The Economic Consequences of the Political Instability in MENA Region

الآثار الاقتصادية لعدم الاستقرار السياسي في منطقة الشرق الأوسط وشمال أفريقيا(MENA)

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Abstract:

This paper focuses on studying and evaluating political instability and its implications for the economies of selected countries from the Middle East and North Africa region during the period 1996-2017 using World Development Indicators (WDI), the results of the study indicate that political stability is an important factor for economic performance. as The results of the analysis showed that the political stability index and the absence of violence have a significant impact on macroeconomic variables such as the variable unemployment, inflation and GDP growth of selected countries from the Middle East and North Africa region.

Keywords: Political instability; economic performance; Unemployment; inflation; MENA countries.

Jel Classification Codes: O11, O40.

ملخص:

تعنى هذه الورقة البحثية بدراسة وتقييم عدم الاستقرار السياسي وتداعياته على اقتصادات دول مختارة من منطقة الشرق الأوسط وشمال أفريقيا (*MENA*) خلال الفترة 1996-2017 ،باستخدام مؤشرات التنمية العالمية (*WDI*) ، تشير نتائج الدراسة أن الاستقرار السياسي عامل مهم للأداء الاقتصادي، كما بينت نتائج التحليل أن لمؤشر الاستقرار السياسي وغياب العنف تأثير كبير على متغيرات الاقتصاد الكلي والمتمثلة في متغير البطالة والتضخم ونمو الناتج المحلي الإجمالي لبلدان مختارة من منطقة الشرق الأوسط وشمال أفريقيا.

كلمات مفتاحية: عدم الاستقرار السياسي، الأداء الاقتصادي، البطالة، التضخم، دول الشرق الأوسط وشمال إفريقيا.

تصنيف **JEL :** O11، O40.

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1.INTRODUCTION:

Economic growth literature tries to explain the differences in growth path across countries, within a single country, and across decades. One of the suggested reasons for differences in economic growth is the political situation and the level of political instability. (Abdelkader, 2017)

Middle East and North Africa (MENA) countries, like Tunisia, Egypt, Libya, Yemen and Syria, suffered from low levels of democracy, which resulted in a high level of political instability (the Arab Wakening or Arab Spring, which occurred at the end of 2010 and the beginning of 2011) (Abdelkader Hossam, 2015), Where Political instability can have serious consequences on the economic performance. It affects the economy in that it increases uncertainty about future economic situations and policies. Political instability is linked with the likelihood of having demonstrations, strikes, forms of violence, crimes, coups, regimes reversals, and government collapse. Thus, political instability is associated with the concept of a “failed state”. It affects business and investment environments, as well as the decisions of producers, consumers, and of all stakeholders involved in the country's economy. It may represent a serious threat to economic performance and may hamper a country’s development. (Murad & Alshyab, 2019)

the World Bank's MENA Economic Monitor expects GDP growth in the region to remain flat at between 3.1% and 3.3% for 2015 and 2016. For the first time in four years, the region faces a fiscal deficit due to the prolonged conflict and political instability in some countries, low oil prices, and the slow pace of reforms. These factors are also contributing to low investment and high unemployment. (Devarajan & Mottaghi, 2015) In light of the above, we can raise the following problem: **What are the economic consequences of the political instability in Middle East and North Africa Region?**

The paper is articulated as follows: (Section1) provides an overview on previous studies on political instability and economic performance, while (Section 2) discusses the political instability in MENA Region. Then, some facts on political instability and Economic Performance of a selected sample from the

MENA Region will be presented (Section 3), concludes the paper.

2. Literature review

The connection between political instability and macroeconomic variables still remains in the center of the scholarly debates since it is one of the continuing relationships in the social and political economies. Furthermore, this type of correlation has been an issue of concern for a long time; because the empirical studies revealed different findings for different regions, different countries, and for different periods.

In the present, there have been abundant of paradoxical negotiations when multiple and sundry estimations related to the association between political indicators and economic variables have been predicted. Although the political risks consider as a key obstacle to economic activities, however, so many firms keep investing in instable countries environments, these forecasted results are divided between positive relationships; as proved by the discussion of Bueno about the instability; as the latter enhances the policy ideas competition, which will lead to efficient government policies implementation and will have an indirect positive impact on economic growth. Moreover, the negativity hypothesis, which has been supported by the majority of scholarly; political instability, in general, is bad for economic efficiency. In conclusion, several researchers in the field have yielded highly different findings, and still, no agreement has been reached as to what this relationship really looks like. (Elbargathi & Al-Assaf, 2019)

Political instability causes uncertainty in economic policies in general. It is known that uncertainties adversely affect investments and entrepreneurship activities. Uncertainties caused by instability can also influence politicians' goals and objectives. The ruling party can give up its promises by extending its term, increasing its voters, or by making short-term political changes in order not to give opponents the opportunity. Political instability adversely affects economic performance, causing policy makers to change policy more frequently (Aisen & Veiga, 2011)

It is generally accepted that political stability must be ensured for economic performance to be good. When voters are skeptical about politicians' equity, or if there is a communication problem or instability between political institutions; economic affairs do not go well, uncertainty increases in markets and distrust begins. Insecurity makes it difficult to conclude investment contracts between economic partners. Because the parties that will assume the role of arbitration between the parties and the collateral to be given by the parties will approach with suspicion. Political instability leads to uncertainties and has a negative impact on economic efficiency. In addition, due to the decrease in investment has a negative impact on growth. (ŞİMŞEK, 2015)

Where the nexus between political instability and economic growth has been one of the most important topics in empirical research in economics in the last decade. The major goal of this research was to establish the structure of causal interrelations. Sociologists and economists have tried to test whether a stable political system is a vital precondition for economic growth or whether economic growth creates the foundations for political stability. (Gurgul & Lach, 2013)

It is widely believed that political instability is detrimental for the economic growth performance of countries. Indeed, there are various studies that report a negative and significant correlation between political instability and economic growth (e.g. (Barro, 1991) ; (Perotti, 1996) ; (Ades & Chua, 1997)).

(ALESINA, ÖZLER, Roubini, & Swagel, 1996). in their seminal work studied political instability and growth in a sample of 113 countries for the period of 1950–1982 and found that countries with higher political instability, the propensity to change government is high, suffer lower growth. In other words, political instability and economic growth are deeply interconnected. The unstable political environment may reduce investment activities and the growth, conversely, poor economic performance may lead to government collapse and political unrest. However, they also found that low economic growth does not affect political instability. A great number of research have been carried out on political instability and economic growth

In their more recent work, Aisen and Veiga found negative association between political instability and economic growth by using advanced panel data econometric technique, system GMM, on 169 countries for the period of 1960-2004; it was also found that political instability reduces GDP growth rates significantly (Aisen & Veiga., 2013)

(Fosu, 1992) used cross-national data and a single equation model to investigate the effects of political instability on economic growth in Sub- Saharan Africa over the 1960–86 period and found a significantly negative direct relationship between political instability and economic growth, As (Fosu A. K., 2001), independent effect of instability on growth is positive. When interacted with physical capital, instability negatively affects growth

(Jong-A-Pin, 2009) uses a factor analysis to examine the effect of 25 political instability indicators and their effect on economic growth. The main finding is that higher degrees of instability of the political regime lead to lower economic growth.

using cross sectional analysis (Barro R. J., 1990) found that economic growth is affected negatively by political instability as property rights are hardly implemented in unstable political situation. (Devereux & Wen., 1998) argued that unstable political situation discourages private investments which in turn affects economy negatively. (Alesina & Perotti, 1996) used three different variables to proxy for the political instability and found it causing a decrease in economic growth, show that socio-political instability generates an uncertain politico-economic environment, raising risks and reducing investment.

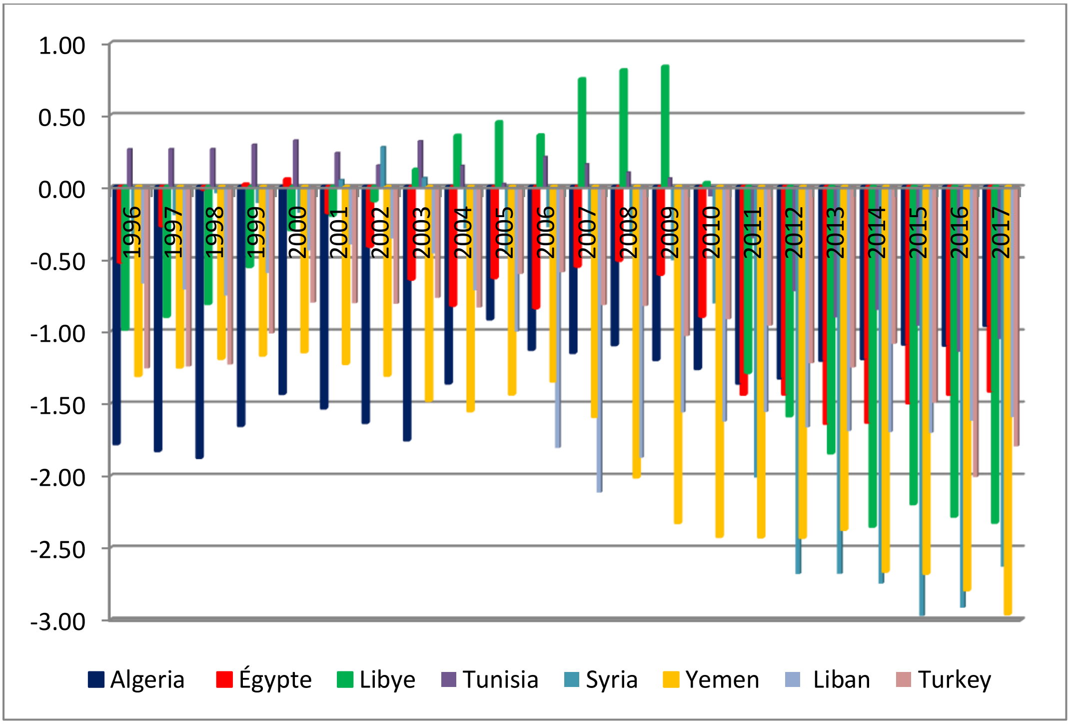
(Younis, Lin, Sharahili, & Selvarathinam, 2008) investigated the effects of various political instability factors on economic growth for selected Asian countries during 1990-2005. The study found close relationship between political stability and economic growth and the results showed that the role of political stability is more important than economic freedom.

3. Political Instability in MENA Countries

The Middle East has long been one of the most unstable regions in the world, and there are no present prospects for change in the near future. This instability is the result of ongoing conflicts and tensions, and a variety of political tensions and divisions. It also, however, is the result of a wide variety of long-term pressures growing out of poor governance, corruption, economic failures, demographic pressures and other forces within the civil sector. (Cordesman, 2018)

Below we review the index of Political Stability and Absence of Violence , which Measures perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including politically-motivated violence and terrorism For a sample of countries in the Middle East and North Africa.

Fig.1. Political Stability and Absence of Violence/Terrorism



Source: Data from database: Worldwide Governance Indicators

The causes of political instability in the Middle East are many. The first is economic underdevelopment. All countries in North Africa, the Levant, the Arabian Peninsula and the rest of Western Asia are underdeveloped. Oil wealth has not removed this feature. It may have raised standards of living in parts of the region and created a small number of very rich families. But even those Gulf states where per capita incomes are higher than anywhere else in the world are still underdeveloped. Their manpower resources are limited and poorly endowed with technical and professional skills. Their institutions are bureaucratic and inefficient. These economies depend entirely on a single commodity, and lack, therefore, the diversified productive structures capable of sustained economic growth (Mabro, 1992)

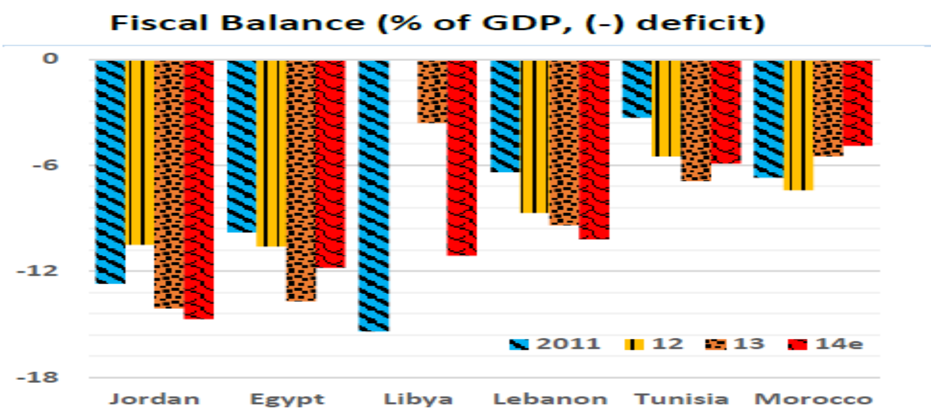
3.1. Key Economic Causes of Instability:

Impact of poor governance and corruption and State barriers to economic progress, doing business, Lack of effective development, excessive state and governance sectors with gross over employment and Poor income distribution, low incomes, poverty, Population pressure, urbanization, youth bulge, dependency ratio burdens and Unemployment and disguised (non-productive, low paid) unemployment and Lack of real career opportunities, equity, cronyism and nepotism, Catalytic incident or crisis, Impact of conflict or political crisis. (Cordesman, 2018)

4. Political instability and economic performance of a selected sample from the Middle East and North Africa

Economic prospects in the Middle East and North Africa (MENA) remain flat. Growth in MENA is expected to slow down in 2015 and range between 3.1 and 3.3 percent according to the World Bank and consensus forecasts respectively, and continue on the same path in 2016, If the security situation in Libya improves and oil exports increase, the regional average could surge to 4 to 5 percent in 2016. The main reasons for the continued, sluggish growth are: prolonged conflict and political instability in Syria, Iraq, Libya and Yemen; low oil prices that are dragging down growth in oil exporters; and the slow pace of reforms that is standing in the way of a resumption of investment. The continuation of this situation will significantly hurt the overall unemployment rate, now standing at 12 percent, and poverty in the region. Fiscal deficits are mounting, leaving the region with a deficit of 8 percent of GDP in 2015, after 4 years of surpluses. At this point, the overall economic outlook for MENA remains tepid, though longer term forecasts, if the regional conflicts subside and necessary reforms are implemented, could be more optimistic. (Devarajan & Mottaghi, 2015)

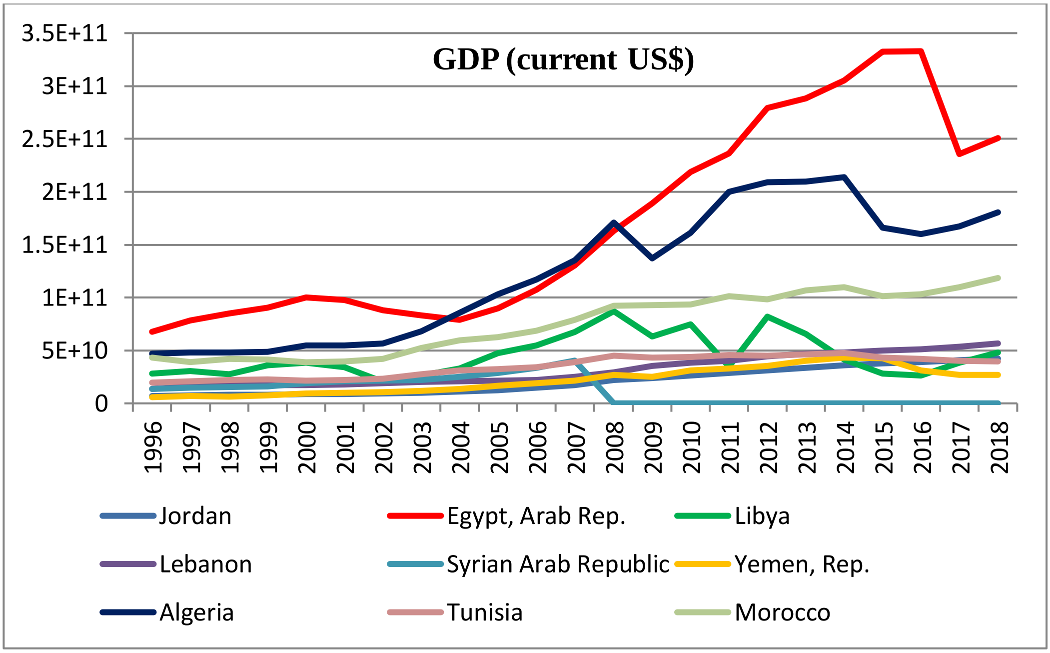
Fig.2. Fiscal Balance (% of GDP)



Source: Devarajan, Shantayanan, and Lili Mottaghi., 2015, p07

A snapshot of the Middle East and North Africa (MENA) today reveals a diverse and discouraging picture. Syria, Iraq, Libya and now Yemen are mired in violent conflicts that are devastating people's lives, infrastructure and national economies, with spillovers to neighboring countries such as Lebanon, Jordan and Tunisia. The cost of the Syrian war and spread of the Islamic State alone have been estimated at $35 billion in terms of lost output between mid-2011 and mid-2014. The transition countries of Morocco, Tunisia, Egypt and Jordan are slowly but steadily reforming their economies, albeit in a context of anemic growth, high fiscal deficits and rising youth unemployment. (Devarajan & Mottaghi, 2015)

Fig.3. Gross Domestic Product (GDP) in current US$



Source: World Bank's World Development Indicators (WDI)

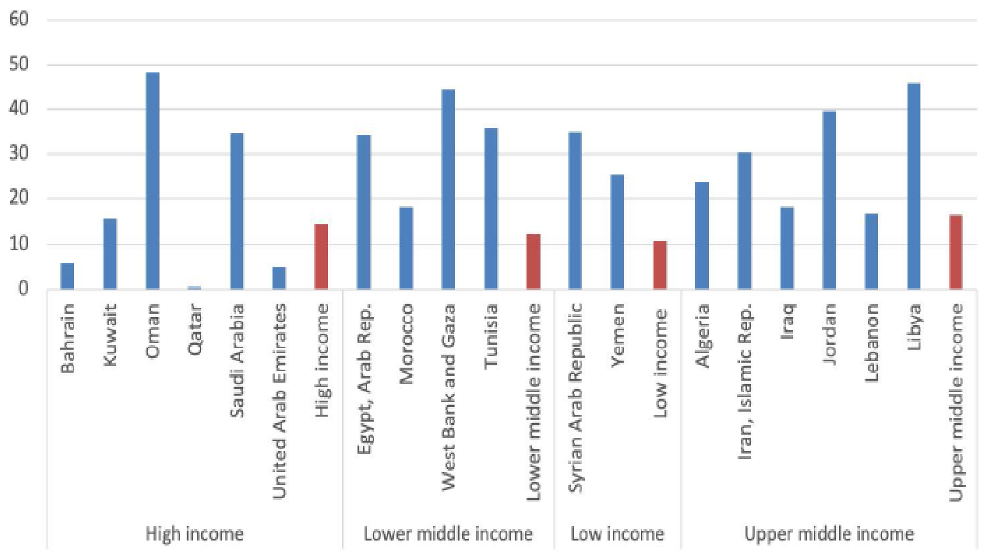
Growth in the Middle East and North Africa region is estimated to have slowed to 2.7% in 2016, reflecting fiscal consolidation in some countries and oil production constraints in others.

The failed ceasefire in Syria, the ongoing war in Yemen, the fight in Iraq against the Islamic State group, and the political crisis in Libya were part of a continued cycle of conflict in the region that has led to mass displacement, loss of life, and destruction of infrastructure. Cross-border spillovers in the form of disrupted trade, fiscal pressures from spending demands related to refugees and security, and loss of revenues from tourism have caused damage to the region and had international ripple effects.

Growth slowed sharply in the Gulf Cooperation Council countries to 1.6% as oil sector weakness spread to non-oil sectors. At the same time, output is estimated to have accelerated in the Islamic Republic of Iran to a 4.6% pace and in Iraq to a 10.2% rate thanks to large gains in oil production and, in the Islamic Republic of Iran, to a recovery in agriculture, automotive production, trade and transport.

Among oil-importing economies, growth in Egypt dipped slightly to a 4.3% pace in fiscal year 2016 as foreign currency shortages held back manufacturing and the tourism industry slowed. Morocco eased to an estimated 1.5% in 2016 on a drought-related contraction in the agricultural sector. (Bank, 2017)

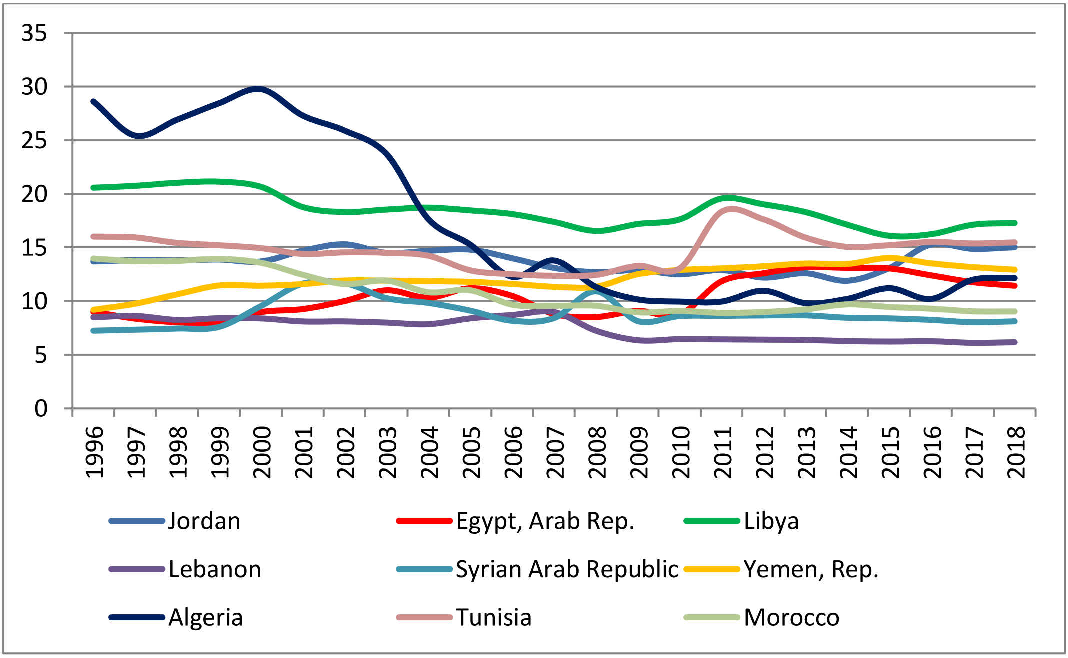
Fig.4. Youth Unemployment (% of total labor force ages 15-24), 2017



Source: Dadush, Uri., 2019.p03

The youth unemployment problem in MENA is part of a more general problem of low labor participation rates and total unemployment. Except the high-income Gulf countries, the total employment ratio in MENA is low compared to countries at similar levels of income, lower by some 15-percentage points. There is also a high variation within the high-income MENA countries with the United Arab Emirates and Qatar having the highest employment to total population ratios while Oman and Saudi Arabia are characterized by the lowest ones. The employment-to-total-population ratio of Oman is lower than the average of lower middle-income countries. (Dadush, 2019, p. 03)

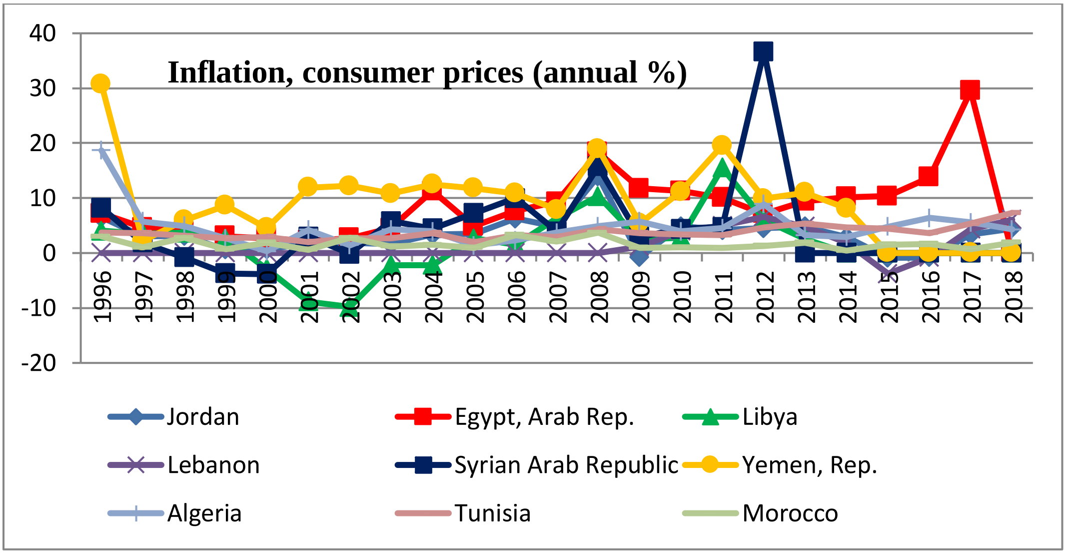
Fig.5. Unemployment Rate



Source: World Bank's World Development Indicators (WDI)

Unemployment rates in the MENA region are the highest in the world . An estimated 17 million workers, or around 12 percent of the MENA workforce, were unemployed in 2001 (LABORSTA, 2004)3. Unemployment rates for MENA youth (age 15-24) are also the highest in the world. An estimated 7.9 million young workers were unemployed in 2001 – over 25 percent of the young economically active population in the MENA region. The adult unemployment rate in MENA, estimated at 7.8 percent in 2001, while also the highest in the world, was not significantly different than the 7.7 percent adult unemployment rate of the transition economies of Eastern Europe and Central Asia (EECA). (Kabbani & Kothari, 2005)

Fig.5. Unemployment Rate



Source: World Bank's World Development Indicators (WDI)

From 1996 until 2000 regional inflation, weighted by GDP, declined from 11.5 percent to 2.5 percent. Since 2000, however, this trend was reversed. A small increase in 2001 was followed by increases in every year until 2008 when inflation jumped into double digits and was again a priority policy issue. The global financial crisis has at least temporarily brought down inflation and reduced the urgency of addressing this issue, but understanding the reasons for the recent increases can help address any post crisis resurgence in inflation that may emerge. (Crowley, 2010)

5. CONCLUSION*:*

This paper has allowed us to study the impact of political instability on the economic performance of a selected sample of MENA countries, based on data provided during the period 1996-2017, the results of the analysis indicate that political instability has a significant impact on performance indicators. Macroeconomics such as inflation and unemployment have a strong impact on GDP growth for MENA countries. The results did not contradict previous studies that show that political stability is an important factor in achieving economic results.

The impact of political instability on the overall economic performance in the countries of the Middle East and North Africa is highlighted. During the nineties, when the MENA countries recorded the highest inflation and unemployment rates, mainly due to the weak political and economic institutional framework and the result of violence and political instability,

In light of the results of the analysis obtained from this study, it can be concluded that political stability is an essential and important factor for achieving economic growth and raising the level of economic performance. In addition, one of the priorities that the MENA countries must work with is to adopt economic policy and provide political stability with the aim of reducing uncertainty and moving towards sustainable growth.

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