led to resentment and opposition.” Okruhlik, “Rentier Wealth, Unruly Law, and the Rise of Opposition,” p. 297.

<sup>18</sup> Daniel Brumberg, “Authoritarian Legacies and Reform Strategies in the Arab World,” *Political Liberalization and Democratization in the Arab World. Volume 1, Theoretical Perspectives*, eds. Rex Brynen, Bahgat Korany, and Paul Noble (Lynne Rienner, 1995), p. 233.

<sup>19</sup> Although almost the rule, rent seeking in MENA has been a highly risky endeavor, especially lately, as the amount of revenue accrued from it from oil, labor and tourism has been volatile and unpredictable.

<sup>20</sup> Brumberg, “Authoritarian Legacies and Reform Strategies in the Arab World,” p. 239.

<sup>21</sup> For essays on the different liberalization experiences in MENA in the 1980s, see Iliya Harik and Denis Sullivan, eds, *Privatization and Liberalization in the Middle East* (Indiana University Press, 1992). See also, Henri Barkey, ed, *The Politics of Economic Reform in the Middle East* (St. Martin’s, 1992).

<sup>22</sup> David Waldner, *State Building and Late Development* (Cornell University Press, 1999), p. 28.

<sup>23</sup> As Okruhlik puts it, MENA states have opted for “system maintenance in the guise of liberalization from above . . . (hoping to) co-opt wider circles of the political public and direct political and religious organizations into acceptable and controllable channels.” Okruhlik, “Rentier Wealth, Unruly Law, and the Rise of Opposition,” p. 305.

<sup>24</sup> Bradford Dillman, “Global Markets and Democratization in North Africa,” Paper presented at the Twenty-Eighth World Congress of the International Political Science Association, August 1-5, 2000, Québec, Canada, p. 11.

<sup>25</sup> *Ibid.*, p. 9.

<sup>26</sup> Nazih Ayubi, *Over-Stating the Arab State: Politics and Society in the Middle East* (London: I.B. Tauris, 1999), p. 199.

<sup>27</sup> Kiren Aziz Chaudhry, “Economic Liberalization and the Lineages of the Rentier State,” *Comparative Politics*, Vol. 27, No. 1, October 1994, pp. 17-19.

<sup>28</sup> Monte Palmer, Ali Leila and El Sayed Yassin, *The Egyptian Bureaucracy* (The American University in Cairo Press, 1988), p. 30. This is by no means limited to the self-declared “progressive” states of the region (Iran, Iraq, Syria, Egypt, Libya and Algeria), but also includes the oil monarchies which, in fact, created very extensive and deeply entrenched welfare states. See Field, *The Merchant*, p. 58.

<sup>29</sup> Volker Perthes, “The Private Sector, Economic Liberalization, and the Prospects of Democratization: The Case of Syria and Some other Arab Countries,” Ghassan Salame, ed., *Democracy without Democrats? The Renewal of Politics in the Muslim World* (London: I.B. Tauris, 1994), p. 258.

<sup>30</sup> Clement M. Henry, “The Crisis of Money and Power: Transitions to Democracy?” *Islam, Democracy, and the State in North Africa*, ed. John Entelis, p. 181.

<sup>31</sup> In the words of a journalist, “in this very personal and ad hoc scheme of management, nobody tries to plan a company’s development, produce formal budgets or work out a system of departmental responsibilities. Companies evolve from month to month in response to the various opportunities and problems that arise and the amount of cash they have available.” Field, *The Merchant*, p. 294.

<sup>32</sup> *Ibid.*, pp. 20-1.

<sup>33</sup> See, for example, Meliha B. Altunisik, “A Rentier State’s Response to Oil Crisis: Economic Reform Policies in Libya,” *Arab Studies Quarterly*, Vol. 18, No. 4, Fall 1996, p. 56.

<sup>34</sup> See, for example, Hrair Dekmejian, “The Rise of Political Islamism in Saudi Arabia,” *Middle East Journal*, Vol. 48, No. 4, Autumn 1994, pp. 627-643; John Ruedy, ed., *Islamism and Secularism in North Africa* (St. Martin’s, 1994); and Youssef M. Choueiri, *Islamic Fundamentalism* (London: Pinter, 1997).

<sup>35</sup> Richards and Waterbury, *A Political Economy of the Middle East*, pp. 348-9.

<sup>36</sup> Timothy Piro, *The Political Economy of Market Reform in Jordan* (Rowman & Littlefield, 1998), p. 73; Susan Waltz, “The Politics of Human Rights in the Maghreb,” John Entelis, ed., *Islam, Democracy, and the State in North Africa* (Indiana University Press, 1997), pp. 81-3; Daniel Brumberg, “Survival Strategies vs. Democratic Bargains: The Politics of Economic Reform in Contemporary Egypt,” *The Politics of Economic Reform in the Middle East*, ed. Henri Barkey, pp. 84-5. For a detailed examination of IMF-mandated reforms in North Africa in the late 1980s and the early 1990s, see Henry, “The Crisis of Money and Power: Transitions to Democracy?” pp. 177-204.

- <sup>37</sup> Bjorn Olav Utvik, "Filling the Vacant Throne of Nasser: The Economic Discourse of Egypt's Islamist Opposition," *Arab Studies Quarterly*, Vol. 17, No. 4, Fall 1995, p. 29.
- <sup>38</sup> For a discussion of "the failure of ideology" in the Middle East, see Richards and Waterbury, *A Political Economy of the Middle East*, pp. 321-2.
- <sup>39</sup> Dirk Vandewalle, "Breaking with Socialism: Economic Liberalization and Privatization in Algeria," *Privatization and Liberalization in the Middle East*, eds. Iliya Harik and Denis Sullivan, pp. 192-3.
- <sup>40</sup> Kiren Aziz Chaudhry, "Economic Liberalization in Oil-Exporting Countries: Iraq and Saudi Arabia," *Privatization and Liberalization in the Middle East*, eds. Iliya Harik and Denis Sullivan, pp. 162-4.
- <sup>41</sup> Jahangir Amuzegar. "Khatami and the Iranian Economy at Mid-Term". *Middle East Journal*. Vol. 53, No. 4, (Autumn 1999), p. 540.
- <sup>42</sup> World Trade Organization, *Participation of Developing Countries in World Trade*, p. 2.
- <sup>43</sup> Richards and Waterbury, *A Political Economy of the Middle East*, pp. 26-7.
- <sup>44</sup> Alan Richards, "Economic Pressures for Accountable Governance in the Middle East and North Africa," *Civil Society in the Middle East*, ed. Augustus Richard Norton (Leiden: E.J. Brill, 1995), p. 74.
- <sup>45</sup> Richards and Waterbury, *A Political Economy of the Middle East*, pp. 28-9.
- <sup>46</sup> Sullivan, "Globalization: Trade and Investment in Egypt, Jordan and Syria since 1980," p. 39.
- <sup>47</sup> Mehran Kamrava, "Military Professionalization and Civil-Military Relations in the Middle East," pp. 67-92.
- <sup>48</sup> Richards and Waterbury, *A Political Economy of the Middle East*, p. 340.
- <sup>49</sup> Ahmad Hashim, "The State, Society, and the Evolution of Warfare in the Middle East: The Rise of Strategic Deterrence?" *The Washington Quarterly*, Vol. 18, No. 4, Autumn 1995, p. 53.
- <sup>50</sup> See, for example, Lisa Anderson, "Peace and Democracy in the Middle East: The Constraints of Soft Budgets," *Journal of International Affairs*, Vol. 49, No. 1, Summer 1995, pp. 25-44; Mikael Linden, "Military Expenditure, Government Size and Economic Growth in the Middle East in the Period 1973-85," *Journal of Peace Research*, Vol. 29, No. 3, 1992, pp. 265-70; and Francis Adeola, "Military Expenditures, Health, and Education: Bedfellows or Antagonists in Third World Development?" *Armed Forces and Society*, Vol. 22, No. 3, Spring 1996, pp. 441-67.
- <sup>51</sup> World Trade Organization, *Participation of Developing Countries in World Trade*, p. 11.
- <sup>52</sup> See the WTO's *Trade Policy Review* for Egypt (June 1999), Israel (September 1999), and Turkey (October 1998).
- <sup>53</sup> For more on parallel economy in MENA, see Rebecca Miles Doan, "Class Differentiation and the Informal Sector in Amman, Jordan," *International Journal of Middle East Studies*, Vol. 24, No. 1, February 1992, pp. 27-37; and Deborah Harrold, "The Menace and Appeal of Algeria's Parallel Economy," *Middle East Report*, January-February 1995, pp. 18-22.
- <sup>54</sup> In fact, in some of the urban areas of Ghana, Pakistan and Peru, the informal sector is estimated to form as much as 60 to 70 percent of the urban labor force. Michael Todaro, *Economic Development*, 6th ed (Addison Wesley, 1997), p. 270.
- <sup>55</sup> Henry, "Crisis of Money and Power," p. 196.
- <sup>56</sup> Dervis, Babcock and Devlin, "Intraregional Trade among Arab Countries."
- <sup>57</sup> Stephen Haggard and Robert Kaufman, *The Political Economy of Democratic Transitions* (Princeton University Press, 1995).