NATION, STATE AND INTEGRATION IN THE ARAB WORLD

Project Director and Series Editor:
Giacomo Luciani, Istituto Affari Internazionali, Rome

Volume I THE FOUNDATIONS OF THE ARAB STATE
Edited by Ghassan Salamé

Volume II THE RENTIER STATE
Edited by Hazem Beblawi and Giacomo Luciani

Volume III: BEYOND COERCION: THE DURABILITY OF THE ARAB STATE
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Volume IV: THE POLITICS OF ARAB INTEGRATION
Edited by Giacomo Luciani and Ghassan Salamé

Volume II:

The Rentier State

Edited by
HAZEM BEBLAWI and GIACOMO LUCIANI

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Contents

This series is dedicated to the memory of
Malcolm Kerr and Marwan Buheiry

Foreword

The Arab State is a series of four collective volumes exploring the origins, foundations, impact and stability of Arab States. This volume is the second in the series, and is specifically devoted to an analysis of the economic foundations and impact of the state in Arab countries, characterised by the peculiar nature of the revenue of the state and the extraordinary importance of rentier income in the Arab economies.

The series is the result of a collective research effort organised by the Istituto Affari Internazionali over a period of three years, under the general title of 'State, Nation, Integration in the Arab World'. This undertaking was made possible by a generous main grant from the Ford Foundation, and an equally generous additional grant from the International Development Research Centre (IDRC) of Canada. The latter was specifically devoted to support the work of Arab scholars writing on economic issues. Further financial support was received from the Italian Ministry of Foreign Affairs, and from the Commission for Cultural Exchanges between Italy and the United States.

Some of the chapters sponsored by the IDRC had a very extensive statistical section, and could be published in this volume only in partial form; others we were obliged to leave out of this volume altogether. The reader who is interested in gaining access to this material should ask from IDRC a copy of their Manuscript Report n. MR 135e, entitled 'Public Finance in the Arab Countries', which contains all papers supported by them *in extenso*.

The Istituto Affari Internazionali worked in cooperation with the Panteios School of Political Science in Athens, which was responsible for the organisation of two international gatherings, allowing authors of different chapters to come together and discuss their ideas in depth. As a result, while these are collective volumes, we believe that they have reached a degree of homogeneity which is not normally found in these undertakings. The Panteios School also supported one of the meetings with its own funds, decisively contributing to the success of the project.

Help was received also from the Gustav E. von Grunebaum Centre for Near Eastern Studies at the University of California

Los Angeles, which hosted me in February and March 1984 and again in the Fall of 1986.

The project was directed by an international steering committee in which the following participated: Roberto Aliboni, Director, Istituto Affari Internazionali; Hazem Beblawi, Chairman, Egyptian Export Development Bank; Ursula Braun, Consultant, Stiftung Wissenschaft und Politik; Marwan Buheiry, Director, Centre for Lebanese Studies; Alexander Cudsi, Professor, Panteios School of Political Science; Adeed Dawisha, Professor, George Mason University; Omaymah Dahhan, Professor, University of Jordan; Georges Sabagh, Director, The Gustav E. von Grunebaum Center for Near Eastern Studies, UCLA; Ghassan Salamé, Professor, American University of Beirut; and I. William Zartman, Director, Africa Program, SAIS, Johns Hopkins University.

The committee played a major role, and I as director of the project am very substantially indebted to its members for their advice in planning the research effort and selecting contributors. Some of the members also served as editors for a volume, thus exercising closer responsibility on the material included in it.

I received substantial help and advice also from other friends. Ali Hillal Dessouki was expected to be on the committee, but a variety of circumstances prevented him from participating in its deliberations. I did, nevertheless, greatly benefit from his generous advice and detailed comments, during numerous interviews in Cairo. My debt to him is indeed very substantial. I also greatly benefited from the friendly advice that I received from Judy Barsalou of Ford Foundation in Cairo, Ann Lesch of American Field Staff in Cairo, Andrew Watson of IDRC in Cairo, and Garry Sick of Ford Foundation in New York.

My personal thanks also to the staff of the IAI who contributed with sympathy and dedication to the complex organisation of this undertaking.

The shape of this project was deeply influenced by the advice of two friends who unfortunately did not live to see its conclusion: to their memory the steering committee decided to dedicate the four volumes.

I had met Malcolm Kerr in Los Angeles when the project was still in its planning stage, and he gave me valuable advice at that time. I asked him to be a member of the committee, but he was then expecting to be appointed President of the American

University of Beirut. He insisted, however, that he wanted to be associated with the project, so much so that the first meeting of the steering committee was hosted by him at Marquand House in June 1983. He participated in our deliberations then, and contributed to the formation of the basic decisions which shaped the project. His assassination was a tragedy for us personally and professionally, and has marked a disastrous turning point in West Beirut's struggle to remain one of the intellectual centres of the world.

The same negative turn of events finally drove Marwan Buheiry out of Beirut. Marwan was, personally and intellectually, a living example of West Beirut's intellectual curiosity and non-sectarian spirit. He participated intensely in the work of the steering committee and in the meetings connected with this project, until death struck unexpectedly, in exile.

It has been an honour and a very educational experience for me to serve as the director of this project, and I wish to thank all contributors for the very many things I learned. I hope that the reader will find these volumes as instructive as preparing them was for me. Any shortcoming, as usual, should be ascribed to my responsibility only.

Giacomo Luciani
Director of Studies
Istituto Affari Internazionali

Introduction

Hazem Beblawi and Giacomo Luciani

The years 1973–82 will probably be remembered in history as witnessing the emergence of a new 'Arab phenomenon'. OPEC, the Yom Kippur War, petrodollars, the Camp David Accords, PLO, fundamental Islam, Sabra and Chatila, were catchwords of the mass media during the decade. It is no wonder then, that never before has there been so much interest and scholarly work devoted to the newly rediscovered Arab phenomenon as can be seen these days. Furthermore, the terms Islam and Arabs are very often used interchangeably. Every aspect of the Arab phenomenon is now under close scrutiny, be it Arab nationalism, the role of Islam, Islamic art, the specificity of the Arab language, characteristics of Moslem cultures and values, etc. The present volume is part of this trend.

This volume, as well as the others in the same series, proposes to draw attention to an insufficiently explored aspect of the Arab phenomenon, the evolution of the economic role and foundations of the state in the Arab region. As part and parcel of the Arab phenomenon, an essential transformation has taken place in the Arab political system, specifically affecting the role of the state.

In the Arab world, the modern notion of the state suffers from strong attachment to competing notions, in particular, the notion of Arab nationalism and or the notion of Moslem community (*umma*). The modern state appears, nevertheless, to be continuously gaining new ground and progressing, imperceptibly perhaps, but no doubt solidly.

Whether we like it or not, we believe that the contemporary system of Arab states is here to stay. Against all romantic conceptions of a unified Arab nation, economic factors have worked to diversify and consolidate existing states. While integration is still the order of the day (as another volume in this same series clarifies), it will come as a result of relations and negotiations among separate independent countries. This result is not unrelated to the fact that oil revenues accrued to the periphery of the Arab world, thus creating new competing centres of power and new rivalries and, hence, a conflict of interests between rentier and non-rentier states as shall be illustrated.

Nevertheless, the oil states today face tremendous challenges, as oil revenues start to decline. Few expected that the decline would come so soon. Everybody knew it would come, but it was expected later rather than sooner.

Under the new conditions, the Arab states must either complete their transformation into secular polities with basic democratic regimes and productive systems or increasingly rely on police and repression. The latter course may maintain power in the same hands for some time, but will contribute little towards solving the basic problem, which is to give increased strength to productive activity and rely on its progress to increase state revenue from domestic sources.

Efficient production, capable of sustaining the economy and competing on world markets, is in many cases possible. But it requires certain basic steps which governments have been understandably reluctant to take. The public must be convinced that it has to pay for the state, not rely on it. Public revenues must be devoted to productive uses, not to subsidising private consumption or paying for costly weapons systems or prestigious schemes. Reforms of public management must be undertaken, and coherent policy decisions made on crucial policy variables such as subsidies, interest and exchange rates.

These are difficult decisions. However, the experience of other developing countries shows that societies often support governments making painful decisions when these are proposed by credible leaders under emergency conditions. The emergency is already there, although society is not always informed of it and in many cases is cushioned from it in all possible ways. One hopes the Arab states will find credible leaders.

The volume is devoted to a discussion of interrelations of the economic base with the cultural, social and political structures, and of its impact on the role of the state. The importance of the analysis of economic variables can hardly be overestimated, but the *thrust* of the discussion is only understood when viewed in the perspective of socio-cultural transformations discussed in other volumes.

The contribution of economics to the notion of the state is important. On the one hand, the economist can apply to the

notion of state the tools of analysis and the theoretical apparatus developed in the economic science. The use of the economist's techniques can shed new light on the notion of the state. On the other hand, and probably more importantly, recent economic developments in the Arab region have enormously affected the notion of the state, both in its relation to its subjects and to other states. Recent developments in available resources, trade, terms of trade, technology, financial instruments, monetary and fiscal policies, have had far-reaching implications on the notion of the state. This has been particularly true for the Arab states as of the 1970s.

Much of the literature on economic development revolves around the question of the role of the state. While some authors are inclined to attribute to the state a more limited role than others, this role is, in any case, substantial. As a minimum, it consists of the provision for security and guarantee of law and order, the establishment of modern economic legislation, the management of money supply, the surveillance of fairness of markets and the creation of basic infrastructure. Economic development cannot occur if the state does not offer certain preconditions and create an appropriate legal and political environment.

At the same time an abstract concept of the state prevails in most of the literature on economic development; a state whose policies, or politics, are considered as being exogenous variables, that are not closely related to the economic structure and social realities of the country. As a consequence, only too often specific states are urged to adopt policy packages that are politically irrelevant to them, and sometimes would quickly bring about their ruin. The assumption that the state is a neutral and homogeneous entity and that all states are alike, is one of the major limitations of a purely economic approach and one of the good reasons why a political economy approach is needed.

As is often the case, the same objection cannot be raised against the Marxist tradition, or the *dependencia* school, the two largely overlapping.

Literature on 'dependence' developed a theory of dependent classes generating dependent states (Baran, 1957). This approach has led to some interesting attempts to interpret the spread of authoritarian rule in certain regions, with particular reference to Latin America (Cardoso and Faletto, 1967).

The main emphasis in the most common *dependencia* approach is on international economic linkages: insertion in the world capitalist market is decried and countries are called to stand up on their own feet, which is understood as meaning to reduce linkages with the world economy. Yet it is now increasingly clear that autarkic and isolationist policies are often disastrous, and in any case cannot be maintained forever. Consequently, the notion of independence — political and economic — is increasingly removed from reality: no country can be said to be independent. On the contrary, all countries are interdependent, and even if they participate in the game of interdependence with widely different bargaining power, no country can be said completely to lack room for independent behaviour, even without isolating itself from the rest of the world.

The suggestion that countries should stand on their feet and rely on themselves *is* valid. Simply, this suggestion should not be taken as meaning economic isolationism. It should, on the other hand, be understood in the sense that the state must rely on domestic sources of income, if not exclusively, certainly more than is frequently the case.

The goal of this volume is not to offer a renewed discussion on the role of the state in the process of economic development. Two of the chapters do indeed discuss the sectorial development policies adopted by some of the Arab states; however these are not analysed *per se*, but rather as indicators and manifestations of the nature of the state. The discussion on the nature of the state tries to innovate both on the Marxist tradition and on the *dependencia* approach because it concentrates attention on the structure of public finance rather than purely on class relations or on external economic linkages.

It should be clarified at this point that the term 'state' has two overlapping meanings in ordinary usage. First, state is taken as being the apparatus or organisation of government or power that exercises the monopoly of the legal use of violence. In this meaning, the state does not coincide with society, although it may be the expression of the latter, and certainly rules over it. The second meaning of state is almost synonymous with that of society and indicates the overall social system subject to government or power (Giddens, 1985).

For the purpose of our discussion we shall define the nature of the state as being *the combination of essential indicators describing the relationship between the state and the economy.*

There are four major dimensions to the nature of the state:

(1) the size of the state relative to the economy, as measured by the ratio of state expenditure to GDP;
(2) the sources and structure of the income of the state;
(3) the destination of expenditure of the state;
(4) laws and regulations affecting economic life.

Of the above-mentioned dimensions, this volume concentrates on the first two, and to a lesser extent on the third and fourth. While a concentration of attention on specific aspects always inevitably detracts from treatment of others, we believe that there are valid reasons for this approach. Laws and regulations almost inevitably have implications on public finance. In most cases, these implications are direct, in other cases they indirectly influence the sources of income of the state and the tax basis. They may, for instance, influence the level of profits in the private sector, or the relative size of the private and public sector, and it so happens that the public sector seldom is a source of revenue for the state in the same way as the private sector. Thus, to a certain extent, laws and regulations may be analysed through the vantage point of public finance (see the way in which strategic policy decisions are related to public finance realities in the chapters by Oualalou and Jaidi, and Chatelus).

The structure of expenditure is often studied much more closely than the structure of revenue sources. Yet expenditure decisions cannot be taken independently of revenue realities. Revenue and expenditure may be assumed to be linked in two ways. First, there is a dimensional link: total expenditure cannot vary independently of total revenue. In this respect, it is, of course, true that expenditure normally exceeds revenue, however in the final analysis expenditure is limited by revenues. Expenditure can exceed revenue if the state resorts to credit either from the domestic or from the international economy, or to money creation. There are limits to either of these alternatives: the lack of development in the domestic financial market limits the possibility of tapping domestic savings; the discretionality of foreign banks and the IMF limits the possibility of resorting to external borrowings; the danger of uncontrolled inflation limits resort to the printing press.

While financial orthodoxy is not very frequent, it is still a fact that in numerous cases specific policies were abandoned less for ideological motivations than for fiscal ones. The retreat from many plans for greater socialisation of production in countries like Egypt. Tunisia and Algeria were closely connected to the fact that it is easier to impose taxes on a private sector than on a 'socialist' one. If this were not the case, the socialist sector would support the socialist state, and the transformation could continue through to the marginalisation of the private sector. On the contrary, however, the increasing importance of the socialist sector has almost inevitably led to an impoverishment of the tax base supporting the state (except when enterprises earning rent from abroad were nationalised), and this in turn has eventually led to a reversal of policies and to renewed importance of the private sector. One is reminded of Ibn Khaldun:

> You, O King, went after the farms and took them away from their owners and cultivators. They are the people who pay the land tax and from whom one gets money. You gave their farms as fiefs to your entourage and servants and to sluggards. They did not cultivate them and did not heed the consequences. (They did not look for the things) that would be good for the farms. They were leniently treated with regard to the land tax (and were not asked to pay it), because they were close to the king. The remaining landowners who did pay the land tax and cultivated their farms had to carry an unjust burden. Therefore, they left their farms and abandoned their settlements. They took refuge in farms that were far away or difficult (of access), and lived on them (the Mobedhan addressing King Bahram b. Bahram of Persia, p. 239).

The link between revenue and expenditure also works in the opposite direction: the availability of revenue causes an increase in expenditure. In the case of many oil-exporting countries it is rather clear that policies have been adopted principally because money was available. This is especially the case for those policies which are primarily aimed at the resdistribution of oil rent, such as policies of aid to other developing countries, or land acquisition programmes in Kuwait. A good deal of 'development' expenditure was approved without too much concern for the need of what was being bought (especially in infrastructure) simply because money ought to be spent. Refusing to spend available revenue is not an effective way to keep power, as the

colourful history of Sultan Said of Oman demonstrates. Finally, one reason for the phenomenal increase in military expenditure in the region is to be found in the ease with which large sums of money can be spent in procuring the latest military gear.

But leaving aside the case of the Gulf oil producers and of Libya, revenue acts as a limit rather than as a stimulus to expenditure. If we look at it from a dynamic point of view, what this means is that the state is permanently faced with expenditure obligations that exceed financial resources available to it, and must strive to expand the latter. This is the basic reason why the state must have an interest in the prosperity and economic well-being of its country. Ibn Khaldun wrote in this respect: 'There also is a statement by Anosharwan to the same effect: "Royal authority exists through the army, the army through money, money through taxes, taxes through cultivation, cultivation through justice . . ."' And he goes on to suggest that a ruler must be just because this is a prerequisite for expanding cultivation, thus increasing tax revenue, thus reinforcing the ruler himself.

It is normally assumed that economic growth *per se* reinforces the state and stabilises the regime: this however appears to be a questionable assumption in the face of the social and cultural dislocation that economic growth often entails. Fast economic growth may lead to an even faster growth in expectations, which may be and frequently are frustrated by later developments, undermining the stability of the state. It is, however, clear that economic growth reinforces the state in this respect: that it allows the state to increase its income, therefore in turn to increase expenditure and 'buy off' political consensus. That political consensus may be acquired through state expenditure is a vastly safer assumption, although not a conclusion to be taken for granted, as is done only too often. It is in order to underline the limits to the effectiveness of state expenditure as a tool in buying consensus that we included a final chapter on Iran. This series focuses on the Arab countries, and a chapter on Iran is an exception: we have no claim to have provided a thorough discussion on Iran, but we thought that it would be important to devote some attention to a contrasting case that would be in the back of the reader's mind anyhow.

In the context of the Arab region, opting in favour of industrialisation and economic growth has historically been closely related with the growing role of nationalist ideologies and the fight against foreign domination. It became clear that economic growth and, in particular, industrial growth are a prerequisite to the strengthening of the state and its ability to resist outside aggression. While this is not simply a matter of public revenue, because the strength of the state is influenced by other factors as well, and military might is, in particular, influenced by technological capability, it is, nevertheless, clear that the state needs access to increased revenue first and foremost.

Along this line of reasoning, one is led to visualise state development expenditure (i.e. investment in the reinforcement of the domestic productive base) as being motivated by the need to increase income at a later date. Thus a qualitative link is also affirmed between expenditure and revenue, whereby the ratio of investment to current expenditure is expected to be a function of the structure of state revenue and the perceived need to increase it in future years. This leads to the hypothesis that development policies and the structure of expenditure are a function of the structure of revenue.

It is on the basis of these considerations that we decided to focus our attention on the size of the state budget relative to total GDP and on the structure of its income sources.

It is clear that both the relative size of the state and the structure of income is a function of the level of development. If a country is very poor, it cannot normally sustain a state which is complex and diversified. Poor countries can only 'afford' embryonic states, that limit themselves to performing a few essential functions in connection with law and order and external defence, in most cases in a highly ineffective way. The state will absorb a small percentage of GDP; it will remain a fragile entity, which is constantly confronted with the danger of collapse when faced with challenges from within and or from without. No Arab state belongs nowadays to this category, but some, like North Yemen, were in it not too many years ago. In most other cases, Arab states were destroyed or easily subdued by European imperialism because of their extreme weakness.

As an economy develops, so the relative size of the state budget increases, and the structure of income sources evolves. In fact, the size of the state budget tends to increase faster than GDP, leading to a constantly increasing share of state expenditure over total expenditure.

At the same time, one needs more than just to increase the size of the state to generate economic growth. Many Arab countries learned this in a painful way, through the experience of broken expectations following a rather indiscriminate tendency in favour of *étatisme*. The strengthening of the role of the state permitted the attainment of certain fundamental goals, but failed in the attainment of others.

A further correlation may be established between growth and the increasing role of certain sources of income, in particular direct taxation on personal and corporate income. Suffice here to recall that direct taxes accounted for 88 per cent of tax revenue in the USA (1983), 73 per cent in Japan (1985) and 57.2 per cent in the UK (1983). In this case, a good argument can be made that the dual proposition also holds true: in other words, the development of a modern fiscal system and a growing reliance on direct taxes are two essential, if often forgotten, ingredients of an effective development policy package. In fact, taxation does not only serve the purpose of raising income for the state, but is also a redistributive tool, this being in particular the case for progressive taxation on income.

While their taxation systems are underdeveloped, governments in the Arab countries have in most cases tended to play a crucial role in fostering economic development, and specifically in the industrialisation process. As a consequence, they have tended to rely on methods of imposition, both explicit and implicit, that carry seriously distorting consequences on some key economic variables. Resources are transferred from one sector to the other by manipulating prices in a variety of ways. This affects, in particular, the terms of trade of agriculture *vis-à-vis* industry, and of the countryside *vis-à-vis* the urban concentrations. In most cases, the state has intervened in the selection of crops and obliged farmers to sell at artificially low prices, in order either to gain a profit or to contain the cost of living for the industrial workers and in the urban areas. Whatever the specifics, governments have in this way tended to hide or reduce the gap in their fiscal resources. Finally, although taxation on foreign trade is commonly justified by the need to protect infant domestic industrial activity, it also plays an important role in replenishing the coffers of the state, and the latter commonly becomes the prevailing preoccupation of the government, again leading to distortions and inefficiencies. At the same time, the lack of an efficient taxation system combined with the relative underdevelopment of the financial system practically implies that printing money is the only instrument available to fund the deficits in the government budget. This has created an inflationary bias that administrative measures (administered prices, rent controls, artificially low interest rates) have repressed but not eliminated. On the whole, the combination of these factors has created an environment which is not conducive to sustained economic and industrial growth.

The weakness in the taxation systems in the Arab world and the extraordinary reliance of Arab states on sources of revenue from outside their boundaries has long been noted. That this fact could not but have momentous consequences on the politics and development perspectives of the Arab countries has also been underlined by various authors. Thus, for example, Galal Amin writes:

> While oil revenues finance the whole of investments in the oil countries as well as a good part of those of Lebanon, foreign aid finances the whole of Jordan's investments and a good part of those of Egypt, Syria and the Sudan. But whether financed by aid or by oil revenue, whatever is invested in both cases is not the result of any obvious sacrifice borne by the investor. This helps to explain why the government of an oil-rich country or of a country receiving vast amounts of foreign aid can enjoy a degree of stability which is not explicable in terms of its domestic economic or political performance. It also explains why wasteful expenditure is in the nature of both . . . Moreover, a government receiving vast amounts of either foreign aid or oil revenue is not likely to feel the urgent need for raising productivity, for increasing or diversifying exports or for tapping other sources of savings. Tax laws are likely to be lenient and tax evasion and income inequalities tolerated (Amin, 1974: 49–50).

Thus the importance of the composition of state revenue is recognised, but it has failed to be developed into a categorisation and a discussion of the nature of the state. The idea that states based on external sources of income are substantially different from states based on domestic taxation has led to the proposition of the concept of rentier state. This was first proposed with reference to Iran by Hossein Mahdavy (1970: 428–67), and the expression has been used by various authors subsequently, but no rigorous and complete treatment of it has been offered yet.

The concept of the rentier state is at the centre of attention in most chapters in this volume. While on the one hand the concept is at first sight a simple one, and it is clear that the peculiar nature of the income sources of many Arab states conditions their political behaviour and development policies, on the other important problems emerge as soon as analysis of the rentier state concept is pursued. This volume offers neither a final solution to these problems nor a unified point of view: it offers what the editors would call a structured debate around them.

The first major question which is raised is exactly what is meant by 'rentier state', and what is the relationship between state and economy. A first possibility is to focus exclusively on the state, independently of the economy, and define as rentier any state that derives a substantial part of its revenue from foreign sources and under the form of rent (i.e. because specific conditions allow it to be the direct beneficiary of income derived from selling goods or services at prices well above their production costs). This is a rather restrictive definition that says little about the economy. Alternatively, one could put greater emphasis on the economy, and define the concept of 'rentier economy', which is either an economy substantially supported by expenditure from the state while the state itself is supported from rent accruing from abroad or more generally an economy in which rent plays a major role. A rentier state is then a subsystem associated with a rentier economy.

The first step in this discussion is necessarily a reconsideration of national accounting practices and conventions as they apply to oil-producing as well as other Arab countries. This task is accomplished in Chapter 1, 'Income Measurement in Arab States', by Thomas Stauffer. Stauffer argues that revenue from oil and other mineral sources should not be considered as being part of current income, as it represents a finite and nonrenewable resource. Furthermore, migrants' remittances are commonly treated as capital movements, rather than current income, leading to an overstatement of domestic income in the labour-importing countries, and to an underestimate of the same, for the labour-exporting countries. National accounts, in practice, also need to be reconsidered in order to isolate the rent flows, and measure their importance both statically and dynamically. Various proposed modifications throw a new light on relative economic strength and performance of Arab states, which is relevant for the rest of our analysis, and will become increasingly important for all purposes as the decline in the size of the oil rent progressively reduces the extreme distortions that the oil boom brought about.

Against this background, the concept of a rentier economy is explored in the chapters by Hazem Beblawi, Mahmoud Abdel Fadil and Michel Chatelus, while in the chapter by Giacomo Luciani the accent is on the rentier state (or, as he prefers to say, allocation state). In his definition of a rentier economy, Hazem Beblawi insists on three essential features: (1) rent cannot be the only kind of income in the economy, but it should predominate; (2) the origin of the rent must be external to the economy, as 'pure internal rent boils down to a situation of domestic payments transfer'; (3) a minority in the population must be engaged in the generation of the rent, while the majority is involved only in the distribution or utilisation of it. A rentier economy 'would in all probability' generate a rentier state, and is in any case strictly connected with the spread of a rentier mentality, which in turn has important political and developmental consequences.

Abdel Fadil is rather inclined to accept the definition of rentier economy as one which is substantially supported by the expenditure of a rentier state:

> In such oil-rentier economies, *the state becomes the main intermediary between the oil sector and the rest of the economy*. It receives revenues which are channelled to the economy through public expenditure, and since public expenditure generally represents a large proportion of national income, the allocation of these public funds between alternative uses has great significance for the future development pattern of the economy.

Finally, Michel Chatelus refers to the concept of 'circulation economies' that he already introduced in a previous article:

> We will simply delineate rent as any income not originating from the productive activity of the concerned unit, the flows and dimensions of which are not directly linked to the beneficiary's activity (i.e. any income the amount of which is determined for the most part by decisions the concerned unit cannot control). We will then distinguish 'production economies' and 'circulation economies'. Rent economies are an 'ideal-type' of the latter: individuals, groups, even the state, compete for the control of rent. In our view, most economic activities are to be considered a means of ensuring income circulation, rather than production-oriented behaviour . . . In most Middle East Arab States, a growing part of the population depends for its living, either directly or indirectly, on unrequited transfers. Money comes from expatriated relatives, patrons or tribal elders, state allocations. There is at best a tenuous link between individual income and activity. *Getting access to the rent circuit is a greater preoccupation than reaching productive efficiency* (Chatelus, 1984: 255–6).

As for Luciani, he believes the essence is in the origin of state revenue, not necessarily in its rentlike character:

> Thus if we look at the origin of state revenue, we should rather speak of 'exoteric states' — being states predominantly based on revenue accruing directly from abroad — and 'esoteric states' — predominantly based on domestic revenue and taxation. Yet, a different way of looking at the same distinction may be more enlightening, and this relates to the predominant function of the state. From the latter point of view the relevant distinction appears to be one between 'allocation' and 'production' states, depending on which of these two functions, mere allocation or production and reallocation, is the necessary preoccupation of the state . . . We may define allocation states all those states whose revenue derives predominantly (>40 per cent) from oil or other foreign sources, and whose expenditure is a substantial share of GDP.

There is, stricly speaking, no contradiction between these various approaches: they are rather complementary. For all practical purposes, whatever the definition adopted, one comes to practically the same conclusions as to which country and/or state is to be called rentier. The only differences are attributable to the differential treatment of migrant remittances. Remittances have grown to become the most powerful redistributive mechanism between Arab countries. Their contribution to the national disposable resources of certain countries is substantial, and an appropriate treatment of them requires a considerable adjustment in the standard definition of their national accounts.

Thus remittances add 38 per cent to the GDP of the Yemen Arab Republic, 24 per cent to the GDP of Jordan and 7 and 6 per cent, respectively, to the GDP of Egypt and Morocco (Stauffer). The GDP of the receiving countries ought to be reduced in parallel, but the reduction is much more limited in percentage terms (e.g. in the case of Kuwait it is 3 per cent).

Remittances may, on one hand, be considered as being a form of rent because 'insofar as the migrant worker commands a higher wage abroad than at home, his remittances are quasi-rents to the extent of the difference between the remittance amount and the net value added which the worker might have contributed had he remained at home' (Stauffer). Thus remittances fuel a rentier mentality: 'A basic characteristic of a rentier mentality is that it embodies a break in the work-reward causation . . . Reward becomes a windfall gain and not the result of systematic hard work; it is situational, hence vulnerable and opportunistic' (Beblawi). Whenever remittances are important it becomes true that 'getting access to the rent circuit is a greater preoccupation than reaching productive efficiency' (Chatelus). On the other hand, if the emphasis is strictly on the rentier state as distinguished from the rentier economy, remittances do not generate a rentier state: 'Neither are migrants' remittances a source of income from the rest of the world, because they belong to the migrant, not to the state. The state may attempt to tax the income of migrants, but is in no position to do so before it is repatriated. It is only after remittances have entered the domestic economy . . . that they can be taxed' (Luciani).

At the same time, the practical importance of the discrepancy in the treatment of remittances is minimised by the fact that the state in the countries concerned also receives unrequited transfers that are larger than the remittances themselves. The clearest case is Jordan, in which a very high proportion of the state budget is, and always was, paid with subsidies accruing from abroad directly to the state. Unrequited transfers received by Egypt and Morocco are not quite as important, but they are in any case more important than remittances. It is only in the case of North Yemen that the state does not quite deserve to be called rentier if one looks at the origin of its revenue, while it should be so called if one looks at the importance of rent generally in the economy. This may indeed help to explain why the Yemeni state is so weak and society so characteristically 'anarchic': the problem derives exactly from the fact that

citizens receive large rents from abroad that the state can tap only with difficulty, while the state itself benefits from relatively more limited transfers. This fact can be related to Beblawi's observation that in a rentier state 'only few are engaged in the generation of the rent'. But even in the case of the Yemen, grants from foreign governments have been very important in certain years; thus in 1975 out of a total revenue of 795.5 million rials grants provided 415.1 million. In subsequent years, grants fluctuated while tax revenue increased very rpaidly, thanks to various duties on imports, whose rapid growth was the immediate consequence of migrants' remittances. But grants still were some 30 per cent of total revenue in 1981.

It is important to stress at this point that one cannot meaningfully ask which definition is right and which is wrong, as they are all legitimate and useful in stressing various aspects which are relevant for a political economy interpretation of the Arab countries. If the emphasis is laid on the broader economic framework and on the attitude of the citizen towards work and economic activity, then the emphasis must necessarily be on the importance of rent income in the economic system as a whole. On the contrary, if the emphasis is on the rules of the political game and on the institutions and policies of the state, then it is logical to focus on the state. Each author uses the definition which is more appropriate to his specific topic, and the various approaches are complementary.

A second controversial point is whether we can find both rentier and non-rentier states within the Arab world, or whether on the contrary all Arab states tend to behave in accordance with the rentier state paradigm. If all Arab states can be called rentier we come to a vision of an Arab economy which is fundamentally homogeneous in this respect. If, on the other hand, rentier and non-rentier states coexist in the Arab world, this is a discriminatory factor that begs powerful consequences. In the literature, notwithstanding the very evident diversity of structural parameters in the Arab economies, the tendency is rather to underline common factors. It is exactly for this reason that in this case an effort was made to test the opposite hypothesis, i.e. that structural parameters substantially affect the nature of the state and of the economy, and lead to a polarisation within the Arab world.

But even as we try to underline the polarisation, it is clear that no simple two-way categorisation holds: Beblawi's 'semi-rentier states without oil', Luciani's 'induced allocation states', Chatelus's 'generalisation of the rentier state hypothesis'. In short, reality provides us with a full spectrum of different shades and colours. While it is important to attempt to define concepts clearly, any categorisation which is proposed inevitably appears to be too rigid, and a number of ambiguous cases must be dealt with.

Thus characteristically Arab states adopt policies that are much more homogeneous than one would expect on the basis of their diverging opportunities for receiving revenue from abroad. It is as if a rentier mentality prevailed in all Arab states, including those that do not in fact deserve to be called rentier. At the beginning of this introduction we formulated the hypothesis that expenditure policies must be influenced by the perceived need to raise increased revenue at a future date: this hypothesis does not appear to be supported by the behaviour of Arab states in the last 15 or 20 years. On the one hand, and this is by far the most striking aspect, we find countries that cling to expenditure policies that are detrimental to economic growth and very clearly cannot be sustained in the long run. They do so out of a perception of a lack of any politically acceptable alternative, or sheer shortsightedness; they evidently feel, in any case, that somehow somebody will bail them out: here again is the rentier mentality at work. If the state perceives that it is easier to increase its income from outside sources than from domestic sources, its interest in sound and efficient economic growth rapidly wanes.

The best-known case of perverse expenditure mechanisms is the one linked to subsidies on certain goods which are considered to be 'basic necessities'. Attempts at cutting down on subsidies have been quite clumsy, and have in most cases triggered popular riots that the regimes perceived as being a serious menace. At the same time, there is broad professional agreement on the fact that subsidies are not applied to basic necessities only, and benefit the middle class as much as, if not more than, the lower classes. The fact that the state is unable to cut down on one type while maintaining the other is a manifestation of the rentier mentality prevailing in the middle class. And the fact that the outbursts of violent opposition triggered by cuts in subsidies are so worrying to the state is a manifestation of the weak political base of the state itself, and the lack of democratic legitimation. In fact, cutting subsidies is in a sense not qualitatively different from raising taxes: either of the two is politically

feasible only if the state enjoys solid democratic legitimation, justifying the degree of repression which may on some occasions be necessary.

But what is even more detrimental is the fact that non-rentier states have often adopted rentier-like policies with respect to the industrial sector. As Michel Chatelus points out in his chapter, this is not so much a question of degree of state involvement, because the state also plays a very large role in countries like South Korea or Taiwan, which are successfully industrialising. Rather, it is a matter of attributing too many political objectives to the industrial system one is creating: 'It is the very industrialisation process which contributes to state-building rather than the state which helps to build a national industry.' 'In many countries of the region one can observe the prevalence, from the late 50s to the mid-70s, of an industrialisation ideology which privileges political considerations over purely economic considerations and constraints.' But there are exceptions, such as Morocco and Tunisia, among the non-rentier states; while for Egypt the resistance to reform of public industry, and the persistent tendency to overstaff in order to alleviate the unemployment problem, manifest a continuation of the allocative mentality.

At the same time we find Arab states certainly qualifying for inclusion in the category of rentier states, that appear to be genuinely preoccupied with their long-term sources of income and have adopted efficient industrialisation policies. Chatelus, for one, draws a clear cut distinction between Kuwait and the UAE on the one hand and Bahrain, Qatar, Saudi Arabia and Jordan on the other. He underlines that the GCC may become an effective answer to the need for coordination among industrialisation plans of different Gulf countries, and one, in any case, that has no parallel in the rest of the Arab world. Converging with these observations is the contrast between the Libyan and Algerian experiences which is proposed in the chapter by Dirk Vandewalle.

Policies towards agriculture are discussed in the chapter by Hamid Ait Amara: they offer another interesting point of view to judge the different approaches of rentier and non-rentier states. The latter have historically tended to privilege agrarian reform, socialisation of agricultural production and controls on production and prices in order to minimise the cost of living for urban workers, and indirectly the cost of the industrialisation effort. Some borderline rentier states, like Algeria and Iraq, have tended to conform to this general model; others have more squarely tried to develop domestic production by offering very high prices and various incentives to producers. The growing dependence on imports of agricultural products is stimulating a revision of *dirigiste* policies, with an increase in prices and a decrease in administrative control: and, apparently, a tendency to greater homogeneity in agricultural policies. However, the fact remains that rentier states guarantee much higher prices: indeed, it is not clear whether the reduction in oil revenue will force a limitation in transfers to agriculture. At the same time, the increase in domestic agriculture production achieved by some countries, e.g. Saudi Arabia, cannot be denied.

One final trait which is common to the expenditure pattern of the Arab states is the extraordinary importance of military expenditure. While for some countries the need to be protected against foreign aggression is there, it is a fact that military expenses are a very serious drain on national resources for certain states and have strongly negative consequences on long-term development perspectives. The importance of rent highlights the role of military capability, because the source of rent becomes more valuable and thus more vulnerable. It is also true that military force is an element permitting states with insufficient access to their own sources of rent to become recipients of rent circulated by other states.

But the inflow of oil revenue into the region, from which all other rent flows directly or indirectly depend, appears headed for a substantial reduction in the coming years. Quantities of oil exported and prices received for them are both on the decrease: rent circulation will be drastically curtailed.

How will Arab states react? For some of the major Gulf oil producers and possibly for Libya it may be a matter of cutting unnecessary expenditures: in this case they will still be rentier states, simply at a reduced level. But for all others, and possibly also for some of the former, cuts in expenditure will not suffice to balance the accounts under the new conditions.

The question of revising the structure of taxation on the domestic economy is thus posed. From this point of view, Arab states find themselves in sharply different positions. Fiscal legislation is quite different in the Maghreb than in the Mashreq, and it is clear that history and the colonial experience, especially

in the former colonies and protectorates of France, left a substantial mark on fiscal legislation. As Oualalou and Jaidi clearly explain in their chapter, in Algeria, Tunisia and Morocco, taxation, and particularly direct income taxation, is a primary source of revenue for the state. On the contrary, both Mauritania and Libya suffer from very weak fiscal systems. There is also a difference between the former three countries, in as much as Morocco is alone in attempting to seriously reform and modernise its taxation structure. Tunisia and Algeria do have a base on which to improve, now that it will be necessary to do so. Outside the Maghreb, only Egypt has a long established fiscal tradition, as the chapter by Hesham Garaibeh documents. The other countries will have to start developing a system of taxation essentially from scratch.

From a political point of view, it is likely that progress in the direction of modernisation of the fiscal systems will occur only if it takes place with some parallelism in all Arab countries. It is difficult for individual states to adopt more modern fiscal systems and fight against pervasive evasion, when in neighbouring countries, that are linked by a plurality of economic ties, nothing of the sort takes place. A substantial reinforcement of fiscal instruments of the rentier states would cause a modification in their nature: but this is not, *per se*, a good reason to expect that such a modification will not take place, although it is clear that it would raise more than one problem and meet more than one obstacle. The issue is closely connected with the question of legitimation and to the development of democratic institutions. It is a recurring historical truth that demands for democratic participation become louder, sometimes unrestrainable, whenever the state must ask for sacrifices, be they under the form of increased revenue or reduced expenditure.

Thus it is clear that the Arab states are heading towards important modifications in their public finance, which will entail important modifications in the rules of the political game. It is quite possible that they will re-emerge stronger out of this difficult juncture. To the extent that they succeed in strengthening their domestic bases and reducing reliance on external support, this will indeed be the case.

In the face of the sharp fall in oil prices, the objection could be raised that this is a book on rentier states at a time when the latter are disappearing, at the end of the 'rent era'.

For this reason, it is important to underline that rentier states are not found only in the twentieth century and in the Middle East, but are a common feature of world history; and that some, if not all, Arab countries will maintain their rentier nature notwithstanding the fall in oil prices. Thus the decade 1974–85 may be regarded as one in which the rentier phenomenon attained extraordinary proportions and became particularly visible, but not the only one in which rent was at work.

The state of the Roman Church, the Spanish Empire in the seventeenth and eighteenth centuries, the Principality of Monaco, Peru at the time of the guano boom, countries substantially dependent on foreign aid — be they least developed countries or the state of Israel — are all examples of rentier states from different times and/or regions. Rent was not born with oil, even less with expensive oil.

Oil may become cheaper, but rent will not disappear from Arab politics as a factor shaping equilibria and rules of the game. Some of the Arab states simply lack the resource base or minimum conditions that would allow them to become significant agricultural or industrial producers. Their lifestyles are inextricably tied to oil and the rent it generates, and they can credibly outlive oil only if this rent is permanent.

For these countries, a reduction in rent revenue accruing to the state necessarily implies a reduction in expenditure, but is not likely to imply a significant reduction in dependency on rent, because alternative sources of revenue are meagre.

The situation is different for the countries in which the state has access to some rent, but alternative sources of domestic taxation exist or may be developed. For them, the question which will be posed of the political conditions under which a transition from a rentier state to one based on democratic legitimation is possible.

It is almost inevitable that this transition will be difficult. Power structures based on rent are well entrenched, and the decline in available rent will be widely felt in the population, precipitating protest and disturbances that states are accustomed to dealing with heavy-handedly.

But if there is dubious flexibility in most states to accommodate popular demands, there is also little flexibility from the public, because the rentier mentality is hard to extinguish. Expectations, individual behaviour and political beliefs will continue to be shaped by the extraordinary experience of the decade 1974–85, even if oil prices stay at a very low level for a long time.

The mere uncertainty surrounding oil prices, the fact that under almost any imaginable scenario a part of public opinion will think that they could be higher, ensures that rent will remain a central issue in domestic and inter-Arab political debate.

1

Income Measurement in Arab States

Thomas Stauffer

INTRODUCTION

This chapter addresses the question of measuring national income and national economic performance with particular reference to the Arab states of the Middle East. It indicates the adjustments to the existing national income accounts which are needed in order to obtain more meaningful measures of income which permit appropriate comparisons among the states of the area or with states elsewhere in the world.

The present system of national income accounting (SNA) involves accounting conventions which are not well suited to certain Third World economies. The concepts of national income accounting were originally evolved beginning in the late 1930s to meet the demands of the industrial economies of Europe and certain of the conventions and standards which emerged, while indeed appropriate for integrated industrialised economies, are much less appropriate for economies which are heavily dependent upon depletable resources, like oil, or where transfer of labour income looms large in the resource balance of the host or recipient economy.

Many — if not most — of the economies of the Middle East are characterised by an unusual degree of dependence upon non-renewable assets, such as oil or phosphates, or upon unrequited transfers of foreign aid in the form of grants or concessional loans, or upon quasi-rents such as the income from remittances or emigrant labour or the locational rents of pipelines and canals.

The contribution of these unrequited resources or liquidations

of capital (mineral resources) is so large, that the structure of the economies is dominated not by domestic factors of production but rather by the process of adapting to and incorporating the economic rents or external flows of resources.

There is no need for special income accounts for Middle Eastern states and the Arab states are not unique in receiving aid, portfolio income, or receiving or transferring labour remittances. These issues arise more generally in measuring income in countries as diverse as the United States, the Pacific island of Nauru, Lesotho and Switzerland. However, the sheer size of these flows in the case of many states and the relative magnitude of the requisite adjustments, dictate that the special aspects of these sources of income must be reflected more carefully in the construction of the national accounts and in the measurement of income.

The adjustments are indeed quite large for some countries. The national incomes of the oil exporters, which are the most egregious examples of the difficulties in measuring income, are overstated by factors of between two and five; i.e. the incomes, when corrected for depletion of the wasting oil asset, are between 20 and 40-odd per cent off the conventionally reported values. Conversely, the national incomes of states such as Jordan or the two Yemens, which benefit from sustained flows of workers' remittances, are understated by between 30 and 50 per cent.

The adjustments are also a prerequisite to interpreting economic affairs in these states and in particular are absolutely necessary in the case of many of these states with regard to three of the most important uses of income in analysing political-economic behaviour:

Comparisons of income

Rankings and comparisons of national incomes are misleading, without these adjustments, since the relative changes differ so markedly across countries.

Measuring dependence

The dependence of the economies upon resource rents, transient sources of income, unrequited transfers or debt accretion is not reflected in the standard measures of income.

Interpreting performance

Illusions of growth result when economies benefit from injections of rents or external resources and these effects must be separated out in order to assess the extent of self-sustainable growth.

In the following sections of this chapter we shall outline the sources of incomparabilities in interpreting national income, distinguish between static or technical adjustments and dynamic adjustments, and illustrate the effects of adjusting for the major sources of distortion in a select set of cases.

The second part develops a taxonomy of the rents and other sources of revenues which require special treatment in the measurement of national income or economic performance, indicating those where adjustment to the national accounts is necessary and those other sources, such as aid or locational rents, where the accounts need not be adjusted but where the income or GDP/GNP must be interpreted carefully.

Part three turns to the measures of economic dependence and the dynamic contribution of rents to income, sketching the mechanism of the 'rentier multiplier' and showing that rents and unrequited resources generally contribute more to reported national income than would appear even in the revised or adjusted national accounts, so that the extent of dependency is still greater.

The last part illustrates adjustments as applied to a number of Arab economies in order to highlight the different types of corrections and to show how the measures of both performances and dependency are sharpened.

ISSUES IN INCOME MEASUREMENT

The measurement and interpretation of income for many of the states of the Middle East is complicated by those states' unusual degree of dependence upon special resources, i.e. economic rents, labour remittances, or foreign aid. In this and the

following section we shall indicate how the national income accounts must be modified to include these effects or how supplementary measures must be introduced in order to characterise the economies.

In this section we shall present a taxonomy of the sources of revenue which require special treatment or interpretation and, for those three which require respecification of income — extractive rents, portfolio income, and workers' remittances — we shall indicate the adjustments to GDP or GNP which are needed.

Taxonomy of receipts

The array of 'special resources' is shown in Table 1.1, which lays out the taxonomy of special flows into or out of the major Arab economies of the Middle East. The impact and relative importance of each type of flow differs from country to country and will be discussed in the last part with respect to specific examples: here we shall pursue only the general features.

Table 1.1: Flows of rents and external resources: Arab economies of the Middle East

	Portfolio income	External capital	Quasi-rents	Mineral	Rents location
Egypt	0	+ +	+ +	+ +	+ +
Jordan	+	+ + +	+ +	N	0
Kuwait	+ + +	0	– –	+ + +	0
Morocco	0	+ +	+	+	0
Tunisia	0	+ +	+	+	N
Saudi Arabia	+ + +	0	– – –	+ + +	0
Yemen (North)	+	+ + +	+ + +	0	0

+ = inflows – = outflows N = positive but small 0 = not material

Extractive rents

The largest anomaly in measuring income in the Middle East results from the petroleum sector, since the production of oil is the liquidation of a finite asset, so that oil income must be interpreted much more carefully.

Conceptually, the same question arises with regard to all extractive industries, including phosphates which are important in several Middle Eastern countries. However, the share of rents in market value is very much less in all other mineral industries and the discussion hereafter will focus upon oil.

Oil revenues consist of two components: (i) the factor costs, i.e. the payments to the labour and capital involved in discovery, development and production of the oilfields; and (ii) the value of the finite resource itself.

Most of the price of oil in the Middle East consists of economic rent. Actual costs in the Middle East under current conditions are a small fraction of the market price of oil, so even in the case of high-cost oil between 80–85 per cent of the total revenues are indeed economic rents attributable to the generally favourable cost conditions in the Middle East and the high value of oil in energy markets. More typically, rents comprise 95–97 per cent of gross receipts (low-cost oil).

The difference between the value of the oil and the costs of production can be interpreted two ways. It can be viewed as a quasi-rent to the inframarginal producer or as a drawdown of the capital value of the finite stock of a depletable resource.

Locational rents

A second source of economic rent is that derived from the geographical advantage associated with pipelines and canals. Revenues from oil pipelines and canals loomed larger in the Arab economies in an earlier period when they were principal sources of foreign exchange receipts to Egypt and Syria.

In this case the rent is the difference between the transportation tariff or toll and the full costs of providing the services, where the latter are payments to factors of production. In contrast to the trend in oil rents, these locational rents have declined steadily because technology has eroded the cost advantages of the shortcuts.

Today locational rents are a major item only in the case of Egypt, where the gross receipts from the Suez Canal are about one-fifth of earned foreign exchange (excluding aid).

Portfolio income

Portfolio income in the form of receipts of interest or dividends

is important in the Arab Middle East. This is in marked contrast to most areas of the Third World, where most countries are characterised by net outflows on interest accounts. A subset of Middle Eastern countries, the Arab oil producers of the Gulf, are large net investors and thus receive large net flows of investment income.

Moreover, for that set of countries — the larger oil exporters of the Gulf — portfolio income is large in relation to current levels of oil exports, so that it must be considered when measuring the economic resources available to the country.

This item is exceptional because it is positive and relatively large, whereas usually the adjustment to GDP for portfolio income is negative and relatively small.

Labour remittances

Labour remittances are large elements in the balance of payments of many Middle Eastern countries, such as Jordan, Egypt, or the two Yemens, which are net beneficiaries. In Arab states with large non-resident labour forces, their remittances flow in the opposite direction, as is the case for Kuwait, Libya, Saudi Arabia and the UAE.

For the host countries remittances by expatriate labour are direct costs, but for the beneficiary countries there may be some element of economic rent in the receipts. In so far as the migrant worker commands a higher wage abroad than at home, his remittances are quasi-rents to the extent of the difference between the remittance amount and the net value added which the worker might have contributed had he remained at home.

Capital receipts

Capital inflows are important in certain states and contribute significantly to disposable national economic resources in a number of cases. These inflows take several forms: (i) borrowing; (ii) direct investment (relatively rare); (iii) unilateral transfers in the form of aid; (iv) drawdowns of foreign exchange reserves.

External capital sources in a number of cases provide such a large fraction of available resources that they must be considered in any effort to interpret growth, in particular in efforts to assess the extent of self-sustainable growth. Moreover, for shorter-term assessments the drawing down of reserve balances, which has been important in some years, for example, in the YAR, must also be considered.

These external resources have profound impacts upon the host economies and must be considered beyond the usual framework of national income analysis. Certain flows — remittances and oil revenues — call for a basic adjustment of the accounts, which currently do provide a meaningful treatment of those items.

Portfolio income is included in the GNP, but not the GDP, so that GDP figures become quite misleading for those cases where portflio income looms large. We shall illustrate this effect in the case of Kuwait.

Finally, all rents, because they are transfers which are not offset by commitments of domestic factors of production, exercise a multiplier effect upon national income which transcends the usual static framework of income accounting and thus requires special attention (this will be treated later). The adjustments described in this section estimate the share of the different elements in GNP or GDP but do not purport to measure the contribution, i.e. the amount by which the income is increased by the given flow of resources. The difference between share and contribution — the static versus the dynamic concepts — is critical because the adjustments tend to underestimate the real roles of each factor in the host economy.

Adjustments to income

Of the special resources detailed above, only certain are income and hence will be considered here. For two sources — mineral revenues and workers' remittances — the national income concepts are indeed inappropriate and it is necessary to modify existing accounting practice if the sources of revenue are to be properly reflected. Standard conventions treat oil receipts as income but workers' remittances as capital, rather than payments to labour and hence as income.

Thus two key elements in the national accounts of many of the Arab states are handled in the opposite way to that which is intuitively and economically more meaningful. Without adjustment for these two effects, the reported incomes of oil exporters are seriously overstated. Similarly, with regard to remittances, the incomes of host countries are overstated while those of beneficiary countries are correspondingly understated, since workers'

remittances are not included at all in the national accounts.

Mineral rents

There is no established precedent for adjusting national incomes for the depletion of a wasting asset. The standard procedures for national income accounting, established when resource rents were small and when the question was not material, exclude any depletion charge. The existing systems of national income accounting recognise the full value added in the oil sector as income, and incorporate no form of depletion charge to correct for using up the finite or wasting asset.

Paradoxically, however, while there is no provision for depletion of a non-renewable resource, there are deductions for consumption of reproducible assets. National income accounts do recognise depreciation for renewable capital assets and also allow adjustments for changes in the inventories of reproducible goods. The precedent for adjusting for changes in asset stocks exists and by direct analogy the argument for adjusting for the consumption of non-renewable resources is more compelling.

What is needed is a 'depletion allowance' which would subtract from the GDP the contribution of the wasting or finite asset, leaving only the income otherwise generated from reproducible, non-wasting assets. This calculation of a depletion charge involves measuring the current value attributable to the resource itself.

There is broad consensus that the value of the resource is the economic rent, i.e. the difference between the market value of the resource, such as oil or phosphates or any mineral, and the costs of production. The costs must include a return to all capital employed in the mineral sector, so the rent is whatever is left after the full costs of production have been debited.

This rent is measurable. Let us consider in Figure 1.1 the case where oil sells for $29 per barrel, operating costs are 79 cents, and the capital employed is $3650 per b/d. The costs of capital involve both a depreciation charge and a return. If the depreciation lifetime is 10 years, the depreciation charge is thus $1.00 per barrel. At an interest rate of 15 per cent the return to capital must be $1.50/barrel, and the rent is the price less all the mentioned charges.

The rent thus equals $29 minus $3.25, or $25.75/barrel. The depletion charge, which is the resource value, is therefore $25.75 per barrel. The charge amounts to some 85-plus per cent of market value, a relationship which is broadly typical for many OPEC oil producers.

Figure 1.1: Calculation of resource value

Price	$29.00
Operating costs	(0.75)
Depreciation	(1.00)
Imputed return	(1.50)
Rent (resource value)	$25.75

The basic adjustment for depletion is the rent, and it must be subtracted from the oil or mineral sector GDP to get the reproducible value-added in the mineral sector.

Adjustment of the GDP of a mineral-exporting country therefore involves two distinct steps: (1) determination of the mineral rents; and (2) deducting their full contribution to the GDP.

The 'Non-depletable GDP' (ND-GDP) is the value of the GDP adjusted for the contribution of the wasting asset and the magnitude for this correction differs widely across the oil-exporting countries. In Table 1.2 we illustrate this adjustment for Kuwait and Saudi Arabia, two Arab oil producers, and — to indicate the broader applicability of the principle — the analogous adjustment for an industrialised oil producer: Norway.

Table 1.2: Adjustments in mineral rents for Kuwait, Saudi Arabia and Norway, 1980 (billions of national currency)

	Kuwait	Saudi Arabia	Norway
GDP	7.3	473	284
Oil rents	5.1	320	45
ND-GDP	2.2	153	239
Reduction	70%	67%	16%

The depletion charge reduces the apparent income or GDP of both Kuwait and Saudi Arabia by almost three-quarters, so that only about one-fourth of the conventionally reported GDP is attributable to domestic factors of production and the rest is in effect the irreversible liquidation of capital.

Similar adjustments are applicable even to industrialised countries, but there the relative magnitudes are much less. Even

though the US is the second largest oil and gas producer in the world, the depletion correction amounts only to 3 per cent of GDP. Although the oil and gas sectors in the US are the second largest in the world, they are none the less swamped by the sheer size of the US economy. The adjustment for Norway amounts to about one-sixth of reported GDP, although a more comprehensive analysis would show that most of the ostensible growth in Norway since 1973 is directly the result of the expanding oil sector which reveals a higher dynamic dependence than indicated above.

The need for such adjustments is quite clear. The distortion due to omission of a depletion charge is so large for the cases of Saudi Arabia and Kuwait that their unadjusted incomes cannot meaningfully be compared with those of other states.

Remittance income

Labour remittances are incompletely and somewhat inconsistently treated in the present system of national income accounts. Such remittances are either treated as capital outflows or as factor income, depending upon an essentially arbitrary criterion of terms of residency:

Factor income — if the worker is resident in the host country for less than one calendar year, as is the case with seasonal labour, his income is treated as factor income paid abroad and debited against the GNP of the host country.
Private transfers — if the worker is resident for longer than one year, his remittances abroad are treated as captial transfers and are not debited against GNP.
Recipient countries — remittances are usually treated as capital inflows and not reported as part of the GNP, since the source is deemed to be a non-resident.

In the Middle East today, however, it is unrealistic not to recognise remittances as income, both from the standpoint of recipients and also the host countries. Irrespective of whether the individuals might rotate or change, large pools of expatriate labour remain in the host countries and the recipients continue to enjoy large flows of remittance receipts.

Remittance income should therefore be debited against GNP (host country) and credited to GNP (labour source country), since the legal distinction as to duration of sojourn is less important than the economic significance of the flows themselves.

We note that labour payments by foreign contractors usually are included within the contract installments, so that remittances attributable to contract labour are usually already included as part of services imports (host countries) or as part of services receipts (source countries). The discrepancy with regard to remittances arises principally in the case of workers directly employed by local firms.

Two options exist for incorporating workers' remittances into the measures of income:

(1) Add to GNP, thereby generalising the existing metric.
(2) Define a new measure 'National Disposable Income' (NDI) which equals the GNP plus (minus) remittance receipts (payments).

We shall report the adjusted figures as NDI in order to highlight the adjustments, since it is not established practice to debit/credit the GNP for remittances and it would, thus, be misleading to retain the same designation for the adjusted measure.

MEASURES OF DEPENDENCE

Given the importance of external resources to most of the economies of the Arab Middle East it is necessary to establish better measures of the degree of dependence of those countries upon such resources.

Static dependence

The basic measure of dependence involves defining the toal resources available to the economy, earned as well as rents and transfers of all kinds, and specifying what share of that total is contributed by the external or special resources. The static measure involves generalising the measure of income to reflect the large flows of external resources which are not recognised as 'income' or which are unrequited.

The steps are:

(1) Define the concept of 'National Disposable Resources' (NDR) which is equal to:
GNP
plus: IMPORT SURPLUS
plus: NET DEBT REFINANCING
(2) Aggregate rents, quasi-rents and external resources. Remittance income must be segregated since it is a factor payment, and only a part constitutes a rent. External resources include gross aid, as distinct from net borrowings, in order to reflect fully the flow of new resources.
(3) Define dependence as the ratio of special resources, or any component thereof, to the National Disposable Resources (NDR).

This measures the resources which the economy commands, irrespective of how financed or garnered. It is equal to the sum of domestic consumption and investment, plus any borrowings used to refinance or roll outstanding debt. The refinancing is included because borrowings undertaken to repay debt are additions to disposable resources.

Similarly, in measuring capital availability, it must be measured gross, rather than net, in order to reflect the full flow of funds and, in particular, to capture the extent of the country's exposure to financial markets in any year.

Dynamic dependence (rentier multiplier)

The degree of dependence is typically greater than calculated using the static measures, since unrequited resources — such as aid or mineral rents — exercise a multiplicative impact upon the recipient economy which may be expressed as the 'rentier multiplier'.

The rentier multiplier is similar to the familiar Keynesian multiplier in that it specifies how an injection of funds causes a larger increase in effective demand and thus leads to an increase in income greater than the net injection.

The rentier multiplier differs in that it is created not by deficit spending, for example, but by the injection of real resources in the form of export mineral rents or, more generally, unrequited transfers or receipts of all kinds.

Let us consider oil sector income. All but a small portion accrues to the government because factor costs are so small. The government saves some and may spend directly on imports, such as arms. For the remainder, the government purchases local currency with the foreign exchange and spends this domestically. The recipients — civil servants, contractors, etc. — spend on imports, whereby funds then leak out of the economy, but the domestic receipts are respent and often some leak out as imports in the second round, and so on.

The direct impact of oil revenues is deducted when we deduct the rents, but we note that the rents contribute further to domestic income and consumption insofar as they are spent in the domestic economy. The above definition of ND-GDP/GNP is incomplete and does not even approximately address the question of measuring the oil or oil-rent independent income.

We capture this indirect or dynamic effect via the rentier multiplier, which then estimates the contribution to the non-oil income which arises from the spending of the oil rents in the non-oil sector. This effect can be large; about one-half of the ostensible non-oil sector in Kuwait is generated by spending oil revenues and a large part of the ostensible growth of the economy since the 1960s is simply an expansion associated with expanding oil spending, where only non-tradeables, such as many services like government or commerce, are 'produced' domestically and most or all manufactured goods are imported and paid for out of oil revenues.

The rentier multiplier is less constrained than the usual multipliers because:

(1) There is no foreign exchange constraint — the injected funds are generated by unrequited foreign exchange receipts.
(2) Imports are usually freely available to satisfy induced demands.
(3) Complementary factors are also available within certain bounds:
  (a) labour can be absorbed from the non-monetary traditional sector;
  (b) immigrant labour can be mobilised where indigenous supplies are insufficient.

The constraints on the rentier multiplier mechanism must be tested in each case: in general, the multiplier is greater than one and the range, in practice, seems to be 1.3 to 1.6. The static

measures of dependence defined above must be appropriately increased to allow for this dynamic effect.

The rentier multiplier is applied only to the rents derived from foreign transactions. Domestic rents, such as from domestic oil sales at the world price, do not generate a multiplier mechanism, since debit and credit items offset each other to terms of second order.

Remittances may not command a full multiplier, even though earned in foreign exchange, because of the opportunity cost of that labour. The actual rent component must be analysed in each case. In Jordan, for example, emigration has created a labour shortage in certain sectors, which is only partly offset by an inflow of Egyptian and Asian workers.

The rentier multiplier must be defined more carefully if modified definitions of income are used. If remittance outflows are debited against income, the net contribution to National Disposable Income is less in each round so that the multiplier can be much smaller by virtue of the greater leakage.

COUNTRY CASE STUDIES

We shall now turn to illustrating the adjustments and considerations discussed earlier in general terms and show that, in certain cases, the ambiguities in determining income can indeed be quite large and thus are non-trivial.

Kuwait

The economy of Kuwait is particularly interesting because all three of the major adjustments are necessary. The economy is heavily dependent upon oil, so that a large fraction of the reported GDP is extractive revenue, the exhaustion of the wasting asset, and thus should not be interpreted as income.

Further, portfolio income from Kuwait's large accumulation of overseas financial assets has increased to the point where it is approximately equal to current oil revenues. Consequently, the distinction between 'domestic' (GDP) and 'national' (GNP) products is quite large. Finally, labour remittances are also large; slightly more than one-half of the population of Kuwait consists of expatriate workers without Kuwaiti citizenship, who remit large sums annually back to their homelands or into overseas accounts.

Oil rents

The first adjustment needed is the subtraction of the oil sector rents, i.e. the difference between the value of oil production and the factor costs of production (labour, capital and purchased inputs).

In 1981 the oil sector rent was approximately equal to KD 4041 million. The oil rents alone amounted to almost two-thirds of the reported GDP for that year (KD 6764 million) and the overwhelmingly dominant role of oil in the formal income accounts is quite clear.

The Non-depletable GDP (ND-GDP) is a better measure of the 'income' of Kuwait, since the oil rents are derived directly from the depletion of a finite asset and thus cannot be interpreted as income. The ND-GDP, i.e. the measure of national income stripped of the contribution of the liquidation of geological capital, is therefore much less — i.e. KD 2722 million (see Table 1.3 and Figure 1.2).

Figure 1.2: Adjustments to income, Kuwait

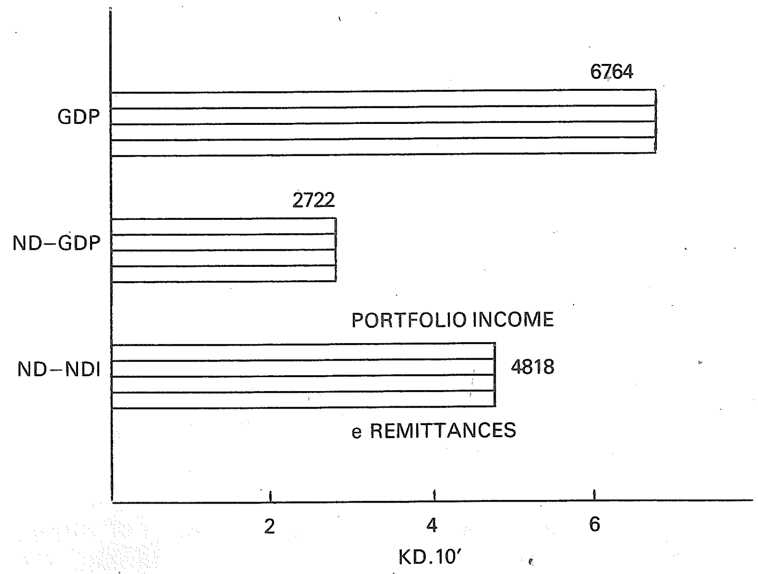


Table 1.3: Kuwait, 1981 (millions of KD)

1.	Gross domestic product (GDP)	6764
2.	Extractive rents	–4041
3.	Non-depletable GDP	2722
4.	Net factor income	2288
5.	Non-depletable GNP	5010
6.	Remittances	–192
7.	National disposable income	4818
8.	National disposable resources (1+4–6)	8860

The non-depletable income of Kuwait, accordingly, is 40 per cent lower than the figure reckoned in the conventional national income accounts which include extraction rents as income. This measure of GDP, however, is still greater than the oil-independent GDP because the subtraction of the oil rents from the total still does not adjust for the dynamic contribution of the oil rents to the so-called non-oil sector.

Portfolio income

In the case of Kuwait, however, even the improved measure of non-depletable GDP is incomplete and gives an inadequate picture of the resources available to Kuwait for consumption. The portfolio income in 1981 amounted to KD 2288 million, which came to more than half the oil revenues. This income, derived from deposits, bonds, real estates, stocks and other investments overseas, was largely collected by the government through official holdings, but almost one-third accrued to the Kuwait private sector.

The gross national product (GNP) includes net investment income and, in this instance, provides a much better measure of Kuwait's ability to spend and thus in this context is a much more meaningful measure of income. The non-depletable GNP, which includes the portfolio income but excludes oil sector rents, thus is KD 5010 million, and portfolio income has the effect of almost doubling the measured income exclusive of current-year oil rents.

Labour remittances

The 500,000-plus expatriates in Kuwait annually remit large sums abroad, and this outflow should be deducted in measuring the GNP since, as discussed earlier, the income accruing to temporarily domiciled foreigners is not really national in an operational sense.

The official figure for private transfers abroad, as reported by the Central Bank of Kuwait, is KD 192 million for 1981. This is essentially equal to the difference between the gross income of the expatriates and their local expenditures in Kuwait.

It is a low estimate because it does not include any savings by such expatriates in Kuwaiti financial institutions, and because it includes only those transfers made through financial institutions. This figure includes important outflows since many of the workers from the subcontinent or Sri Lanka — an important fraction of the total — frequently remit through the money-changers.

The revised figure for the GNP — the non-depletable National Disposable Income (NDI) — comes to 4818 million dinars, and a more likely estimate, allowing for unreported remittances, would probably be closer to 4500 million. The adjustments for remittances thus amounts to between 4 and 10 per cent of the non-depletable national income and is material, even though in this case it is of course swamped by the basic adjustments for oil rents and portfolio income.

Dynamic adjustment

Kuwait is a striking example of an economy in which the rentier multiplier plays an important role. The critical preconditions of factor mobility and sizeable receipts of rents and quasi-rents are both satisfied. Imports can freely meet induced demand; the economy is quite open — tariffs are relatively low, and only a handful of domestically produced goods enjoy significant tariff or quota protection. Labour constraints, at least until recently, are also minimal; labour moves relatively freely and the expatriate population now numbers more than one-half of the total and accounts for a still larger fraction of the workforce.

Government expenditures are the driving force in the economy, but Kuwait is all the more interesting in this regard because the government receives from portfolio two-thirds of budgeted domestic outlays. Hence in the case of Kuwait both portfolio income and oil rents contribute to the multiplier's impact.

The non-depletable GDP is shown in Table 1.4, together with a range of values for the estimated ND-GDP adjusted for the multiplier effect of the government's domestic spending of its oil revenues.

The dynamic adjustment can be quite large, reducing the

Table 1.4: Adjusted GDP measures, Kuwait, 1980 (millions of KD)

Gross domestic product	7374
Oil rents	(5157)
Non-depletable GDP	2217
Dynamically-adjusted GDP	1052–1650

apparent non-oil GDP by another factor of two and revealing a still higher dependence upon oil than results from the static adjustment for the oil rents.

The lowest estimate, KD 1052 million, is based upon the upper bound for the possible rentier multiplier, while the higher figure involves the lower bound, so that the dynamically adjusted oil-independent GDP lies in between.

Another way to view the importance of oil revenues to the non-oil sector is to measure the oil revenues against the total resources at the disposal of the non-oil sector. Here we view the non-oil sector as independent, and for the non-oil sector the oil receipts are unrequited transfers. Total resources then consist of the value-added in the economy outside of oil, plus the net factor revenues from abroad (portfolio income minus workers' remittances), plus the oil revenues collected by the government from the oil sector. On this basis oil rents constituted 4041 million KD out of total disposable resources of 8859 million, or almost half.

Subtraction of the oil rents understates the contribution of oil to the economy and hence the degree of dependency. Oil contributes 46 per cent of total expenditure in the non-oil sector, which is indicative evidence of the importance of oil revenues even in that part of the economy which is ostensibly technically defined to exclude oil. Thus both the dynamic multiplier analysis and the analysis of disposable resources in the non-oil sector illustrate the critical consideration that the straightforward calculation of GDP or GNP shares will underestimate the real contribution of rents.

Yemen Arab Republic

The Yemen Arab Republic (YAR) offers another extreme case where adjustments are large in relation to the conventional measure of national income and also where the degree of dependence upon external or special resources is inordinately high.

Income adjustments

Remittances from Yemenis working abroad, primarily in Saudi Arabia, are as important to the YAR's economy as oil is to most of the major oil exporters. Yemen's earned foreign exchange receipts, including interest of the Central Bank's foreign exchange holdings, were $270 million in 1980, which covered only 15 per cent of the $1.8 billion in imports. Gross remittances from Yemeni workers amount to $960 million in that year and covered about two-thirds of the total import deficit, the remainder being paid by aid.

Table 1.5: Yemen Arab Republic, 1980 (millions of YR)

1. Gross domestic product (GDP)	11919
2. Gross national product	12656
3. Remittances	4578
4. National disposable income (2 + 3)	17234
5. Capital and aid inflows	2877
6. National disposable resources (4 + 5)	20111

The adjusted GNP (NDI) includes a credit for net remittances, i.e. gross receipts from abroad, less the stream of remittances sent abroad by expatriates in the Yemen. This adjustment increases the figure for the GNP, from 12.7 billion riyals to 17.2 billion, a correction of 35 per cent or more than one-third (or 38 per cent of the GDP).

Dependence measure

In 1980 the Yemen benefited from two additional flows of external resources. First, it received large flows of official foreign aid from diverse sources in that year, plus some additional amounts from Saudi Arabia which were not reported in official statistics. Second, it drew down its foreign exchange reserves to supplement remittance and aid receipts and sustain its import levels, and total capital flows — aid, plus loans, plus withdrawals of reserve balances, amounted to 2.9 billion riyals or almost one-quarter of the GDP.

The overall degree of dependence upon special resources is the sum of aid, remittances and reserves drawdown which amounted

to 7.46 billion riyals — equal to 63 per cent, almost a full two-thirds of the GDP. Thus the non-income resources available to the YAR are very large in relation to reported income, and the GDP, as usually defined, is a very poor measure of the income, which should include the remittances.

The GDP in the case of the YAR is an even poorer measure of resources, which must recognise the aid and consumption of reserves, as well as the remittance income. As shown above, the GDP in this instance understates total resource availability by almost 40 per cent.

Jordan

Jordan is still another case where the GDP seriously understates the economic resources at the disposal of the economy, and hence understates the extent to which domestic consumption is very much greater than domestic production. As in the case of the Yemen Arab Republic, both workers' remittances and foreign aid are very large, constituting well over two-thirds of Jordan's total foreign exchange receipts.

Income measurement

In the case of Jordan the only adjustment to the GNP is that due to net remittance receipts, which added 20 per cent to the reported figure (see Table 1.6). In 1981, Jordan received JD 344 million in workers' remittances, but this was in part offset by 52 million in remittances sent out of the country by non-Jordanians

Table 1.6: Jordan, 1981 (millions of JD)

Gross domestic product (GDP)	1199
Remittances	292
Capital and aid	733
National disposable resources	2224

employed in Jordan. The net remittance income thus came to JD 292 million. Remittance outflows have steadily increased in importance since Jordan currently suffers from a labour shortage, due to extensive out-migration, and Egyptians and some Asians are now employed in the country to offset the missing work force.

The remittance income (net) alone added almost one-quarter to the resources generated domestically and also to the officially reported measure of the GNP. Another measure of the very great importance of remittances to Jordan is the fact that net receipts are one-third higher than total export revenues from all sources.

Resource availability

Jordan also received large amounts of aid, primarily in the form of unilateral grants and the remainder largely as highly concessional loan finance. In 1981 grants amounted to JD 480 million, almost all of which came from Arab oil-producing states of the Gulf, the small residue coming from UNRRWA and other UN agencies.

Total special resources were almost equal to the GDP itself and thus effectively doubled the resources available to the Jordanian economy. Loans (253 million dinars) and aid totalled 733 million dinars, equivalent to fully 61 per cent of reported GDP. Aid and remittances together aggregated to 1025 million dinars, an amount equal to 86 per cent of GDP, which is indicative of the extraordinary dependence of the Jordanian economy upon the political-economic environment which generates both the aid and the employment opportunities for Jordanians and Jordan-domiciled Palestinians.

Evaluation

This case illustrates particularly well the inadequacy of GDP as a measure of income or of disposable resources. It also highlights how consideration of the special sources is necessary in order to assess the fragility of the Jordanian economy in terms of its remarkable exposure to exogenous developments.

The income is understated because remittances, unlike aid, are earned income, and the Jordanian national income is in substance one-fifth higher than usually reported because of the exclusion of workers' remittances. The resources are also seriously understated by almost a factor of two, so that the single figure of GDP provides poor insight into real levels of consumption, which exceed real product by almost the same multiple of two.

We get further insight into the critical role of non-income resources if we examine the rate of capital formation in Jordan. *Pro forma* the rate of saving in Jordan out of GDP is 43 per cent which is phenomenally high. However, if we compare savings with total resources, rather than GDP, we find that the rate is 24 per cent — i.e. one out of every disposable four dinars within the Jordanian economy is saved. However, if we relate total savings of JD 515 million to total aid and borrowings of 733 million, we find that domestic saving is, in fact, negative — borrowings and unilateral savings exceed total gross domestic capital formation, which presents quite a different picture of performance.

Egypt

Egypt is a more complex case, because it combines features from remittance and aid-dependent economies, such as Jordan or the Yemens, with those of rent-dependent states such as Kuwait. Egypt receives a large remittance income, as well as large rents and quasi-rents from oil exports and the Suez Canal, respectively.

Income adjustments

Both the GDP and the GNP of Egypt require adjustment to reflect the large rents from exportation of oil and also the even larger income from remittances. Together remittances and oil rents come to two and one-half billion pounds or almost 12 per cent of GDP.

Oil rents are less than the value of total production because of domestic consumption and relatively high costs of production. For 1982 they were estimated as 1.12 billion Egyptian pounds. Although Egypt is currently a moderately large oil producer, somewhat more than half of Egypt's total output is consumed domestically.

The economic rents attributable to the volume of oil output consumed within Egypt are in fact virtually nil since domestic prices for oil products are very much below world prices. Thus only net oil exports contribute to the total oil rents, and the rents in turn are less than export values after deducting the volumes attributable to the foreign companies for paying costs and their returns on capital. The oil export rents are approximated as 1.1 billion Egyptian pounds for 1982, in the absence of better data.

The net effect of the adjustments to Egypt's GNP is surprisingly small, however. The adjustment to get the non-depletable GNP (ND-GNP) is only some 5 per cent so that the ND-GNP

Table 1.7: Egypt. Adjustments to income (billions LE)

Gross national product	23.0
Oil rents	−1.1
Remittances	+1.5
Non-depletable GNP	23.5

must be reduced by that amount. The adjustment for workers' remittances is proportionately larger — amounting to 6.5 per cent of the GDP. The two adjustments essentially offset one another — a reduction by 5 per cent on one hand and an increase of 6.5 per cent on the other results in a net upward revision in the reported GNP by only 1.5 per cent.

Table 1.8: Resource balances, Egypt

1. National disposable resources		27.9
GNP		23.0
Import surplus		3.9
Debt rollover		1.1
2. Gross rents and transfers		5.6
Aid and capital		2.6
Rents and quasi-rents		1.5
Oil		(1.1)
Canal		(0.4)
Remittances		1.5
3. Dependence	21%	

Resource availability

The total resources available to Egypt exceeded the GNP by a significant amount in the test year 1982. Total resources equal the GNP plus the import surplus and debt rollover, or LE 27,928 million. The total external resources, including gross receipts of aid and loans, amounted to LE 5570 million, so that rents and external capital contributed 21 per cent to total consumption and investment in Egypt. Most of this represented pure rents or unrequited transfers, since remittances, which are only partly rents, totalled only about 25 per cent of the gross amount.

Morocco and Tunisia

Table 1.9 contains similar data for Morocco and Tunisia. By now the reader will be familiar with the methodology, and I will spare him the details. In both cases adjustments are relatively small; however, in the case of Morocco, National Disposable Resources are quite a bit larger than GDP, mostly because of unrequited transfers.

Table 1.9: Morocco and Tunisia (1982)

	Morocco (1982)		Tunisia (1982)	
Gross domestic product (GDP)	88.5		3992	
Extractive rents		2.5		339
Remittances		5.5		170
Other factor income		1.3		−116
Non-depletable GNP	92.8		3707	
Capital and aid		15.1		461
National disposable resources	107.9		4168	

CONCLUSIONS

The economies of the Middle East are strikingly dependent upon exogenous or unrequited resources, to a degree which requires the use of more refined economic instruments in order to distinguish between expansion and growth and to establish bases for comparing them with other economies.

The first set of reinterpretations involves more precise definitions of income derived from wasting assets such as oil, or workers' remittances. Kuwait exemplifies the significance of the depletion adjustment which is needed in order to distinguish between revenue and income in the case of a wasting asset like oil. Its depletion-adjusted GDP is only 40 per cent of the nominal value.

Extractive rents are also collected by Egypt (oil), by Morocco (phosphates), and by Tunisia (phosphates and oil). In these cases, however, the adjustments are much smaller (see Table 1.10), reflecting the modest rents in phosphate production and the low levels of oil production in relation to the domestic non-oil sectors. The Tunisian and Egyptian incomes require a downward adjustment of 9 and 5 per cent, respectively, while that for Morocco is only 3 per cent.

Table 1.10: Comparative measures of income

	Jordan	Kuwait	YAR	Egypt	Morocco	Tunisia
Income adjustments	+24	−29	+38	+1	+3	−4
Rent	N	−60	N	−7	−3	−9
Capital	61	nr	24	12	17	12
Portfolio	N	+34	N	N	N	N
Remittances	+24	− 3	+38	+7	+6	+4

Egypt collects rents both from the Suez Canal and oil, but the income needs to be adjusted only for the oil rents, since the Suez Canal is not a wasting asset in any useful sense of the term. The rents from the Suez Canal must be separately noted in analysing dependency, because they are unearned in the technical sense that the net locational rent is not a payment to factors of production, so that it adds to the resources available to the government for redistribution.

The adjustments differ in sign and in magnitude, so that they must be analysed case by case. The diverse impacts of the adjustments are seen in the first line of Table 1.10. The net adjustment for Kuwait is downwards and is the result of three different elements working in different directions:

(1) A sharp downward correction for the oil rents.
(2) A small debit for outflows of workers' remittances.
(3) A sizeable increase because of the portfolio income which is included with the GNP.

The adjustments net effectively to zero for Egypt — the overall correction is plus 1 per cent — while there are small upward and downward adjustments for Morocco and Tunisia, respectively.

The extent of the dependence of the economies upon special resources — aid, mineral or other rents, and remittances — is also varied, but all are much more tied to exogenous unearned or unrequited resources than most countries. Aid alone is equivalent to 61 per cent of Jordan's GDP, while it makes up 24 per cent of North Yemen's and 17 per cent of Morocco's. Remittances equal 38 per cent of Yemen's GDP and 24 per cent of Jordan's, but only 4–6 per cent for Egypt, Morocco or Tunisia. In the case of Kuwait, the adjustment is negative, but quite small — only 3 per cent.

In all cases, however, the share of these exogenous resources in the GDP seriously understates their contribution to the level of national income, since the static calculation does not include the rentier multiplier, the multiplicative impact upon a host economy of infusions of unrequited resources. The contribution to GDP or income of the rents or quasi-rents will almost always be greater than the share in GDP or income.

The full scope of the multiplier mechanism can only be approximated. It depends upon how the funds are spent, how much of the spending leaks into foreign savings, remittances, or imports, which in turn depends upon the state of the economy. The multiplier also depends upon the extent to which labour and production capacity is available in the host country to meet the induced demand.

The preconditions for the working of the multiplier thus can differ. In Kuwait imports and labour are freely mobile, so the multiplier is relatively unconstrained. In Egypt, the YAR and the Maghreb until recently there was a pool of unemployed or underemployed labour which could be drawn into the workforce whenever disposable income was increased due to increased infusions of rents or aid.

More recently, however, economies like the Yemen and Jordan have shown signs of overheating, and the unearned resources or remittance receipts now contribute in a growing measure to local inflation, bidding up not merely the prices of non-tradeable goods, such as real estate, but also putting serious pressure on local wage levels.

Another measure of the fact that dependence is greater than the share of the rent in GDP is the fact that the rents pay for a disproportionate fraction of total imports or, indeed, total goods consumed in the host country. We observe that 69 per cent of resources spent in Kuwait in the non-oil sector are of exogenous origin, while in the YAR and in Jordan the share in the domestic economy is over 40 per cent.

This is equivalent to a very high share of the goods consumed or invested, since most of the domestic value added is in the form of non-traded services, such as government wages, public services, and commercial margins on imports of goods paid for by the exogenous resources.

Because the dependence upon exogenous resources is so large there are two distinct mechanisms contributing to the appurtenances of growth — one is the usual process of investment leading to a larger productive base and the second is the rentier mechanism, a process of expansion or illusory growth funded solely by growing expenditures of unrequited funds. It is critically important to distinguish between these two in order to measure real growth and thus to assess the economic prospects of these states.

2

The Rentier State in the Arab World

Hazem Beblawi

INTRODUCTION

The concept of a rentier state has gained renewed interest with the advent of the oil era and the emergence of the new Arab oil-producing states.

In a celebrated passage, Adam Smith distinguished between rent and other sources of income: wages and profit. 'Rent', says Smith, 'enters into the composition of the price of commodities in a different way from wages and profit. High or low wages and profit are the causes of high or low price; high or low rent is the effect of it' (Smith, 1960: 412). A rent, it is to be remembered, is not merely an income for landlords, but generally a reward for ownership of all natural resources. 'Mines, as well as land', affirms Ricardo, 'generally pay rent to their owners and this rent, as well as the rent of the land, is the effect and never the cause of the high value of their produce' (Ricardo, 1962: 590). The same applies to all natural and differential endowments: location, climate, etc. In its general usage, the term 'rent' is reserved for 'the income derived from the gift of nature' (Marshall, 1920). Rent in this broad sense exists in all economies, abeit in different degrees.

It is not the purpose of the chapter to discuss the economic concept of rent and its various forms: rent/quasi-rent, scarcity/differential rent etc. In modern economic analysis an efficient management of resources would call upon rent as much as on other factor prices. No value judgement is implied, rent is an economic price or factor income like any other price.

It remains true, however, that social scientists — including economists — suspect a difference between 'earned' income and effortless 'accrued' rent. Religious ethics, and then the capitalist instinct for work salvation, helped create a long tradition of hostility against non-earned income.[1] This was reflected in a deep-rooted mistrust of the economic profession against rent and rentiers. Classicial economists — Malthus apart — and later Marx have few kind words to say about rent and rentiers. Rentiers as a social group were thus assaulted by both liberal and radical economists as unproductive, almost anti-social, sharing effortlessly in the produce without, so to speak, contributing to it.

A rentier is thus more of a social function than an economic category, and is perceived as a member of a special group who, though he does not participate actively in the economic production, receives nevertheless a share in the produce and at times a handsome share. The distinguishing feature of the rentier thus resides in the lack or absence of a productive outlook in his behaviour.

It is important to emphasise here that it is the social function of the rentier rather than his legal status of private ownership, that is usually evoked with undertones of discontent. The contrast between the rentier and Schumpeter's entrepreneur is striking as well as instructive. Dynamic, innovative, risk-bearing, Schumpeter's entrepreneur is the antithesis of the rentier.

Such stereotype rentier is, of course, a caricature. In fact 'pure rent in the strict sense of the term is scarcely ever met with; nearly all income . . . contains more or less important elements, which are derived from effort invested' (Marshall, 1920: 350).

The emergence of the new oil states in the 1970s and their promotion to the forefront of world trade and finance resuscitated the concept of rentier economies. A windfall wealth of unprecedented magnitude in such short time revived the idea of unearned income, hence the epithet of rentier economies. The impact of the oil phenomenon on the role of the state and on economic behaviour in general has been so profound in the Arab world during the seventies as to justify special treatment. The concept of a rentier state is chosen for lack of better concepts to characterise the prominence of the oil economies in the Arab region.

A RENTIER STATE: ELEMENTS FOR DEFINITION

The purpose of an attempt to define a rentier state is not to reach an abstract notion of such a state but to help elucidate the impact of recent economic developments, in particular the oil phenomenon, on the nature of the state in the Arab region.

Certain characteristics should be kept in mind in view of the definition of a rentier state in our context. First, there is no such thing as a pure rentier economy. Each and every economy has some elements of rent. A rentier economy should be defined as one where rent situations predominate. This, of course, is a matter for judgement.

Second, and this is very important, a rentier economy is an economy which relies on substantial *external rent* (Mahdavi, 1970: 428). The externality of the rent origin is crucial to the concept of a rentier economy. The existence of an internal rent, even substantial, is not sufficient to characterise a *rentier economy*, though it could indicate the existence of a strong *rentier class* or group. A pure internal rent cannot be sustained without the existence of a vigorous domestic productive sector. In such a case, a rentier class is only one face of the coin, the other face would be a productive class. Internal rent is no more than a situation of domestic payment transfer in a productive economy. An external rent, on the other hand, can, if substantial, sustain the economy without a strong productive domestic sector, hence the epithet of a rentier economy.

Third, in a rentier *state* — as a special case of a rentier economy — only few are engaged in the generation of this rent (wealth), the majority being only involved in the distribution or utilisation of it. The distinction between generating wealth and its utilisation is not always clear. It can, however, be accepted that the creation of wealth is the cause of all other activities and the utilisation is only the effect. It is true that interactions always exist between various activities, blurring the cause-effect relation. In the case of the oil-producing countries, the role of oil revenues is so overwhelmingly obvious that it can be approximated to be the cause of other activities.

A rentier economy is thus an economy where the creation of wealth is centred around a small fraction of the society; the rest of the society is only engaged in the distribution and utilisation of this wealth. The respective roles of the few and the many can hardly be overstated for the concept of a rentier economy.

Accordingly, an open economy with high foreign trade is not a rentier state, simply because it relies on the outside world, even if it generates its income from natural endowment (e.g. tourism) in as far as the majority of the society is engaged in the process of wealth generation.

Fourth, a corollary of the role of the few, in a rentier state the *government* is the principal recipient of the external rent in the economy. This is a fact of paramount importance, cutting across the whole of the social fabric of the economy affecting the role of the state in the society. The role of the government as the principal recipient of the external rent is closely related to the fact that only few control the external rent. In fact, the 'economic power' thus bestowed upon the few would allow them to seize 'political power' as well, or else induce the political elite to take over the external rent from them without major political disruption. A predominantly rentier *state* will accordingly play a central role in distributing this wealth to the population. This brings us close to a distinction proposed by Giacomo Luciani, that is, between productive and allocative states (see Chapter 3).

Having characterised the main features of a rentier state, it is important to emphasise that the choice of such a concept is based on the assumption that such an economy creates a specific mentality: a *rentier mentality*. The basic assumption about the rentier mentality and that which distinguishes it from conventional economic behaviour is that it embodies a break in the work-reward causation. Reward — income or wealth — is not related to work and risk bearing, rather to chance or situation. For a rentier, reward becomes a windfall gain, an *isolated* fact, situational or accidental as against the conventional outlook where reward is integrated in a *process* as the end result of a long, systematic and organised production circuit. The contradiction between production and rentier ethics is, thus, glaring.

It is also assumed that the pre-eminence of the oil countries has not only brought to the fore a contradiction between production and rentier ethics, but more seriously, has meant the prevalence of the rentier economy. A decade of the oil era shows that the whole of the Arab world, oil rich as well as oil poor, is becoming a sort of oil economy with various undertones of rentier mentalities. This development has affected the role of the state in the whole Arab world.

THE OIL STATES: MULTILAYERS OF RENTIERS

The Arab oil states represent, it has been said, the example *par excellence* of rentier states. With oil exports' revenues, the Arab oil states depend on external rent. Oil revenues represent more than 90 per cent of budget revenues, 95 per cent or more of exports. Also, only a small fraction of the population is involved in the generation of oil revenues, the rest being engaged in the use of the oil wealth. No more than 2 to 3 per cent of the labour force is engaged in the production and distribution of the oil wealth, which adds 60 to 80 per cent to the GDP, as conventionally measured. Nevertheless, this fact does not preclude genuine productive activities outside the oil sector. Finally, oil revenues (rent) accrue directly to the state or the government. The Arab oil states thus correspond to our definition of rentier states. The role and the nature of the state has been greatly affected by this fact.

The state or the government, being the principal rentier in the economy, plays the crucial role of the prime mover of the economic activity. Rent that is held in the hands of the government has to be redistributed among the population. Special social and economic interests are organised in such a manner as to capture a good slice of government rent. Citizenship becomes a source of economic benefit. Different layers of beneficiaries of government rent are thus created, giving rise, in their turn, to new layers of beneficiaries. The whole economy is arranged as a hierarchy of layers of rentiers with the state or the government at the top of the pyramid, acting as the ultimate support of all other rentiers in the economy. It is important to add here that the rentier nature of the new state is magnified by the tribal origins of these states. A long tribal tradition of buying loyalty and allegiance is now confirmed by an *état providence*, distributing favours and benefits to its population.

The conventional role of the state as provider of public goods through coercion — mainly taxation — is now blurred in the Arab oil states by its role as a provider of private favours through the ruler's benevolence. Public goods and private favours have thus gone together in defining the role of the state.

With virtually no taxes, citizens are far less demanding in terms of political participation. The history of democracy owes its beginnings, it is well known, to some fiscal association (no taxation without representation). The government's budget in the oil states remains a one-sided document, an expenditure programme, a promise to spend money and distribute benefits to the population with virtually no levy on them in terms of taxes or similar impositions.

Kuwait was probably the one to introduce into the Gulf area the concept of distributing part of the oil wealth to the population which eventually evolved into that of the welfare state. The shrewd Sheikh Abdullah al-Salim of Kuwait made the fundamental decision that he (the state) should share part of the oil rent with the population. The role of the government was thus defined as being primarily a partial distributor of oil wealth among the population. In his quest to create vested interests among notable Kuwaiti families round the new states in the early 1950s, Sheikh Abdullah al-Salim introduced the system of government land purchase, at prices hardly related to market value. No more than a decade or two later, the same system was adopted by other Gulf states: Qatar and UAE. In Saudi Arabia, the practice of land gifts was already in force since the 1920s and 1930s. With the annexation of Hijaz in the pre-oil era, the pilgrimage royalties (another source of rent) gave Ibn Saud the means to distribute favours (land). The government continued to grant land to relatives, ministers and anyone else it wished to favour. The recipients sometimes sold their land to private developers, but the biggest and most generous buyer was always the government itself (Field, 1984: 99). The early relationship between oil revenues and land speculation — the proper domain for rent and rentier — can be seen here. Later developments, as we shall see, made land as well as shares a prosperous source of rentier speculation.

Of course, governments in the oil states outgrew their role as distributors of favours and benefits and embarked on the modern function of providing public goods and services to their population. Governments are providing their populations with a wide range of genuine public goods and services: defence, national security, education, health, social security, employment, an impressive network of infrastructure, etc. The level and quality of these public goods and services are usually adequate, sometimes excellent. They are also provided free or at very low cost to the beneficiary. However, the original sin remains, sometimes open but mostly latent, thus vitiating the provision of these public goods. It is reported that 'if a prince heads a ministry or some other government department, it is

accepted that he is entitled to draw on the budget of that department or take a share of its spending in major projects' (Field, 1984: 101–2). To a certain degree, all government contracts are seen as royal favours. Their origin as part of the ruler's benevolence does not fail, thus, to exhibit their peculiarities.

The distinction between public service and private interest is very often blurred. There seems to be no clear conflict of interests between holding public office and running private business at the same time, and it is not infrequent to use the one to foster the other. Sometimes high-ranking public officers (ministers) take the trouble to form their private businesses under the names of their sons, brothers or similar *prête-noms*. In fact, huge development projects, joint ventures, agents, tenders and awards of hundred million — sometimes billion — dollar contracts have provided opportunities for those in public office to use their positions for private gain (Beblawi, 1982: 216). The practice varies from one oil state to another; it is most conspicuous in Saudi Arabia and least apparent in Kuwait. In Saudi Arabia, contracts are given as expression of royal gratitude. Contract brokers, commission fees for the ruling elite, lobbying the royal family, etc., are not unusual practices in the Gulf areas. Some names earned notorious reputations in this respect; Adnan Khashoggi, Mahdi Tajir, Princes Muhammad Bin Abdel-Aziz, Muhammad Fahd, Sultan Bin Abdel-Aziz are only the most visible (Field, 1984).

The government not only distributes benefits and favours to its population, but it is also the major and ultimate employer in the economy. Every citizen — if not self-employed in business and/or not working for a private venture — has a legitimate aspiration to be a government employee; in most cases this aspiration is fulfilled. Though utterly free enterprise oriented, the number of government employees in the oil states is only matched by socialist-oriented states. Civil servant productivity is, understandably, not very high and they usually see their principal duty as being available in their offices during working hours (*Al Dawam*).

If governments are the principal rentiers in the Arab oil states, they are by no means the only ones. Trade and business professions in many cases consist in no more than taking advantage of special situations entrusted to them by law or fact. Merchants are favoured by existing laws. It is the law in oil states that foreign companies may sell their products only through local agents. Most states insist that foreign companies should also take local merchant partners if they want to operate on their soil. In any case, foreign companies find it difficult to deal with local bureaucracy without local partners or sponsors (Field, 1984). The big trading houses, the family conglomerates that are involved in all business matters owe their wealth, in one way or another, to some rent situation. Being a sales agent if the classical road to business and hence to wealth. Big family names in the oil states are intimately related with one or more brand names; e.g. in the car distribution business we have Alghanim with GM in Kuwait; Juffali with Mercedes in the truck business in Saudi Arabia, and Bisher and Al-Kazmy with the same company in Kuwait; Futtaim with Toyota in Dubai and Al-Sayer with it in Kuwait; Galadari with Mazda in Dubai . . . The list is long indeed ('Arabian Trading', *Financial Times*, 23 January 1985).

Not only should distribution agents be exclusively nationals but also the practice of most professions and trades be restricted to nationals. This legal restriction has been established to counter the well-known shortage of professional and skilled labour. The result is the appearance of a peculiar function, that of the sponsor, *al-kafil*. This is someone, a national of course, who offers his name to expatriates to exercise various trades and professions under his name, in return for a share of proceeds (rent). The *kafil* mentality, where citizenship is becoming a sort of financial asset and hence a sorce of income, transcends national/expatriate relations, to become, even among nationals, a normal feature of everyday life. For example, in Kuwait, during the euphoria of the stock market, it was the habit of the government to allocate a certain number of shares for each Kuwaiti citizen in new public shareholding companies. A very active trade in 'citizenship' (*ganaci*) took place, where those not interested in buying their shares would sell their rights — as attested by the citizenship certificates — to others. Citizenship is not only an affective relation between man and his homeland, it is also, or primarily, a pecuniary relation.

Oil rent thus gave rise, in turn, to a secondary wave of rent generations: second order rents. Two areas seem to distinguish themselves as rent centres: real estate and stock market speculation.

Land, it was said, has played a major role in the process of trickling down oil money from governments to private individuals. The readiness of governments to purchase land at higher

prices sustained ever-growing prices for real estate. A very profitable business was created round land speculation with some very active brokers. Government was always prepared to act as the ultimate buyer.

The ingenuity of some land brokers soon introduced a very powerful instrument to keep real estate prices high even in face of credit squeezes, liquidity shortages and/or government's momentary reluctance to inject money into land purchase. This was the so-called forward market or post-dated cheque system. Kuwaiti brokers masterminded these new techniques and extended them imaginatively — and dangerously — to stock market transactions. Growing prices for real estate and stocks cannot be sustained indefinitely unless they are matched by a growing injection of liquidity to back up demand for these assets. Sooner or later there comes a time when liquidity is not forthcoming and the market comes to a halt if not a collapse. This is where the role of the forward transaction which provides the market with a new instrument for credit creation at the disposal of the speculators, bypassing the banking system, comes in. Each speculator becomes something of his own bank, capable of adding to liquidity by issuing his own IOUs which are more or less accepted in the market (real estates, stock market). In final analysis, liquidity is created through bank intermediation in the exchange of obligations. With forward transactions and the issuing of post-dated cheques, speculators assume the role of informal banks and pay for their deals by increasing their own liabilities.

A forward deal is a spot deal with credit, where the buyer gets the commodity (shares, land, etc.) at the time of the transaction and pays forward with a post-dated cheque with a premium (an interest rate or rather a usury rate) which can vary between 50–200 per cent per annum. At maturity, he can either roll over the cheque with another more attractive premium (an offer which the other party usually cannot refuse), or if his creditor refuses the offer, he can just borrow from the market by buying another commodity (shares) on a forward basis (another post-dated cheque to a third party) and selling it on the spot market to get the cash to pay his first creditor. The game can continue indefinitely in as far as dealers are prepared to accept each other's post-dated cheques. In fact, there was a general tacit agreement to continue the game, with everyone issuing and receiving post-dated cheques at the same time. Cheques were rolled over and every second new cheques were added to the market thus giving the illusion of ever-growing fortunes. These were the rules of the mirage wealth creation or the big casino later known as Soukh el-Manakh. A money machine — the dream of all speculators — was invented and nothing could stop the attractiveness of Soukh el-Manakh. Young graduates left their jobs for the new gold mine, early retirements took place, 'creative' companies invested heavily in the stock market, thus scoring huge profits and offsetting their losses in their normal lines of business. Even off-shore bankers and more sober institutions and professionals were tempted by the new phenomenon. New companies were created every day, giving rise to new share-offerings on the market and accordingly fresh opportunities for new wealth. Social life was also transformed: politics was no more a subject for discussion, and even gossiping, a favourite pastime, was fading away. The new and almost only talk of the town was centred on share prices and the new shares coming on to the market.

The end of this fancy world is well-known to all. The Soukh el-Manakh dream turned into a nightmare. In July 1982 some dealers, sensing the imminent difficulties of the market, began to cash their cheques ahead of time. A minor crisis was thus turned into a full-scale crash. The age-old adage that what goes up — artificially — must come down, was finally vindicated in Kuwait (Beblawi and Fahmi, 1984: 173).

The government role in the development of this speculative activity can hardly be overestimated. Not only did governments indirectly help speculations, but in many instances were directly involved in supporting speculative markets. When the Kuwaiti stock market faced its first setback in 1976/7, the Kuwaiti government was prompted to bail it out. Even in 1982, when the Kuwaiti government refused to repeat the role it played in 1976/7, it compensated the so-called small investor — defined as one owed no more than KD 2 million ($6.75 million): no small reward for speculators. In both cases, a number of key members of government and parliament were deeply involved in the stock speculations.

The juxtaposition within Arab oil states of a rentier economy and a productive economy is paralleled by the coexistence of two social communities: nationals and expatriates. Expatriates are called upon to help fill the gap in available manpower in oil states. More often than not, these expatriates assume productive

activities to satisfy the growing needs of the society. They earn their living by the work they do. The relationship work-reward is actually maintained in their case. Rent economy, on the other hand, is normally confined to nationals; the privileges it conveys hardly extend to expatriates.

The contrast between the two communities is striking as well as revealing. Nationals live more in a rentier economy and associate with its financial manna all the political rights of citizenship. On the other hand, although earning their living in a more productive manner, the impact of the rentier economy on expatriates is far from negligible, giving rise to serious corruption of the productive system and work ethics. Even if they form the core of the productive manpower, expatriates nevertheless remain alien to the body politic. Though they serve the country, live — and also die — on its soil, they are not part of it. Expatriates are thus part of the labour force but not of the society. The material life of expatriates is usually comfortable and by no means comparable to the living conditions in their homeland. Their emotional life is, none the less, unstable, terribly wanting in security and lacking a sense of belonging.

The political cleavage between the two communities widens as the economic rent to citizens increases. Restrictions on exptriates' professional mobility as well as their political integration increases with the increase in the oil wealth. The contrast between the less abundant years of the 1960s and the more affluent 1970s is very significant. Regardless of the vocal rhetoric of Arab nationalism, in the 1970s the political elite in the oil states, no matter whether right- or left-wing, advocated a narrow local nationalism and restirictive benefits to expatriates.

THE NON-OIL STATES: SEMI-RENTIERS WITHOUT OIL

The Arab non-oil states are by no means rentier states in the sense previously outlined. The predominance of the oil phenomenon on the whole region is, however, such that many non-oil Arab states are showing increasing signs not dissimilar to those witnessed in oil states.

Let us first draw attention to the fact that because of oil wealth, the whole Arab area — oil rich as well as oil poor — has assumed strategic value in the world chessboard. The area as a whole, particularly neighbouring countries, have gained location rent.

Military and political aid to preserve and/or introduce super-powers' — as well as mini-powers' — influence in the area, is a major source of external rents to many states. Otherwise remote and poor states (e.g. Somalia) would hardly receive alternately Russian and American aid. In the 1960s Egypt received the highest Soviet aid to a foreign country, to become, together with Israel, the highest American aid recipient in the 1970s and 1980s. Syria, Jordan and South Yemen are other examples.

Rhetoric aside, inter-Arab aid was related, to some extent, to its effect on the stability and tranquillity of oil rent in oil states. Very often Arab aid to fellow Arab states was used in much the same way as domestic redistribution of oil revenues: to buy allegiance or rather avoid trouble. Pan-Arabism and Arab money were, to a great extent, and in different hands, the stick and the carrot, used to bring about a very subtle equilibrium in sharing oil rent. By conferring and/or withholding super-legitimacy over individual states, the advocates of pan-Arabism used their political clout as a source of financial aid. By distributing and/or promising aid, the carrot in the hands of the oil states helped them buy peace and stability. Arab finance was thus more a counterpart than a complement to pan-Arabism. It is no wonder, then, that Arab financial flow to Arab brothers coincided with the retreat of the pan-Arab system after the 1967 war, which 'marked the Waterloo of pan-Arabism' (Ajami, 1978/9). In the wake of the October 1973 war, it was Sadat and Assad — 'revisionists' or 'correctionists' of the pan-Arab doctrine — who obtained Arab finance. With the decline of Egypt's role in mobilising Arab public opinion, particularly after Camp David, the Baghdad Summit relieved the Arab oil states of their financial commitments to Egypt, shifting them to more assertive Iraq, Syria and the PLO. The subsequent Iraq-Iran war proved to be quite a drain on their treasury. The Baath party, which is in power in both Iraq and Syria, though two competing factions, is notorious for its unscrupulous and ruthless practices *vis-à-vis* its opponents. Some oil states — Kuwait and UAE for example — had the privilege of actually experiencing firsthand such practices when a number of attacks and/or bombings took place on their territory. They had, of course, the tact and discretion to turn a blind eye to these 'accidents'. But the message is clear.

External location rent is also evident in so-called transit countries (Mahdavi, 1970). Suez Canal revenue and oil pipeline royalties are major revenue sources to some countries, e.g. Egypt and Syria.

Workers' remittances are becoming one of the major foreign exchange sources in some non-oil states. Yemen is a well-known example where remittances represent more than 85 per cent of GDP. Workers' remittances are becoming the biggest single source of foreign exchange in Egypt as well. In Syria, Lebanon, Tunisia, Algeria and Morocco, workers' remittances play a very important role in their balance of payment adjustments. It is not easy to equate workers' remittances to external rent. From the worker's point of view, he is earning his income at the cost of effort and work. From the recipient country's point of view, remittances are, nevertheless, more akin to aid or non-requited money transfers.

All told, various elements of external rent play an increasing role in non-oil Arab states. In Egypt, for example, it is estimated that about 45 per cent of its GDP is represented by exogenous — read rent — elements in the form of oil revenues, workers' remittances, foreign aid, Suez Canal revenue and tourist expenditure. It is also to be noticed that most of these revenues accrue directly to the state or the government. The epithet of semi-rentier state is, thus, not far-fetched.

The semi-rentier nature of non-oil states is not without its effects on the role of the state and on citizens' behaviour. Government favours are now embodied in a welfare doctrine. Subsidies of all kinds pervert the economic system. A huge bureaucracy, sort of a new rentier class, is getting a substantial slice of the government's accrued rent. Though individually very low-paid, civil servants as a social group are a very expensive element in view of their contribution to the country's productivity (it is often thought that they contribute negatively to the growth of the economy).

It is also interesting to see how each source of external rent has bred its own chain of second-order rentiers. In Egypt, for example, a prosperous trade has been developed around workers' movement to the Gulf. Also, money dealers have grown immensely to process workers' remittances. American aid helped create a flourishing consultancy — legal, technical, economic, etc. — business to prepare proposals for aid consideration. A new social class — lawyers, consultants, financial analysts, lobbyists, brokers, etc. — is on the rise everywhere.

Finally, when not direct recipient of the rent, the state, because of its external origin, quite often tactfully courts the rent earners. Suffice it to observe tax exemptions and other incentives given to workers' remittances, foreign banks, tourism, etc. Governments do their utmost to sweeten their normal coercive practices. They are willing to appeal and not to impose. Economic liberalisation, *infitah* or whatever, is everywhere.

CONCLUSION: AN OIL ARAB ECONOMY

It seems from the foregoing that the oil phenomenon has cut across the whole of the Arab world, oil rich and oil poor. Arab oil states have played a major role in propagating a new pattern of behaviour, i.e. the rentier pattern. Oil as the primary source of rent in the Arab region has generated various secondary rent sources to other non-oil Arab states. To the first-order rentier oil states is thus added a second-order non-oil rentier strata. The impact of oil has been so pre-eminent that it is not unrealistic to refer to the present era of Arab history as the oil era, where the oil disease has contaminated all of the Arab world. Be it oil revenue, or workers' remittances, or strategic location, or *el-kafil*, or Soukh el-Manakh, they are all consequences of the oil phenomenon, and have been accompanied by a serious blow to the ethics of work. Income is no longer a reward of serious and hard work, it is very often related to special circumstances, chance, location, etc. In a word, we are living in a rentier universe which has affected both the state and the citizen.

NOTE

1. 'The religious valutaion of restless, continuous, systematic work in a wordly calling, as the highest means to asceticism, and at the same time, the surest and most evident proof of rebirth and genuine faith, must have been the most powerful conceivable level for the expansion of that attitude toward life which we have here called the spirit of capitalism.' Weber (1959: 127).

3

Allocation vs. Production States: A Theoretical Framework

Giacomo Luciani

Possibly nowhere more than in the Arab world is the crucial importance of the economic foundations of the state as clearly borne out by historical developments in contemporary times. The contrast between the six thousand year old record of centralised state structure in Egypt and the total lack of any stable authority structure in the Arabian Peninsula until well into the present century could not be more marked. Ecological and economic factors have conditioned the existence of state structures and the geographic reach of their authority throughout Arab history.

Thus one does not need to accept any schematic and deterministic model to point to the importance of the economic foundations of state structures in shaping the basic parameters of Arab politics. Economic realities condition the total resources that any single state structure can muster — and until only a few decades ago these resources were in some cases simply insufficient to permit the consolidation of states that, as a consequence, disappeared as fast as they arose. Second, the nature of the predominant productive processes conditions certain basic parameters of existing state structures, such as the degree of centralisation and the tendency to authoritarian rule. Finally, the nature of the sources of income of the state influences the basic rules of political life in each individual country. While this chapter will be devoted primarily to a discussion of the latter aspect, the first two aspects must also be kept in mind, as they are equally important.

In the preceding lines we have already implicitly made use of a distinction that must be defined for the rest of this chapter. In

English usage the term state is almost always meant to indicate an independent country as well as the structure of power and authority that exercises the attributes of sovereignty within it. In this chapter we address the question of the nature of the state only in the latter of the above mentioned meanings.

ECONOMIC REALITIES AND THE 'SIZE' OF THE STATE

A state structure will tend to be stable in history if it commands sufficient resources to guarantee its own survival. This implies primarily the ability to resist outside aggression, but it implies as well the ability effectively to exercise its authority over the territories that fall — or are generally believed to fall — under its sovereignty. The resources that are needed to enforce state authority are greatly variable as a function of structural (geographic, demographic) and political realities, and the ability to resist outside aggression is also a function of the intensity of such aggression. Thus it is difficult to say whether a given economic system does or does not offer the potential to sustain a stable state structure. Yet it is evident from Arab history that in many cases, states could be wiped out when exposed even to small-scale aggression, and in other instances states were in fact not able to exercise their authority over territories that they nominally controlled and that no other state claimed for itself.

It is only with the colonial era and the valorisation of oil resources — two interconnected developments — that state structures appear to have consolidated and extended their authority over their entire territory. In many cases, the colonial state structures were the first to effectively rule their claimed territories and almost all the state structures that existed in Arabia until World War II could only survive thanks to British subsidies. Even after World War II, a fortuitously independent Libya could not really sustain a state structure until oil exports began in the late 50s. Still in 1960, British aid and American payments for the leasing of the Wheelus base accounted for 35 per cent of Libyan GNP and substantially all the state's revenue (Luciani, 1976: 121–3).

Oil has drastically changed the picture. In most cases, it has provided the weaker state structures with abundant financial resources. In other cases, states in poor and weak countries, while not blessed with oil revenues, still manage substantially to

increase their income, by encouraging migration or otherwise tapping foreign resources, both regionally and internationally. Thus today it is very rarely the case that the very existence of a state structure is endangered by the lack of resources; still, the relative importance of the resources supporting each state is greatly variable.

One is tempted to believe that differences in state income per subject (i.e. *per capita*) reflect differences in *per capita* GDP, on the basis of the assumption that the ability of individual states to appropriate a certain share of GDP is a constant in the short term. Yet this is certainly not the case for the oil-producing countries, where the causational chain is inverted, and state income determines GDP rather than the other way round. In these countries, differences in *per capita* GDP simply reflect the variable income opportunities and spending preferences of each state structure — indeed state income cannot in any meaningful sense be considered as being part of GDP until it is actually spent, and then only in so far as it is spent domestically.

CAN ONE SPEAK OF 'HYDROCARBON SOCIETIES'?

The stability of state formations is increased if, beyond being able to appropriate resources for their own ends, they also play an economic role which objectively increases the sum total of resources available to the country that they run. While this is, in itself, neither a necessary nor sufficient condition for stability of state formations, it is reasonable to expect that states that perform a useful economic function will be more easily accepted in the specific form and configuration that they take. Thus the character and behaviour of state formations is influenced by the prevailing features of economic life in the countries that they rule.

With reference specifically to the Middle East, the importance of water as long as the prevailing economic activity is agriculture has repeatedly been noted. There is, of course, Wittfogel's stress on hydraulic societies (1957: 48–9). His argument appears to us today greatly overextended, and it has been criticised from a historical point of view. Yet, it is difficult to deny, as we look at the history of what is today the Arab world, that the extraordinary resilience of state formations based in the Nile and the Mesopotamian valleys, respectively, as contrasted to the extreme variability of state definitions elsewhere, has a great deal to do with water and irrigation.

Yet the importance of water and its availability or lack of it in shaping political institutions and political life, and ultimately dictating the essential characters of state formations, does not necessarily point in the direction of Wittfogel's argument. More recently numerous authors, and especially anthropologists, have pointed to the importance of water management in shaping the social and political life of specific communities (Eickelman, 1981: 48–72).

The political impact of oil may be said to be in many ways similar to that of water, and at the same time different in a few crucial respects.

Oil, of course, is a liquid. This is more than a superficial coincidence because it means that the production and transportation of oil is best effected through the creation of an integrated network of hydraulic installations. There is an intrinsic need for centralised coordination: the latter was often provided by non-state entities in the industrial countries and internationally (e.g. Standard Oil before 1911, the informal 'understanding' between the major international oil companies thereafter, or regulatory agencies such as the Texas Railroad Commission). But in the Middle East no such entities were available indigenously and the task was viewed naturally as pertaining to the state.

Furthermore oil, just as complex irrigation, requires a 'specific type of division of labour' (Wittfogel, 1957: 22): one which clearly defines a technocratic layer that has the geological, chemical and financial knowledge necessary successfully to manage oil operations.

Another similarity is that oil, like water, is found in 'basins' and 'provinces'. While the need for integrated management is felt *strictu sensu* only at the level of the individual field, much can be gained through coordination at a higher level as well. This has had consequences over the territorial definition of Arab states: not only did certain demarcations become very contentious, but others almost ceased to be. Regions with no oil shelved the secessionist tendencies that they might have cherished in past times (Hijaz) or accepted federal arrangements with oil-rich neighbours (the United Arab Emirates); or the central location of the oil basins compensated for strongly rooted centrifugal forces. In the case of Libya, the three regions of Tripolitania, Cyrenaica and the Fezzan were effectively glued

together by the fact that most oil lies squarely between them.

But there are important differences as well. A first crucial difference between oil and water is that the former does not require the mobilisation of large numbers of the population. Quite to the contrary, oil production is a highly automated business, in which few are employed, and a relatively high percentage of those few are specialised full-time labour. The vast majority of the population is not involved at all in oil operations.

A second capital point is that oil, differently from water, is of no immediate interest to the survival and well-being of the vast majority of the domestic population. To be sure, oil products are consumed, but direct access to oil is not important *per se*, as direct access to water was and still is. What is important is access to oil *revenue*, that enables the consumer to buy a wide array of goods, including oil-derived products. Thus the vast majority of the domestic population is not involved with oil either as far as production or as far as utilisation is concerned. Their interest is in oil revenue, i.e. it is mediated, and mediated by the state.

A very important corollary of the second difference is that oil is mostly utilised abroad. Be it in crude or refined form, oil has value only to the extent that it is exported. Oil is not traded domestically in the oil-producing countries. Because oil valorisation implies a relationship with the rest of the world, it tends naturally to fall within the responsibility of the state and creates solidarity among its subjects.

Thus the specific characteristics of oil production and trade may well be said to have an impact on the stability and configuration of state formations. Yet it would be a mistake to follow Wittfogel's lead and propose a theory of the 'hydrocarbon society'. There is a distinct danger of exaggerating the argument and overlooking the fact that oil, just as water, is not the only significant dimension.

The point is that in the latter decades many aspects of economic life have tended to increase the economic role and impact of the state. Independently of the ideological orientations of each government, international realities have forced individual states into taking some fundamental steps such as issuing a fiduciary monetary instrument to be used within their boundaries or adopting complex economic legislation. While in most cases foreign trade has always been regulated, the significance of such regulations has increased because of the growing importance of international trade on commonly expected standards of living. Furthermore, in most instances the state vested in itself the responsibility for the upkeep and improvement of basic infrastructures: roads, transportation, mail, telephone, power, water, etc., to the point that today hardly any economic activity is conceivable which is not in someway related to and conditioned by the active presence of the state.

The tendency towards a direct state role is, of course, very significant from the political point of view. State formations that appeared to be entirely artificial and haphazard at the time of their creation 50 years ago or less are nowadays a deeply-rooted reality which would be quite difficult to modify. Thus any attempt to portray oil-producing countries as hydrocarbon societies would be an unacceptable simplification.

OIL AND THE NATURE OF THE STATE

While we should not speak of hydrocarbon societies and states, it is a fact that oil production appears to have a strong and decisive influence on the nature of the state. It does so through its effects on the structure of state revenues and the ratio between revenues that are obtained domestically and revenues that are obtained from abroad.

The key factor in this discussion is a precise understanding of what it is that makes the difference. Sometimes, a decisive importance is attributed to the fact that oil is the source of state income and that oil revenue includes a predominant rent element (Stauffer, see Chapter 1 in this volume). Hence the concept of 'rentier state' which is sometimes adopted to characterise the state in oil-exporting countries. While this concept captures the essence of the problem, a certain number of clarifications are needed:

(a) there are other rent-like sources of revenue which accrue directly to the state besides oil: thus rentier states are not necessarily oil exporting states;
(b) some important flows of income containing a rent component do *not* accrue directly to the state, in which case we should not speak of a rentier state, although we may well characterise the economy at large as being rentier, in the sense adopted by Beblawi (Chapter 2) and Abdel-Fadil (Chapter 4);
(c) it is essential that the income of the state not only be in the

nature of a rent, but also be earned abroad; if it were earned domestically the nature of the state would not be substantially affected.

It is for these reasons that I prefer to propose a new categorisation that, instead of looking at the nature of the income of the state, looks at its origin, domestic or foreign. The essential impact of oil production and exports is that they free the state from the need of raising income domestically. It is oil exports that play an essential role in this respect even more than oil production *per se*: the state in a country in which a lot of oil is produced but none exported may or may not be called rentier, but does not appear to be essentially different from any other state whose income depends on domestic sources. In both cases it is the overall strength and productive capacity of the domestic economy that conditions the income of the state. On the contrary, if oil is mostly exported, and the income of the state is mostly linked to the exportation of oil, then that state is freed from its domestic economic base and sustained by the economic base of the countries which are importing its oil.

Thus if we look at the origin of state revenue, we should speak rather of 'exoteric states' — being states predominantly based on revenue accruing directly from abroad — and 'esoteric states' — predominantly based on domestic revenue and taxation. Yet a different way of looking at the same distinction may be more enlightening, and this relates to the predominant function of the state. From the latter point of view the relevant distinction appears to be one between 'allocation' and 'production' states, depending on which of these two functions — mere allocation or production and reallocation — is the necessary task of the state.

A rentier or exoteric state will inevitably end up performing the role of allocating the income that it receives from the rest of the world. It is free to do so in a variety of ways: among the various purposes for which money is spent, the strengthening of the domestic economic base may be included, but not necessarily so. Even if this happens to be one of the goals of the state, as long as the domestic economy is not tapped to raise further income through domestic taxation, the strengthening of the domestic economy is not reflected in the income of the state, and is therefore not a precondition for the existence and expansion of the state.

On the contrary, whenever the income of the state is based on tapping the domestic economy through whatever assortment of fiscal instruments, the state can grow and perform an allocative function only to the extent that the domestic economy provides the income which is needed to do so. Growth in the domestic economy is one of the various 'luxuries' that the state can buy with its oil income in one case, it is an essential precondition for its existence and growth in the other. Clearly, all states aim at performing an allocative function, because in a sense this is what politics is about; and all states perform some allocative function. However for those that depend on income from abroad, allocation is the only relationship that they need to have with their domestic economy; all others ride their domestic economies.

Besides oil, other sources of income from abroad accruing directly to the state are transportation infrastructures of an international relevance and aid, be it economic, military or political — although the fact that it is sometimes in kind or tied limits the freedom to allocate it among different alternative purposes.

On the other hand, taxation on international trade is not a source of income from the rest of the world because the burden of such taxes falls on the domestic consumer or producer, not on the foreign importer or exporter. Neither are migrants' remittances a source of income from the rest of the world because they belong to the migrant, not to the state. The state may attempt to tax the income of migrants, but is in no position to do so before it is repatriated. It is only after remittances have entered the domestic economy (and generally not immediately after because of the need to encourage migrants to repatriate their income) that they can be taxed and become a source of income for the state. By then, the state is taxing the domestic economy. In fact, the importance of migrants' remittances is what imposes the distinction between a rentier economy and an allocation (or rentier) state: whenever remittances are important, this tends to give a rentier character to the economy as a whole, but the economic base of the state is not changed.

We may define allocation states as all those states whose revenue derives predominantly (more than 40 per cent) from oil or other foreign sources and whose expenditure is a substantial share of GDP.

The primary examples of allocation states are found in the Arab Gulf countries. In Kuwait, oil income alone accounted for 62 per cent of total revenue in 1982, down from 84 per cent in 1980; however, if investment income from abroad (31.8 per cent

of total revenue in 1982) is added, the share of total revenue accruing from foreign sources reaches as high as 94 per cent. According to conventional standards of national accounting, government revenue reached a peak of 94.2 per cent of GDP in 1981, but fell thereafter as oil revenue declined more rapidly than GDP. Before 1982, government revenue was considerably larger than expenditure, but the difference was reduced thereafter, as expenditure increased while revenue shrank. Government expenditure reached a peak of 53 per cent of GDP in 1982, and declined thereafter. Finally, if GDP figures were to be revised in accordance with the accounting standards suggested by Stauffer, government expenditure would account for a considerably larger share of GDP (or, in Stauffer's terminology, ND-GDP). Yet, if we adopt Stauffer's approach, we should also revise government income, and define a 'permanently sustainable' income level by detracting oil rent — which would wipe out government income almost entirely. These accounting exercises are useful in understanding the nature of the relationship between government income and GDP in a country like Kuwait.

Most Arab Gulf countries are in the same position. In Oman, government expenditure was 55.5 per cent of GDP in 1978. It declined to a minimum of 40.6 per cent in 1980, and grew thereafter to reach 47.3 per cent in 1982. The Omani budget has shown a tendency to close with a deficit. Revenue from oil and grants from abroad account for 90 per cent (1982) of total revenue.

In Saudi Arabia, in a year (1984) of weak petroleum prices, oil revenue accounted for 64 per cent of total revenue and income from investment abroad generated approximately another 18 per cent. Thus the government solidly depends on income from abroad, but at the same time it accounts for a smaller share of GDP. In 1977 — when the budget closed with a solid surplus — government revenue accounted for 66.3 per cent of GDP; this ratio fell to 50.1 per cent in 1981. As expenditure overtook income in the following years, the composition of GDP also changed and starting in 1983/4 the private (non-oil) sector generated more than half of GDP.

Outside of the Gulf, Libya is likely to fall into this category, but Libya's budget is drawn very unconventionally, making comparative analysis impossible.

Finally, both Jordan and Syria fell into the allocation state paradigm, at least temporarily. In Jordan, government expenditure fluctuated around 50 per cent of GDP according to IMF statistics (1981: 52.4 per cent; 1982: 45.1 per cent); but inclusion of public independent entities would bring the ratio to an impressive 85 per cent (*MEED*, 4 January 1985: 12). In the case of Jordan, grants from abroad started in a significant way in 1979, when they reached a peak value of 54.4 per cent of total revenue. Thereafter they declined, and in 1984 they were budgeted at 24.1 per cent of total revenue. In Syria, grants accounted for 40.9 per cent of total revenue in 1979, and 30 per cent in 1981; it is however, not clear whether all grants are included in the budget. Syrian government expenditure was 38.8 per cent of GDP in 1979 and 38.1 in 1981.

In the case of Algeria, hydrocarbon revenue (including gas) accounts for a diminishing share of total revenue (67 per cent in 1981, 53 per cent in 1984) (*MTM*, 24 February 1984: 429). Government spending accounts for 84.8 per cent of GDP. Algeria is, thus, a borderline case.

So are, for different reasons, Bahrain and Iraq. In both cases oil and grants are the major source of revenue (Bahrain: 78.5 per cent of GDP in 1982; for Iraq no recent data are available), but government expenditure accounts for a relatively smaller share of GDP: in Bahrain, it was 40 per cent in 1977 and declined to 34.6 per cent in 1981, while in Iraq government revenue was 26.8 per cent of GDP in 1978 and 25.3 per cent in 1980.

Minor oil exporters with relatively large populations, such as Egypt and Tunisia, cannot be called allocation states. In Egypt, non-tax revenue, which includes oil revenue as well as revenue from the Canal, but also includes some typically domestic revenue, accounts for 23.8 per cent of total revenue, while government expenditure is 47 per cent of GDP. The latter fact is far from extraordinary: the qualitatively important fact is that this level of expenditure significantly exceeds revenue, and revenue, in turn, is largely derived from the domestic economy. In Tunisia, oil revenue in 1981 was 18.6 per cent of total revenue and pipeline fees and grants added only 0.7 per cent. Again, government expenditure was significantly larger than revenue, and accounted for 37.3 per cent of GDP (1981). In other Arab countries such as Morocco, the relative importance of foreign sources of income is even less.

Thus it is seen that the Arab world is fairly clearly divided between allocation and production states, and the former comprise countries that are not oil producers, but receive substantial income from abroad on different grounds.

POLITICAL RULES OF THE GAME IN AN ALLOCATION STATE

In what respect should we expect that the rules of the political game will be different in an allocation state?

In countries where the state is of the production type the largest part of the population derives its income from sources different from the state itself. In socialist regimes, a majority may be employed in publicly-owned industry, rather than in the more narrowly defined state machinery. Because of its need to rely on taxation (or in the case of socialist regimes, on income from publicly-owned industry), the state has an interest in expanding the income base on which taxes can be levied. Economic growth is the primary goal of the economic policy that all production states adopt: but no economic policy is neutral from a distributional point of view, and the polarisation of society into a variety of interest groups struggling to influence economic policy is a necessary corollary. Although the precise political implications of tax levying may vary according to the nature of the tax itself, in most cases the operation requires a large degree of acceptance on the part of the population. Tax evasion can be repressed if it is a marginal phenomenon, but when it becomes the rule the cost of tax collecting becomes much too high. This establishes a link between the ability to raise taxes and legitimacy, which is captured in the saying 'no taxation without representation'. Although the immediate link between taxation and representative democracy may well not exist, as countless examples demostrate, it is a fact that whenever the state essentially relies on taxation the question of democracy becomes an unavoidable issue, and a strong current in favour of democracy inevitably arises. This is the result of the fact that people will naturally be induced to coalesce according to their economic interest, and those groups that find no way to influence the decision-making process in their favour claim appropriate institutional change. The state for its part must give credibility to the notion that it represents the common good: it therefore tends to propose a national myth whose purpose is that of overcoming the conflict of interest that the very existence of the state creates or exacerbates. National myths may have a variety of specifications: their least rhetorical expression is the notion of GNP or GDP, and the stress on the goal of economic growth as seen in isolation from distributive preoccupations.

None of the above is to be found in an allocation state. The state, being independent of the strength of the domestic economy, does not need to formulate anything deserving the appellation of economic policy: all it needs is an expenditure policy. Because state revenue itself is the largest part of GDP, the simple act of spending domestically will maximise GDP growth. The only relevant problem to an allocation state is extracting the maximum potential revenue from the rest of the world: this, however, has little to do with the domestic economy. Because an allocation state only spends and does not tax, its expenditure policy can only indirectly damage some of its people; it will, on the other hand, usually be seen as benefiting everybody.

That benefits are unequally distributed is not relevant for political life, because it is not a sufficient incentive to coalesce and attempt to change the political institutions. To the individual who feels his benefits are not enough, the solution of manoeuvring for personal advantage within the existing setup is always superior to seeking an alliance with others in similar conditions. In the end, there is always little or no objective ground to claim that one should get more of the benefits, since his contribution is generally dispensable anyhow. Were this not the case, the individual would usually find himself in a position whereby he could increase his income if he left the country and sought employment elsewhere; but normally allocation states pay well. Because Exit (Hirschman, 1970) normally involves a considerable loss of income, Voice becomes a dangerous proposition and Loyalty will be popular with a vast majority of the population.

Loyalty is to the system, not to individuals in power. A lot of scheming may be expected to go on in allocation states along the time-honoured pattern of court politics, but this will seldom, if ever, develop into a truly political debate. Democracy is not a problem for allocation states. Although they may find it expedient to set up some kind of representative body to vent and control some of the resentment that even court politics generates, these bodies inevitably have a very tenuous link to their apparent constituency: their debates are followed with indifference by the public and the ruler can disband them and meet practically no resistence whatsoever. More commonly, representative bodies do not exist at all and to the need of establishing them little more than lip service is paid. Even such lip service is intended more to serve the wishes of public opinion

abroad than to satisfy any substantial pressure domestically. The fact is that there is 'no representation without taxation' and there are no exceptions to this version of the rule.

It is only in the case that an allocation state fails, or is widely believed to fail, to take full advantage of the possibility of receiving income from the rest of the world that substantial political opposition may develop. While in fact opposition groups may be numerically limited, they sometimes find themselves in a position to overthrow the existing political order. The result is generally a different institutional setup, although in no way a more democratic one. The history of Libya and possibly Iraq is exemplary in this respect: in both cases the ruling family was seen as being subservient to foreign interests not just from a political point of view, but from a revenue point of view as well: they were forfeiting revenue. It is in this respect that corruption becomes important: inequality of distribution is not an issue, but if the search for personal advantage leads to a failure in cashing in fully the potential rent it develops into a very important one. The reason is that while inequality of distribution can only be corrected by benefiting some and damaging others and each individual generally is not entirely clear on which side he is going to be, mismanagement of the revenue potential of the state can be corrected by benefiting practically everybody in the country.

An allocation state does not need to refer to a national myth and, as a matter of fact, will usually avoid doing so. A national myth, when it coincides with the boundaries of the country itself, may be interpreted as a basis to claim a say in the allocation process. The patrimonial non-national state is, on the other hand, best adapted to being an allocation state, because its origin naturally restricts the number of people who have a say.

Because they do not refer to an appropriately sized national myth, allocation states may avoid having a clearly defined constituency. While this behaviour will clearly tend to perpetuate and possibly reinforce the importance of traditional segmentary politics and kin groups, the fact that most of the GNP is made of government expenditure practically ensures that few or no alternative groupings will develop. The small number of hands employed in the oil business makes it possible essentially to buy off the possibility of unions developing in that sector. Elsewhere, the lack of industrial establishments, and more generally of productive activities, will prevent a union structure and culture from developing. Unions are born in factories because the latter enclose a large number of workers that share common interests. From factories, unions can spread to other sectors and smaller establishments: but it is very difficult to start unionisation from the service sector or from a petrochemical plant. Very mild repression is all that is needed should someone fancy imitating foreign experiences.

The same is largely true for parties. As the politics of allocation states leave little ground for economic interests of citizens not belonging to the elite to be represented, parties will develop only to represent cultural or ideological orientation. In practice, Islamic fundamentalism appears to be the only rallying point around which something approaching a party can form in the Arab allocation states; plus of course the government-inspired parties, wherever they exist.

In actual practice, the distinction between allocation and production states becomes blurred at the margins. Algeria is becoming less and less of an allocation state, while Egypt and Tunisia do enjoy some income from abroad and thus are not purely production states. Apparently, the only differences is in the degree of budget tightness: if money is available, there is less concern for return on unit spending; as money grows scarcer, results are expected of projects that are undertaken. It is impossible to differentiate sharply between states that undertake industrialisation as a tool for political control and states that do so because they expect positive economic returns and increased revenue.

Yet the fact remains that even limited revenue from abroad dramatically improves the state's ability to buy legitimacy through allocation and increases regime stability. Iraq since the early seventies and Algeria almost since independence have had remarkably stable power structures. The major example to the contrary seems to be Iran: but there the Shah was more preoccupied with promoting aggressive industrialisation, even at the cost of exacerbating class conflict, than with buying political support. His successors have done little in the direction of democratisation, but their concoction of populism, Islamic revival and appropriate use of oil money to buy consensus at the retail level (taking care of the poor, improving life conditions in the rural villages) seems to be working quite a bit better than most observers expected. Plus, of course, there is the gruesome rhetoric of war.

ACTUAL POLICIES AND THE NATURE OF THE STATE

The case of Iran clearly demonstrates that the nature of the state is not a rigid determinant of government policies. The latter may well diverge from what we would expect on the basis of the analysis of the nature of the state. If policies do so, they may be expected to be unstable, as they will lead to economic and/or political contradictions which will eventually force their change. Thus the proposed distinction between allocation and production states is far from being an easy tool that allows us to predict which policies are used, but may improve our understanding as to whether policies currently being enforced are likely to be stable or not.

It is specifically important to recognise the existence of allocation states and the fact that they constitute logically coherent political systems which can display considerable stability if the appropriate policies are adopted. The latter are not the same as those that we would deem appropriate for production states.

Much of the literature on the Arab political system suffers from the assumption that there is but one 'modern' model of state, and stability can be gained, in general, only through 'modernising' policies. This approach does not explain genuinely 'reactionary' mass movements, such as in Iran, and leads to endless paradoxes. Witness Michael Hudson's concept of 'modernising monarchies': a monarch ruling a patrimonial state is not exactly what most people would call 'modern' — in fact, they often call it 'traditional' or 'feudal'. Something must be wrong there: a modernising monarch should be expected to promote democratisation and gradually evolve into a ceremonial head of state in the northern European tradition. Yet these monarchs and ruling families, although they love modern technology and use computers and jets, have apparently no intention of sharing their power or changing their role.

The concept of allocation state makes it possible to overcome the paradox. The ruling patrimonial monarchies are neither traditional nor feudal. Feudal they never were; traditional they may be in the sense that they have a tradition, not in the sense that they are the same thing as 20 or 30 years ago. Appearances may not change much (in fact, they have changed quite a lot) but the substance is entirely different: those 'traditional' rulers today head complex and sophisticated allocation states. It so happens that the patrimonial form of government is very well adapted to the specific character of allocation states and vice versa; it is, on the other hand, particularly ill suited to the characters of production states. But democracy, which has advantages in the case of production states, has strong disadvantages in the running of allocation states.

Allocation states are neither better nor worse than production states from a moral point of view, and they are neither more nor less modern. Each has its own rules of the game and evolves along a different path. There is no reason to expect that eventually they will converge towards some kind of standard modernity.

ON RELATIONS BETWEEN ALLOCATION AND PRODUCTION STATES

Relations between allocation and production states are not easy. Each group projects a different model of international relations, according to its specific interests and security preoccupations.

To neighbouring production states, the resources that are available to allocation states are a source of frustration and envy. To them, the best solution would be to wipe out the allocation state altogether, and appropriate its sources of income. This is, however, impossible and nobody quite expects things to go this way: but somehow this fundamental tension remains latent and permeates all relations between the two types of political formations. Allocation states, on the other hand, naturally tend to project internationally their characteristic pattern of buying consensus at home: thus they propose themselves as sources of income to the neighbouring production states, and in doing so, initiate a process that may turn the latter into allocation states. But while production states are interested in appropriating income and allocation states are ready to share theirs, this will not lead to harmonious coexistence, because the question of who is in control is inevitably left open.

The balance of the game depends on the relative importance of the financial resources that the allocation states have available relative to the military potential and economic needs of the production states. If the latter feel stronger, as in the fifties and early sixties, they will propose a model of inter-Arab relations based on a pan-Arab ideology that has clear revolutionary undertones and proposes the dissolution of existing

separate state structures. On the other hand, when allocation states feel stronger they will propose again a pan-Arab ideology, but one in which the Islamic component dominates and the revolutionary one does not exist and inter-Arab affairs are primarily seen as cooperation among independent Arab heads of state.

In the phase of production-state hegemony, the Arab world was dominated by Egypt, which is by far the most important political formation in this respect. Whenever production and economic growth are seriously the main problem of Arab politics, Egypt moves in to the fore. But military defeat and economic disaster coupled with growing oil prices seemed to change the definition of power in the Middle East: there was, as Kerr writes, 'the new belief that power grows, not out of the barrel of a gun nor out of the appeal of a revolutionary leader or movement, but out of an ample state Treasury' (Kerr and Yassin, 1982). Thus Egypt lost the lead and Saudi Arabia took it over again using arguments that were extremely appealing, including to the Egyptian leadership. After an attempt at acquiring its share of the oil income in the least expensive way by exploiting Qadhafi's Nasserite enthusiasm through the union in 1972–3, the Egyptian state was confronted squarely with the prospect of turning into an induced allocation state, subservient to the wishes of Saudi Arabia. But, apart from pride, this solution was barred because the money that was being offered was simply not enough to guarantee the ability to buy domestic political consensus in a complex and populous country such as Egypt. In order to establish a stable induced allocation state in Egypt one needs considerably more money than the Saudis were willing to offer, and Sadat turned to the USA, which he expected to be both willing to provide abundant aid in the short term and capable of opening new development prospects in the longer term. With Mubarak, the importance of domestic production, industrial growth and exports are being stressed anew. The country still relies heavily on income from the outside world, but the state perceives itself as being a production state.

Syria and Jordan provide the best examples of induced allocation states. These countries are crucial to the security concerns of the Gulf allocation states, because they are in the front line facing Israel, because they — singly and together — hold the keys to keeping the PLO under control, and finally, because they may be useful, in quite opposite ways, in containing Iran. This allows the two countries to extract very considerable income relative to their size, while at the same time being almost totally free of interference in their domestic policies. Yet an induced allocation state is not a stable formation: its very existence may be seriously undermined by international developments or by the weakening of their purveyors of funds.

Allocation and production states project two conflicting models of regional integration. In this sense, while they both are inevitably attracted by a pan-Arab national myth, the real content and meaning that each attaches to this myth is different. After the demise of the Nasserist approach proposing political unity with no intermediate steps — in essence, an attempt to wipe the traditional Arab monarchies off the political map — today Arab unity is sought through gradual processes of regional integration. To the production states, the main objective of this integration is the acquisition of a wider economic space that would allow their industrial sectors to benefit from economies of scale. The production states are aiming at a kind of regional cooperation that will regulate migration, liberalise trade and financial flows within the region and establish protection *vis-à-vis* the rest of the world. They are interested in mechanisms that will generate a preference for financial placements within the region, rather than in the global markets. Although the specific situation of the Arab region is in many ways different, they are attracted by the European model, whereby political unity is sought by creating an economic framework within which private contacts and initiatives are allowed to multiply, up to a point when the region would be effectively unified and political unity would cease to be controversial.

The allocation states have a completely different set of interests and goals. Because they are structurally dependent on imports for almost all consumption and investment goods, they are extremely reluctant to give preferences to any other country and attach priority to being able to shop freely. For the same reason, they wish to be able to invest their suplus funds anywhere in the world. *De facto* they need immigrant labour, but do not wish to formally acknowledge this by signing treaties with the countries of origin. In their present investment plans, access to the markets of industrial countries is much more important than protected access to a regional market. To them, regional cooperation and integration is more of a political and security affair. Regional integration is a framework for cooperation among sovereign governments and the individual citizen or

corporation is not expected to play much of a role. The purpose of this intergovernmental cooperation is to defuse and solve local conflicts and improve security conditions. The final goal is not at all some form of political Arab unity, but rather the survival of the allocation states. The pan-Arab national myth then becomes the ideological cover that legitimises a certain degree of interference in the domestic affairs of other countries in exchange for grants and subsidies. Ideally, integration as pursued by the allocation states includes only primary or induced allocation states.

THE LONG-TERM EVOLUTION OF ALLOCATION STATES

The concept of allocation state does not seem to offer a clear evolutionary pattern. It is possible that, being influenced by the opinion and counsel that emanates from the rest of the world, some of the allocation states will seriously pursue a process of diversification of their domestic economic base and gradually turn into production states. Their political orders may also gradually evolve and today's patrimonial rulers may slowly develop ways that are typical of Scandinavian monarchs.

On the other extreme, we may imagine a situation in which the allocation state continues unchanged until the last drop of oil is exported. At that point, the state may simply fold up and the country be deserted, most citizens having accumulated enough of a fortune to allow them to live elsewhere. Today's oil capitals may be turned into ghost towns whose role would be restricted to issuing passports and providing diplomatic protection to a largely expatriate body of citizens. Such states would not face a security threat because they would interest nobody: just as Liechtenstein or San Marino, they would not need to worry about their defence. Once the likely duration of oil reserves is considered, plus the possibility of accumulating financial assets that would allow the state a theoretically permanent source of income, this scenario is not to be ruled out for some of the less populated countries in the Gulf, possibly even for Libya.

In an intermediate case, the allocation state is confronted with greater demands than it can accommodate and gradually turns into a production state. We may expect this to be the case for both Algeria and Iraq. These are not patrimonial states anyhow, thus a transition in the nature of the state may occur with less political trauma.

The point is, that since oil, which is the main economic foundation of the allocation state, is a depletable asset, allocation states are necessarily a passing phenomenon. But how fast in passing? As things stand today, they can all count on another five or six decades of good life. And that is a long time.

CONCLUSION

This chapter discussed the question of the economic foundations of the state in the Arab world and underlined the importance of factors that are traditionally recognised in literature — such as conditions for water supply — as well as other factors, such as conditions of oil production and more generally the increasing role of the state in economic life. Attention was focused on the sources of revenue of the state and a distinction was proposed between allocation and production states. Of course, economic conditions do not explain all aspects of the behaviour of a state and economic factors cannot be reduced to the simple dichotomy of allocation versus production state. This is one analytical tool that may be added to others in order to achieve a better understanding of Arab realities.

The proposed distinction might be relevant outside of the Arab world as well. Oil then ceases to be the primary factor: still, in many countries the state primarily depends on income from abroad rather than from its own citizens. While aid-giving is an important dimension of today's international relations and a necessary instrument to spread development, the fact that it may generate induced allocation states is possibly not sufficiently recognised. The growing importance of international realities is allowing an increasing number of power structures to become essentially independent of their natural domestic constituencies: whoever has power has access to foreign resources that effectively elevate him above most challenges from within. Most frequently, commentators underline the instability of the developing countries, but in many cases it is the stability of some obviously rotten and unpopular regimes that should surprise us. Stability may, in fact, mean political immobilism, which is seldom for the better: what is frozen is not necessarily peace, but conflict; not freedom, but oppression.

4

The Macro-behaviour of Oil-rentier States in the Arab Region

Mahmoud Abdel-Fadil

BASIC FEATURES CHARACTERISING THE ECONOMIES OF OIL-RENTIER STATES

There exist a number of socio-economic features that characterise the economies and societies of oil-rentier states (Mahdavi, 1970: 428–67). The most important feature is that the vast oil revenues received by the governments of these countries have very little to do with the productive effort of the community as a whole. Oil export prices are, in fact, totally divorced from costs of local production, as 'the input requirements of the oil industry from the local economies — at least for the inputs that have an opportunity cost — are so insignificant that for all practical purposes one can consider oil revenues almost as a free gift of nature (Mahdavi, 1970: 429).

Thus oil revenues are primarily in the nature of external collective rent. External in the sense that oil revenues depend on a variety of international factors and the collective bargaining power of oil exporting countries and accrue theoretically to the whole community.

In such oil-rentier economies, *the state becomes the main intermediary between the oil sector and the rest of the economy.* It receives revenues which are chanelled to the economy through public expenditure, and since public expenditure generally represents a large proportion of national income, the allocation of these public funds among alternative uses has great significance for the future development pattern of the economy.

The 'oil boom' of the 1970s generated a 'spending boom' unparalleled in the history of the oil-rentier states in the Arab region. The newly acquired financial resources induced policy-makers to revise upward their growth targets and to embark on massive public expenditure programmes. The dramatic growth of public employment and the expansion of the area of provision of public goods and services (i.e. education, health, housing, communal services, etc.) in many oil-rentier states in the 1970s, constituted an important instrument of redistribution of oil revenues among various groups of the community. In the mean-time, the absolute level and the relative share of current public expenditure on 'national defence' and internal security reached new heights.

Infrastructure projects tended to absorb the largest share of the total public expenditure in construction activities. The reason for this is that such infrastructure fulfils immediate needs related to consumption activities in the oil-rentier states.

The crucial role played by construction activities within the public investment programmes in Arab oil-dependent states may be deduced from the colossal sums of money allocated to them, especially for big infrastructural projects.

In fact, all governments in oil-rentier states were tempted to spend a sizeable portion of their revenues on lavish highways or housing schemes rather than in enlarging the goods-producing capacity of the country. According to some observers, 'there are a number of reasons for this: public works yield high immediate political results and the results are visible to all to see' (Seers, 1979: 237).

None the less, the important point to be stressed here is that, because of the high import intensity of these construction activities, extensive government expenditure programmes (both current and capital) in oil-rentier states tended to generate negligible inter-sectoral linkages within the domestic economy.

As a result, the linkages between the oil sector and the rest of the economy are very limited in oil-rentier states, as its contribution to economic activity has been mainly through the availability of financial resources and government spending. The 'multiplier effects' of public spending open up immensely profitable possibilities of investment in housing, real estate, trade and distribution (the main fields of private capital formation) (Seers, 1974).

A consequence of the rentier state — according to Ruth First — is that:

> The usual development process is reversed. Instead of the progression from agriculture to industry to services, oil provokes the growth of only the third sector (services), directly in the shape of all the ancillary services that the oil companies need: accommodation, pipelines and storage tanks, supplies to the desert and provision for the army of workers (foreign and Libyan). The tertiary sector, always disproportionate in underdeveloped societies, thus grows to elephantine proportions (First, 1980: 120).

In the case of Libya, 'Agriculture which, before oil, had supported the greatest majority of the population, suffers a serious reverse. Labour rushes towards the urban service sector, agricultural production declines, and a new cycle commences: the use of oil revenues to purchase food' (First, 1980).

As the oil boom in such societies has generally taken place against the background of long centuries of relative stagnation and poverty, so strong tendencies to maximise present consumption have emerged in all oil-rentier societies. The experience of continuous and sometimes dramatic increases in oil revenues over a small number of years reinforced tendencies in favour of present consumption (ECWA, 1979: 9). Over the years, the life-styles of consumers in the oil-rentier states have become heavily geared to imports of goods which cannot be produced locally.

Those vested with political power in the oil-rentier states tend to forget that oil revenue will inevitably decline in due course, and aim simply at achieving temporary prosperity (Seers, 1978). Here lies a crucial paradox that best characterises an oil-based rentier society: 'security over the medium term affords a period of grace during which the complex tasks of economic development may be carried out with enhanced means. But this very security, which could enable a country to take the long view, influences the time preferences in favour of the present and tends to shorten the time horizon of the planners and policy makers' (ECWA, 1974: 9).

Given the limited size and the narrow skill structure of the labour force in these economies, the local supply of skilled labour tends to be very limited. Consequently, basic services and activities need to be manned by imported expatriate labour — a tendency which gives rise to the earnings of 'quasi-rent'[1] by the technical and professional groups of imported labour, for the relationship between productive effort and financial reward becomes weak in the case of oil-rentier states.

On the other hand, the temptation is great for native government employees to turn into a class of 'pure rentiers' by collecting a handsome rent on their citizenship titles.

Such active rent-seeking behaviour by most individuals in rentier societies affects people's perception of the working of the economic system. As Ann Krueger rightly pointed out, 'If income distribution is viewed as the outcome of a lottery, where wealthy individuals are successful (or lucky) rent-seekers, whereas the poor are those precluded from or unsuccessful in rent-seeking, the market mechanism is bound to be suspect' (Krueger, 1974: 302). The ultimate outcome of this process is that the rent-seeking mentality becomes a self-perpetuating one, and a dominant feature of the economic activity of these societies.

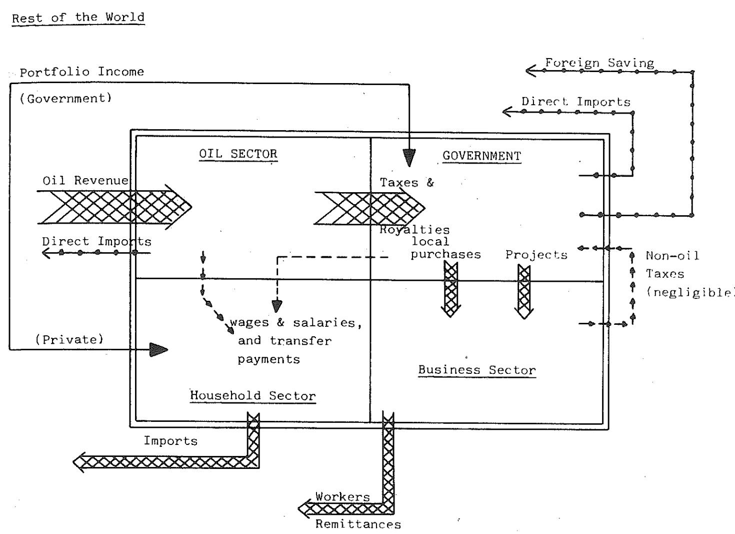
THE MODE OF INTERACTION BETWEEN THE EXTERNAL OIL RENT AND THE INTERNALLY-GENERATED TYPES OF RENT WITHIN THE DOMESTIC ECONOMY

Since oil revenues constitute the primary source of rent in an oil-rentier state, the mechanism of 'internal recycling' of the oil rent within the national economy through the state budget (i.e. programmes of public spending) gives rise to a variety of secondary types of rent. Government expenditures which give rise to these secondary types of rentier income are: (i) project expenditures such as construction; (ii) transfer or welfare payments such as the land purchase programme in Kuwait (see Figure 4.1).

On the other hand, the state recycles part of the oil rent externally, through overseas portfolio investment. The mechanism of 'external recycling' of oil rent reinforces the rentier character of the oil-rentier states, as overseas portfolio investment adds new types of rentier income (i.e. dividends and interests) to the national disposable income.

As a result, a new pattern of *a tripartite alliance between the state, the new business elites* (i.e. merchants, contractors and financiers), *and circles of international financial capital ermerges*. Figure 4.2. depicts the dialectical relationship between these three agents as well as the feedback effects underlying the *modus operandi* of oil-rentier states in the Arab region.

Figure 4.1: Flow of economic resources in a rentier state



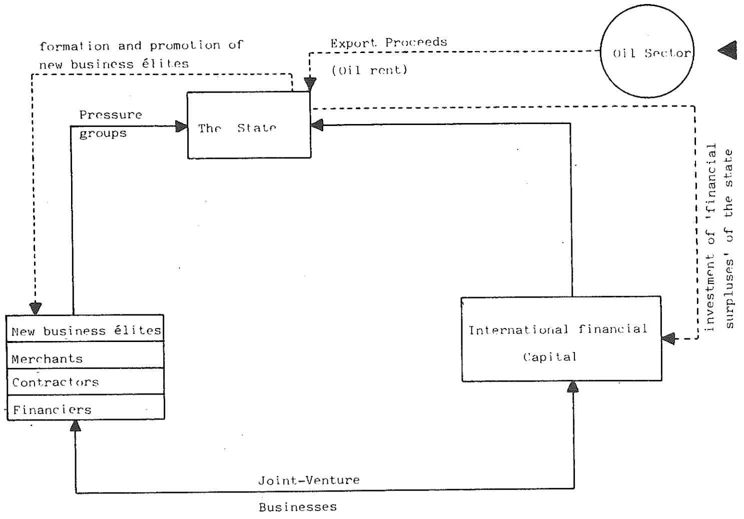
Source: *The Dynamics of Petroleum Dependency: Growth in an Oil-Rentier State*, p. 26.

None the less, the degree of dependence on various types of external rentier income — (i) oil rent; (ii) locational rents; (iii) other mineral rents; (iv) workers' remittances; (v) portfolio income — is not usually confined to the recorded volume of various types of external rents and unrequited transfers. For it is well known that all types of external rents and unrequited transfers exercise multiplicative effects upon the recipient economy.

In this respect Thomas Stauffer suggests a new kind of multiplier called the 'rentier-income multiplier' to capture the full extent of dynamic dependence of rentier states on external rents and unrequited transfers. The rentier multiplier is similar to the familiar Keynesian multiplier in that it specifies how an initial injection of external rents causes a larger increase in effective demand and thus leads to an increase in national disposable income greater than the initial injection (Stauffer, this volume, pp. 33–5).

In the case of oil rent, all but a small part of total oil revenues

Figure 4.2: The dialectical relationship between the state, new business elites and international capital in an oil-rentier state



accrue to the government. The government normally saves a certain portion of these oil revenues (e.g. reserves for future generations) and spends directly on imports such as arms, high technology packages and consultancy services. For the remainder, the government pays wages and salaries to its employees, spends money on purchases of goods and services 'which add to income, even if the goods are imported, because of the domestic component of the retail markets' and on project expenditures such as construction.

The recipients of these funds — civil servants, local merchants and contractors — spend part of this money on imports, which then leaks out of the national economy, but the rest of the money is respent at home and a second-round effect is generated, and so on.

This shows the asymmetrical effects of the multiplier process, as these effects are more localised in certain sectors (i.e. construction, trade and finance) and among certain socio-economic groups.

In the case of 'non-oil' semi-rentier states such as Egypt, the Arab Republic of Yemen and Jordan, workers' remittances —

the most potent form of rentier income — are usually subject to an important multiplier process.

If we assume that E(t) denotes consumer expenditure in period (t), which depends on workers' remittances in period (t_{-1}), and the average propensity to consume out of remittances is C, then we may formulate the '*workers' remittances multiplier*' as follows (Abdel-Fadil, 1985):

$$Y = \text{increase in aggregate spending} = \frac{E}{1-c+m} = \frac{E}{1-(c-m)}$$

where m is the marginal propensity to consume imported goods and services.

Another formulation of such a multiplier is given by Professor Brian Van Arkadie in the following form (Van Arkadie, 1977):

$$\frac{1-t}{1-c+m}$$

where t is the proportion of emigrants' remittances which substitutes for domestic earnings.

In general, we may note that the higher the propensity to save out of remittances and to import out of consumer spending — financed by remittances — the lower would be the value of the multiplier within the domestic economy (Abdel-Fadil, 1985).

THE TABLEAU ECONOMIQUE FOR RENTIER STATES: THE CASE OF KUWAIT AND NORTH YEMEN

The purpose of this section is to examine the role of the oil rent category — as a specific historical form of economic surplus — in affecting the dynamic macro-behaviour of a whole class of rentier states.

This would provide an analytical basis for a new typology of various oil-based societies, based on differentiated rules of appropriation, allocation and the recycling of oil rent within the society.

An attempt will be made here to apply a modified version of the tableau économique of F. Quesnay, to serve as a useful tool of static macro-economic analysis. In fact, the French school of the 'Economistes' or 'Physiocrats' of the third quarter of the eighteenth century, was the first to view the 'feudal mode of production' as the creation of a 'surplus', primarily consumption goods, available for unproductive use to support government activities and the cultural life of feudal seigneurs.

Quesnay's *tableau économique*, first printed in 1758, represents an early pioneering step towards the two overlapping and related kinds of investigative work that many economists now carry on and call 'national income analysis' and 'mathematical economies' (Phillips, 1955). In his *tableau*, Quesnay analysed the circulation of the celebrated *produit net* among the different classes of society, the search for which was the central point in Physiocratic analysis.

The *tableau économique* is a representation of Quesnay's analysis of a socio-economic process as a pattern of interrelated flows: labour, inputs and resources in economic production, output and sales of products, incomes and outlays necessary for the continuing operation of the national economy.

The *tableau* displays three simple general truths of national income analysis. The first is that the economy or the economic universe is a system of interdependent variable quantities which are interrelated to the extent that when any of them change, all are, in time, bound to change together in more or less determinate relationships. The second point is that there is always, throughout a social economy a circular flow of wealth (income and expenditure), i.e. expenditures by producers on production become the incomes of consumers which, when spent by them, buy the products and become the producers' revenues and the sources of their new expenditures on new production, etc. The third point is that, within an economy, a set of conditions of a general equilibrium of all the related variable quantities and forces exists, such that when all variables come into play, all economic activities will have then attained their relative optimal economic situations or positions.

Description of the *tableau*

The *tableau* depicts the economy as an ever-growing circuit on the basis of Quesnay's conception of circular flows. Quesnay divided the economy into three social classes. These are:

(a) *The productive class* with which production expenditure is

associated. Productive expenditure is employed in the primary sector in order to perpetuate wealth in the form of food, drink and raw materials for manufactured goods.

(b) *The sterile class*, whose sterile expenditure is on manufactured commodities and foreign products.

(c) *The proprietor class*, to which accrues a revenue from the productive class, in return for the rental services provided by that class.

Unlike Quesnay's agrarian economy, the Kuwaiti economy consists of more than three social classes. This is mainly because of the existence of a large non-Kuwaiti labour force. Instead of a productive class, a proprietor class and a sterile class, we have in our *tableau* two major subdivisions consisting of Kuwaitis and non-Kuwaitis.

Non-Kuwaitis are by definition wage earners only, since rent and dividends do not accrue to them because of restrictions on ownership of property and company shares. Non-wage income is restricted mainly to Kuwaiti industrial capitalists, traders and landowners. Civil servants are divided between Kuwaiti and non-Kuwaiti classes at roughly 40 per cent and 60 per cent, respectively (1976 data). There is no Kuwaiti agricultural labour.

A further fundamental difference, with respect to Quesnay's *tableau*, is the existence of factors of production other than land, namely capital and labour.

Revenues generated by the *oil sector* can be regarded as the base of the *tableau*, being the main contributing sector to formation of GDP and to government revenue. Other sectors are also included in the *tableau* in order to capture the main socio-economic features of the Kuwait society. Such a modified version of the *tableau économique* approaches the modern construction of Social Accounting Matrices (SAMs) (Barna, 1973).

Main features revealed by SAM 79 for Kuwait

The rest of the world account

(1) Investment income from abroad is distributed as follows:

Government	58%
Financial sector	16%
Other private	26%

with the government getting the largest share followed by other private.

Table 4.1: SAM 1979 for Kuwait (millions of KD)

Payments to / Payments from	1	2	3	4	5	6	7	8	9	10	11	12
FACTORS												
1. Land												
2. Labour												
3. Capital												
KUWAITI CLASSES												
4. Kuwaiti Landowners	12											
5. Kuwaiti Traders and Industrial Capitalists			18007		448	276		19		904	6	249
6. Kuwait Civil Servants												
7. Kuwait Adm. and Tech. Staff												
8. Kuwaiti Industrial Labour												
9. Kuwaiti Other Labour												
NON-KUWAITI CLASSES												
10. Non-Kuwaiti Professionals and Adm. and Tech. Staff												
11. Non-Kuwaiti Agricultural Labour												
12. Non-Kuwaiti Industrial Labour												
13. Non-Kuwaiti Other Labour												
14. Non-Kuwaiti Civil Servants												
SECTORS												
15. Agriculture												
16. Industry			354									
17. Oil				2204								
18. Construction												
19. Trade and Finance			483									
20. Other												
21. State			532									
22. Capital Account												
23. Rest of the World		147										
24. GRAND TOTAL	12	147	19376	2204	448	276		19		904	6	249

Table 4.1 — *continued*

Payments to / Payments from	13	14	15	16	17	18	19	20	21	22	23	24
FACTORS												
1. Land												
2. Labour												
3. Capital											920	920
KUWAITI CLASSES												
4. Kuwaiti Landowners												12
5. Kuwaiti Traders and Industrial Capitalists	76	4436										24421
6. Kuwait Civil Servants									1231			1231
7. Kuwait Adm. and Tech. Staff			3	203	253	13	194	129				795
8. Kuwaiti Industrial Labour				48								48
9. Kuwaiti Other Labour					268		7	8				283
NON-KUWAITI CLASSES												
10. Non-Kuwaiti Professionals and Adm. and Tech. Staff			15	952	412	486	2194	1111				5170
11. Non-Kuwaiti Agricultural Labour			83									83
12. Non-Kuwaiti Industrial Labour				1511	161							1672
13. Non-Kuwaiti Other Labour						998	177	1714				2889
14. Non-Kuwaiti Civil Servants									1162			1162
SECTORS												
15. Agriculture											36	36
16. Industry									35	929	272	1590
17. Oil									15	7458	4781	14458
18. Construction												
19. Trade and Finance												483
20. Other									2695			2695
21. State					9275			147				9954
22. Capital Account									3401			3401
23. Rest of the World									1646	62		1855
24. GRAND TOTAL	76	4436	101	2714	10369	1497	2572	3109	10185	8449	6009	70195

* Institutions   Sum of Expenditure** = 70195   Sum of Receipts* = 73158   ** discrepancies represent errors and omissions

(2) Workers' remittances (in cash) represented as an expenditure by labour as a factor of production to the rest of the world, are at 147 million KD. This gives an average propensity to remit of 1.3 per cent out of total non-Kuwaiti wage income (1976) which is extremely low by any standard.
(3) Oil export revenue (94 per cent of total exports) accounts for the impressive figure for export proceeds compared to the total import bill.

Kuwaiti classes account

(1) Non-wage income is concentrated in the hands of *Kuwaiti industrial capitalists and traders*, and not those of the landlords who have an extremely meagre share of total non-wage income.

Distribution of non-wage Kuwaiti income accruing to industrial capitalists and traders was reported to be as follows (total does not add up due to rounding):

	%
Return on capital	72.3
Investment income from abroad	1.3
Interclass transfers in the form of rent	1.8
Rent payments by Kuwaiti civil servants	1.1
Rent payments by Kuwaiti industrial labour	0.1
Rent payments by non-Kuwaiti professionals	3.7
Rent payments by non-Kuwaiti agricultural labour	0.0
Rent payments by non-Kuwaiti industrial labour	1.0
Rent payments by non-Kuwaiti other labour	0.3
Rent payments by non-Kuwaiti civil servants	18.2
	100.0

(2) State payments to civil servants are split at 51 and 49 per cent between Kuwaitis and non-Kuwaitis, respectively. The sectoral distribution of Kuwaiti administrative and technical staff wage bill is as follows:

	%
Agriculture	0.4
Industry	25.5
Oil	31.8
Construction	1.6
Trade and Finance	24.4
Other	16.2
	100.0

The smallest Kuwaiti wage-earning class in Kuwaiti industrial labour, which accounts for 2 per cent of the total Kuwaiti wage bill.

Non-Kuwaiti classes account

Total non-Kuwaiti wage bill is distributed as follows:

	%
Administrative and technical staff	47.6
Agricultural labour	0.8
Industrial labour	15.2
Other labour	26.3
Civil servants	10.6
	100.0

Income accruing to administrative and technical staff is distributed across sectors, as follows:

	%
Agriculture	0.3
Industry	18.4
Oil	8.0
Construction	9.4
Trade and finance	42.4
Other	21.5
	100.0

It is clear from the above that the total wage bill is definitely concentrated in the hands of non-Kuwaitis at 82.4 per cent. Furthermore, non-wage income represents 91.2 per cent of total Kuwaiti wage and non-wage income.

The state account

	%
Oil revenue	93.2
Investment income	5.3
Other	1.5
	100.0

The oil revenue figure consists of oil exports plus royalties from oil companies, sales revenues and taxes. The wage bill represents 35 per cent of total expenditure by the state.

The capital account

About 88 per cent of total gross fixed capital formation is accounted for by the oil sector in 1979.

The *tableau économique* for the Yemen Arab Republic, 1973 and 1982

The Yemen Arab Republic (YAR) constitutes a typical example of a semi-rentier state heavily dependent on workers' remittances and aid flows emanating from neighbouring Arab oil-rich states.

An attempt is made here to construct a Social Accounting Matrix (SAM) for North Yemen for two points in time: the financial year 1972/3 and the calendar year 1981, in order to capture the increasing rentier nature of the Yemeni society (see Tables 4.2 and 4.3).

All figures are in money terms, and goods and services are valued at current market prices. The unit of currency is the riyal (= 100 *fils*). The rows represent total deliveries to the activities of the economy or total production, while the columns represent total receipts from the activities of the economy or total purchases.

The semi-rentier nature of the Yemeni economy becomes obvious by 1982, as recorded workers' remittances amounted to 1484 million YRs as compared to 252 million YRs in 1972/3.

The property and entrepreneurial income from the rest of the world as well as other current transfers from the rest of the world (i.e. aid flows and grants), reached about 4 billion YRs in 1981 as compared to 350 million YRs only in 1972/3. All in all, current rentier income accruing to the Yemeni economy amounted to around 5 billion YRs in 1981 (or about 40 per cent of the gross domestic income).

The impact of the increasing role of the various types of rentier income on the Yemeni economy can be easily gleaned from the dramatic change in items of gross domestic expenditure, as shown in Table 4.4.

Table 4.4: Pattern of gross domestic expenditure in 1973 and 1982 (at current prices) (millions of YRs)

	1973 (1)	1982 (2)	Ratio (2)/(1)
Government final consumption expenditure	365	3899	10.6
Private final consumption expenditure	2707	13927	5.1
Gross final capital formation	456	6039	13.2
Increase in stocks	120	190	1.6
Exports of goods and services	128	1457	11.3
Less: Imports of goods and services	−929	−10875	11.7
Total expenditure on the gross domestic product	2847	14637	5.14

The increasing dependence on various types of rentier income in the formation of national disposable income may be deduced from Table 4.5.

Table 4.5: National disposable income (millions of YRs)

	1973 (1)	1982 (2)	Ratio (2/1)
Compensation of employees (domestic)	600	4465	7.4
Compensation of employees from the rest of the world[a]	252	1609	6.3
Operating surplus (domestic)	1973	7542	3.9
Property and entrepreneurial income from the rest of the world[a]	75	506	6.7
Indirect taxes	208	2265	10.8
Other current transfers from the rest of the world[a]	391	4121	10.5
National disposable income	3499	20508	5.8

Note: a. Rentier and semi-rentier types and income.

The two matrices also reveal the declining importance of the agricultural sector in generating the domestic operating surplus (i.e. economic surplus) as it, in 1981, accounted only for 44 per cent, while that of trade increased its share to 27 per cent. The manufacturing and construction sectors slightly increased their share in total operating surplus to account for 5.9 per cent each. A major development, which took place over the period 1972–81, was the dramatic increase in the role of the financial sector. This sector's share in domestic operating surplus (before

Table 4.2: SAM 1972/3 for Yemen (millions of YR)

Payments to / Payments from	1	2	3	4	5	6	7	8	9	10	11	12
FACTORS												
1. Labour							101.9	4	21.8	57.6	1.5	27.1
2. Capital and Land							917.1	12	65.2	68.4	45	349.9
INSTITUTIONS												
3. Households	747	1592.4				−45.6						
4. Private Business												
5. Public Business												
6. Government		9.6	6.8	4.6	31							
ACTIVITIES												
7. Agriculture												
8. Mining												
9. Manufacturing												
10. Construction												
11. Utilities												
12. Trade and Hotels												
13. Transport												
14. Real Estate Serv.												
15. Community Serv.												
16. Gov. Serv.												
17. Private Serv.												
18. Financial Inst.												
19. Imputed Bank Charges												
20. Commodities			2188			317	164	5	129	158	7	47
21. Indirect Taxes							7		20			3
22. Capital Account				383.4		−72.4	10	1	11	4	1	6
23. Rest of the World												
24. TOTAL	747	1602	2194.8	388	31	199	1200	22	247	288	54.5	431

Table 4.2 — *continued*

Payments to / Payments from	13	14	15	16	17	18	19	20	21	22	23	24
FACTORS												
1. Labour	15.5	0.9	1.3	250	8	5.6					252	747
2. Capital and Land	46.5	99.1	17.7			32.4	−39				30	1602
INSTITUTIONS												
3. Households											320	2613.8
4. Private Business												
5. Public Business												
6. Government									147			199
ACTIVITIES												
7. Agriculture								1200				1200
8. Mining								22				22
9. Manufacturing								247				247
10. Construction								288				288
11. Utilities								14				14
12. Trade and Hotels								431				431
13. Transport								116				116
14. Real Estate Serv.								111				111
15. Community Serv.								30				30
16. Gov. Serv.								328				328
17. Private Serv.								9				9
18. Financial Inst.								46				46
19. Imputed Bank Charges												
20. Commodities	40	9	10	76	1	6	39			381	62	3639
21. Indirect Taxes	3	1						113				147
22. Capital Account	11	1	1	2		2				20		381
23. Rest of the World								684				684
24. TOTAL	116	111	30	328	9	46		3639	147	401	664	

Table 4.3: SAM 1981 for Yemen (millions of YR)

Payments to / Payments from	1	2	3	4	5	6	7	8	9	10	11	12
FACTORS												
1. Labour							427.9	38	274.5	603	26	231.1
2. Capital and Land							3069.1	112	410.5	610	81	1877.9
INSTITUTIONS												
3. Households	5294	6961				30.3						
4. Private Business												
5. Public Business												
6. Government		450	170	165.2	264							
ACTIVITIES												
7. Agriculture												
8. Mining												
9. Manufacturing												
10. Construction												
11. Utilities												
12. Trade and Hotels												
13. Transport												
14. Real Estate Serv.												
15. Community Serv.												
16. Gov. Serv.												
17. Private Serv.												
18. Financial Inst.												
19. Imputed Bank Charges												
20. Commodities			12942			3043	1040	60	1083	2005	116	246
21. Indirect Taxes						252	106		117	24		14
22. Capital Account			2323.1			3.9	45	6	52	43	4	65
23. Rest of the World												
24. TOTAL	5294	7411	15435.1	165.2	264	3329	4688	216	1937	3085	227	2434

Table 4.3 — *continued*

Payments to / Payments from	13	14	15	16	17	18	19	20	21	22	23	24
FACTORS												
1. Labour	84	5.4	9	1958	24	129					1484	5294
2. Capital and Land	229	538.6	103			831	−705				454	7411
INSTITUTIONS												
3. Households											3579	15864.3
4. Private Business												
5. Public Business												
6. Government									2280			3329
ACTIVITIES												
7. Agriculture								4688				4688
8. Mining								216				216
9. Manufacturing								1937				1937
10. Construction								3085				3085
11. Utilities								227				227
12. Trade and Hotels								2434				2434
13. Transport								699				699
14. Real Estate Serv.								637				637
15. Community Serv.								205				205
16. Gov. Serv.								3111				3111
17. Private Serv.								26				26
18. Financial Inst.								1084				1084
19. Imputed Bank Charges												
20. Commodities	229	70	74	1146	2	86	705			5641	1130	29618
21. Indirect Taxes	87	18	9			20		1633				2280
22. Capital Account	70	5	10	7		18					2928	5641
23. Rest of the World								9636				9636
24. TOTAL	699	637	205	3111	26	1084		29618	2280	5641	9636	

deducting banking charges), jumped from 2 per cent in 1972/3 to 20 per cent in 1981.

Although national savings increased from YRs 383 million in 1972/3 to YRs 2300 million in 1981 (i.e. a sixfold increase), their capacity to finance investments has greatly declined, and paradoxically enough, dependence on foreign finance grew dramatically. While the deficit on the current account of the balance of payments in 1972/3 amounted only to 20 million YRs, (i.e. 5 per cent of investment expenditure), in 1981 net borrowing covered 53 per cent of the funds required to finance investment. The growing investment saving gap reflects the fact that most of the increase in income is being absorbed by consumption, which reduces the saving capacity of the economy.

Moreover, an increasing proportion of aggregate spending leaked out in the form of increased demand for imports, as can be witnessed from the drastic volume of imports reached in 1981. In sum, the structure of domestic production has shifted towards service sectors such as trade and finance. In the meantime, agriculture has been neglected, and lost the prominence it used to enjoy. In the past, it was the major source of operating surplus within the Yemeni economy.

THE OIL-RENTIER STATES AND PROBLEMS OF INTERTEMPORAL DISTRIBUTION OF WELFARE AND WEALTH

It is important to recognise that whether we set the time horizon next year or next century is going to make a considerable difference to attitudes towards the direction of structural change in an oil-rentier economy. But there is very rarely unanimity on the location of the time horizon within a given community. Hence we must demarcate the socio-economic group (or groups) in which power is vested. Once the pattern of time preference of this dominant group (or groups) is located, maximisation of the welfare of this group (or groups) over a given period of time implies the imposition, paternalistically, of a certain time horizon of social choices on all who do not happen to share the same location of the time horizon (Van de Graaff, 1967: 93–6).

In most oil-rentier states, there seems to be a wide acceptance of the simple value judgement that the preferences of our contemporaries are to be given great weight, and those of unborn

generations to be given a negligible weight in the formation of people's attitudes towards intertemporal choices. The presence of a strong pure time preference among members of the powerful business community in oil-rentier states may be conceived of in the words of Sir Roy Harrod:

> We may be dead at the future date and not rate the welfare of our heirs as highly as our own. The desire to use the money now is reinforced by animal appetite. Greed may be thought to be as appropriate a name for this attitude as time preference, though less dignified (Harrod, 1956: 37).

It is generally agreed that the rate of investment in any society determines — to a large extent — what may be called the intertemporal distribution of welfare. Its optimum rate depends on the extent to which society thinks it desirable to sacrifice present welfare for the benefit of the never-ending succession of future generations. But the important thing about the optimum (or target) rate of investment is the very close connection it bears to the political (or collective) decisions we make regarding the time horizon of intertemporal social choices, and the size of the terminal capital equipment. In short, the optimum (or target) rate of investment is essentially a 'political' matter (Lerner, 1944: 262).

Thus if contemporaries in an oil-rentier economy are exhausting their oil resources at a very high rate without leaving enough reproducible resources for the future generations, planners and policy-makers in these countries may wish to interfere to override individual time preferences and enforce extra conservation of oil resources. Hence future generations will at least have more 'oil in the ground' even if they would have preferred reproducible resources.

That is the reason why several writers on the theory of planning have taken as their starting point the Pigovian assertion that individual preferences ought not to count where decisions affecting the future are concerned, since individual men lack a 'telescopic faculty' and tend to underestimate future satisfactions (Pigou, 1932: 25).

On the other hand, the current policies of oil production and public expenditure in oil-rentier states raise a major question relating to the inter-generational equity aspect of the distribution of the benefits of oil wealth, given the different mechanisms by which vast amounts of oil revenues become concentrated in a few hands.[2]

Under the socio-political conditions prevailing in these states, the outcome of the current policies of oil production and recycling of oil revenues amount to a *de facto* de-nationalisation of the oil wealth stored in the ground, which is supposed to belong to all members of the community concerned.

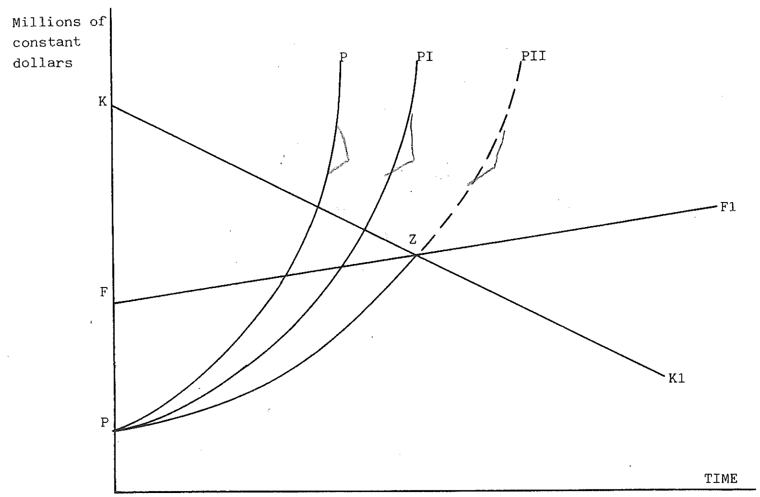
ALTERNATIVE DYNAMIC TRANSITIONAL PATHS OF OIL-RENTIER STATES

In their study of the Kuwait economy, M. Khouja and A. Sadler set up a simple analytical model designed to illuminate some future transitional growth problems in oil-rentier economies (Khouja and Sadler, 1979). The analysis is based on the assumption that all government and private sector holdings of foreign assets are entirely deployed for the purpose of generating new forms of rentier income to replace depletable oil revenues. The problem the model addressed itself to may be stated as determining the level at which earnings of foreign exchange can be utilised while at the same time permitting an accumulation of foreign assets in the face of depleting oil resources so that the income flow from foreign earnings can be maintained at a level consistent with the optimum growth condition (Khouja and Sadler, 1979: 157–8).

Figure 4.3 illustrates the dynamics of transition from one type of rentier economy (dependent on external oil rent) to another type of rentier economy (dependent on external rent earned on financial assets held abroad). The diagram[3] illustrates the build-up of income on foreign assets over time in the face of constant or falling foreign revenues from oil and their relationship with levels of foreign exchange requirements.

The net foreign exchange requirements are determined by the difference between the sum of imports for consumption and investment purposes together with remittances minus non-oil exports. In the diagram KK′ represents falling annual oil revenues over time, while the line FF′ represents the growing annual net foreign exchange requirements referred to earlier. The third curve PP denotes the real income generated from the national financial assets held abroad at each point in time. But the falling oil revenues over time would result in a diminishing

Figure 4.3: The building of income on foreign assets over time



addition to foreign assets from oil source, thus causing a flattening of PP to PP′.

The different paths of transition may be mapped out as follows. As long as the rate of reduction in KK′ is less than the rate of increase in PP′, the level of GNP will go on increasing over time but at a diminishing rate. On the other hand, if KK′ falls at a faster rate than the rate of increase in PP′, the prospects for future GNP growth depends on whether the two curves will intersect above or below the FF′ line. For, as long as the intersection point is above the FF′ line, foreign exchange earnings are in a position to supplant oil revenues and at the same time to allow a net surplus to augment foreign assets. If the point of intersection is below the FF′ line, the level of GNP will not be sustained in the long run without structural alterations in the domestic economy to reduce the level of FF′ (Khouja and Sadler, 1979: 159).

If we assume a flattening of the curve PP corresponding to income from foreign investment as in PP′, all three curves as drawn now intersect at one point (Z). This would indicate that the rentier income from foreign financial assets is just sufficient to supplant declining oil revenues. At this point there is no further accumulation of foreign assets, but the country's foreign exchange requirements would always be satisfied. The intersection of PP′ with the other curves at Z also indicates that foreign investments have already reached the level where they are generating sufficient rentier income to take over from oil as the main foreign exchange earner and to provide funds which regenerate themselves (Khouja and Sadler, 1979: 160).

While very useful in giving valuable insights into some of the basic problems which face oil-rentier economies the Khouja-Sadler analysis outlined in the preceding paragraphs remains couched in terms of comparative statics. In fact, many dynamic aspects of the transitional problems, especially those relating to uncertainty over oil prices, world inflation rates and foreign exchange rates, are brushed aside. For it is well known that oil revenues and earnings on financial assets held abroad are subject to serious risks arising from the high rates of world inflation and foreign exchange fluctuations caused by the instability of the key international currencies. Under these conditions, it is hard to accept the Khouja-Sadler assumption of positive real yield on foreign assets (i.e. the rate of return exceeds the rate of inflation) at every future point in time.

Moreover, there are many other dynamic factors which need to be taken into account in order to assess the viability and feasibility of the assumed transitional path as depicted in Figure 4.3. A scenario based on a few simplified assumptions was devised by Hazem Beblawi (1978: 19), to show that, 'other things being equal', the potential claims of oil-rentier countries on the exports of goods and services of the most industrialised countries (especially the USA) will be unexpectedly high, when they start the annual servicing of financial assets accumulated by the oil-rentier states.

We may thus contend that the transitional path from one form of rentier economy to another, under the conditions of declining income from oil, is highly unstable and is surrounded by many uncertainties which may well reduce the welfare of future generations. And, in the absence of well-defined policies on the directions of home investment and the diversification of the domestic economy (at the individual country the regional level), it is impossible to draw any safe conclusion about the capability of an oil-rentier economy to steer a transitional course to a self-sustained growth path.

Ideally, the national interest would be best served if the oil resources were depleted at a time when the highest possible level

of development and diversification of the domestic economy has been attained, a possibility which is highly unlikely under the prevailing set of policies in Arab oil-rentier states.

NOTES

The author wishes to thank Ms Mayar Farrag and Ms Rasha Abdel-Hakim, both research assistants at the American University in Cairo, for their valuable help in compiling data and constructing Social Accounting Matrices for Kuwait and North Yemen.

1. Quasi-rent may be defined as the return to a seller of a good or service over and above its opportunity cost when the good is temporarily in fixed supply. The concept was applied by Alfred Marshall to the determination of the price of capital in the short run when the supply of capital is fixed. The owners of capital receive a payment which differs from the opportunity cost of using that resource by the amount of quasi-rent. In the long run, when the factor can be augmented or depleted, the equilibrium price will reflect the cost of alternative uses. Quasi-rent exists because prices in the short run are not in equilibrium. Marshall used this concept as an element in his explanation of the rate of profit.

2. In the case of Kuwait, this was apparent in the government's land acquisition programme. Purchase of land by the government was considered the simplest and quickest method of distribution of national oil wealth among the Kuwaiti population. Thus a total of more than KD one billion (equivalent of US $3.4 billion) was disbursed through the land acquisition programme during the years 1952–75. The government, in fact, distributed by this means about one-quarter of its total oil revenues during the period from 1946 to 1971. *The funds allocated to this programme in these years exceeded the country's investments in foreign assets and were almost equivalent to all government development expenditure during the same period.* The government was paying for the purchased land sums of money far in excess of what it was worth.

The programme implemented in the sixties has been sharply criticised for being an indiscriminate and inequitable way of distributing oil revenues and for failing effectively to invigorate the Kuwait economy because the private sector invested abroad a large part of the funds received under the programme. The programme has, however, been revived since 1974 on a seemingly more rational and systematic basis with allocation representing about 10 per cent of total government expenditure. See Khouja and Sadler, 1979: 44–5.

3. The figure is a slightly modified version of the diagram which appears in Khouja and Sadler's book on page 158.

5

Policies for Development: Attitudes Toward Industry and Services

Michel Chatelus

INTRODUCTORY REMARKS

The purpose of this chapter is to investigate industrial structure and policies and the extension of the service sector in Arab countries in the light of the production versus allocation states paradigm. Starting from the simple distinction between those Arab states where allocation prevails (those states able to live from oil revenues), and those whose spending capacity depends both on the country's production and on the state's capacity to raise taxes on this production, we discuss whether this two-way distinction may be utilised as the central tool of analysis, or whether it is only one among several criteria and determinants of the situation in the Arab states. The varying impact on the state building process in the Arab world, of the allocative opportunities and productive constraints mix, will be the central theme of the chapter: the principal issue remaining is the appreciation of the relative weight to be attributed to each of them if we wish to understand the successive stages of the industrial and service growth in the Arab states.

Our objective is hence to analyse, evaluate and explain, not to present a complete description of the industrial and service sector in the Arab world. It is necessary here to clarify a potential source of ambiguity. We do not believe in the existence of such an entity as 'the Arab economy'; for only political arguments can be called upon to support this concept; economic realities do not offer convincing proof (Amin, 1980; Brahimi, 1978; Sayigh, 1982). We shall refer therefore to a diversified set of Arab economies, using different regroupings of the concerned

states depending on the aspect we intend to study. In this perspective, the gathering of all states in a single group may be a meaningful approach to dealing with basic trends and influences whenever their consequences concern all states, equally affected by the same environment and subject to identical pressures and constraints.

The first part of this chapter will present an analytical background and discuss the main hypotheses relating the distinction between the allocation/production states to their attitudes toward industry and services. Keeping the main distinction as a useful analytical reference, we will note the necessity of introducing more complex criteria to explain state policies. The second part will examine the industrial development process in the light of the state's regulation of domestic and external revenues sources. The service sector will be the object of a similar analysis in the last part of the chapter.

ANALYTICAL BACKGROUND AND MAIN HYPOTHESES

Allocation or production states: a paradigm revisited

Starting from the simple allocation/production paradigm, we are led to successive revisions and qualifications in order to cope with the growing complexity of relations of Arab states to oil rent. Various alternative definitions have been utilised to classify Arab states, and a rapid glance at some of the most widely used expressions may facilitate the understanding of the underlying hypothesis. We find distinctions between surplus and deficit Arab countries, between oil rich and poor states, between production and circulation economies, rentier and recipient states, oil dependent and tax dependent states, etc.

In current IMF publications, Arab countries are divided into three groups, all of them under the major heading 'developing countries': a first list of 'oil-exporting countries' comprises Algeria, Iraq, Kuwait, Libya, Oman, Qatar, Saudi Arabia and the United Arab Emirates; in a second list we have 'non-oil countries', classified as 'net oil exporters', namely Bahrain, Egypt, Syria and Tunisia; the other Arab countries belong to the residual group of 'net oil importers' (International Monetary Fund, 1984; World Bank, 1984). In the often quoted statistical tables of its yearly *World Development Report*, the World Bank re-groups oil countries with high income (Kuwait, Libya, Oman, Saudi Arabia and the United Arab Emirates) in a specific group, while other Arab states, whether oil exporters or not are ranked in the lengthy developing countries table, according to their *per capita* GNP (ECWA, 1984). All those groupings are drawn from one simple assumption: the pertinence of a dualistic approach to the analysis of the behaviour of states, with a fundamental contrast between allocation in oil-rich states and production in other states. A slightly modified approach is presented in a recent report by the UN Economic Commission for Western Asia (ECWA, 1984): it proposes to divide Arab countries into three groups: in a first group we find oil countries with small populations, i.e. Gulf countries and Libya; a second group consists of oil countries with relatively more diversified resources and larger populations (Algeria and Iraq); all other Arab states are in a third group. The fundamental reference in such a grouping remains unchanged.

Observing the political economy of state industrialisation in the Arab Middle East (Chatelus and Schmeil, 1984) we suggested a generalisation of the rentier state hypothesis (another name for the allocation state paradigm) to the great majority of Arab states. Induced allocation effects in non-oil states are just as determinant as direct allocation in oil countries. Simply delineating rent as an income not originating from the productive activity of the concerned unit, the flows and dimensions of which are not directly linked to the beneficiary's activity (i.e., any income the amount of which is determined for the most part by decisions the concerned unit cannot control), we distinguish 'production economies' and 'circulation economies'. Rent economies are an ideal type of the latter: individuals, groups, even the state, compete for the control of rent. In that view, most economic activities are to be considered as means of ensuring income circulation, rather than production-oriented behaviour. Arab states exemplify to a large extent this ideal type. We are struck, indeed, by the overwhelming importance of oil as a rent for the whole region. For major producers, oil is a quasi-exclusive source of original income depending to a great extent on non-national decision centres. Most activities are therefore 'subsidised' by products of oil revenues. For non-oil countries — even when a genuine productive sector exists — a growing part of economic activity is linked to oil money produced through labour and capital movements. The incongruity

between 'resources' and 'uses' in national accounting terms is much higher in most Arab countries than in developing countries in other parts of the world. The resource deficits of Middle Eastern states such as Egypt, Jordan, Syria or Sudan are just as massive and cumbersome as oil surpluses have been for a long time for Saudi Arabia, Kuwait or the United Arab Emirates.

In this context, the role of the state is paramount: it is the unavoidable instrument of resource allocation whether in liberal or socialist regimes. Paradoxically, the state plays an even more determinant role in the economic activities of liberal countries through budgetary expenditures (in Saudi Arabia, public spending accounts for over half the GDP), state-controlled or state-supported enterprises, food subsidies, administered prices, etc.

In most Arab countries, a growing part of the population depends for its living, either directly or indirectly, on unrequited transfers. Money comes from expatriate relatives, patrons or tribe elders, or state allocations. There is at best a tenuous link between individual income and activity. *Getting access to the rent circuit is a greater preoccupation than reaching productive efficiency.*

Anti-productive biases both influence economic behaviour and distort economic choices. Economic behaviour is biased in a rent-dominated economy by individual or even corporate group tendencies competing to increase their share of the circulating income. Given that goal, productive activities are not efficient. They stand as second-best choices for groups of individuals who are more or less excluded from the rent circuit. In most cases, handling productive activities is the 'privilege' of expatriates, immigrants and minorities. Reluctance to do productive work is a widespread attitude among dominant groups. In any case, most people have not much to gain from the risks and pains of active work when they get easier benefits from rent sharing through sponsoring, import trade, brokerage, or real estate and housing speculation. Economic choices are distorted by the contradiction between rent-controlling political strategies which aim at stability and the unavoidable emergence of new social values which a successful economic strategy would necessarily imply.

The case of industrialisation is a good example of this contradiction which compels economic agents to follow the path of what we call a 'failure-oriented policy'. In that respect, industrialisation policies are less committed to selecting objectives (giving them priorities, implementing those goals), than to selecting appropriate *means* (of spending money, distributing income, providing power, hegemony or rent control). A global view on the very limited successes and major failures of industrial policies in Arab states, oil rich or not, in the late 1970s, seemed to confirm the generalised rentier state paradigm. Even though Arab rulers pay lip service to industrialisation, their allegedly consistent industrial strategies hardly go beyond spending programmes. No real answers are given to such fundamental questions as linkage effects, economies of scale, labour training, market size, or insertion in the world economy.

Despite some remarkable exceptions (such as the Bahraini dry dock and aluminium plant), there is little or no coordination between industrial perspectives in the various Middle East Arab states. Competition for prestige or leadership often leads to redundant projects. Optimal allocation of resources on a regional basis is not a determinant preoccupation. Most 'productive' investments reveal a preference for infrastructure, public works, construction, and expensive 'big projects' that are vulnerable in an unfavourable economic environment.

Confronted with the major problem of building domestic order and regional stability, the Arab states tend to use economies as a way of solving strategic puzzles. It is the very industrialisation process which contributes to state-building rather than the state which helps to build a national industry. The strategy of industrialisation is therefore part of a strategic plan.

If the above analysis is pertinent, the generalised rentier hypothesis may significantly improve our understanding of attitudes toward industry in most Arab states. Useful as it may prove, it none the less accounts for only a part of the overall picture, just as the simple two-way distinction throws light on only another part of the same picture. Actual conditions prevailing in the Arab world reflect a more complex reality, calling for less simplifying assumptions than were used at the height of the oil boom. Disparities within each group of states tend to enlarge, reducing the explanatory contribution of any single classification criterion. Similar attitudes are observed in states belonging to the production or to the allocation category, while policies concerning external revenues and their utilisation reveal striking contrasts within a given category.

Political turmoil in the Middle East, the changing world economic outlook, depressed markets for oil and oil-related products, reduced income for pure allocation states, justify the introduction of new parameters in the model, differently affecting various Arab states. State policies have to integrate a growing number of unfavourable factors, and so do private economic agents' behaviour. The adjustment process will differ from one state to the other. Production and allocation still constitute a basic reference, with a special mention for the generalised allocation hypothesis; however, the analysis of the actual situation requires the introduction of new criteria and the abandonment of a simple, single, clear-cut distinction between two types of states. As oil income dwindles and the first stage of an infrastructure-dominated investment policy comes to maturity, allocation states deeply need precise policy guidelines, while the nature and consequences of the induction process in states receiving transfer income is greatly modified.

A reassertion of the role of the state and its implications for allocation attitudes

New constraints and changing attitudes may be observed through the evolution of the role played by the state in Arab economies. Many countries have inherited a strong public sector and a high level of state intervention in the working of the economy. Three levels of 'state presence' in the economy may be distinguished (Chatelus, 1984: 101): as a builder of infrastructure, the state creates the necessary conditions for the effective working of a productive system, whether public or private. This is a case of the 'philosophy of infrastructure development' (Bowen-Jones, 1984).

At a second level, the state behaves as an allocative agent. In the Gulf it distributes to the great majority of nationals at least part of oil revenues: it is a question of survival. In oil-poor countries it has to establish and maintain some sort of allocation policy (through food subsidies, for instance).

At a third level, the state directly competes with the private sector by taking direct charge of productive activities and acting as the major economic agent, especially through a system of public enterprises or state-controlled business concerns. In most Arab countries, whether capitalist or socialist, the public sector dominates industrial production, investment and employment.

The present state of affairs in the Arab world produces a trend toward the privatisation of the economy, which has important implications for the attitudes toward industry and services.

The relaxation of economic controls, the 'opening' of the national market to foreign goods and capital, the sale of public shares to private interests, or the new emphasis laid upon the introduction of market considerations and efficient managerial attitudes in the public sector, are some of the expressions of a general tendency affecting, with a varying intensity, most Arab countries. The wide range of concerned states extends from Saudi Arabia to Algeria and Egypt. Privatisation may be analysed in a certain sense as a move towards the reconsideration of allocative and circulation attitudes by direct or induced rentier states. Since massive allocation of income by the state is limited by economic constraints, governments will try to reach a more satisfactory balance between available resources and distributed income.

Evidence of such a tendency is apparent in the public expenditure commitments and budgetary measures adopted in several Gulf states. In short, there are currently some *major reconsiderations of salient features of the welfare state*. In Kuwait, we observe deliberate attempts to remove the welfare mentality to which the population has been accustomed by long growing oil revenues: for instance highly subsidised gas and oil prices were increased sixfold in 1982/3. The prices charged for electricity and water may well be increased significantly; they are currently sold much below cost, which encourages waste (in 1982/3, the subsidies on those items reached almost 800 million dollars.) It is also reported that ministers talk increasingly about the possible introduction of charges for medical care which is now absolutely free. In Saudi Arabia, there have been cuts in the subsidies paid in petrol, electricity, water and certain foodstuffs, though the amounts involved have not been great. In the UAE, charges for medical care for non-nationals were introduced in May 1983. (Non-nationals have to buy both a yearly medical card and cover the costs of major operations.) Unprecedented talks about income tax are reported. It would be premature to conclude that 'the end of the welfare state' is near, but proper consideration should be given to the multiple signs of economic pressures on the largesse of the allocative state (*Financial Times*, 23 Feb. 1983 or 25 April 1985).

In 'non-oil' countries (or should we call them production states?), the objective of political survival, supported by induced rent income, has for many years fed an uneasy but somewhat manageable compromise between limited domestic resources, increased needs and a minimum level of mass consumption. Subsidies for popular consumer goods, especially food and kerosene, have become the omnipresent political means utilised to limit wage escalation and ensure a minimal redistribution toward the lowest income groups. Today few, if any, states escape the 'subsidy trap'. Under IMF pressure (or more plainly under financial necessity), recurrent attempts have been made from Morocco and Tunisia to Egypt and Syria to reduce the food subsidy bills. This burden can absorb up to 30 or 40 per cent of budget allocations, as is the case in Egypt.

The immediate political upheaval provoked by increases in basic food prices (especially bread and edible oil) gives full credence to the notion of 'allocation policy for survival'. 'Bread riots' have deeply shaken Morocco, Tunisia, Egypt and Sudan. Algeria alone was able to reduce significantly subsidies on basic commodities, by including food price increases in a broad wage revision and economic reform package. Unfavourable economic effects (waste, budget deficits, high import bills, low prices for local producers) and perverse social results (subsidised goods do not necessarily reach the highly needy, especially in rural areas) impose upon governments in one form or another a reduction of the food bill by reducing the gap between food costs and food sales prices. This is not only a necessary constraint of any 'privatisation policy' (which some attack as an 'IMF dictate'); it is a critical issue which conditions any improvement of the working of the economic system. All countries are concerned. Clearly there is a trend toward less allocation in allocation states and a growing burden of allocation constraints in would-be production states.

States and production: changing attitudes in the Arab world

New conditions in the world economy leave little choice to the Arab states: the necessary shift in the economic structure toward more productive activities and the reduction of dependence on external income should cease to be a mere ritual invocation: new sources of diversified income have to be found. Efficiency in production and a better control over allocation-induced attitudes are urgent necessities for all states. Signs of changes in attitudes responding to this challenge are multiplying, although the burden of the past still decisively influences the present poor performances of the productive sectors in both oil and non-oil countries. The privatisation drive and the trends toward less direct allocation revenues do not imply a reduced role for the state. On the contrary, in efficient production economies, the role of the state is paramount.

A brief glance at some of the 'new industrial countries', such as Korea or Taiwan, reveals the magnitude of the place occupied by the state in a successful industrialisation process. The nature and content of the state intervention, the specificity of the economic planning process, help, by contrast, to delineate the reasons of the reduced efficiency of state intervention in most Arab 'production states'. Several aspects of state intervention in a country like Korea are worth observing as illustrative examples of this contrast. The state determines the objectives of the country's economic strategy and the content of the leading (interrelated) industrial choices through an efficient long-term planning process. Therefore, planning does not appear as the expression of the state political vision of economic development through a catalogue of projects, but as an instrument of guidance and stimulation for all concerned economic actors. Global planning is complemented by sectorial programmes. In Korea, for example, successive programmes have been devised for shipbuilding in the 1960s, for machinery and equipment and nuclear energy in the 1970s, and for electronics in the early 1980s. When necessary, the state invests directly in the recommended activities and creates appropriate institutions to help and follow-up plan implementation. We should also mention the importance of the channelling to industry of local financial capacities and the crucial role attributed to technological formation and the development of a national engineering capacity. *The state emerges as an active engine for industrial growth*, not only through the industrial projects it promotes, finances and controls, but through the overall impulsion and cohesion it brings to the industrial sector (Courlet and Judet, 1981).

In the Arab context, such a prescription requires drastic changes in attitudes and rapid solutions to several urgent problems. In entering the world market for high technology — high capital products, such as petrochemicals, aluminium

derivates or fertilisers, Arab industries cannot rely on excessive subsidies and state privileges. They have to be fair competitors, in order to avoid tariff barriers in Western countries. Regional cooperation, such as it develops between members of the GCC, requires well-monitored projects of proven feasibility. Joint ventures with foreign firms have to break even in a reasonable period. All these requirements imply a favourable economic environment created by the states, and a new type of industrial policy.

In the domestic economies, the heart of the argument is to be found in the consequences on consumption of the increases in oil income and purchasing power created throughout the region by the wide circulation of oil-linked revenues. Not only do growing food dependency and soaring food imports highlight the demand for more to eat and a better diet, but a great number of consumer goods have become very common even in low-income countries (Egypt or Yemen, for instance). The greatest part of those increased consumption needs was satisfied through growing imports as long as sufficient rent income was available. Public spending has been the most powerful channel to encourage private consumption (including budgetary subsidies). Under the prevailing conditions, state spending thus creates supplementary demand much more rapidly than state investment and public production can match by a corresponding increase in supply.

The only possible answer is for the state to support private production activities; such support can be understood as a direct consequence and natural outcome of public spending. Populist inclinations in such countries as Egypt, Algeria, Syria or Iraq are less and less compatible with developmentalist attitudes (implying high investment ratios and massive capital accumulation). With declining external income to pay for imports and the irreversibility of new consumption patterns, the necessity to meet growing consumption needs imposes on the Arab governments new alternatives or combined attitudes toward the production sector. They may try to stimulate positive responses from the private sector through various policy measures: profit rehabilitation, credit facilities, tax exemptions, relaxation of controls, etc., and/or they may aim at increased efficiency in the public sector.

Concerning the first point, in recent years, most governments in the Arab world, whatever their past or present commitment to socialism or state control, have conceived and implemented specific measures to encourage private production and stimulate the initiatives of independent producers. From the official recognition of the 'non-exploitive character' of small-scale private property in Algeria (Bernard, 1984) to the adoption of credit facilities, tax exemptions, customs duty facilities, etc., numerous cases of policy measures in favour of private initiative and investment can be noted. Saudi Arabia encourages light industries by reducing almost to nil land acquisition costs, and providing long-term per cent loans and almost cost free electricity. Not surprisingly, Qatar, Kuwait and the Emirates have adopted similar policies of 'subsidised privatisation' (as an intermediate step between direct state intervention and pure market activities).

Small and medium size enterprises are a favourite target for any private sector investment policy, as they appear both politically safer than powerful companies and economically complementary to large public sector undertakings. Most development plans or economic programmes pay due tribute to the essential functions to be fulfilled by those enterprises. In the Gulf countries, substantial achievements have been recorded in Saudi Arabia, where the fourth plan (due to start in 1985), will be 'above all a plan for the Saudi private sector' (*Financial Times*, April 1984). Several hundred enterprises run by small entrepreneurs already exist, mostly in food processing, building materials and mechanical work. A qualified observer speaks of 'the great surge towards industry witnessed in Saudi Arabia in the past three years'. In Qatar, Bahrain, Kuwait or the UAE, similar efforts to encourage local businessmen to take over joint ventures or to launch new enterprises (partly making use of the output of national industries: aluminium, steel, chemicals) have met with uneven but not totally insignificant responses. Cooperative developments within the Gulf Cooperation Council countries should be of great aid. Presently, the products of private industry represent 3 billion dollars of savings in imports in GCC countries (Daddab and Mihyuddin, 1984).

'Small is beautiful' seems to be the motto behind the scenes in the recent economic measures adopted in Algeria where two kinds of small businesses have been encouraged: local public enterprises and private sector activities. Their extension is a priority objective in the third quadrennial plan; several specific laws were passed in their favour in 1981 and 1982. Jordan, Morocco and Tunisia, among others, have multiplied measures favouring small and medium sized firms. Though Moroccan private capital is conspicuously reluctant to invest in industry, Jordan and Tunisia have obtained encouraging results. In Syria and Iraq, legal dispositions encouraging private industrial investment have met with very limited success so far; this is because the would-be entrepreneurs have doubts about the governments' political conversion to the ideological legitimacy and economic efficiency of private enterprise.

On the other end of the economic spectrum, the whole system of state capitalism and state control over the main productive activities, often through bureaucratic and highly inefficient public enterprises, is under critical examination: direct (but partial) answers are expected from the restructuring of the public enterprise system. Algeria aimed at breaking feudalities by dismantling the giant 'sociétés nationales' and fragmenting them into smaller independent entities, easier to control and to manage efficiently. The underlying idea is that smaller companies should prove more sensitive to preoccupations of efficiency, escape the excess costs of huge state monopolies and invest personal responsibility in their managers. In Egypt the abolition of the general organisations by law 111 in 1975 was considered a step toward more effective responsibility on the part of company heads (Waterbury, 1983). The absolute necessity of improving the performance of public enterprises is a recurrent theme in the political and economic literature of all countries with a large public production sector. Algeria's President Chadli and Prime Minister Brahimi have often insisted in public in the last two years on the low productivity and lack of efficiency of the public sector. In October 1984, President Chadli asserted that (public enterprise) 'profits were legitimate as long as they were genuine profits' (*Le Monde*, 19 Sept. 1984). A 1980 report on Syria mentioned a debate on 'whether the private sector should be given a greater role either directly or indirect *through the public sector adopting some of its techniques* to gain efficiency' (McDermott, 1983). In Sudan, rehabilitation plans for big farm projects and sugar factories strongly rely on the adoption of market incentives and privately oriented management criteria: for example, it is recommended that tenants of public land be charged for inputs and their incomes be determined according to their effective production. In Algeria, one of the main targets of the 1980–4 plan is decentralisation, for political as well as managerial reasons. The introduction of competitive behaviour between enterprises in the public sector is often presented as a means of improving productivity and increasing efficiency (such proposals are often made in Egypt and Algeria).

The trends we have just decribed do not invalidate the Middle Eastern Arab states paradigm (extended with some qualifications to Maghreb countries) of circulation and allocation dominated economies. However, they did add two important perspectives. The first is the fact that political survival cannot be guaranteed any longer by a skilful allocation policy dominated by a few oil-rich states; production aspects are becoming increasingly important. There is an urgent need for state legitimacy based on efficiency in the productive sector, rather than on its position in the allocative circuit. Second, the increased role of market forces and private agents reacting to government stimuli and price incentives will not necessarily provide Arab economies with the desperately needed efficiency in private and public management. Allocation biases remain extremely influential and legislative changes cannot, by themselves, change economic conditions: the final outcome has yet to be determined.

ATTITUDES TOWARD INDUSTRY: AIMS AND ACHIEVEMENTS

Industrial objectives in a political perspective

In many countries of the region one can observe the prevalence, from the late 50s to the mid-70s, of an industrialisation ideology which privileges political considerations over purely economic conditions and constraints. When oil resources are available, they temporarily strengthen the policy toward industry. The declared ambitions of several important states, often newly independent or having just achieved total emancipation from Western control, are to establish the economic basis of autonomous growth: the political process of state building is closely connected to the economic-political process of establishing an industrial infrastructure. Disappointing results recorded in the manufacturing sector clearly point to the unfavourable consequences of such overdetermination by political considerations (the allocative aspect of which is evident). We may tentatively

distinguish four categories of states, according to the amount of money they can allocate to industry, the past and present importance of value added manufacturing activities and the intensity of allocative influences on productive choices.

The most significant and controversial category is constituted by *'pure' allocation states*, essentially the six members of the Gulf Cooperation Council (GCC) on the Arabian Peninsula: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. They claim to diversify their economy through industrialisation and the development of productive activities, spending part of their oil income on huge infrastructural works and large industrial projects. Until recently, there was little or no coordination between concerned states (even within the United Arab Emirates) and duplication was conspicuous whether in infrastructure (seven international airports within a hundred mile range) or in plants and manufacturing units: aluminium smelters, fertiliser and petrochemical plants, dry docks, etc., seemed to multiply and lead to harmful competition. With the limitations imposed by a shortage of labour, relatively small markets and the strong dependency of most projects on the availability of free oil and gas, the authenticity of the claim for 'diversification by industry' has, of course, to be questioned. To a large extent, oil states tried to buy legitimacy through conspicuous spending on spectacular industrial schemes.

When the oil glut led to the reduction of the Gulf States' revenues, the greatest part of the expensive basic infrastructural work had been completed (water desalination plants, electricity generators, transportation networks, gas collecting installations, etc.), paving the way to the much hoped for 'exchange of assets' (Kerr and Yassin, 1982: 167), where industry would replace oil as a major source of income. A first wave of big industrial projects has also recently been completed: refineries, fertiliser complexes, aluminium smelters, steel mills are now realities in Qatar, Bahrain, Saudi Arabia and Kuwait. There are technical succcesses, and a few financial successes as well: ALBA (Aluminium of Bahrain), QASCO (Qatar Steel Company) or QAFCO (Qatar Fertiliser Company), the HADEED steel mill in Saudi Arabia, and fertiliser units in several states. There are also numerous cases of abandoned projects, delays, overcosts and low-capacity utilisation, due either to changing economic conditions and suddenly depressed markets, or to technical and manpower difficulties.

Qatar and Bahrain represent particular cases, where value added in manufacturing accounts for a sizeable share of GNP. Bahrain's industrial achievements benefited from regional cooperation and Arab joint ventures actively supported the well located, small and oilless state's industrialisation policy. A limited but dynamic industrialisation process is now working in Bahrain, with a second generation of industrial projects, including important private investments, due to mature in the coming years. Income from manufacturing accounts for 10 to 15 per cent of GNP. Qatar also displays industrial realisations making a systematic use of gas as cheap feedstock and fuel, and absorbing surplus capital. Qatari long-term development plans have established the customary heavy industry units: fertilisers, steel rolling, petrochemicals and cement. The list of first-generation massive projects has apparently now been completed and much attention is now paid to the expansion of Qatar's second tier of industrialisation (downstream activities) and to the encouragement of greater participation of the private sector in industry. Industrial income reaches 10 per cent of total GNP.

The contrast between Qatar and Bahrain on one side and Kuwait on the other, illustrates the wide range of attitudes in allocation states. Industrial ambitions of Kuwaiti ruling elites have always been limited, and cautious plans for industrial diversification have been shelved in the recent period in response to the reduction of oil income and in order not to exacerbate the expatriate labour problem. With the apparent indefinite postponment of a large-scale petrochemical project which had been adopted in principle in 1982, oil refineries and a fertiliser plant remain the only heavy industries in the country (we should however remember that half the petroleum exports are now refined products). Allocation attitudes and the 'rentier state' mentality have thus been recently reinforced by the evolution of the environment. A choice has been implicity made (and is now more overtly uttered) not to develop a heavy industry base from which to derive downstream manufacturing industries. Earmarking part of the oil revenues for a Fund for Future Generations, Kuwait has given preference to investment abroad: 'good will' allocations through direct aid to Arab countries and the Kuwait Fund for Economic Development, regional investment through participation in joint ventures in Gulf countries and other Arab countries. Due to the early start of the Kuwaiti economy, a number of industrial enterprises produce intermediate and

consumer goods. Manufacturing contributes from 5 to 7 per cent of GNP. Increased competition, the recession in the Gulf and the aftermath of the financial crisis of Soukh el-Manakh, will impose a drastic revision in the management of existing industries and the adoption of more efficient methods; few existing indutries presently meet the criteria for survival. Kuwait state policy toward industry clearly reveals the limitations of productive efforts in a pure allocation context (investment income is half the size of oil income). With local specificities (especially in Dubai), the United Arab Emirates and Oman display a similar trend in their attitude toward industry.

Saudi Arabia, another pure allocation state in the original stage, illustrates the obstacles which must be overcome in order to implement an efficient policy to reduce dependence on oil, and establish a productive industrial sector. Present achievements do not offer clear-cut answers concerning the possibility for an oil state to escape the allocation trap. A long-term development policy, aiming at the rapid industrialisation of the kingdom, was adopted in the mid-70s. Beside the construction of several big petroleum refineries, Petromin (a specialised state institution) was charged with the building, operation and marketing of the products of a number of huge industrial projects. These projects respond to two principal criteria: they utilise the country's huge hydrocarbon (especially gas) resources, and they do not require abundant manpower. Over-ambitious schemes elaborated during the frantic years of the oil boom had to be reconsidered. A manageable, although sizeable programme for ten major industrial units (not including refineries), eight of which are in the petrochemical sector and two in iron and steel production, was adopted and implemented. Two specifically conceived industrial sites in Jubail and Yanbo were built to house the petrochemical projects (and later the second-generation industries). Major Japanese and American firms are SABIC partners in joint ventures (except for one project which saw the withdrawal of Dow Chemical). Those foreign giants will have the responsibility for the bulk of the marketing of the new products (ethylene, methanol, low-density polyethylene, urea, etc.) which are already on stream or were due to be in the first part of 1985. Saudi Arabia is adding 4 to 5 per cent production capacity to the world chemical output. When three petroleum refineries presently under construction are completed, the first stage of Saudi industrialisation will be achieved. We are thus entering the decisive stage: the development of a second generation of intermediate industries oriented toward local and regional markets (and not exclusively exporting on world markets), utilising part of the output for heavy industry and establishing links with the dynamic but vulnerable private sector manufacturing consumer goods. The crucial test will be the ability of industrial enterprises, both public and private, to live on their own with decreasing state support and to face increasingly fierce competition. Saudi industry, like other Gulf states' industry, remains to a large extent the expression of a spending process depending upon allocative attitudes. It has yet to prove itself capable of becoming a genuine source of income, alternative to oil income.

In a second category, we will place states long dominated by a *strong industrialisation ideology*: Algeria, Libya, Iraq or Syria. They put high hopes in the emancipation potentialities of a voluntarist economic policy, as part of a strong reaction against colonialist domination. In the case of Iraq, Algeria and Libya, oil income is a unique and important source of investment finance. In the case of Syria, the meagre surplus has to be enlarged by transfer revenues. Nationalised enterprises and heavy investment in basic industries are the preferred instruments of the state political commitment to industry.

We can briefly examine the Algerian case as a good illustration of the potential achievements and the harsh constraints of such an approach. Algeria's strenuous post-independence efforts to conquer economic independence as a key to political independence led to the construction of a strong industrial basis, financed by oil revenues. The Algerian experience has attracted much attention and given rise to extremely divergent appraisals (Thiery, 1982). The price paid for forced industrialisation has been heavy: a slow increase in individual income and consumption, particularly a complete neglect for the housing sector and public utilities; a soaring imported food bill, a consequence of the virtual collapse of the agricultural sector; poor management and reduced capacity utilisation in big state-controlled complexes unable to extend the expected backward and forward linkage effects. Bureaucratic controls and political rigidity led to quasi-stagnation of industrial production in the early 80s. An allocation-induced attitude paradigm applied to Algeria points to the disturbances introduced by the existence of oil income: excessive importance given to political criteria at the expense of

economic considerations; extremely high investment rates (over 40 per cent of GNP) extending capacity beyond efficient utilisation; underestimation of the dismal performance of agriculture as long as the growing food bill could be settled with the hydrocarbon rent. On the positive side of the balance sheet, Algeria can claim a more sensible use of its oil and gas resources than that observed in other oil states, fewer social inequalities (although they might be increasing), a potential ability to assess past performances and to take care more efficiently of agricultural needs and decentralisation necessities. An optimistic point of view may consider Algerian shortcomings and the high cost of developing gas reserves and building heavy industry bases as the unavoidable price of a learning process — the *entrance fee* a state has to pay to master a development process; dividends come later. A more sceptical perspective will reluctantly accept such an emphatic assertion and consider that allocation-induced biases have ruined Algerian potentialities and that oil has been 'the worst thing that could ever happen to Algeria'.[1]

Egypt is in a category by itself, although the same political attitude as found in the preceding group prevailed in the Nasser era. The 'industrialisation of Egypt' is less felt as a political choice than as a 'must', the desirability of which stems from the necessity to create employment opportunities and to increase a desperately small *per capita* income. Furthermore, the Egyptian industrial potential was not negligible in the late 60s (it exceeded probably that of all other Arab countries together), while the financial resources available for industry were dramatically insufficient. One specificity of the Egyptian case today lies in the ambiguities of the state attitude toward the appropriate means to encourage and finance industrial expansion, while the industrial objective remains unquestioned (which is not necessarily true of the states in the first group). The *infitah* policy (Kerr and Yassin, 1982; Waterbury, 1983) undoubtedly reinforced allocation induced behaviour in the Egyptian economy, with skyrocketing manufacture and food import bills and a rapid increase of the share of external income (worker remittances, Suez Canal tolls, oil revenues, tourism, foreign and Arab capital) in GDP. The recorded foreign investment in industrial projects, either in free zones or in joint ventures with Egyptian private or public capital, is rather disappointing. The greatest part of foreign capital has been allotted to financial and tourist services, real estate and speculative construction. The present development plan (1982–3 to 1987–8) allocates a sizeable amount of money to industrial development, with high priority for food, clothing and housing in order to reach self-sufficiency by the year 2000. Another priority is for non-oil exports, expected to rise by 13.5 per cent a year, to offset the anticipated decline in oil income. The public sector still accounts for three-quarters of the industrial investment under the five-year plan (about $7.5 billion), and for two-thirds of the production. There is, however, an obvious allocation aspect in the attitude of the state toward public enterprises: they are used as a means to re-distribute income to the people through below-cost prices and excess employment. The recent reorganisation of the public sector in 1983 went only halfway toward an authentic reassertion of the role of the public sector as a means of efficient production. The main question is the degree of compatability between the extreme dependence of the Egyptian economy on external resources and its conversion to productivity, efficiency and competitive attitudes in the industrial sector. It is a source of concern to notice that the most convinced opponents of this dependency upon external resources are also the most reluctant to give the public sector the autonomy and the financial means allowing it to become the stronghold of Egyptian industrial expansion. How long is it possible to allocate through the public sector revenues it is unable to earn?

We find in a fourth category countries where a *limited state commitment to industrialisation* ideology does not prevent *an active and often efficient industrial policy*. Tunisia, Morocco, Jordan and, with limitations, pre-war Lebanon may be numbered in this category. Industrial exports account for a sizeable part of total exports; medium and small-sized enterprises expand in a favourable environment. The nature of the relationship between the state and the emergent category of 'bourgeoisie d'affaires' is open for discussion. In the three countries (we exclude Lebanon), natural mineral resources are the basis for an export sector developed through public investment. A growing part of the phosphates output (in all three countries) or potash (in Jordan) is processed in heavy installations within the country. The manufacturing sector, strictly speaking, is largely private and the share of export in manufacturing value added is significant: either exports to regional markets (Jordan) or in the framework of some sort of international division of labour (Morocco and Tunisia). In order to reduce unemployment and

lessen dependence upon mineral exports, industrialisation has been recently stressed as a priority, especially in Tunisia. Although external revenues are important in these countries (particularly workers' remittances in all three, oil in Tunisia, grants and aids in Jordan), allocation biases are certainly less predominant than in the other categories of states: a major step toward a production economy has been accomplished.

From attitudes to achievements: Arab industry in perspective

The present dimension of the industrial sector in the Arab countries accurately depicts the ambiguities and contradictions of the Arab states' attitudes toward industry in the last 25 years. Global figures of industrial output should, of course, be taken with caution, but they offer us a general perspective.[2] Starting at a very low level of industrial development in the late 50s (except in the case of Egypt), the rates of growth of the manufacturing sector in Arab states were high in the 60s and 70s, as compared to the average of developing countries; and an increase in the annual rate of growth was recorded in most countries for the period 1970–80 as compared to 1960–70 (such is the case for Egypt, Algeria, Morocco, Tunisia and Jordan). Among countries which achieved an annual rate of growth of manufacturing value added (MVA) exceeding 10 per cent during the years 1970–2, are Libya, Jordan, Algeria, Tunisia, Morocco; Egypt is not far from this score with 9.2 per cent. The ECWA region as a whole reached a 7.6 per cent annual MVA growth rate in the 1960s and 10.7 per cent in the 1970s (in constant prices). These encouraging results should not however lead us to overestimate the absolute and relative weight of industrial achievements in Arab countries. The share of the manufacturing sector in total GDP reaches only 8.2 per cent in the ECWA region and 8.6 per cent in the Arab world. In 1982, the manufacturing sector exceeded 10 per cent of GNP in four countries only: Egypt (27 per cent), Morocco (16 per cent), Tunisia (13 per cent) and Jordan (13 per cent). Only in Egypt is the value of industrial production large: about $4.500 million; Saudi Arabia ($3.568 million) and Morocco ($1.960 million) are the only other countries whose industrial production exceeds $1 billion. The percentage of manufactured goods in total exports is sizeable in four countries only: Egypt (8 per cent), Morocco (28 per cent), Tunisia (23 per cent) and Jordan (43 per cent).

In terms of employment, attitudes toward industry are sharply contrasted in pure allocation states as opposed to other states. In the former, concerns about the growing number of expatriate workers have affected the drawing up of industrial policy and lowered industrial ambitions (especially in Kuwait). The 'exchange of manpower for hard currency' (United Nations, 1983), a paramount dimension of the allocative attitude, has been strongly questioned from the manpower exporting country point of view as well. Manufacturing, in any case, is not a great labour user, particularly in the heavy industry projects where labour requirements are minimal. In the other categories of states, employment objectives are essential, and the recent drive to encourage the private industrial sector has its roots in the urgent necessity of increasing 'genuine' employment. Official statistics of the workforce in the manufacturing sector should be carefully scrutinised, as an increase in the number of wage earners may be the mere consequence of an allocation bias in the industrial policies: a measure of growing inefficiency. State enterprises, for instance, are often overstaffed and labour redundancy expresses political and social constraints on the productive sector. This has long been the case in Algeria, Syria, Iraq and Egypt. The recent evolution towards more productive behaviour and efficiency-oriented management implies drastic cuts in subsidised employment, and an increasing demand on the private sector to create new jobs (Algeria openly admits this perspective). Very little is known about employment in small companies and in the 'informal sector'. Empirical studies, however, convey the idea that the informal sector is much more dynamic and efficient than is generally expected, for instance in Tunisia or Morocco. The role of the state in taking into account and fostering this form of private entrepreneurship must be analysed.

A brief glance at the sectoral distribution of manufacturing activities confirms the contrast between oil economies and the other economies. The chemical industry, in its early stages of development, accounts for the bulk of recent massive industrial investment, concentrated in a few allocation states. With the recent coming on stream of the major petrochemical projects in Saudi Arabia, this tendency will be strengthened. In 1980, value added in chemical manufacturing in the Arab world had already reached $8.5 billion, half of which was in Saudi Arabia. The

weight of petroleum-linked fertilisers and chemical intermediate products exported (mostly on the world market) will increase in the future, thus reinforcing productive activities in allocation states; this does not necessarily imply successful diversification. In other countries, the traditional 'big three' industries of developing countries take the lion's share of manufacturing value added: food; textile, clothing and leather products; building materials. Food industries, according the ECWA estimates,[2] represent around 10 per cent of Arab MVA. They are concentrated in a few states like Egypt, Algeria, Morocco, Syria and Iraq and are almost totally oriented toward the domestic market. If we add Tunisia to this group of countries, we will find the great majority of the clothing and textile industries, which rank third in Arab manufacturing with around 14 per cent of MVA. The only other manufacturing sector worth mentioning is iron, steel and metal working, which suffers however, as does the Arab manufacturing sector as a whole, from the weaknesses of backward and forward linkages. Either export-oriented for a few very specific projects of an extroverted nature (aluminium smelting, oil refining, chemicals), or limited to a small domestic market for traditional consumer goods, Arab manufacturing lacks an intermediate and equipment sector. The bulk of capital goods and heavy engineering products are imported, while agriculture (long neglected), cannot provide the food industry with the basic agricultural raw materials it transforms.

In conjunction with the necessary steps to reduce the structural industrial imbalance, Arab industry has to improve its efficiency and to modify the nature and scope of state intervention in the productive sector. We have already dwelt upon the imperative reconsiderations of state attitudes and of the allocation content of industrial policies. We may briefly present the essential consequences for the industrial situation, either in allocation states or in production states. The end of the almost limitless oil funds available for all industrial enterprises implies drastic changes for the business community in Gulf countries. The trend in Gulf economies is well summarised in a recent study of the Saudi economy; 'In effect, the Saudi economy is becoming more normal. The government argument is that the days of the 30 to 100 per cent profit margins were bound to end at some point and that if the kingdom is to become a diversified modern economy, its companies must operate as companies do elsewhere' (Field, 1985). Similar comments are presented on the evolution of the economic situation in Kuwait, where 'the only industry that is going to succeed at this time is one that is well managed, with operating costs well trimmed, local tastes researched and the final product well marketed' (Evans, 1985). These efficient management constraints are not limited to oil-rich countries hit by depressed oil markets; we find them in all countries, and they concern public enterprises as well as private businesses.

At the same time, as some allocative aspects of industrial activities are questioned or suppressed, state support to industry is needed more than ever, and government, which continually encourages the private sector, remains the main locomotive for growth, in Saudi Arabia, as in Algeria, Egypt or Jordan. The main change concerns the forms of intervention and its general outlook: industry is less and less a channel for spending money with little concern for the productive result. The states' new interest in efficiency and competitiveness leads to more articulate industrial policies combining national preferences, financial incentive and, when possible, reduced direct subsidies. In many cases, cheap finance is available for business enterprises; for instance the Industrial Bank of the Emirates makes loans for industrial projects at 4.5 per cent with a three-year grace period; in Kuwait, industrial loans are set at 5 per cent and in Saudi Arabia at 2 per cent. Barter deals are increasingly imposed on foreign contractors who have to find suppliers and must propose local industrial counterparts in order to be awarded contracts. (Of course, this is more favourable to domestic industries than the better known barter agreements where the contractor gets petroleum in payment.) Pressures are also exerted on foreign companies for a rapid increase in the share of nationals — both qualified workers and staff — in their total payroll. Protectionism is not excluded, it tends to become part of a more active policy; the necessity to ensure competitiveness on regional or even world markets is now part of the picture, and direct support through subsidies cannot be the only answer.

Arab industrial growth will depend very much in the future on the capacity of the Arab states to coordinate their activities and to fully endorse *the regional and international dimensions* their industrial sector requires. The constraints of economic rationality and financial balance will thus increasingly limit allocation-induced attitudes in industrial policies. From that point of view,

regional integration is important to both oil and non-oil countries. Until recently, the creation of Arab joint ventures was the most visible form of Arab cooperation. A first step was taken by the Arab Economic Council of the Arab League, which created the Arab Potash Company. Later on, the Council for Arab Economic Unity (CAEU) set up four industrial projects in Jordan, Iraq and Syria, and the Organisation of Arab Petroleum Exporting Countries (OAPEC) has been active in promoting joint ventures among its member states (for example, it created the giant ship repair drydock in Bahrain). The concept of Arab joint ventures provides, however, only a partial answer to integration needs in the Arab world. Because it was based primarily on political considerations, the creation of the Gulf Cooperation Council (GCC) in 1980 did start a new era in Arab economic cooperation. The coordination of economic plans and industrial projects, the systematic search for complementarity, the gradual establishment of a common market between the six member states, will strongly influence governments' attitudes and compel them towards realistic industrial polcies. The second generation of industrial projects in Gulf countries will not stand a chance of success if the market is not extended to the whole peninsula at least. Concerning the international market for petrochemicals and other export oriented products, it is important to avoid competition between Gulf countries, and to compensate for the consequences of cyclic fluctuations as much as possible by coordinating investment decisions. Each single state has to take into account other states' projects and this is a limit to prestige investments devoid of real economic sense.

There are *no equivalent moves* in other parts of the Arab world, and no sign that GCC may expand to include other ('production'?) states. The present industrial situation in non-oil countries, however, brings into focus the importance of regional coordination to overcome the high unit costs and low efficiency due to the insufficient size of individual domestic markets. The reduction of external revenues accruing to the states of the region will diminish their import capacity as well as their ability to allocate growing subsidies to inefficient local producers in order to satisfy local demand. The only sensible way out, hence, will be a regional approach to the problem of mass production of consumer goods in local industrial establishments; this implies more cooperation and less allocation. Turning to the intermediate goods sector and the new production lines required in the near future, each individual state has to give up its exclusive point of view in order to implement a regional design. Purely political considerations and predominantly allocative use of available funds will cease to be valid criteria as concerns industrial policies.

ATTITUDES TOWARD SERVICES: ALLOCATION THROUGH SERVICES AND PRODUCTION OF SERVICES

The evidence of different attitudes in production and in allocation states should be more striking in the case of services than in industry. The basic idea is that extending the number and the quality of services provided to the people is the foundation stone of an allocation state and the condition for its survival, while production states severely limit, for financial reasons, the quantity and quality of services they offer. Although this might appear self-evident, this statement still needs analysis and qualification. A conceptual clarification is required, in order to distinguish among very different types of services, displaying analytical links of various forms with the productive economy. The complex relations between states' financial and economic situations and their attitudes toward services will then be briefly considered.

Services: a meaningful economic category in the light of the production-allocation paradigm

The term itself is full of ambiguities. Figures in national accounts are rough estimates and may be misleading as 'all branches of economic activities which do not belong to the agricultural sector (agriculture, forestry, fishing, hunting) or to the industrial sector (mining, quarrying, manufacturing, construction, water electricity and gas), are registered as services' (World Bank, 1984). The economic nature of services, treated as a 'residual' sector, is thus extremely vague and uncertain, and further hypotheses must be introduced in order to analyse the place and role of services in the economic system. At any rate, a systematic distinction between productive and unproductive sectors is of limited validity, for the notion itself is questionable. There are, on the one hand, services which are the products of a

spending process: their quantity and their quality will thus depend directly on the amount of money allocated to them. There are, on the other hand, services which can generate money and increase the flows of revenue in the economic circuit. Whether initial 'productive work' is a prerequisite for the existence of both categories is an important but metaphysical question not pertaining to our present study. Delays and time lags may have a decisive impact on the issue: services which are money-absorbing in the short run, and the expansion of which requires an allocative capacity, such as education or health, may prove eminently favourable to production in the long run. The generalisation of such concepts as 'human capital' or 'investment in human capital' to analyse the extension of these services, as well as the dubious productive value to be attributed to giant prestige infrastructure or oversized industrial projects, point to the weaknesses of the basic opposition between productive and unproductive characteristics of an activity.

The analysis of services and attitudes toward services in the production-allocation states hypothesis leads us to utilise a fundamental distinction between *income-generating services and income-utilising services* (nothing to do with the usefulness of the services, but everything to do with production and allocation attitudes). The main income-generating services are transportation and transit activities, tourism, financial services, part of housing activities, research-development and engineering services, etc. The most important income-spending services are educational services, health and social services, the supply of subsidised goods, personal services, etc. Commercial activities or housing services may be considered, depending on the situation, as income-generating or income-spending.

Some significant trends in the production and allocation of services in Arab states

Despite the aforementioned limitations in the use of global figures, statistics on the growth rate of the service sector in a group of Arab countries provide useful information on the general evolution. Taking countries for which we have comparable data, we observe a firm tendency during the period 1970–82 for services to grow at a higher annual rate than GDP. In Egypt, Sudan, Morocco, North Yemen, the gap reaches 3 to 4 points per year; Saudi Arabia's situation is similar, while the difference is much greater in Kuwait, Libya and most probably in the United Arab Emirates. Some countries where we have identified a stronger propensity for industrial growth — Algeria, Jordan, Tunisia — display a different picture: the growth rate for services does not exceed that observed for GDP[2] (World Bank Development Report, 1984: ref. 3). Looking now at the share of services in GDP, the situation is changed, especially if we utilise non-oil GDP to calculate the ratio in oil rich states. The share of services is close to 50 per cent in most non-oil-dominated states: Egypt, Sudan, Morocco and Syria, the major exception being Jordan where it reaches 64 per cent. In oil countries, the ratio of services to non-oil GDP reaches 70 per cent in Algeria and exceeds 80 per cent in Kuwait, Saudi Arabia and Libya.

The main differences between 'pure allocation states' and the other states fundamentally rest on the absolute amount of money they have the capacity to allocate to certain types of services. There are no clear indications of significant divergences in the structure of public expenditure between the various categories of states, but in oil-based economies, public expenditures are a much greater part of total domestic expenditures and, of course, total income *per capita* is much higher: for example, Saudi public expenditures in fiscal year 1982/3 ($71 billion) well exceeded twice the Egyptian GNP of 1982 ($26.4 billion). Great amounts of money are thus allocated to education, health and various aspects of general welfare. This allows the citizens of Gulf countries to benefit from free (and even subsidised) education, subsidised electricity and water, often subsidised housing, and other health and welfare advantages which have often been described. A particular characteristic of many of these allocative services rests on their 'imported' nature: foreign employees far exceed the number of local workers in most services, particularly education and health: 100 per cent foreign staff is not uncommon. A striking example of huge spending expressing the importance of allocative attitudes is manifest in the developments in the higher education field. Each Gulf country, with the exception of Oman, has established at least one university; there are seven in Saudi Arabia. The Saudi government has spent $2 billion on the King Saud University project near Riyadh, which will handle over 20,000 students (in 1985). There are almost 100,000 university students in Saudi Arabia, and $7 billion was spent in 1984 for the seven universities. The cost of financing nationals' studies abroad has to be added to local spending on education in Gulf countries. With the lack of finance in non-oil countries, despite the high priority granted to education (10 per cent of public expenditures in Egypt and Jordan, between 15 and 20 per cent in Tunisia and Morocco) (IMF, 1984), the creation of a mass education service meeting minimal quality criteria has often failed to get beyond a purely symbolic stage.

Expenditures on health absorb a much smaller part of public expenditures in most non-oil countries: on average they do not exceed one-third to one-fourth of spending on education. The ratio is higher in oil countries where state expenditures on health are more than half those on education: these countries record an extremely rapid decrease in the number of inhabitants per doctor (utilised as a measure of improvement in the health sector); the reduction is tenfold in Saudi Arabia between 1960 and 1980, and 15 times in Oman. In Kuwait and the United Arab Emirates, we find a ratio of fewer than 1,000 inhabitants per doctor, a figure quite comparable to that found in Western industrialised countries. The situation is less favourable in other countries. But there are striking contrasts between Morocco, for instance, where the situation is bad — indeed worse than it was 20 years ago — and Tunisia where it has much improved. Surprisingly enough, Egypt, which has for years implemented a policy aiming at the satisfaction of the basic needs of the masses, displays a ratio of 970 inhabitants per doctor, which compares favourably to the ratio we find in oil countries; finding adequate financing to maintain such services and improve their quality will certainly represent an increasingly difficult challenge for the Egyptian authorities.

Not all developments in the service sector concern costly activities with little direct influence on domestic sources of income. There have been important improvements in the transportation sector in the Arab world, particularly, but not exclusively, in Gulf countries. This applies first of all to port infrastructures which have ceased to be the crucial bottleneck they were for a long time. Due consideration has also been given in many countries to the expansion and improvement of roads and even railways, and to connections with neighbouring countries. National shipping fleets have been developed by Kuwait, Saudi Arabia, Iraq and Algeria. Transit activities are a valuable source of income for Jordan, Dubai in the United Arab Emirates and

POLICIES FOR DEVELOPMENT

even Kuwait (where re-exports account for more than 80 per cent of non-oil exports). Tourism is a major source of foreign exchange and its contribution to the solution of unemployment problems is significant in Egypt, Morocco, Tunisia and increasingly in Jordan. Activities of this kind, however, as well as the development of luxury housing bought by Arab capital, or certain transit revenues, while generating additional income in the concerned countries, may reinforce allocation attitudes there, as their flows escape national controls and increase dependency upon external revenues.

Some oil countries have looked for diversification in financial activities, and are building a network of investment companies, banks and insurance activities in order to create financial centres partially replacing Western financial markets for local capital. Bahrain took the lead in 1975 by launching an offshore banking market. The volume of business steadily increased in the late 70s and early 80s, reaching $61 billion in August 1982. Since then, the market fluctuations have expressed the changing situation of the oil revenue outlook. More specifically, the financial policy of Saudi Arabia exerts a decisive impact on Bahrain's OBU (Offshore Banking Unit) results. The Offshore Banking Centre contribution to Bahrain's income is not negligible. Kuwait's ambitions and real capacities to become a regional financial centre have been shaken by the Soukh el-Manakh crisis and its lasting aftermath. Egypt and Jordan in the other group of countries, have also stressed the development of banking facilities: the Amman Financial Market is a small but efficient realisation. The near future will bring an answer to the crucial question concerning development in the financial sector: has Arab finance acquired the skills and the strength it needs to become an autonomous source of income? Or is it still a mere by-product of oil revenues, an allocation device unable to outlive the reduction in those revenues?

This brief overview of major tendencies in the service sector provides an incomplete perspective on the multiple developments in the last ten years. However, it confirms the main arguments of this study. Oil states allocate considerable amounts of money through services which constitute a basic instrument for self-assertion and claims for legitimacy. The financing of a welfare state, the benefits of which may be restricted to nationals, is a major component of allocative attitudes, while the economic rationality of service extension has been long

neglected. In other states, the extension of services meant to improve social conditions and satisfy basic needs has been limited by lack of resources, although part of induced allocation income is financing budgetary expenditures on social services. Income-generating services try to attract an increased share of regional oil revenues.

Recent trends in the region point to the need to reconsider oversimplified assumptions about such contrasting attitudes. Facing declining oil revenues, and anxious to reverse the unfavourable consequences of allocative attitudes toward industries and services, allocation states try to foster income-generating services, and to limit the expenses due to their welfare policies. They tend also to reduce subsidies on free or low price goods and services. They will increasingly found their claim for legitimacy on the usefulness of their spending and on the long-term perspecitives of an authentic diversification away from direct oil revenues. The other states, under political constraints and strong popular pressure, have little choice but to maintain and extend the provision of allocative services: free education, minimal health facilities, public utilities and low-price housing, food subsidies, etc. Such demands have been encouraged by the relative abundance of induced oil income in the past, whatever the level of production-linked resources. With such constraints on allocation, production states will have to prove increasingly productive in the future.

Clearly, the simple two-way distinction between allocation states and production states is increasingly confused, even when applied to the attitude toward services.

NOTES

1. To quote the remark (off the record) of a former senior manager of Sonatrach.

2. The World Bank and ECWA are the main sources for statistics. Very scarce data is available for Iraq and Syria in the recent period. The figures utilised to analyse the main trends concern Algeria, Egypt, Jordan, Kuwait, Libya, Morocco, Saudi Arabia, Tunisia and United Arab Emirates. ECWA members are the Arab countries of Asia and Egypt (for the recent years).

6

The State, Social Classes and Agricultural Policies in the Arab World

Hamid Ait Amara

For a growing number of Arab countries, it is no longer a question of which part of the agricultural surplus should be appropriated by the state, but rather that of a correct evaluation of national resources to be devoted to the rapid development of agricultural production, in order to make up for past negligence and to re-establish essential economic and social equilibria. While the 1960s were marked by a relatively high rate of investment and productivity growth, the 1970s saw a considerable decrease of the relative role of agriculture in the economy and the beginning of a process of marginalisation and restructuring of the countryside. The Arab countries have become extremely dependent upon foreign supplies to meet their food consumption, and devote a growing share of their currency reserves to cover imports, and of their budgets to support the price levels of primary food items.

At the beginning of the 1980s, a majority of Arab countries initiated policies in favour of agricultural development. Public authorities very substantially raised financial contributions to the agricultural sector, aid to the modernisation of farms, and agricultural prices, in order to stimulate production and improve producers' incomes.

In certain cases the new orientations have brought about a significant change in the nature of relations between the state, various peasant groups and the urban working classes. The rise in the price of agricultural products reduces the purchasing power of fixed-income earners, and in order to achieve the objectives that were set for the growth of production, the state would like to rely more on market-oriented farmers, and reduce

the role of the small peasants. Hence the food crisis, which almost all the Arab countries must confront, threatens the system of class relationships built up during the 1960s and 70s.

THE RETREAT OF AGRICULTURE

Since the 70s, the economy of Arab countries has undergone extensive restructuring, marked by the retreat of agriculture to the benefit of other sectors, and other sources of savings becoming more important for development.

The turning point was obviously the increase in oil production and prices which led to a substantial increase in hydrocarbons' export revenue.

This flow of new resources and revenue marginalised the relative importance of agricultural exports in foreign trade. In the 60s, agriculture accounted for 30 to 50 per cent of total exports (26 per cent for Algeria, 35 per cent for Tunisia, 33 per cent for Syria, 50 per cent for Egypt). At the beginning of the 80s, it accounted on average for only 5 per cent of export revenue (1 per cent for Algeria, 7 per cent for Tunisia, 4 to 5 per cent for Egypt).

In Egypt, between 1974 and 1980 oil exports, tourism, revenue from the Suez Canal and migrants' remittances totalled more than 90 per cent of current account revenue. Cotton had been the main agricultural export (at the beginning of the 60s generating 50 per cent of hard currency earnings): its exports dropped by almost 25 per cent. Other agricultural exports — citrus fruits, potatoes, onions and rice — have likewise declined in volume due to the growth in domestic demand and to the poor progress in production.

In Syria, cotton exports, which fluctuated between 200 and 250,000 tons per year in 1967/73, fell to 155,000 tons in 1976/7 and 117,000 tons in 1980.

Algeria practically stopped exporting its agricultural products in the middle of the 70s. In 1980/4 hydrocarbons made up 97 per cent of export revenues. In Tunisia oil products and derivatives hold first place — 880 million Tunisian dinars in 1983 — then come textile products — 339 million — and agricultural exports total only 86 million.

All traditional Arab exporters of agricultural products experienced the same marked decline of the role of agriculture in foreign trade, with the exception of Morocco, which is not an oil-producing country (along with Lebanon and Jordan). In the case of Morocco there was a small decline in the share of agricultural over total exports because of an increase of manufactured exports.

The restructuring of economic activity around the hydrocarbon sectors and, to a lesser extent, around manufacturing and services, has considerably weakened the relative importance of agriculture in gross domestic product. In Egypt between 1975 and 1980 the share of agricultural in the GDP fell by 7.5 per cent. It went from 30 per cent in 1960 to 16 per cent in 1981. The same happened in Syria where agricultural GDP went from 30 per cent in 1963 to 18 per cent in 1981; in Jordan from 9 per cent in 1979 to 7.3 per cent in 1982; in Morocco from 29.2 per cent in 1970 to 18 per cent in 1982; in Tunisia from 20 per cent in 1970 to 12.4 per cent in 1982; and in Algeria, finally, from 10.9 per cent in 1970 to 7.3 per cent in 1983.

Table 6.1: Agriculture in GDP, 1981

Country	Agricultural domestic product as % of total
Algeria	8.00
Tunisia	12.40
Morocco	18.00
Libya	2.00
Iraq	9.00
Jordan	8.00
Syria	18.00
Democratic Republic of Yemen	10.00
Yemen Arab Republic	29.00

Source: *Situation mondiale de l'alimentation et de l'agriculture*, 1983.

Except for the Yemen Arab Republic, the agricultural GDP is below 20 per cent everywhere, nearer to 15 per cent on average (see Table 6.1). In the 70s, the share of agriculture in total GDP declined because of a perceptible fall in the rate of growth of agricultural production. The latter was greater than 2.5 per year in the 60s, but fell to 1.5 on average in the period 1970/80.

Despite the large relative decline in agricultural value added, the population active in agriculture maintains a preponderant position in the structure of employment: 41 per cent in Egypt with more than 4 million *fellahs*, 30 per cent in Syria, 25 per cent in Jordan, 30 per cent in Tunisia, 24 per cent in Algeria, 35 per cent in Morocco. True, this represents an important relative decline compared to the 60s, but it must be pointed out that in absolute numbers the population active in agriculture has slightly increased in all countries.

However, the decrease in agricultural growth and the reduction of agriculture's role in the economy are apparently not in all cases due solely to the increase of oil revenue. In Morocco this trend principally reflects the crisis of the export-oriented model of agricultural development.

Countries which chose to maintain or deepen their participation in international trade in agricultural products must face particular problems. This is the case of Morocco and to a lesser extent of Egypt, Tunisia and Jordan, which decided to play the card of 'comparative advantage', and export high value added products while importing products with lower relative prices.[1]

With the progressive closure of their traditional markets abroad these countries today face a serious crisis in agricultural exports, affecting in particular Morocco and Tunisia, which have closer ties with the European Economic Community. The north shore of the Mediterranean has, over the last decade, become a surplus producer of many agricultural products and is heading towards self-sufficiency in those Mediterranean products that until now had been exported by the countries of the south shore. The entry into the EEC of Portugal and Spain, following that of Greece, leads to the expectation that in the foreseeable future European markets will be closed not only for Morocco and Tunisia, but for Egypt as well.

Morocco was estimated to have had losses in the region of 126 million US dollars in 1980/1 because of the enlargement of the EEC: Tunisia lost some 100 million dollars.

The development of agricultural exports was accompanied by concentration of resources in production for export, benefiting the irrigated lands and the large commercial farms (which in Morocco, for example, generate almost 80 per cent of agricultural exports), to the detriment of dry farming zones and peasant food producing farms.

The state encouraged investment in irrigation and extended aid to farms in the regions that produce export crops. This policy has had important social effects, increasing income differentials between categories of farmers and hindering the expansion of a majority of the peasants.

The failure of this agricultural development strategy poses further problems. At a time when sectors which for two decades have received the greatest part of state resources are not as profitable as they used to be, it is necessary today to invest further in order to correct economic and social imbalances in the rural world, and gear production to local demand.[2]

The retreat of agriculture has paradoxically been accompanied by a perceptible improvement of the standard of living in the countryside. Peasants and farmers have, generally, benefited on various grounds from the diffusion of the oil rent. For countries like Egypt, Jordan, Tunisia or the Yemen, diffusion of the oil rent occurred through migration to the oil-producing, capital surplus countries (Saudi Arabia, the smaller Gulf states, Iraq and Libya). Migration greatly affected the countryside, and in the case of Egypt it was estimated that agriculture lost around 15 per cent of its adult workforce, which is to say about 1.5 million peasants between 1975 and 1978 (Sainte Marie, 1984).

The flow of remittances to the countryside has meant not only that the micro-farming concerns of a numerically important group of the peasants have been kept active, but also that household consumption has been improved in a substantial way. Nevertheless, part of the agricultural population moved to urban areas or to non-agricultural activities in rural areas; this was the case in Algeria, Syria, Morocco and in Tunisia; in Tunisia double employment is now found among the farmers. Changes of activity or residence predominantly involved agricultural wage labour, landless peasants or peasants with very little land. This caused a decline in the supply of wage labour, and an improvement in the rate of employment of the poorest social groups. Agricultural wages have risen appreciably: in the most favourable cases (Algeria) agricultural wages have caught up with industry, while in the least favourable case (Morocco) the gap relative to non-agricultural salaries has remained stable.

Thus, in Algeria, the guaranteed minimum wage in agriculture was made equal to that of industry and services in 1980. It went from an index of 100 in 1970 to 437 in 1980, progressing much more rapidly than the average non-agricultural wage index. In Tunisia the minimum guaranteed wage more than doubled between 1977 and 1983, but it still only represents 70 per cent of the guaranteed interprofessional wage. In Morocco, the substantial increase — 40 per cent in May 1979, or 10.5 dirhams a day against the previous 7.25 — failed to narrow the gap

between agricultural and non-agricultural wages.

The general evolution also entails a widespread process of proletarianisation of the smaller peasantry, which in increasing numbers must find complementary sources of income outside agriculture. The extent of double employment in agricultural households in Algeria, Tunisia, Morocco and Egypt manifests a deep crisis in subsistence production, and how difficult it is for small-scale farms to stay in business. Thus an improvement in revenue is sought rather through an increase in the supply of labour on the employment market than through increased sales of farming products.

Improving urban and rural incomes led to rapid growth of demand for food. The caloric intake, which was between 2,000 and 2,300 calories at the end of the 1960s, has gone up from 2,500 to 2,900 calories in most of the Arab countries. Availability of food has increased by 15 to 20 per cent on a *per capita* basis, and in certain countries (Algeria, Tunisia) one can even see a big reduction in the food consumption gap between rural and urban communities.

This favourable evolution basically relied on imports, leading to growing dependence on foreign supplies to meet the demand for basic staples: cereals, dairy products and sugar.

An analysis of the agricultural food situation over the period 1973/83 shows that for a majority of the countries in the Arab world food imports grew rapidly while domestic production of basic items declined on a *per capita* basis. Yet one can distinguish two groups of countries: a first group, comprising Saudi Arabia, Syria and Libya, in which production *per capita* has perceptibly increased; and a second in which it decreased by 10 to 15 per cent on average. Thus the *per capita* production index in Egypt went from 99.13 in 1974 (1974/7 = 100) to 90.6 in 1984, in Iraq it went from 92 to 76, in Algeria from 93 to 82.8, in Morocco from 106 to 87.8 and in Tunisia from 94 to 86.7 (FAO, 1985).

The food deficit for the Arab world more than doubled in this period, totalling some 20 million tons of cereals (see Table 6.2), 2 million tons of sugar, 300,000 to 350,000 tons of meat, slightly more than 100,000 tons of butter and between 100,000 and 150,000 tons of powdered milk.

Since the beginning of the 1980s the cereal deficit has yet again increased for all Arab countries, except Saudi Arabia and Libya which have partially reduced their foreign deficits. The Maghreb

Table 6.2: Cereal imports of selected Arab countries in 1980 (000 tons)

Jordan	451	Morocco	1,821
Kuwait	535	Algeria	2,992
Lebanon	678	Iraq	2,476
Tunisia	776	Saudi Arabia	3,063
Libya	816	Egypt	6,028
Syria	997		

Source: *Economie et géopolitique des échanges de céréales en Méditerranée*, IAM, Montpellier, 1985.

Table 6.3: Food self-sufficiency rate — wheat, 1977/81

	Egypt	Morocco	Tunisia	Algeria
1969	86	94	83	70
1979	54	63	56	40
1983	30	40	47	26

Source: FAO, *Production Yearbook*, 1984.

countries and Egypt have the biggest deficits; Algeria and Egypt, in particular, import more than half of their total food requirements.[3]

In Algeria, with the exception of the excellent harvest of 1985, average cereal production (durum wheat, common wheat, barley) has been stagnating at 1.8 million tons for about 50 years and that of wheat at 1.3 million tons. Total wheat consumption is estimated at 4.5 million tons. Local production, therefore, covers only about a quarter of national requirements. Egypt assigns only one million feddans to wheat cultivation — less than for cotton which is exported — and the harvest is lower than in 1974–6 (1,960 million tons, as against 1,815 million tons in 1984). (See Table 6.3.)

Food imports take up a growing part of available currency and contribute to the growing foreign trade deficit (Morocco, Tunisia, Egypt). The cost of foodstuffs imports in 1983 was 3 billion US dollars for Egypt, 2 billion for Algeria, 0.8 for Morocco and 0.4 for Tunisia. The retreat of agriculture, the increasing importance of the food deficit and the expected decline in oil production (Algeria, Tunisia, Egypt) have led to the adoption of new policies for agricultural growth.

A NEW AGRICULTURAL POLICY

The new policy is based on an option in favour of accumulation in agriculture and an increase in agricultural revenue, in opposition to strategies which prevailed in the past, and aimed at transferring the agricultural surplus to other sectors of the economy. This orientation is found in varying degrees in most countries — Algeria, Morocco, Tunisia and Syria — with the exception of Egypt, which still appears to aim at a growing integration of its agricultural system into the international market. One should also distinguish the case of capital surplus countries like Saudi Arabia or Libya, which have completed massive investments in order to enlarge a limited agricultural sector.

Investment in agriculture

The new policy is characterised in the first place by an increase in public budget allocations in favour of agriculture. Apart from Egypt, where agricultural public investment has dropped from 24.7 per cent of the total in 1965 to 16.6 in 1970 and to 4.2 per cent in 1980, most other countries have seen a sharp increase in agricultural investments.

In Morocco the amount of investment in agriculture — including irrigation and agricultural water management — which stood at 5,468 billion dirhams for the period 1973/7, increased to 19,635 billion for the period 1981/5. In the case of Tunisia, this amount went from 197 million dinars in 1972/6 to 1,360 million in 1982/6 and in Algeria from 2,683 billion Algerian dinars in 1970/3, to 5,850 billion in 1974/7, to 10 billion in 1980/4.[4]

While public investment in agriculture declined in the 70s as compared to the previous decade, we witness today a strong recovery of the share of investment going to agriculture. In Tunisia, this share stood at 20 per cent for the decade 1961/70, fell to 13 per cent in 1971/80, then increased again to 17 per cent for the period 1981/6. In Algeria, agricultural investments were below 8 per cent on average in 1970/9, but appropriations went up to 12 per cent in 1980/4 and to 14.4 per cent of total investment in 1985/6. A new situation, indeed, whereby the agricultural sector receives in most Arab countries a share of public finance which is larger than its contributions to the GDP.

Privately funded investment remains small when compared to the public effort, reaching some 13 per cent in Morocco, somewhat less in Tunisia, and 10 per cent in Algeria. One can, however, generalise the question posed by Hachmi Alaya (1984) for Tunisia:

> whether the volume of investment allocated to the agricultural sector is not greater than its absorption capacity, especially with respect to that part which is financed by the banks. Necessary conditions — in the organisation and technical training of the farmers, in the farming of state lands, in agricultural prices, in the supply of production inputs to the farmers, in the marketing of agricultural products — do not seem to be as yet all met to the extent that would warrant the planned growth of the sector.

This is especially true in Algeria where, despite a clear improvement, the rates of realisation in comparison to appropriations were only 65 per cent in 1970/3 and 68 per cent in 1974/7.

The structure of investment shows a concentration on irrigation, which receives more than one-third of all funds going to the agricultural sector (see Table 6.4). In Morocco, where the spread of irrigation is a characteristic feature of agricultural policy, land irrigated by the larger dams has risen to 540,000 ha. Public entities invested the equivalent of 9,500 million DH in the hydro-agricultural sector between 1968 and 1980, which is to say, a yearly average of 792 million DH, with the aim of reaching 1,000,000 ha irrigated by large and medium-sized water projects.

In Libya, irrigated land has risen to 80,000 ha, and a project being carried out by a South Korean company should, with almost 4,000 kilometers of canalisations, drain the water tables of the southern desert and bring the water to the lands of the

Table 6.4: Share of hydraulic investment over total agricultural investment

Morocco		Tunisia		Algeria	
Period	%	Period	%	Period	%
73/77	33.3	72/76	39	70/73	31.3
78/80	71.1	77/81	43.6	74/77	29.9
81/85	39.9	82/86	78.2	79/82	40

north, increasing the irrigated area by 180,000 ha (at a total cost of 10 billion dollars) (Burgat, 1985). Saudi Arabia has likewise undertaken vast hydraulic investments to tap the shallower water tables; this allowed her over the last years to turn her wheat deficit into a surplus.[5]

Syria will double its irrigated surfaces, which are already quite vast (650,000 ha), following the completion of the Euphrates dam, thus bringing the total irrigated land to some 1,200,000 ha. Finally, Iraq has hydraulic infrastructure covering some 1,200,000 ha which, though underutilised to an extreme, should allow for a significant growth in production.

Implementation, however, is uneven and varies depending on the country. Saudi Arabia, Libya, Iraq, Syria and Morocco have progressed at a rapid rate and have today some impressive facilities, superior to those of countries like Tunisia, Algeria and Jordan, whose modest programmes could not buy more.

Egypt, however, has considerably slowed down on irrigation programmes, which initially (in 1954) had been expected to cover 2.5 million feddans. From 1954 to 1984 only 912,000 feddans were effected, of which 670,000 were brought into production, mostly before 1975. In the last 12 years, 70,000 feddans have been added to the cultivated land, while it is estimated that 25,000 to 40,000 feddans are lost each year to urban expansion. With 45 million inhabitants and an annual demographic growth rate of 2.5, Egypt experiences growing demographic pressure on its lands (see Table 6.5).

Hydraulic investment aims at removing natural constraints to production. The Mediterranean climate along the thin littoral belt progressively deteriorates into a semi-arid or arid climate over the much wider farmable land surfaces of the interior. Countries like Egypt, Libya and Saudi Arabia cannot cultivate

Table 6.5: Egypt, evolution of the ratio of population to cultivated land

Year	Population in 1000s	Total cultivated surface in millions of feddans	Cultivated surface per person (in feddans)
1960	26,085	5,900	0.23
1966	30,075	6,000	0.23
1970	33,200	6,000	0.18
1976	38,228	6,128	0.16
1980	42,000	6,300	0.15

Source: Ministry of Irrigation, Cairo.

without irrigation. But in all other regions, the annual rainfall is insufficient as well, and a large part of arable land does not receive enough water for crops.[6] This is the case not only of Jordan, Syria and Iraq but, in the western Mediterranean as well, of Tunisia, Algeria and Morocco.

Aridity and insufficient water supply characterise the climate, limiting production and yield. Because production is sensitive to rainfall conditions from one year to the next, it fluctuates. With irrigation one can hope for a sizeable increase in the volume of production and a better yearly control over yields.

Table 6.6: Agricultural population per hectare of arable land, 1981

Iraq	1	Algeria	1.3
Tunisia	0.6	Morocco	1.3
Jordan	0.6	Egypt	7.5
Syria	0.8		

Source: FAO, 1983.

The water mobilisation programmes are all the more important because Arab countries have only a small potential for expanding cultivated land. Demographic growth dramatically limited the ratio of arable land to population and the outer boundaries of cultivable land have been reached everywhere (see Table 6.6). Irrigation, therefore, is an essential step to increase agricultural productivity and pass from extensive to intensive agriculture.

Mechanisation of agriculture

The modernisation of agricultural cultivation methods and equipment is the second aspect of the new agricultural policy. The state wants to achieve growth in agricultural productivity by increasing mechanisation services, introducing fertilisers and other chemical products, and improving the livestock. To this end, tax reductions, credit and subsidies have been introduced. Thus, for example, large subsidies are granted to encourage fertiliser consumption, and aid is given for the use of other production factors; imports of agricultural material are exempted from customs duties and taxes; the purchase of tractors is subsidised, and the state offers free services in fertilisation,

veterinary care, plants and seeds and mechanised work. Credits to farmers at improved rates are obtained more easily. In Tunisia, for example (but the same could be said of Algeria, Morocco and Syria), the operation of the *Fond spécial de développement agricole* (FOSDA) went from 14,000 million in 1974 and 18,000 million in 1977, to 65,000 million in 1982. In 1981, the National Bank of Tunisia doubled the funds allocated to farming loans from 20 million DT to 48 million Tunisian dinars.

Mechanisation is the most remarkable aspect of the agricultural investment policy. Improved agricultural wages and state support led to a widespread diffusion of mechanisation in all Arab countries often coupled with a trend to increased concentration of production.

In Algeria, the number of tractors has more than doubled since the beginning of the 70s — from 26,000 to 58,000 units — with an acceleration of growth in the last five years. In Tunisia, only 18 per cent of farmers used mechanical traction in 1962, whereas in 1976 that percentage had increased to 55 per cent and in 1980 to 58 per cent (Ramdhane, 1983). The tractor pool went from 20,000 units in 1976 to 28,000 in 1983. The same holds true for Morocco, Egypt and Syria where there has been a quantitative and qualitative increase in mechanical implements, concentrated for the most part in large and medium-sized farming concerns. Correspondingly, small-scale concerns have limited access to mechanisation and run up against growing difficulties in cultivation because of the substantial drop in domestic livestock.

In general, agricultural modernisation depends on a greater absorption of industrial inputs, which many countries must import, either totally or partially. Egypt and Algeria have created an industrial sector which is capable of partially satisfying agricultural needs, but Morocco, for example, has to spend more than 22 per cent of its total agricultural imports on the acquisition of material on foreign markets. In other words, in most cases the mechanisation of agriculture has some drawbacks and contributes to the trade deficit.

Agricultural prices

But certainly the most innovative aspect of the new policy concerns agricultural prices. During the 60s and the first half of the 70s, prices were the basic instrument for mobilising the agricultural surplus. The state rigorously pegged the prices of the main basic products, agricultural raw materials (cotton) or foodstuffs (cereals), at a level that was lower than that of world markets. Agriculture thus contributed to the creation of employment in the urban sector by assuring a cheap supply of basic foods.

The increase in the prices of agricultural products, which most Arab countries decreed since the beginning of the 80s, represents an important change of mind with respect to the utilisation of the agricultural surplus and, more generally, with respect to the redistribution of GDP.[7]

Prices of products controlled by the state were increased — cereals or cotton, milk, oil, sugar; the prices of other products — meat, fruits and vegetables (Algeria, Tunisia, Egypt) — were liberalised.

The Maghreb countries have thus experienced a substantial increase in the price of cereals (wheat) (see Table 6.7).

Table 6.7: Evolution of cereal prices — durum and common wheat in national currency, per 100 kg

	1979	1980	1981	1982	1983	1984	1985
Durum wheat							
Tunisia	7.6	8.6	9.6	11.0	14	14	15
Morocco	70	125	140	140	140	140	140
Algeria	—	125	140	140	140	160	200
Common wheat							
Tunisia	7.0	7.7	8.7	12.8	14	14	14.5
Morocco	70	125	140	140	140	140	150
Algeria	—	110	130	130	130	150	190

In Tunisia, cereal prices have seen an annual average increase of 14 per cent, those of milk of more than 22 per cent. Bovine meat prices were liberalised at the end of 1982 after a 16 per cent annual increase, and mutton prices were liberalised at the end of 1979; since then a veritable explosion has occurred. In Morocco, the increases have been somewhere in the region of 47 per cent for wheat, 17.2 and 16.9 for beets and sugar cane, 42 per cent for oil seeds, 34 per cent for milk.

In Algeria, prices have risen more sharply, 60 per cent for durum wheat, 65 per cent for common wheat and dry vegetables, upward of 150 per cent for milk. In Syria, the government increased the purchase price of cotton by 44 per cent in 1981/2 and by 20 per cent in 1982/3 (World Bank, 1983). Finally, in Egypt, the price increases which occurred in 1979/80 were more modest. Wheat prices gained 9 per cent, rice 15.4 per cent, sugar 27.6 per cent. The price paid for cotton has remained at a much lower level compared to the world market (World Bank, 1980).

Generally speaking, price increases for basic products — cereals, dairy products, dried vegetables — have been very high in most of the countries in recent years. Domestic prices, with the exception of Egypt, are well above import prices, something which clearly indicates a reversal of the tendency seen in previous decades.

However, the growth of public financial aid to agriculture is principally aimed at encouraging commercial farming, on which the state relies in order to achieve its objectives for agricultural growth. Mechanisation, consumption of intermediary inputs and credits are, for the most part, channelled to the larger market-oriented farms. At the same time, funds that used to accrue to the smaller and poorer peasantry through different state institutions or the cooperatives that were created in the 1950s and 1960s, are reduced or altogether cancelled.

This consequence is implicit in the generalised trend towards 'state disengagement' *vis-a-vis* the social categories that in the past benefited from agrarian reform programmes (Egypt, Algeria, Tunisia, Syria). Tunisia was first in 1971 in terminating her attempts at agrarian reorganisation based on cooperatives, and in starting a process of liberalisation of the agricultural sector and privatisation of land tenure. Until the beginning of the 1980s, however, it maintained a rigorous system of control over prices, which limited the development of commercial farms and protected the competitive position of the small peasant farmers.

Since 1982 (Law 82-67, 6 August 1982) the land belonging to the state (almost 400,000 ha of good land) can be leased for an approved length of time, not to exceed 30 years, to Tunisian joint stock companies called 'companies for agricultural improvement and development', in which the state directly or indirectly owns a share of the equity (art. 10); or to private individuals. Thus in 1982/3, some 15,000 ha were ceded to Tunisian-

Kuwaiti or Tunisian-Saudi private organisations, as well as to Tunisian private entities.

In Morocco, the large capitalist farms specialising in export crops have won the largest share of state investments and aid, and will continue to play a vital role in the new agricultural strategy.[8]

But it is Egypt where the system supporting the small peasant farmers since the 60s was most thoroughly dismantled by a series of measures implemented after 1975: when taken as a whole the latter deserve to be called an 'agrarian counter-reform'. The new banking network, substituting for the service cooperatives, will henceforth cut off farmers who do not have sufficient guarantees from loans for farming and equipment. Relations between landowners and tenants have been reviewed to the benefit of the former. Leases can be transformed with the sole consent of the owner into sharecropping contracts with new conditions set by the owner; in certain cases the latter can even expel the tenant. Finally, taxable income and the amount of the land rent were both increased (Dowidar, 1984).

Finally, in Algeria, public authorities have dissolved the co-operative structures established by the agrarian reform of 1971. The land that had been worked collectively was redistributed to individual farmers, and the service cooperatives which provided the technical assistance and material to certain categories of producers stopped their activities in 1982/3. In particular, the disappearance of the cooperatives' branches handling mechanical implements has resulted in a substantial increase in the rental rate for machinery, affecting the small peasant farmers who can no longer afford the equipment. These measures manifest the state's determination to disengage itself from a category of peasant farmers, because the assistance that it once gave to them, in the form of subsidies and various services has today become too costly.

CLASS RELATIONS AND AGRICULTURAL POLICY

What will be the real impact of the measures taken in favour of agriculture? Are they an attempt at a redefinition of its role in the national economy and its integration in the international context? There is no doubt that up until 'the oil era' agriculture was an essential sector in the economy, the source of a surplus

and of hard currency, that were channelled to the benefit of urban expansion.

During the 70s the state's links with agriculture weakened; imports from abroad to a large extent replaced domestic production, and the countryside was integrated into the employment and consumer markets rather than into the products market. The financial crisis and the fall in outside revenues of the 1980s led to a reorientation of agricultural policies, which however, was not in all cases accompanied by a reversal of the past trend and of the direction of flows in favour of agriculture.

Countries with large capital surpluses which have made big transfers in favour of agriculture, so as to establish or enlarge their agricultural production structures (Saudi Arabia, Libya and Iraq), should be distinguished from countries with small or medium export revenues, whose agricultural sectors suffered a big retreat in the 1970s. In the case of the latter (Algeria, Egypt, Tunisia, Syria, Morocco) it is a question of limiting the damage caused to their agriculture by the expansion of the oil economy.

The first group of countries only had a limited agricultural sector and for the most part financed the development of its agricultural sector and the growth in producers' income by transforming a part of its oil revenues into productive agricultural capital. Libya has devoted large sums to land reclamation, settled peasants on farms of 5 to 25 hectares, depending on the project. The farmers receive houses given them by the state, gardens and orchards. At settlement they receive a monthly allowance of 90 dinars and loans of 5,000 dinars repayable after 15 years, interest free. Technology of the most expensive kind has helped create areas of intensive farming in the middle of arid steppes, and to produce wheat, fodder, fruit, vegetables, milk and meat.[9]

Saudi Arabia has made similar huge investments to exploit shallow underground water sources and expand irrigated land surfaces. In this way it has been able considerably to reduce its cereal deficit.

In the second group of countries, the new orientation in favour of agriculture does not always imply a radical revision of agriculture's relations with the rest of the economy. It is rather a tendency to adjust the role of agriculture to the new conditions prevailing in the economy, rather than a complete break with the traditional model, in which the main function of the agricultural sector was to mobilise a surplus for the benefit of the other sectors. However, compared to the other countries in this group, Algeria offers an example of a situation that is much more favourable to agriculture.

The increase in agricultural prices, even more so than direct measures of support to the factors of subsidies (production, credits, rebates, free loans, etc.), is a good indicator of the tendency towards a recovery in agricultural revenues. In fact, in most cases (Tunisia, Algeria, Morocco, Syria) the agricultural price index has grown more rapidly than the general price index.

In Tunisia, for example, the general consumer price index went from 100 (1977) to 168 (1983) while the index for agricultural foodstuffs for the same period went from 100 to 175.9. The biggest advances were for fruits and vegetables (199.4) and meats (212.2).

In Algeria, the difference is bigger. Against a general index of 306.8 in 1983 (1969 = 100), the foodstuffs index rose to 393.2. As can be seen in Table 6.8, the gap has widened since 1980.

Table 6.8: Algeria, evolution of consumer price index, 1978–83

	1978	1980	1983
Foodstuffs	236.1	297.2	393.2
General index	194.4	239.9	306.8

As in Tunisia, fruits, vegetables and meats recorded the largest price increases.[10] The same observations can be made for the other countries where, in general, the inflation of agricultural product prices is greater than that of non-agricultural products.

Moreover, when considering the evolution in the prices of the factors of production supplied to agriculture, be they produced locally or imported, we come to the conclusion that an improvement in the terms of exchange for agriculture has occurred. Most countries subsidise the factors of production, in some cases to the extent that they are sold at prices well below their cost.

In Algeria, for example, the prices of the main factors of production were frozen from 1974 until 1982, and then only slight increases were introduced; as a consequence, prices are today still half the international ones.

Improvement in the agricultural terms of exchange does not,

in all cases, imply a reversal of financial flows to the benefit of agriculture. Egypt, as opposed to Algeria, is a case where the difference between domestic and international prices is still clearly against local agriculture, notably for basic products such as wheat or cotton, while the increase in the international prices of agricultural machinery is transferred to the farmers in full.

The new policy in favour of agriculture, however, pursues objectives that are not easily reconciled. On the one hand, it has to bear in mind the need for safeguarding the urban purchasing power for food, an important factor for political and social stability, while on the other, it aims at increasing agricultural income by raising agricultural prices.

The control of prices during the 1960s and the beginning of the 1970s was implemented in a way that damaged growth of agricultural incomes, but did not necessarily favour accumulation in industry, contrary to what has been often suggested. In the Arab countries industry only employs an average of 15 per cent of the active population: 17 per cent in Algeria and Tunisia, 14 per cent in Morocco and Egypt. In the latter country, industrial activity has been on the decline since 1975; in 1961 it accounted for only 15 per cent of the GDP and 7 per cent of its production was exported as against 9 per cent in 1973.

It is the services sector which dominates everywhere. It accounts for half of the employment on average, so much so that these should really be dubbed service economies, rather than industrial economies.

Job creation in the services sector and especially in the administration has been everywhere more important than in industry: there is one job in industry for every three in services. The freezing of agricultural product prices at a low level has consequently been an essential instrument for the financing of employment in the tertiary sector.

The massive reliance on imports to satisfy a growing domestic demand caused a relative drop in the prices of local agricultural products.

In some countries (Egypt, Algeria, Tunisia) the state has set up a distribution system for basic products — cereals, vegetable oils, dairy products — which are imported and sold at subsidised prices. Thus a two-tier market for agricultural food produce was created, one functioning under the control of the state and assuring the distribution of basic products at fixed and subsidised prices, the other, distributing local agricultural products at prices fixed by supply and demand.

State expenditure on subsidies to prices reached massive proportions. In Algeria, it rose to some 3 billion dinars, or 6.5 per cent of household consumption. In Morocco, the state was able to give each household an average subsidy representing about 7.3 per cent of the food budget for 1974, 9.8 in 1975, 4.5 in 1979, and 5.6 in 1980. In Egypt subsidies for essential goods (flour, sugar, vegetable oils and other food products) totalled 2.04 billion Egyptian pounds for 1983.

This policy aimed at maintaining the purchasing power of the urban middle and working classes and was made possible by decreasing reliance on domestic production to meet food demand.

During the 80s, however, there has been a rapid and substantial increase in the cost of food, following the rise in agricultural prices and the progressive reduction of government subsidies for consumption.

In Egypt, price subsidies fell by almost 300 million US dollars in 1984. In Algeria, two increases of 22 per cent each were introduced in 1985 for cereals, vegetable oils and other basic foodstuffs. Parallel increases took place in Morocco, Tunisia and Jordan. The liberalisation of prices of local products, fruits, vegetables and meats, led to steep increases. The urban middle classes, and the agricultural wage earners have been the main victims of the rise in the price of foodstuffs and have had to adjust to a sizeable reduction in their purchasing power. Hardest hit by inflation are the petty civil servants, employees and workers, all especially vulnerable to food price increases.

The erosion of real wages has been particularly strong in Egypt, Tunisia, Morocco and Jordan; the first three among these countries experienced serious popular outbursts as a consequence. In other cases, greater outside resources were used to compensate for the effects of the price increases on low incomes. This is the case of Algeria where the government decoupled agricultural producer prices from consumer prices, the former being increased while the latter are kept at a relatively low level. This is why in Algeria salary increases surpassed the increase in the prices of basic products but did not match the increase in those of fruits, vegetables and meats. Put in another way, the purchasing power of salaries has improved for cereals, vegetable oils, dairy products, dried vegetables and sugar but deteriorated for fruits, vegetables and meats.

The rise in the cost of the food ration is a tendency which all countries have experienced. It seriously strains the class relationship built up in the 60s and 70s which for the most part was based on an alliance between the lower middle class, the urban working classes and the peasantry.

The financial crisis and the drop in exogenous revenues imply that the state cannot any more rely on imports and subsidies as a means of controlling domestic prices. In this respect, increases in the administered prices of agricultural products only anticipate new market conditions. The evolution of supply and demand for agricultural foodstuffs demonstrates the new economic and social importance of the countryside, deriving from the worsening of the food crisis in certain countries (Algeria, Egypt, Tunisia, Morocco).

NOTES

1. 'Producing citrus fruits at great expense for export and importing cereals to cover basic needs is consistent with the requirements of the process of integration of the Moroccan economy into the global market'. See el-Malki (1983).
2. This is a profound transformation of the agricultural strategy envisaged by the Moroccan Plan 1984/5. 'To reduce the negative effects of unfavourable international development, curb the food deficit, restrain the rural exodus, try for a new equilibrium at regional, intersectorial and intra-sectorial levels: these are some of the main ideas that arise from developments which the last Five Year Plan 1981–85 has devoted to the agricultural sector' (el-Malki, 1983).
3. Egypt receives almost 44 per cent of world 'food aid' supplied by the USA. Wheat in the form of donation has, however, been progressively replaced by credit sales with no special conditions.
4. The second Five Year Plan 1985–9 allocates 30 billion DA just for agricultural investments to which are to be added 40 billion in water investments.
5. In 1985, Saudi Arabia produced 7.1 million tons of wheat for a consumption of about 1 million tons.
6. In Jordan, barely 30 per cent of land receives more than 350 mm of rain annually, and only 600,000 ha between 200 and 350 mm, the rest being unfit for cultivation. In Syria, 65 per cent of the 18.5 million ha used by agriculture receives less than 200 mm of rain annually. In Algeria, Tunisia and Morocco from one-third to half of all arable land has less than 400 mm of water annually.
7. 'Today's prices and market policy seems to be inadequate, from the point of view of agriculture, which does not make up for ground lost, and from that of the consumer, who pays a higher price. One

might think that the support given to products should outweight the support given farming with prices therefore playing a more determinant role' (Three Year Plan 1978–80).

8. 'It is mercantile agriculture and, in particular capitalist agriculture which will have to not only continue specialising in export crops but develop food production more, too. It is, therefore, mercantile agriculture which will have to assure the food security of the country' (*Revue Marocaine de droit et d'économie du développement*, 1982).

9. At Oubari, for example, 'each farm covers 10 ha. With the farm comes a herd of goats, a tractor, a harvester, an orchard with citrus fruits, figs, a lucerne plantation, a kitchen garden. The holdings are grouped in small autonomous townships each having an electric power station, a mosque, a school, administrative buildings, tarred roads streaking the fields' (Rossi, 1979).

10. The average agricultural price index does, however, conceal very big distortions in favour of producers of fruits, vegetables and meats, to the prejudice of producers of basic produce, cereals, vegetable oils and milk — products for the most part imported and whose prices are fixed by the state.

7

Political Aspects of State Building in Rentier Economies: Algeria and Libya Compared

Dirk Vandewalle

International political economists have lately renewed their interest in the possibility of autonomous development in the less developed countries (LCDs), focusing on the impact of the international economy on state/society configurations within the periphery, and on countervailing strategies available to countries in the periphery.[1] Although some of their general findings are applicable to rentier states as well, the latter exhibit some particular difficulties which this chapter will dwell upon. In Algeria and Libya, the two countries which are used for case study in this chapter, the effort to achieve autonomous development has been particularly strong and has resulted respectively in an attempt to either follow a dissociative development strategy, or in a rhetorically virulent isolationist attitude.

The relative absence of capital scarcity is but one of the unique aspects of rentier states. Revenues are accumulated through the taxation of third parties. The country's own citizens are relatively unproductive, and little demand is put upon them to become productive. In most non-rentier economies the state derives revenues from taxing citizens, goods and services. In the process, rules and procedures are established to ensure the collection of taxes, and a bureaucracy arises to administer the system. A minimum degree of consensus concerning the amount of taxation is arrived at. In return the state compromises with its subjects: no taxation without representation. As Karl Polanyi (1944) has demonstrated, these 'historic compromises' between state and society were hammered out in the nineteenth and twentieth centuries.

In rentier economies such interaction and compromise need not take place, at least not initially. In the Middle East, the convergence between state and society did not take place altogether, or was defined in certain ways by the imposition of colonial rule — French in Algeria, Ottoman and Italian in Libya. State and society remained distinct.

The rentier state can govern by using the rents that it receives. It needs, at best, a few professionals to negotiate the size of the rents with the purchasers-producers. There is little use for an elaborate bureaucracy; the international companies producing the rents also effectively act as tax-collecting agencies for the local governments. There is at the same time little concern for production-oriented behaviour, while attention focuses on income allocation.

The rentier nature of state revenue thus militates against the creation of a strong state or the involvement of its corresponding society. In this light, the massive revenues accruing to the government in a rentier state are a double-edged sword, allowing the local governments to dole out revenues with minimum attention for representation, on the basis of the reverse principle of no representation without taxation.

In Libya and Algeria, at the beginning of the development process, and for essentially historical reasons, the state was weak. The long tutelage under France and Algeria's bloody war of independence had further widened the gap in the ideas of the various participants on what statehood would entail. In Libya, the history of political and economic separation between Tripolitania and Cyrenaica, the creation of the kingdom by the United Nations, and the acceptance of King Idris al-Sanusi as a compromise by far overshadowed whatever cooperation and agreement had existed during the temporary union against Italian colonialism. For most Libyans, the notion of a Libyan state remained an alien concept in a country where a federal state was only proclaimed in 1963. In Algeria, at least until 1965, and in Libya until the 1969 Qadhafi *coup*, policies cannot be said to have reflected collective interests. 'Goals pursued were often those of particular groups closely associated with the leadership, and no agreed upon structure existed to impose policies over the objection of particularistic interests' (Gourevitch, 1978: 901–2).

THE CASE OF ALGERIA

How well have Algeria and Libya performed when faced with these powerful structural limits, i.e. international economic constraints and weak state structures?

In Algeria the *dirigisme* implied in the 1970–3 and 1974–7 Four Year Plans manifested the inclination on the part of the former president Houari Boumedienne in favour of an industrialisation effort led by a relatively small group of decision-makers. This group would not only initiate but also implement economic directives, both locally and regionally. Algerian elite membership consisted of three major groups: the military, the small but growing cadre of bureaucrats and technocrats and, finally, the elites of the single political party, the Front de Liberation Nationale. The party's task of mobilising the population and stimulating political participation was steadily downgraded.

As early as 1965 the emphasis on the formation of technocratic/bureaucratic cadres met with concerted opposition from groups within Algeria unwilling to allow the formation of what they considered to be a privileged class at their expense. But, as in several Middle Eastern rentier states, the Algerian leadership found it relatively easy to circumvent the demands of unions.

The 1965–70 period had already been particularly instructive in this regard. The proposed centralisation of agricultural production and the extension of government control to certain sectors of industry under the 1966 Code des Investissements had led to considerable opposition from the syndicalist movement, particularly the Union Générale des Travailleurs Algeriens (UGTA). Boumedienne's response had been to emasculate all national-level institutions that could challenge the Algerian state. The Political Bureau of the FLN, as well as the National Assembly, were suspended. Real power rested in the Council of the Revolution and the Council of Ministers.

By the third UGTA Congress in 1969 most militant syndicalism had been suppressed. By 1970, the most vocal and powerful opposition had gradually been eliminated or transferred into sinecure positions. Boumedienne had assumed the leadership of the army, presided over the Council of the Revolution and the Council of Ministers, and of the FLN, and held the Ministry of Defence — positions he held until his death in 1978. A number of apolitical technocrats with no constituencies of their own assumed junior leadership positions. The result was a type of leadership in which economic policies had become essentially elitist in concept and method. Depoliticisation, particularly among the youth, had started to take root.

By the end of 1971 the polarisation between those demanding political and economic liberalisation, and those insisting on the development of public property, had hardened. Boumedienne's dilemma was to enlarge popular support for his regime and his economic policies while containing the opposition of the urbanised middle class. The introduction of workers' participation in the industrial sector (the Gestion Socialiste des Entreprises of 16 November 1971) was an example of trying to please the people. Workers' assemblies were created throughout the national companies and their units, to be extended eventually into the private sector.

Clearly aware of the resentment of the urban middle class, the remaining large landowners, the private merchants, and certain technocrats, Boumedienne relied on 'institutionalisation from the bottom up'. Local and regional committee elections (Assemblée Populaire Communale and Asemblée Populaire Regionale) were held in 1967, 1971, 1975, 1979 and 1969, 1974, 1979, respectively. Both assumed administrative duties and management responsibilities, but remained without significant political authority.

Algeria by 1974 had become what William Zartman called a 'co-optive technocratic system' where no group *qua* group had yet institutionalised its efforts at gaining power, despite the emergence of inter- and intra-elite rivalry. The power of the state was strongly centralised in the military and represented on all national decision-making bodies that directed all political activities at the expense of the FLN.

The powerful concentration of power that followed the *redressement révolutionnaire* of 1965 gave way to a *redressement constitutionel* in 1975, largely based on Boumedienne's efforts to further de-emphasise the informal, personalised nature of the political system and on his desire to provide an antidote to the increasingly technocratic nature of Algeria's economy. The Algerian president seemingly tried to steer a course in between the demands made by adherents of the two opposing tendencies. Despite a continued commitment to a technically-oriented development strategy, his new redressement included a new role for the FLN, following a period of inactivity

of the latter between 1965 and 1975. The National Charter of 1976 was to be Algeria's own 'historic compromise', reminiscent of those concluded in Europe decades earlier. The FLN regained its role as the ideological vanguard of the socialist revolution and FLN membership became a *sine qua non* for any type of political participation. But although the Charter had been the focus of intense public debate, only minor alterations had been allowed to its political content.

The two years following Boumedienne's death in 1978 were the acid test for this attempted institutionalisation, and for the future of the public sector. Under Benjedid, a series of sweeping promulgations in 1981 and early 1982 culminated in a new Code des Investissements in which the role of the private sector was reassessed.

Much discussion has focused on whether the economic liberalisation in Algeria (as well as in other Middle Eastern economies) was a sign of state strength or of state weakness. The break-up of the public sector was only in part based on economic considerations. The Algerian state had become sufficiently strong to weather the economic difficulties in themselves, and had put in place an impressive array of instruments to monitor and guide its economy. Political contradictions inside Algeria provided an important motivation. The Charter's historic compromise had proven unequal to the task. Wage scale increases, price subsidy allocations, and social transfers (in the form of family allowances, etc.) were the price paid to incorporate certain crucial groups.

Although the orderly change of power after Boumedienne's death attested to the strength of political institutionalisation, the proposed *infitah* showed the power of those the rentier economy needed most for its economic future. Opposed to these technocrats and administrative elites stood the party elite, the unions, and the students. The conflict was resolved in favour of the bureaucratic/technocratic class. The loss of state power to this relatively small segment, however, had not prevented Algeria from moving in the direction of a bureaucratic polity during the 1970s, 'a political system in which power and national decision-making are shaped almost exclusively by the employees of the state, and especially by the top-most levels of the officer corps, the single party organisation, and civilian bureaucracy, including technicians' (Entelis, 1982: 129).

The single-man concentration of power was tempered by the gradual development of a technocratic system that relied heavily on regularised procedures. This is the modern, bureaucratic form of clientelism that is now overwhelmingly found in Algeria. The traditional sources of power — personal, class, or religious — have been replaced by organisational ones, a process started in the late 1960s.

Although Algeria as a rentier state found itself by most of the indicators specified in this chapter at the high end of the 'political order' continuum (a bureaucratic-authoritarian state with little room for effective pressure group action, a large and effective array of economic policy instruments, and effective use of the national myth in the pursuit of its development goals), it was ultimately the expanding power base of the bureaucratic/technocratic elite (which had been instrumental for the implementation of state capitalism in the first place) and the gradual enlargement of a more productive (but parasitic) private sector to which this elite partially defected, that forced a reconsideration for basically internal political reasons. This elite, substantially nurtured under the rules of a meritocracy, had not found its roots within a dominant Algerian class. Nor was it a comprador class in alliance with outside interests.

It was ultimately, as John Waterbury (1983: 39) has described, for Egypt 'the inability of such elites to muster the political will to undertake far-reaching distribution of domestic assets' that led to the 'political expediency' of *infitah* with its attendant implications of 'financial orthodoxy, economic austerity, and the revivification of private sector interests that then infiltrate the state'.

THE CASE OF LIBYA

In Libya the political turmoil throughout the 1970s created a political climate which was highly unfavourable to the pursuance of an industrialisation strategy, which postulates centralised and coherent decision-making. In the political transition following the revolution of 1969, the Free Officers needed to consolidate their regime in the face of an existing bureaucratic class with close contacts to the West and firmly entrenched in certain sectors of the economy, a mass public overwhelmingly apolitical, and a rural elite which, despite having lost a substantial amount of power, still held considerable sway over the rural population.

Before its first economic plan was announced in 1973, Libya witnessed the creation of the Arab Socialist Union, then the creation of national, provisional and local committees, and finally the demise of the Arab Socialist Union. The launching of the Popular Revolution in April 1973 was described by some as Qadhafi's attempt to rally popular support to his side by attacking the structures of state that were still weak and intensifying his populist policies to redistribute resources to both the lower-middle and lower classes, which had so far least profited from the burgeoning economy.

The rapid removal of part of this old bureaucratic class during the early 1970s created enormous economic (and political) confusion. By the end of 1974 increasing acrimony, pitting a group of middle-class bureaucrats and high officials — technocratic and regionalist in outlook — against a lower-middle class and lower class with traditional and pan-Arab leanings, centred precisely on the future of the Libyan economy. Underlying the disagreement also was Qadhafi's deep mistrust of bureaucratic procedures and of the growing technocrat group within Libya — not as technocrats *per se*, but simply as the embodiment of a modernising group that could potentially gain and consolidate political power.

The August 1975 attempted *coup* in Libya spelled the end of effective policy initiatives by the technocratic group within the country's top political decision-making body, the Revolutionary Command Council. It also marked the beginning of a decade of new political and economic measures that would expand the rentier characteristics of the Libyan economy. Many of these measures were delineated in the Green Book, the political and economic philosophy of which is far from reflecting the needs of a modern state and economy. The official establishment of Basic Peoples' Committees, the appointment of 'secretaries' (formerly ministers) directly by the people, and the 'continuous revolution' inaugurated in 1978/9, culminated in the establishment of workers in public enterprises and the gradual abolition of private property in excess of personal need. Only the banking and, significantly, oil-related enterprises were temporarily saved from take-over.

The 'spontaneous' take-overs of the private economic sector by the militants had a chilling effect not only on relations with foreign companies but also on the ability of the Libyan leadership to guide the economy in the path of rapid reforms. What

Qadhafi referred to as the 'socialisation' of Libya's economy had several perverse effects. The take-overs and the interference by the Popular Committees brought an initial wave of confusion and further inefficiencies. National planning became even more uncoordinated and whatever inter-sectoral planning had been envisioned was lost in the confusion. Indicative of the damage was the decision to demonetise the Libyan dinar in March 1980, perhaps potentially the most radical of Qadhafi's socialist measures. Although in line with other efforts at redistribution, J. A. Allan viewed it as a 'blunt instrument' used only because of Libya's inability to manage its national economy.

It was perhaps only a small example of the juxtaposition that existed by 1980 in Libya — on the one hand favouring a technocratic solution to increasingly complex economic problems that necessitated increasingly sophisticated policy instruments, while on the other hand refusing to cultivate a bureaucracy or local technocracy to guide the effort. If the disparity proved too difficult to bridge, the government often tried to 'outspend' it. In reality, Libyan administrative institutions were unable (or were not permitted) to cope with the demands put upon them by a rapidly expanding economy. Libya's need for top-level managers increased rapidly from 35 per cent of total need in 1974 to 68 per cent in 1978. Worse, however, was that as a result of frequent political disruption and interference, a survival ethic appeared among many of Libya's remaining bureaucrats, 'an ethic that dictated external compliance matched by a covert desire to maximise personal advantage at the expense of the system' (Palmer and el-Fathaly, 1982).

All of the above suggested that the attempts made by Qadhafi to incorporate Libyans into an effective bureaucratic, administrative and political structure, had substantially backfired. Evidence seems to suggest that he had exacerbated Libya's traditional problem with central authority. The Libyan state apparatus, destroyed during the Italian occupation and held in abeyance during the monarchy, had been declared useless by the creation of People's Power as embodied in the creation of the *jamahiriya*. The undercutting of an apparatus meant to provide continuous and consistent administration — something Algeria had been relatively successful in erecting — was legitimated in the Green Book. In this respect events since 1975 can to a large extent explain the Libyan leader's wish to do away with institutions that would — if indeed they could be called bureaucratic or administrative — operate independently from direct supervision. Their replacement by People's Power can be considered Qadhafi's own survival ethic, the use of the national myth for survival.

The continuous uprooting of the domestic bureaucratic organisation in many ways reflects the distrust felt by Qadhafi for a modern state with its specific political, economic and social organisation. The nature of the Libyan rentier state, with its concentration of political power and control over the economic rent, allowed him the luxury of acting upon this distrust. Libya resembled in many ways what Marius Deeb has called a 'precapitalist socialist society' in which the hierarchical bureaucracy of the modern state is held in abeyance and allegiance is bought by means of the rapid inflow of revenues. Paradoxically, it was the impact of capitalism which allowed Qadhafi and other rulers of rentier states to adhere to precapitalist development. As a consequence of economic policies related to the state's rentier nature and its populist strategy, by 1980 Libyan society had become largely irrelevant to the state itself.

Not surprisingly, Libya did not feel the pressure in favour of economic liberalisation in the 1980s. Despite the general uncertainty of the economic situation — or perhaps because of it — spending continued at a fast pace while oil revenues plummeted. The efforts at eradicating private interests from the Libyan economy continued. While development and regular administrative budgets were almost halved between 1980 and 1985, defence and military spending climbed from 700 million dollars to almost 1.2 billion dollars during the same period. The Great Manmade River Project relied overwhelmingly on foreign expertise and, for the first time, Libya imposed a system of indirect taxation to help pay for a development scheme. The share of total revenue accruing from oil and oil-related activities has remained essentially unchanged since the 1969 *coup*, at a level that is one of the highest in the region — in excess of 95 per cent, while IMF statistics show a slight increase in government revenue as a percentage of GDP (this is in clear contrast to Algeria where oil and gas revenues as part of total revenues have dropped from approximately 70 per cent in 1979 to slightly over 50 per cent in 1985).

CONCLUSION

In evaluating the chances of rentier states to develop a diversified economy, John Ruggie's remark about general development in the periphery is applicable: the much-touted international division of labour is 'not really as elastic as its advocates assume, but not quite as rigid as its detractors insist' (Ruggie, 1983: 482). Rentier economies, however, face a host of specific constraints that restrict and channel economic development. These constraints are of an economic as well as a political nature.

Both Algeria and Libya undoubtedly show some of the political characteristics of allocation states. Representation in Algeria, despite the communal and regional elections and the existence of a National Assembly, remains at best a carefully controlled process. Its value remains as a vehicle to deflect serious criticism or opposition. In Libya, the Peoples' Committees have become thoroughly infiltrated by Qadhafi loyalists who ensure that decisions remain in line with those of the Libyan leader. Luciani has correctly singled out the ease with which the nature of their economy allows rentier states to forego worker participation and unionisation; both the Libyan and Algerian case confirm this. But to argue that overall unequal distribution of benefits is 'not relevant for political life, because it is not a sufficient incentive to coalesce and attempt to change the political institutions' (Luciani, this volume: 74), ignores some of the political characteristics that define rentier states. While this phenomenon may be true at the individual level, as Luciani rightly argues, the dynamics change radically once these individuals group themselves, i.e. assume some type of corporate identity. In Algeria, the careful circumscription of formal representation did not prevent the creation of a powerful technocratic corps that strongly defended its corporate interests and in part helped to argue for *infitah*.

The 1969 military *coup* in Libya was the creation of a bourgeois class at the expense of the lower-middle and lower classes. By 1985, an estimated 100,000 Libyans, including an alarming number of those educated in the West, had left the country. The creation of a society geared toward consumption rather than productive participation (admitted by Col. Jallud in several statements) was in several ways directly related to the effects of the regime's political ideology. In rapid succession the local

capitalist class, originally co-opted to play a part in the productive process, and all local entrepreneurship and private rent were abolished. The temptation to look for easy pay-offs, primarily by military spending and by 'buying support', proved hard to resist. In Libya, economic organisation, political participation and bureaucratic efficiency were held in abeyance, resulting in both change and structural economic stagnation.

In Algeria, the government grudgingly and selectively tied its economic fortune to continued economic relations with the industrial world in the hope of selective dissociation in the long run. Libya, on the other hand, continued to reject, almost instinctively, the pressures brought to bear upon it by continued reliance on those countries that provided its revenues. The luxury of isolation from domestic pressure groups, so prevalent in all rentier economies, was fostered by the Libyan leader who, from his assumption of power, demonstrated an aversion to the constraints implied by the concept of a modern state. By 1985, Libya was by all political and economic indicators as much a rentier state as when the Idrisi government was removed in 1969. In all of this, Qadhafi's use of the national myth has been extraordinary. Libya's anti-Western stand and Qadhafi's announcement of his Third Theory as an alternative to capitalism and communism have masked the continued and deepening dependence of the country upon the West. The rent generated by Libya's oil voided the need to extract resources or involvement from its society and indirectly contributed to its ability to forego a governmental bureaucracy and administration.

By 1978, Algeria had systematically extended government control, both economically and politically. And although under *infitah* the role of the state has been somewhat curtailed, its control functions have been largely retained.

The reliance on state capitalism and state entrepreneurship has rapidly increased and complicated the tasks that needed to be performed by the Algerian state. Ironically, Algerian leadership made the same mistake as earlier development theorists of assuming that the government could act as the only hand on the tiller. In the end, it lacked the degree of autonomy to accomplish the goals of state capitalism. Non-technocratic leadership rapidly lost control in favour of a technocratic/bureaucratic elite that by 1978 was politically influential, firmly entrenched within the economy, and crucial to the leadership's survival and to the pursuit of its industrialisation policies.

In contrast to Algeria, Libya never really attempted policies that systematically militated against the centrifugal tendencies of the international and domestic market. The dilemma of the rentier state, with its ability to provide for substantial growth, while missing real development, remained essentially unaddressed. Although power had become highly concentrated, economic and political directives were completely juxtaposed. The Qadhafi government favoured, on the one hand, a technocratic solution to complex economic problems while continuously uprooting groups possessing the necessary skills. The demonetisation issue of 1980, the low savings rates despite skyrocketing revenues, and occasional liquidity crises, manifested the government's inability to control the economy. Most of this could be attributed to lack of policy instruments, neglect for efficiency, and a political system that repeatedly attempted to bypass economic and technical problems by 'outspending' them. In this equation, Qadhafi's statecraft contrasted sharply with that of the Algerian leadership. Acrimony towards the United States, for example, led to a severe loss of control over the quality of technology acquisitions as Libya was forced to diversify its purchases.

The peripheral nature of the Libyan economy can thus, to a substantial degree, be traced to its leadership's political experimentation. The nature of the development strategy envisioned in the early 1970s, with its need for a strong centrally-guided economic system, was compromised by a government that systematically debureaucratised the policy and society. In contrast to Algeria's managerial style of economic policy, Libya has experienced a revolutionary style in which bureaucratic structures were continuously uprooted. In Algeria, the state was instrumental in determining the direction and shape of the development strategy, even though it lost its initiative in the end to a technocratic/bureaucratic elite. In Libya, the state never achieved the ability coherently to implement those policies that would have maximised its chances for greater autonomy in the international economy.

NOTE

1. In this regard the research undertaken on development and political strategies to deal with economic dependence within the small European industrialised countries seems particularly relevant. To a large degree sensitive to changes within the international economy, countries like Belgium, Holland and the Scandinavian countries, have systematically made political 'pay-offs' to societal groups (by means of social pacts, etc.) in order to maximise their economic potential and to further their development. Despite the relative absence of capital scarcity in these small countries and the new rentier states of the Middle East, different state/society relations prevail in each group. These determine, to a large extent, the degree to which compromises can be made, and the outcome of state/society relations. For more information on the small European countries, see Katzenstein (1983).

8

Fiscal Resources and Budget Financing in the Countries of the Maghreb (Algeria, Morocco, Tunisia, Libya and Mauritania)

Fathallah Oualalou and Larbi Jaidi

This chapter describes the evolution and current status of tax revenue in the context of budget financing in the five countries of the Maghreb: Algeria, Morocco, Tunisia, Libya and Mauritania. In all five countries the fiscal organisation inherited from the colonial past is still visible. The complexity of fiscal systems in the Maghreb is a function of diversification of the economy, which was in turn provoked by colonial penetration. Today, the structure of tax revenue, which is derived mostly from indirect taxes, is a reflection of the lack of domestic integration and of the extroverted orientation of Maghrebi countries. Since independence, no important transformation has occurred. Quite to the contrary, the advent of a rentier economy based on oil exports, in particular in Libya and Algeria, has contributed to the reduction of the role of tax revenue in the financing of the budget.

ALGERIA

Algeria derives important financial resources from the sale of hydrocarbons to foreign countries and the Algerian state plays a central role in the economy. State intervention in the organisation of economic life necessitates an intensive mobilisation of financial resources. Hydrocarbons production is the main source of revenue, but in contrast to other Arab oil countries, Algeria has a complete and diversified fiscal system. The latter generates a considerable share of the ordinary revenue of the state. Furthermore, its role in the regulation of economic

activity and its social impact are far from negligible.

From independence to the beginning of the 70s, economic life in Algeria was characterised by the effort to reappropriate national resources and to establish a state apparatus. The fiscal system inherited from the colonial period was not modified with respect to its composition or contribution to budget revenue.

Oil revenue and the Algerian development strategy

During the period 1971–7 an industrialisation strategy was implemented aiming at breaking away from dependence bonds. The essential components of the strategy were the enlargement of the state sector, industrialisation, agrarian reform and reinforcement of the planning system. State intervention in the economy was largely financed by oil revenue. The latter grew very fast because of increases in both price and government take; it came to play a dominant role over the total revenue of the state passing from 23.0 per cent in 1971 to 37.2 per cent in 1974. At the same time, the heavy commitments of the state, and in particular the Treasury loans and anticipations to finance public investment, also greatly increased. Foreign credit was tapped to meet part of these needs, but Algerian debt service remained modest.

Direct public control over production activity and the inflow of oil revenue allowed the funding of the projects included in the two four-year plans in this period (1970–3 and 1974–7). The primary source of funds for public investment was oil revenue. Mobilisation of financial resources from domestic sources remained minimal, and the largest part came from abroad. Domestic savings contributed only 25 per cent of funds utilised under the 70–3 plan, while oil revenue accounted for 31 per cent, revenue of migrants for 16 per cent and foreign aid for 28 per cent (Jacquemot and Raffinat, 1977: 155).

A radical change in the structure of revenue took place in 1974–5. Taxes on the oil sector became the most important item (59.1 per cent), because of the increase in posted oil prices and in the income tax rates applied to oil companies.

Leaving aside the increase in oil revenue, the ordinary fiscal system evolved only very slowly. The relative share of the main category of taxes was but marginally changed, with indirect taxes gaining importance. The financial ease brought by the increase in oil revenue allowed the state to put aside the need to undertake a radical reform of the fiscal system, and make it more adapted to the reality of the economy. Some modifications were nevertheless introduced, in view of improving social justice and redefining relations between enterprises and the state. The first goal was pursued mainly through a tax exemption for income below 500 Algerian dinars and abolition of custom duties on certain essential imports, while at the same time rates were increased on the revenue of corporations and on capital gains connected to the sale of real estate, and indirect taxes on non-essential products were also increased. The second goal was manifested by reductions in fiscal pressure on private enterprises and the self-managed sector. But the most important changes affected relations between the state and public enterprises, with a view to stimulating better management.

A reform was introduced that embodied a new fiscal philosophy with respect to the role of public enterprises in the national economy. Thus the state became more demanding both in terms of economic efficiency and in terms of fiscal revenue.

During the period 1978–84 the development policy was redefined: the industrialisation effort was slowed down, the public sector was restructured, the role of private initiative was redefined, and planning showed a greater degree of pragmatism. While these changes were introduced, the revenue of the state continued to be generated mostly by the oil sector, following the second wave of oil price increases.

The turnaround in the oil market in the 1980s had a considerable impact on the ability of the state to meet its financial needs. In the industrial sector, a critical assessment underlined the excessive development of the hydrocarbons sector and numerous structural deficiencies.

The reorganisation of the public sector became a precondition to improve economic efficiency. Having soon grown to huge dimensions, a majority of the public enterprises were faced with difficult financial and management problems, and became a drain on the financial resources of the state (from which they received subventions or loans) rather than a net contributor to them. The large public enterprises were thus subdivided into smaller specialised units, with decentralised management, following the rule of profit.

At the same time, the rehabilitation of private enterprise was the most evident sign of the change in the conduct of economic

Table 8.1: Algeria, ordinary budget revenue forecasts and allocations 1978–84 in millions of Algerian dinars

Year	1978	1979	1980	1981	1982	1983	1984
Ordinary taxation	14.329	17.2	19.0	22.2	25.4	41.1	49.0
Direct taxes		2.6		3.8		7.6	8.6
Turnover tax		5.4		7.4		14.0	15.9
Contributions[a]		5.0		5.2		6.5	7.6
Customs		2.6		3.9		7.6	8.7
Other taxes		1.4		1.7		5.3	8.0
Oil taxation	18.2	19.6	31.7	46.1	47.6	57.5	56.7
TOTAL REVENUE	32.6	36.9	50.8	68.4	73.1	98.6	105.7
Current expenditure	18.1	20.6	27.8	36.2	42.2	50.4	59.7
Balance on current budget	14.4	16.3	23.0	32.2	30.9	48.2	46.0
Investment expenditure	14.3	16.2	23.1	31.6	42.6	48.2	46.0
Balance on total budget	0.1	0.1	−0.1	−0.6	−11.7	—	—

Note: a. Contributions: excises, profits of fiscal monopoly, taxes on specific services, taxes to use goods, etc.

Source: *Maghreb development*, various issues.

policy. The state tried to define the role of the private sector both more precisely and more broadly.

The negative evolution in the international environment had an impact on the revenue of the state. Oil revenue further increased to reach 68 per cent of total revenue in 1981, but subsequently declined to 57.7 per cent in 1984 (see Table 8.1).

Ordinary fiscal revenue grew from a minimum of 32.1 per cent of the total in 1981 to 46.3 per cent in 1984. While in absolute numbers the various components of ordinary taxation grew unevenly depending on the year and the tax, the overall rate of increase was high. The budget laws introduced numerous changes that had social, economic and technical objectives. None of these measures had a structural character: aside from the 1977 reform of taxation on public enterprises, the Algerian taxation system suffered no major changes in the period.

Direct taxation in the Algerian fiscal system

Income taxation in Algeria is still based on a schedular tax (specific income tax vs. general) applying different rates to different sources of income. Direct taxation is composed of:

(a) A tax on industrial and commercial income. It is characterised by a multiplicity of regimes: thus private corporations pay a higher rate than public enterprises; self-managed enterprises benefit from a reduced rate; new enterprises benefit from a temporary exemption.
(b) Taxation on non-commercial income: this tax applies to income earned by individuals or entities in the exercise of a liberal profession.
(c) Taxation on salaries and fixed earnings.
(d) A complementary yearly tax on the higher salaries.
(e) A tax on financial assets. The tax is geared to discourage the distribution of benefits and favours long-term savings.
(f) A tax on property revenue: it is composed of a tax on inheritance and a tax on donations.
(g) A complementary tax on total revenue: it is added to the individual taxes, with the exception of the tax on salaries, and is progressive; it has but limited yield.
(h) Registration rights: they apply to many legal acts as well as to certain contracts.

TUNISIA

The evolution of Tunisian fiscal policy in the first and second development decades, 1960–70

Following independence and until the end of the decade of the 60s two sub-periods may be distinguished in the evolution of Tunisian fiscal policy. A first transitional period was dominated by the problems of decolonisation and witnessed no change in the structure and conception of the fiscal system as an instrument of economic policy. Financial aid from France continued to dominate investment expenditure. In a second phase, going from 1962 to 1969, Tunisia chose planned development, structural reforms and industrialisation led by the state. This phase witnessed certain adjustments in the fiscal instrument, but no effective integration of taxation into the broader framework of development policy. The failure of the *dirigiste* experience signals the end of the decade, and opens the door to a more liberal orientation.

The financing of the budget in the second development decade

The difficulties experienced during the cooperative experiment prompted the Tunisian government to steer a different course and undertake rehabilitation of the financial situation. In the second development decade, Tunisian development was based on a different set of principles: increased participation of the private sector in the development effort, increased opening to the rest of the world and promotion of exporting industries, intensification of efforts to mobilise domestic and international financial resources to sustain state intervention in the economy.

The second development decade had two contrasting phases. In a first phase (1970–6), fiscal policy introduced further technical changes in the determination of certain taxes aimed at improving the methodology of determination and collection of direct taxes.

Other fiscal measures were introduced with the aim of implementing the new development strategy. First, a system of exemptions (law of 27 April 1972) was created in favour of exporting enterprises. Second, a system of incentives was put in place to encourage the creation of small and medium enterprises and stimulate industrial decentralisation (laws of 31 Dec. 1973 and 3 Aug. 1974). Finally, a new custom tariff was adopted in 1973 which differentiated imports in various categories, increasing effective protection for the import-substituting industries.

These changes in economic strategy and in fiscal policy brought about a considerable increase in the ordinary revenue of the state. It should also be said that during this period economic activity expanded rapidly in the wake of a favourable international situation. The increase in total budget revenue reflects primarily the remarkable increase in tax revenue, which increased 15.7 per cent between 1972 and 1973, further accelerated to 27.4 per cent in 1974 and 30 per cent in 1975, then slowed down to 10 per cent in 1978. However, the relative share of tax over total revenue has not changed during this period (passing from 84 per cent in 1970 to 84.2 per cent in 1976) because of the parallel increase in non-tax revenue from the oil sector. The burden of taxation over GDP increased slightly (passing from 22.8 per cent in 1972 to 27.2 per cent in 1976).

Notwithstanding the positive evolution of tax revenue, public finance suffered a negative turn after 1970. Current expenditure of the consolidated central administration grew at an accelerating pace after 1972. The increase in current expenditure was primarily due to increased subventions and transfers to the *Caisse générale de compensation* and to public enterprises. The total amount of these outlays passed from 54.3 million dinars in 1972 to 144.1 million dinars in 1976. Personnel expenditure also increased from 98 to 172 million dinars, essentially because of increases in the pay of civil servants. Interest on foreign public debt (17.7 million dinars in 1976) was only 4.6 per cent of current expenditure.

In a second phase, going from 1977 to 1980, the relatively high rate of growth resulting from a favourable international environment decreased dramatically. Tensions on prices of imported goods and in domestic financial resources began to have negative effects on domestic as well as external equilibria. The state aimed at supporting economic activity and limiting bankruptcies in the private sector. Public investment, including both investment of the state and of public enterprises, accounted for two-thirds of total investment during the period. Economic stagnation limited the possibility of financing investment with domestic savings and reliance on foreign loans increased. On top of official loans and other forms of aid from abroad, the state tapped the international capital market for the first time in 1977. This tendency was maintained until 1980.

Reliance on foreign credit is partly explained by the fact that the fiscal system was not able to mobilise sufficient domestic resources. New measures introduced between 1977 and 1980 aimed essentially at reinforcing mechanisms of control, combating fraud and rationalising fiscal incentives. The only important innovations were the introduction of a tax on real estate appreciation and an extra tax on certain luxury products to finance expenditure on the part of the Caisse de Compensation. Lastly, certain rates were increased to foster revenue (the maximum rate of the CPE went from 45 to 55 per cent, and customs duties were raised).

These measures allowed a certain improvement in fiscal revenue (see Table 8.2), which increased by a factor of 1.6 between 1977 and 1980, but the rate of increase decelerated at the end of period (going from 23.4 per cent between 1977 and 1978 to 14.4 per cent in 1978/9 and 15.1 per cent in 1979–80). The slowdown is even more marked if social security contributions are included. Consequently the share of total expenditures covered by fiscal revenue practically did not change (69.7 per

Table 8.2: Tunisia, summary of accounts of the Consolidated Central Administration (millions of TD)

	1977	1978	1979	1980
Current revenues	612.2	779.0	939.1	1.108.5
Fiscal revenues	522.3	644.6	735.0	846.1
Direct taxes	102.6	132.3	149.6	194.4
Taxes on goods and services	176.3	203.8	243.0	264.5
Taxes on foreign trade and international transactions	158.5	193.7	234.1	273.3
Other indirect fiscal revenues	28.8	32.0	10.2	11.0
Social security contributions	56.1	82.8	98.1	102.9
Non-fiscal revenues	94.9	134.4	196.1	243.4
Revenue on property	78.5	111.2	175.4	214.4
– of which oil revenue	(53.7)	(69.0)	(129.8)	(173.3)
Other non-fiscal revenues	16.4	23.2	20.7	29.0
Other administration revenues	22.6	8.5	12.9	22.7
Capital revenues	9.2	0.8	2.1	0.7
Of which	13.4	7.7	10.8	22.0
Current expenditures	463.4	559.9	728.2	784.1
Expenditures on goods and services	269.9	308.3	389.3	471.3
Bank interests	21.4	29.9	48.1	50.4
Subsidies and other transfers	172.1	221.7	300.2	267.4
Current deficit or surplus	152.8	219.1	210.9	324.4
Capital expenditure	266.4	285.6	265.4	333.3
Net loans	42.2	43.2	38.0	112.7
Financial deficit	– 132.2	101.2	– 139.6	– 98.9
Finance	132.2	101.2	139.6	98.9
Foreign	95.8	75.5	136.8	80.4
Domestic	36.4	25.7	2.8	18.5
Non-bank loans	46.0	14.9	18.6	26.8
Deposit banks	2.7	17.1	– 21.5	26.2
Monetary authorities	– 12.3	– 6.3	5.7	– 34.5

Source: *Government Finance Statistics Yearbook*, IMF, 1983: pp. 754–7.

cent in 1980 as against 67.6 per cent in 1977), notwithstanding the reduction in capital expenditure. The structure of fiscal revenue was improved and the role of direct taxation increased (passing from 22 per cent in 1977 to 26.2 per cent in 1980) but indirect taxes continued to play a dominant role.

Another characteristic feature in the evolution of current revenue was the increase in revenue from property, and in particular the part of it which comes from the oil sector. This increase largely explains the surplus in the current account, notwithstanding the rapid increase in current expenditure in the years 1978 and 1979.

The increase in current expenditure obliged Tunisia to contain the growth of capital expenditure in order to keep within limits the deficit to be financed, and all the more so as foreign sources became the primary source of financing. In any case, the load and the structure of Tunisian foreign debt remained tolerable with respect to that of other countries in the Third World.

The structure of Tunisian fiscal revenue

According to IMF data Tunisian tax revenue in 1981 was composed of 352.2 million dinars from direct taxes (including 116.8 million of social security contributions), 310.6 million from taxes on goods and services, 338.2 million from taxes on trade and international transactions and 16.4 million from other taxes (including stamp rights for 4.2 million). The total came to 1,017.4 million dinars, equal to 76.3 per cent of the total revenue plus gifts received by the central administration. Direct taxes generate 34.6 per cent of total revenue, but their contribution is reduced to 26 per cent if social security contributions are not included.

Direct taxes

Direct taxation in Tunisia is characterised by the superimposition of two different categories of taxes:

(a) A set of schedular taxes (specific income taxes) with proportional rates that separately affect each type of revenue (revenue from financial assets, industrial and commercial profits, non-commercial profits, fixed earnings and salaries), with no distinction being made between individuals and entities.
(b) An additional tax with progressive rates, called *contribution personelle d'état* or personal state contribution (CPE), that affects the overall revenue of individuals (Magnet, 1969).

The personal state contribution (CPE) was created in 1927 and is added to the various schedular taxes. Total net disposable income after the above mentioned taxes are paid is hit by a progressive additional tax. The structure of rates on the latter has been repeatedly modified: the highest rate is 80 per cent.

Indirect taxes

These are divided into three categories:

(a) Taxes on domestic expenditure, which are further divided in general turnover taxes (production tax, consumption tax, tax on services), excises on consumption and revenue of fiscal monopolies.
(b) Taxes on trade and international transactions.
(c) Rights on legal acts and services.

Taxes on domestic expenditure generated a revenue of 310.6 million dinars in 1981, equal to approximately one-half of the total from indirect taxation.

Taxes on international trade and transactions gave to the state budget a revenue of 338.2 million dinars in 1981, equal to 50.8 per cent of indirect tax revenue.

MOROCCO

General framework

It is impossible to analyse public finance data independently of the general framework of Moroccan economic evolution, with particular reference to the financial situation. The Moroccan economy is experiencing a prolonged crisis which began in 1978. Growth rates are small (2 per cent yearly on average), investments have decreased, traditional exports (phosphates, citrus and early ripening fruits and vegetables) are stagnant. As a consequence the trade balance and the balance of payments show increasing deficits. Twice, in 1978 and 1983, the government imposed restrictive policies in order to reduce the deficits in the state budget and in the balance of payments, yet the former has always been greater than 10 per cent of GDP since 1979 and was heading to 16 per cent in 1983 (at 16 billion dirhams), while the latter was equal to 12.9 per cent of GDP in 1983. Foreign indebtedness was in 1983 equal to 70 per cent of GDP and debt service went from 34 per cent of current balance of payments receipts in 1982 to 42 per cent in 1983.

A recovery plan was elaborated in cooperation with the IMF, aiming at limiting the deficit in the balance of payments to 9 per cent of GDP in 1983 and 7 per cent in 1984. The new policy was applied in three phases: (1) in July 1983 a corrective law of budget was approved, eliminating expenditure under certain items and credits for the purchase of automobiles, and reducing price subsidies on sugar, flour, butter and oil (prices increased 18 to 70 per cent as a consequence), increasing the price of oil products and fertilisers, increasing taxation and, in particular, the standard rate of the TPS — the urban tax — the national solidarity tax and stamp and registration rights; (2) in a second phase the budget law for 1984 reinforced the restrictive policy by cutting expenditure by 5 per cent; (3) finally, in April 1984 a further corrective budget law kept expenditure constant on most items but tried to increase revenue through new extraordinary taxes and a fiscal amnesty. The government was obliged to defer price increases on basic consumption products, because of widespread opposition that had been manifest since January of that year. At the same time liberalisation of foreign trade was pursued by reducing a special tax on imports from 12 to 10 per cent, as well as lowering custom duties. The 1985 budget law followed the same lines and further reduced the special tax on imports to 7.5 per cent.

The structure of the Moroccan budget

Table 8.3 depicts the evolution of the Moroccan budget in 1978–84 and highlights the growing constraints since 1978. As the table shows, current consumption expenditure on the part of the state grew but slowly since 1978. However, transfers to the Caisse de Compensation administering price subsidies grew regularly from 1978 to 1985, notwithstanding the repeated price increases. At the same time, the service charge on public debt to foreign creditors continuously increased, due to the accumulation of foreign loans on the international financial market between 1974 and 1980.

In 1984 fiscal revenue covered 69 per cent of actual state expenditure: a relatively high percentage which can be explained

Table 8.3: Morocco, evolution of the structure of the budget, 1978–84 (millions of MD)

	1978	1979	1980	1981	1982	1983	1984
Ordinary revenue	11,693	13,802	15,193	17,838	20,480	21,094	23,815
Direct taxes	2,625	3,202	3,231	3,650	4,120	4,599	5,300
Customs duties	2,568	2,897	3,530	4,208	4,943	4,452	4,885
Indirect taxes	4,168	4,659	5,487	5,784	7,376	8,290	9,100
Registration and stamp	832	1,186	1,338	1,396	1,702	1,756	2,260
Monopolies	295	215	167	546	1,015	570	500
Public domain	56	50	57	56	55	57	50
Other revenue	349	893	583	901	729	620	620
Office Chérifien des Phosphates	800	700	800	1,297	540	750	1,100
Current expenditure	10,420	12,073	15,310	18,898	20,475	21,525	23,644
Public debt service	1,047	1,360	1,759	2,924	3,144	3,526	4,118
Working expenditure	8,984	10,102	12,124	13,872	15,331	16,367	17,151
Subsidies	389	611	1,427	2,102	2,000	1,632	2,375
Current deficit or surplus	+1,273	+1,729	−117	−1,060	+5	−431	+171
Investment expenditure	−6,629	−9,016	−8,565	−9,612	−12,481	−7,979	−7,410
Extra-budgetary expenditure	−739	+1,018	+1,172	−426	+1,368	+407	
Financial deficit	−6,095	−6,269	−7,510	−11,098	−11,108	−8,003	−7,239
Funding	+6,095	+6,269	+7,510	+11,098	+11,108	+8,003	+7,239
Foreign credit	3,364	4,016	3,911	7,116	6,471	3,392	4,769
Bank loans	2,287	1,319	2,888	3,788	2,197	6,703	2,170
Bank of Morocco	(1,007)	(715)	(1,259)	(1,648)	(1,342)	(2,543)	
IMF	(—)	(—)	(781)	(821)	(2,885)	(839)	
Deposit banks	(1,280)	(604)	(848)	(1,319)	(654)	(3,321)	
Non-bank loans	569	959	447	325	379	190	600
Reserves	−125	−25	264	−131	2,061	−2,282	−300

Source: Government of Morocco, Ministry of the Treasury.

with the reduction in investment expenditure that was financed with foreign credit. In 1982 the same ratio stood at 55 per cent.

Revenue from the public sector supplies but a small contribution to the budget. In 1984 public enterprises contributed less than 4 per cent of the total state budget, and 68 per cent of this contribution came from the Office Chérifien des Phosphates (OCP). Thus public enterprises contributed less than 4 per cent of the total state budget.

The structure of budget revenue

Budget revenue is made up of tax revenue, transfers from public enterprises and public debt. Tax revenue total thus comes to 24,060 million dirhams, equal to 63 per cent of total budget revenue.

Indirect taxes are by far the most important source of revenue, yielding 72.2 per cent of the total, while direct taxes yield 27.8 per cent. This is a manifestation of Moroccan economic underdevelopment, characterised by low personal incomes and the lack of a source of rent from the rest of the world.

There are ten direct taxes; agricultural revenue, that was traditionally undertaxed, was totally exempted in 1982. The two most important taxes are the tax on professional revenue (3,160 million dirhams according to the 1985 budget law) and the withholding tax on salaries (2,180 million). The national solidarity tax, created in 1979 as a complementary direct tax to finance the defence effort imposed by the war in the Sahara, is third with 551 million; the three together account for 88 per cent of total revenue from direct taxes.

The limits of the direct taxation structure are shown by its low yield and excessive complexity. The ten schedular (specific) income taxes have evolved independently of each other through various legislative transformations, with a total lack of coherent and organic design. A general personal income tax is absent, although the creation of the general complementary contribution at the end of the 60s helped to rationalise the Moroccan fiscal system and introduced progressive taxation to improve the tapping of individuals' income.

In May 1985, the government introduced in parliament a fiscal reform project which replaces schedular income taxes with

a general income tax, which would increase equity, improve the determination of the tax base and collection prodedures and unify deductions. The general income tax is to be applied to professional income, agricultural income, salaries, income from real estate and from financial assets.

Indirect taxation is composed of taxes on domestic consumption, a tax on turnover, custom duties and registration and stamp rights.

In the framework of the proposed fiscal reform, a tax on value added should be introduced, taxation extended to wholesale trade, deductions generalised to guarantee the neutrality of the price structure, the two existing taxes unified and the rates reduced to four, with a standard rate of 19 per cent, a high rate of 30 per cent and two reduced rates of 14 and 7 per cent.

Custom duties generate significant resources. For a long time the Moroccan government was inclined to increase taxation on imports to protect local production as well as to increase state revenue. More than ever before, this was the case between 1978 and 1982 to reduce disequilibria in the Treasury and in the balance of trade. But the liberal tendencies that have prevailed since 1983 have led the government to reduce import duties as well as the rate of the special import tax.

Transfers from public and semi-public enterprises are but 4.5 per cent of total budget revenue and 64 per cent of the revenue under this category comes from the OCP. The rest is transferred from the Bank of Morocco (250 million), the postal authority (120 million), the Caisse de Depôt et de Gestion (85 million), and the National Office for Transportation (50 million).

Thus 700 public and semi-public enterprises contribute only marginally to the financing of the budget. This is also due to the failure of public enterprises, most of which receive subventions to cover current and investment expenditure and to finance deficits that are caused by faulty management, to the excessively low prices motivated by social considerations, and to constraints imposed on exporting enterprises by international market conditions.

Public debt has played an important role in the financing of the budget, particularly since 1975. The decline in phosphate demand and prices caused a considerable decrease in financial resources, which had increased in 1973 during a period of passing euphoria and caused a significant jump in the level of public investment. To compensate for the decrease, the government massively resorted to foreign borrowing, encouraged by international financial operators who were suffering from an excess of liquidity in the 70s. Thus external financing became the prime mover in the undertaking of investment projects on the part of the government, public enterprises or financial intermediaries.

Domestic debt has a limited role because of the weakness of local savings. It is expected that revenue from domestic loans will reach 1 billion dirhams in 1985, while the level of discounted external loans would be over 6 billion. Revenue from domestic loans is composed of two categories:

(a) The first, revenue from the sale of Treasury bonds, essentially to financial institutions and the Caisse de Dépot. In February 1985 the Treasury for the first time issued bonds directly to the public. This issue was a total success because of the high rate offered (14 per cent) over a three-year period.
(b) The second, the receipts of a compulsory investment reserve, imposed on corporations paying taxes on profits and yielding 200 million dirhams. This form of forced loan is due to disappear under the proposed fiscal reform.

LIBYA

Following independence and until the beginning of the 70s Libya was a country under the control of external forces and was unable to mobilise the financial resources that were necessary for its development. In the 50s, the Libyan state was one of the poorest in the world. Sparse agricultural resources spread over a huge territory with few natural endowments could not offer to the state sufficient means to engage in the development of the country. Foreign aid, a fluctuating and self-interested source of income, was geared to keep the Libyan economy in a condition of mere survivability. The discovery of the first oilfield in 1957 was the beginning of a process of assured and continuous growth in the state financial resources. Nevertheless, the oil cartel's domination of the exploitation of oil, distortions and bottlenecks introduced in economic structures by the hegemony of the oil sector, and the uprooting of traditional social structures, contributed to creating a favourable environment for institutional change, which took place in 1969.

This was the beginning of a process of policy redefinition,

starting with the reappropriation of national resources, which with the help of increases in oil prices, led to a substantial increase in the revenue of the state. Taxation on the oil sector became the most important, indeed almost exclusive, source of budget revenue, and the total revenue it generated increased enormously. An exogenous source of revenue fueling the intervention capacity of a state keen on spending, it pushed the endogenous sources of government revenue to a mere complementary role. The growth in absolute terms of non-oil taxation is partly connected with economic activities or income redistribution indirectly supported by the oil sector.

After the revolution, two phases may be distinguished in the Libyan economic policy in general and taxation policy in particular. A first phase (1970–75) was centred around the recovery of national resources and characterised by an abundance of financial resources. A second phase (1977–82) was characterised by the effort to diversify the economy and create an economic and social infrastructure, but also by the reversal in international oil conditions and the emergence of domestic bottlenecks.

While oil revenues continued to increase until 1980, Libyan oil production systematically declined. Decrease in world demand and political tensions with the United States, over and above the Libyan preoccupation with exhaustion of reserves, are the main causes of the decline. Exports plummeted in 1981 and 1982, while prices, which had increased until 1981, started to decline in 1982. Oil revenues increased until 1980, reaching 23,200 million dollars, from 7,500 million in 1976. Thus budget revenue increased until the end of the 70s and started to decline in the 80s; in 1981 it was 31 per cent off the previous year (Talha, 1981).

This turnaround took place at a time when the Libyan government had a pressing need for funds to finance its development projects. Under the 1976–80 five-year plan, a costly policy of diversification was begun, whose benefits could only come in the longer term, and which needed to be sustained by the plan for 1981–5. But the ordinary fiscal system, divided into a multiplicity of low-yield taxes, contributes only to a limited extent to the mobilisation of domestic resources. While the revenue derived from it has increased, a large part of it is still directly or indirectly linked to oil activity: state expenditure on salaries for domestic and foreign workers broadens the base of personal income tax; consumption induced from distribution of the oil revenue increases the yield of excises and custom duties, etc. At the same time, the policy of the government has led to a shrinking of the private sector, and consequently to a loss of budget revenue.

Nevertheless, one has the impression that the potential for raising revenue domestically has not been fully exploited.

MAURITANIA

The components and final equilibrium of the Mauritanian budget are intimately linked to those of the balance of payments. Revenue is essentially derived from the tax affecting the exploitation of iron resources, from royalties paid by foreign fishing vessels operating along the Mauritanian coast and by official gifts and transfers or loans from abroad.

Immediately after independence, and until MIFERMA began exploiting iron ore in 1964, tax resources did not suffice to pay for operating expenditures, notwithstanding the latter's paucity. For four years in a row, France funded the budget deficit in view of the special ties between Mauritania and Paris.

In the second half of the 60s revenue from exports of iron ore constituted between 23 and 27 per cent of the total current revenue. One should also add customs duties, which generated 36 per cent of the revenue: it is evident that public consumption was strictly linked to foreign trade.

The remaining revenue came from taxation:

(a) The contribution to support the national defence effort, which reached 745 million oukiyas in 1977 when Mauritania intervened with Morocco in the western Saharan conflict.
(b) Direct taxation, composed of a tax on fixed earnings and salaries (yielding 675 million oukiyas in 1979); an income tax (300 million oukiyas); a tax on profits (475 million oukiyas).
(c) Indirect taxation, including: a tax on the export of copper, which yielded some 40 million oukiyas in 1974, when mining of copper was ended; an excise on consumption of hydrocarbons (200 million oukiyas); a consumption tax (69 million); a tax on tobacco (39 million).

These figures show the stringent limits of tax revenue, both

direct and indirect, due to the small dimensions of the Mauritanian economy. At the same time, the operating budget increased rapidly after 1974 because of the abandonment of the policy of austerity which had continued since 1960, the exodus of nomads from the desert following the drought of the 70s, and the national defence needs between 1976 and 1977.

The investment budget is funded from three sources of revenue: fishing royalties, transfers from the public sector and the surplus on the current budget. Royalties paid by foreign fishing vessels have become the main source of revenue; transfers from the public sector reflect the nationalisation of MIFERMA. They ceased in 1977 because war in the Sahara brought iron ore production to a halt. The surplus in the current budget disappeared in 1974, because of the increase in current expenditure.

In Mauritania, government investment projects are also financed out of special accounts of the Treasury and resources of public or semi-public enterprises. Gifts and loans from abroad are credited to the special accounts. They totalled some 5 billion oukiyas in 1975, 77 per cent of which came from the Arab oil-producing countries and were intended to fund industrial projects whose profitability was later questioned (an oil refinery, a sugar refinery at Nouadhibou, etc.)

Fiscal policy since 1979

The deterioration in the economic situation, the worsening of domestic and foreign financial equilibria and constraints brought on by Mauritanian intervention in the Saharan conflict led to the fall of President Moktar Ouldada. Since then, despite almost permanent political instability, all governments have been obliged to follow a policy of restrictions on expenditure. The budget for 1982 aimed at equilibrium: custom duties and direct taxes were increased and the minimum personal revenue exempted from taxation passes from 45,000 to 80,000 oukiyas. Taxation on houses was reduced to encourage building acitivity.

However, stagnation of iron ore exports, not entirely compensated by the increase in the value of the dollar, and insufficient agricultural production led to a widening of the financial gap and obliged the government to tighten its austerity policy, in accordance with the IMF.

Foreign debt reached an intolerable level because the revenue of many projects funded from abroad was very limited.

Following the accession to power of Lt. Maaouya Sid Ahmed Ould Taya in December 1984 the policy of financial restriction was further reinforced. With a total outstanding debt of 1.7 billion dollars, equal to twice its GDP, Mauritania bowed to IMF recommendations. The price of basic necessities, such as rice, was increased 10 to 20 per cent, and the price paid to producers was also increased. In parallel, Mauritania allowed the oukiya to float and lose about 15 per cent of its value. This facilitated negotiations for new rescheduling of foreign debt.

COMPARATIVE ANALYSIS OF MAGHREBI TAXATION SYSTEMS

The fiscal system of the Maghrebi states have a common origin. Modern taxes were created during the colonial period. The old taxes, based on religion, sovereignty or customs, lost importance after the disintegration of precapitalist modes of production, in spite of numerous attempts at reform which preceded colonial intervention. The colonial administrations pursued an increase in fiscal revenue by, on the one hand, modernising some old taxes, particularly those on agriculture, and, on the other hand, creating new taxes, modelled on those of the colonising power. Progressively new taxation systems, including direct and indirect taxes, were introduced in the Maghreb. Most of the present-day taxes date from this period.

World War II had an important influence on the revenue of these taxes, linked to international economic conditions. Because of restrictions on international trade, customs duties and domestic consumption taxes yielded decreasing revenue. At the same time expenditure was growing, thus necessitating the creation of further direct taxes. Thus a tax on fixed earnings and salaries was imposed in Tunisia (1937) and Morocco (1939), while taxes on corporations were sharpened (in Morocco, Tunisia and Algeria).

Created by the colonial powers to serve their own purposes, taxation systems in the Maghreb are not functional to the development needs of the countries. Following independence, the social and economic turmoil brought by decolonisation and economic development requirements underlined the need to restructure these systems. Yet, more than two decades later, these systems are still essentially the same. Governments have only increased rates, made a few technical adjustments, and implemented partial reforms to substitute new taxes for old ones (e.g. substituting taxes on products and services for taxes on transactions, the agricultural tax for *tertib*, etc.) These partial measures have not greatly affected state revenue or the economy of the Maghrebi countries. Countries which had the most pressing revenue needs (Morocco, Tunisia, Mauritania) enacted the most important changes, at least quantitatively speaking. All the same, the need for in-depth fiscal reform is on the agenda in all the states of the Maghreb.

Although taxation rates on the profit of enterprises, be they private or public, are progressive and relatively high, production units give but a small contribution to state revenue. Development policies based on the creation of development poles (such as in Algeria and Libya) generate large units, financed by slowly maturing investment, operating in an environment with no economic rationality and offering little potential for growth. It is, then, to be expected that enterprises will not generate a financial surplus that may be a base for state taxation. Alternatively, the policies based on light industry (Morocco and Tunisia) and export-oriented small and medium enterprises are accompanied by taxation policies favouring international competitiveness. In this context they benefit from important fiscal advantages which translate into revenue lost to the government.

The weakness of direct taxation in Maghreb public finance is, more generally, a consequence of the pattern of growth in the respective economies. Growth is unbalanced, the industrial sector is weak and disintegrated, the agricultural sector archaic, the services sector plethoric. Deficiencies in productive structures explain the peculiar behaviour of the elasticity of direct fiscal revenue with respect of GDP. This elasticity is strongly linked to exogenous factors (oil and mining) and to modifications in fiscal legislation.

The tendency to introduce numerous minor changes in legislation each year (especially in non-oil countries) manifests the need of the states regularly to increase their revenue to fund their growing commitments, and implicitly, also the lack of a direct link between economic growth and fiscal revenue. In other words, this elasticity is neither automatic nor endogenous; it is an input from the rest of the world or follows legal and/or technical changes.

Consequently, governments have but little control of their tax revenue and cannot use fiscal policy as an efficient instrument of short-term economic policy or long-term planning of revenue and expenditure. Foreign demand determines a large part of fiscal revenue, both directly and indirectly. Because fiscal variables cannot be controlled, formulation of long-term objectives is a myth, rather than an exercise in rational planning. Fiscal constraints and the absence of alternative fiscal policies nullify all attempts at autonomous development.

Despite similarities in their ordinary systems of taxation, the countries of the Maghreb finance their budgets in quite different ways. This differentiation originates in the role of oil revenue (Libya and Algeria) or of external debt (Mauritania, Morocco, Tunisia, Algeria). Thus the tendency for public savings to disappear emerged in certain countries (Morocco and Mauritania) making current expenditure partly dependent on foreign loans or advances from the central bank (Morocco) or even on foreign aid (Mauritania). On the other hand, the allocation of oil revenue to current expenditure allows the oil countries (Algeria and Libya) to bridge the gap between ordinary revenue and current expenditure, while the remaining surplus is devoted to capital expenditure. Tunisia still is in an intermediate position, as current revenue and expenditure are basically kept in line.

While Libya managed to invest a considerable financial surplus abroad in the good years and limited her dependence to a few insignificant loans, Algeria and the other countries regularly tapped international financial markets to acquire the funds needed to speed up economic development. Nevertheless, the debt situation is different in each country of the Maghreb.

Morocco, which relied more than others on this source of financing, was brutally confronted with the problem of managing its international debt, with the usual consequences in relations with creditors (debt rescheduling, structural adjustment programme). Algeria and Tunisia have avoided coming under pressure from international financial institutions, and keep their level of debt within proportions that are compatible with their ability to repay.

In the second half of the 1980s the situation of public finance in the five countries appears far from brilliant.

Morocco will face the need for austerity at least until 1990. While external resources stagnate and import costs increase from one year to the next, the Moroccan state must tighten

restrictions on consumption and investment and cut subsidies while liberalising foreign trade.

Mauritania is in total disarray. Revenues from iron exports and royalties on fishing are insufficient to cope with drought and exodus, and the state must drastically restrict expenditure and accept IMF recipes to obtain a rescheduling of debt.

The financial situation in Tunisia is also critical at times. Government attempts at reducing subsidies on food items are politically unacceptable.

In Algeria, the oil rent permitted a 20-year period of abundance, with important subsidies being extended to consumers and nationalised enterprises. But a growing foreign debt, continuing techological dependence and the decrease in hydrocarbons revenue may lead to unexpected disequilibria.

Finally, in Libya the ratio of oil revenue to population still allows for a relaxed fiscal management but the times of surpluses are clearly gone.

Overcoming disequilibria calls for a reorientation of the means of financing and greater reliance on the domestic economy. Fiscal systems must be revised and enriched to mobilise a maximum of the national surplus and reduce reliance on funding from abroad.

9

Government Income Sources and the Development of the Taxation System — the Case of Jordan, Egypt and Kuwait

Hesham Garaibeh

Higher oil prices and the consequent large oil revenues for oil-exporting countries created a clear distinction between Arab countries. For oil-wealthy countries, revenues generated from oil exports considerably exceeded domestic needs and encouraged governments to engage in extensive internal and external transfers. Governments of oil-exporting countries transferred wealth to the private sector by providing free services and subsidies, and developing societies in which taxation is absent. The accumulation of oil wealth also induced oil-exporting countries to engage in large unilateral transfers to other Arab and foreign countries. The non-oil-exporting Arab countries, on the contrary, had to rely on their domestic revenues, requiring the development of a taxation system, in addition to external aid received from oil-exporting countries. In other words, oil revenues induced oil countries not to impose any significant taxes and remain with an underdeveloped domestic taxation system, while the rest of the Arab countries were obliged to impose different types of taxes to partly finance their development programmes. This, in turn, led to the establishment of a relatively modern taxation system.

Recent developments in the oil market, which resulted in a sharp decline in prices and volume of oil exports, caused some Arab oil-exporting countries to start thinking about establishing a taxation system to generate more revenues to offset the deficit in external revenues. However, these efforts are inadequate for replacing the significant loss in external revenues. The development of a taxation system is needed not only to raise revenues but also for its redistributional effect, as wealth is concentrated among a relatively small number of people.

TAXATION STRUCTURES

A general look at Kuwait, Egypt and Jordan provides an accurate classification of their revenues. While Kuwait is considered a major oil country as most, if not all, of its revenues are generated from oil exports, Egypt is a semi-oil country meaning that some revenues are generated from oil and the rest are generated from other tax and non-tax sources. Jordan is a non-oil country: sources of revenues are confined to internal sources of income such as taxes and fees, in addition to foreign aid. For the purpose of detailing sources of revenues, we will point out the major sources of tax revenues and the structure of the taxation systems in the three countries. Of the three countries, only two, namely Jordan and Egypt, have a comprehensive taxation system. Oil and external sources of revenues are self explanatory.

Jordan

After the economic boom of 1974–82, the Jordanian government found it very necessary to change, amend and up-date the taxation structure in response to the changes in income, cost of living and other economic variations. The most significant changes in the tax structure were introduced and became effective in 1982. The new tax law featured many important changes such as:

Self-assessment

This is where each person is responsible for reporting his income from different sources to the tax department by the end of April each year. Whereas before the new law was introduced, income used to be estimated by tax department employees based on whatever documents they may have had. Under the new law, a tax return is still not final unless it is approved by the tax department, but in general, taxpayers have much more freedom in estimating their income.

Tax exemptions

The new law gives somewhat generous exemptions when compared to the law that existed before. These changes include more exemptions for families, education, house rent and some sources of income such as agriculture.

Larger tax brackets

Under the new law, a progressive tax is imposed on net income according to rates varying from a minimum of 5 per cent for income up to 1,000 JD to a maximum of 55 per cent for income exceeding 36,000 JD (Jordan Tax Department, 1982: 10).

Income is taxable only when consistent and renewable (Khasawneh, 1981: 25). Income from agriculture and interest earned from government bonds is totally exempted.

Corporate tax

This tax is also important in Jordan, especially after the economic boom in which many new corporations were created and realised sizeable profits. The Jordanian corporate tax law distinguishes between corporations according to types of business, with a clear inclination to treat industrial corporations favourably.

According to the new tax law, corporations are taxed at the following rates: industrial, health and educational corporations: 35 per cent; private and non-resident companies: 40 per cent; finance and banking corporations: 50 per cent; limited ownership finance companies: 55 per cent.

Taxes on building and real estate

This type of tax is imposed on the potential rent of the building, which is often underestimated. Tax on buildings is charged at the rate of 17 per cent of rent value. A new amendment to this law was introduced in which 25 per cent of rent value is exempted in Amman and 50 per cent in other cities outside the area of the capital to encourage construction outside the heavily populated capital.

Indirect taxes

Following are the most important indirect taxes used in Jordan:

Customs duties. Imposed on goods imported or exported. This type of tax is the most important in Jordan in terms of revenues. The rate varies according to the goods imported: luxury goods are heavily taxed, also imports with local substitutes are taxed differently to protect production.

Taxes on exports are also used in Jordan at a flat rate of 1 per cent of the value of exported goods.

Excise tax. This tax is usually imposed to restrict demand on certain goods in addition to generating revenue (Buchanan and Flowers, 1975: 307). Accordingly, this type of tax is imposed on goods such as tobacco, cigarettes and alcoholic beverages.

Stamp tax. This is an indirect tax collected on documents obtained from the government and on checks by means of a stamp affixed on each document.

Egypt

The introduction of taxes in Egypt dates back to the 1930s, thus making Egypt the first country in the Middle East to introduce a complete taxation system. The tax structure and rates changed from time to time according to inflation, economic development and government budget. It has also been noted that the increase in taxation rates is largely used to finance the increase in public consumption rather than to reduce the share of aggregate consumption in the economy (Mabro, 1974: 183–4). In other words, taxes are imposed mostly for their revenue effect rather than for distributional purposes. Following are the major types of taxes used in Egypt:

Income tax

Egypt, like Jordan, employs a progressive income tax rate. Income tax rates were determined by law 157 of 1981 (Egyptian Ministry of Finance). Income up to LE 960 is exempted from income tax. Income on the following 480 LE is taxed at 2 per cent. The maximum rate is 22 per cent for income in excess of LE 4800. Law no. 157 featured some changes when compared to law no. 199 and other laws introduced in 1974 and 1978. These changes are reflected in greater income exemptions, wider taxable income brackets and the degree of progression.

For schedular taxes, the highest tax rate is 50 per cent. According to law no. 157, schedular taxes are paid on four types of income: dividends and interest, profits, professional income, and wages and salaries. Income brackets under schedular taxes are different from those for the general income tax.

Corporate income tax

A tax imposed on the net profit of all establishments on an annual basis. Before the new law of 1981, corporate income tax was a flat 40 per cent of net profit earned by corporations. The new law 157 makes a distinction between public sector companies and other individual and partnership companies. Public sector companies pay 32 per cent of their net profit as tax, while individual and partnership companies pay progressive tax rates varying from a minimum of 20 per cent on income up to 1000 LE, to a maximum of 32 per cent on income exceeding LE 4500.

Previously, taxes were levied on partnerships and individual companies at a flat 40 per cent.

Taxes on property

These taxes are levied on property of agricultural land or buildings. Taxes levied on arable land were abolished in 1981, but local taxes imposed by governorates are still in existence at the rate of 14 per cent of the annual rent value of arable lands.

The tax on buildings is assessed on the actual rental value, or on imputed rents if the building is occupied by the owner. The 1981 tax law also abolished taxation on buildings, but local governorates impose building tax at the rate of 10 per cent for non-residential buildings and a progressive tax from 10 to 40 per cent for residential buildings.

Indirect taxes

As is the case in Jordan, and indeed in most less-developed countries, indirect taxes are the most significant source of revenue in Egypt. There are many types of indirect taxes used in Egypt. The following are the most important types.

Custom duties. The most important source of tax revenue in Egypt, custom duties range widely from 0 to 3000 per cent depending on the type of import. Favourable tax treatment is given to capital goods whereas consumer and luxury items are highly taxed to a rate which reaches 3000 per cent on alcoholic beverages.

Custom duties are levied on imports based on their CIF (Cost, Insurance, Freight) import prices. Prices in foreign currencies are translated into Egyptian pounds according to the Central Bank exchange rate.

Development tax. A tax levied on most imports in addition to custom duties to finance economic development. The current development tax is about 5 per cent on most imports.

Export custom duties. A selective tax imposed on a few goods when exported. These goods include raw hides and skins, metal scraps and wastes and antiques. This rate varies according to the product exported, up to a maximum of 5 per cent imposed on antiques of an age exceeding 100 years.

Consumption tax. A selective tax imposed on a list of 53 commodities regardless of their origin (local or imported) such as coffee, tea, cigarettes and beverages.

Stamp tax. Tax levied on a wide range of documents, requiring users to affix a stamp on the document.

Alain Tait has made an attempt to analyse the tax efforts in selected developing countries and ranked the efforts in Egypt as eleventh in a sample consisting of 44 developing countries (Tait, 1979). However, the rapid changes in tax structure and rates make it difficult to analyse the tax capacity or efforts in Egypt.

Kuwait

Owing to the abundance of oil revenue, Kuwait has never used taxation as a source of income, nor as a fiscal tool to influence levels of production, employment, prices or the distribution of income (Central Bank of Kuwait, 1981: 49). The government of Kuwait levies no income, corporate or direct taxes. The main source of revenue comes from indirect taxes. A relatively low custom duty is levied on certain imported luxury items. Custom duties were originally about 4 per cent of imported goods; the rate was increased to 10 per cent in 1971. Foodstuffs and raw materials, in addition to many commodities needed for local industry, are duty free.

GOVERNMENT REVENUES

In this section, we will try to shed some light on the major sources of government revenues and how they have grown in recent years; and will compare the importance of domestic versus external revenues for the sample countries.

Jordan

The fact that Jordan lacks both natural and financial resources is clearly reflected in government revenues. Except for a few years, external revenues have always exceeded domestic revenues both in volume and relative importance.

The recent economic growth achieved by Jordan is mainly attributed to the oil wealth generated in neighbouring Arab countries. Accumulation of oil revenue triggered massive development plans implemented by oil-rich Arab countries. As a consequence, demand for skilled labour, administrators, engineers and other professionals to run the newly created facilities soared up. Jordan stands as a major supplier of educated and skilled manpower. New job opportunities, and higher payments, induced Jordanians to migrate on a massive scale to the oil-rich countries. It is estimated that about 300,000 Jordanians are currently working abroad, a number which is equal to the labour force in Jordan itself.

Government revenues in Jordan are classified according to their source, external and internal. Internal or local sources are also classified into two major groups: tax and non-tax revenues. Following is a detailed analysis of all sources of revenues.

External sources of revenues

As a result of the outflow of Jordanian workers to the Gulf region, remittances to Jordan started to increase as the economic situation in oil-rich countries blossomed. Increasing remittances, coupled with other factors, caused an economic boom in Jordan itself, which led to increased tax and other revenues for the government.

In addition to the remittances from abroad. Jordan was also a major recipient of foreign and Arab aid, which reached its highest absolute level in 1981 when total foreign and Arab aid reached 289.9 million Jordanian dinars, or 24.4 per cent of GDP for that year. It then started to decline.

Table 9.1 shows the magnitude and importance of foreign aid relative to GDP. Clearly Jordan is among very few countries in

Table 9.1: External revenues of the state, Jordan (million JD)

Year	GDP	External revenues	% of GDP
1970	134.4	37.3	21.5
1975	312.4	116.7	37.4
1976	421.6	86.1	20.4
1977	514.2	180.7	35.1
1978	632.2	172.4	27.2
1979	753.0	247.9	32.9
1980	979.5	280.9	28.6
1981	1182.5	289.2	24.4
1982	1343.2	246.4	18.3
1983	1487.6	233.5	15.7
1984	1529.5	252.5	16.5

Source: Central Bank of Jordan, *Annual Report*, several issues.

in the world which heavily depend on foreign aid and grants. This situation was created as a result of lack of internal resources, which obliged Jordan to look for external revenue to compensate the shortage of domestic revenue.

Following are the major items included under foreign revenues:

Budget support. The most significant source of foreign revenues. Budget support mainly comes from Arab oil-rich countries which, under the agreements signed in more than one Arab summit conference, have pledged to financially support Jordan and other 'frontline countries' to enable Jordan to defend itself and have a sound economy. Thus this kind of support takes the shape of donations or grants.

The main problem facing the government of Jordan is the sharp fluctuations in Arab aid listed under budget support. Recently, most Arab oil-rich countries ceased their contribution, with the exception of Saudi Arabia, leaving no choice for the government but to increase local revenues.

Economic and technical assistance. The second source of foreign grants. Economic and technical assistance mainly consists of equipment, studies and other services rendered to Jordan without obligation. The main countries providing this type of foreign aid are the USA, Japan and some European countries.

Development loans. Jordan is increasingly depending on foreign

Table 9.2: Relative importance of domestic and foreign revenues (JD millions)

Year	Domestic revenues	Foreign grants	Foreign borrowing	Other foreign	Total foreign	Total revenues	Total expenditure	% of foreign income in expenditure
1967	25.49	40.29	4.70	.22	44.92	70.41	68.15	65.91
1968	26.27	40.11	5.43	.10	45.64	71.92	80.52	56.68
1969	32.52	38.37	4.72	.65	43.74	76.27	88.41	49.47
1970	30.26	35.42	2.07	.41	37.90	68.10	80.70	46.96
1971	35.75	35.39	3.55	3.50	42.44	78.19	83.14	51.04
1972	42.86	44.47	10.20	1.18	55.85	98.73	101.535	55.00
1973	46.18	43.60	11.44	2.00	57.04	103.23	119.51	47.73
1974	65.74	57.65	15.21	1.33	74.19	139.93	146.62	50.60
1975	82.63	100.61	16.15		116.76	199.39	204.86	56.99
1976	107.53	66.24	19.88		86.12	193.71	262.48	32.81
1977	142.25	122.20	58.51		180.71	322.46	337.84	53.49
1978	158.49	81.69	90.69		172.38	330.88	361.51	47.68
1979	187.89	210.30	37.62		247.92	435.82	515.66	48.07
1980	226.15	202.83	71.56	6.46	280.85	507.01	563.14	55.39
1981	309.19	206.31	75.73	7.22	289.26	598.47	647.10	44.70
1982	360.22	184.50	61.50	.40	246.40	606.61	656.27	40.62
1983	396.00	130.00	101.54	2.00	233.54	629.54	717.65	32.54
1984	437.7	124.00	128.54		252.54	705.26	746.15	33.84

Source: Calculated from the Central Bank of Jordan, *Annual Report*, different issues.

loans to finance its development plans. Total development loans contributed about 44 per cent of all foreign receipts in 1983. Major suppliers of loans to Jordan are the USA, Germany, the United Kingdom and Japan. In the mid-70s Arab oil-rich countries started to provide Jordan with loans through the development funds established in Saudi Arabia, Kuwait, UAE and other countries.

Table 9.2 shows the magnitude and relative importance of foreign revenues and the share of foreign revenues in government expenditure.

Internal revenues

Internal revenues have gained significance in recent years since several countries halted their financial aid to Jordan. Increasing internal revenues is the only choice left to the government to offset the decline in foreign aid.

In the following sections, different types of internal revenues will be discussed.

Tax revenues. Tax revenues constitute, on average, more than 75 per cent of total local revenues. Tax revenues include both indirect and direct taxes. Indirect taxes are the most important source of local revenue constituting more than 80 per cent of total tax revenues and one-third of local revenues. Total indirect tax revenues have been increasing at a steady pace.

Non-tax revenues. Non-tax revenues rank second after indirect taxes in terms of importance in revenue generation. Non-tax revenues are mostly generated from government services or investments and have increased at a yearly rate of 27 per cent in the last five years, surpassing the growth rate of both direct and indirect taxes.

The major item included under non-tax revenue is the interest and profits generated by the government, most of which come from the Central Bank of Jordan whose net profit for 1984 was 45 million dinars, or 91.8 per cent of the total interest and profits item for that year (Central Bank of Jordan, 1984: 47).

Revenues from post. Telegraph and telephones have also increased at a steady rate. But the growth rate has accelerated in the last few years after the installation of a new telephone network which now covers the entire country.

Total non-tax revenues are greater than revenues from direct taxation. This is partly due to low taxable income and widespread tax evasion. Non-tax revenues are not a function of income in most cases and, more important, cannot be evaded. In addition to that, non-tax revenues are usually paid for a visible service, which people tend to be willing pay.

Government revenues in Egypt

The Egyptian economy operated under a liberal system until 1952, then was transformed to a socialist system. In 1974 liberalisation measures were introduced. Under all economic systems, the government maintained a dominant role. Government now accounts for 54 per cent of GDP, 40 per cent of total employment and 70 per cent of total investment (Ahmed, 1984). The increasing role of government in the economy has caused public expenditure to increase at a faster rate than government revenues. The wide gap between government expenditures and revenues is a major problem facing Egypt and will likely remain as a challenge for years to come. Total tax revenues finance about 38 per cent of public expenditure, while non-tax sources cover about 20 per cent of total expenditure, thus leaving a budget deficit of more than 4 billion pounds in 1982. Dependence on foreign and local borrowing seems inevitable to bridge the gap between expenditure and revenues. In the next sections we will discuss major sources of revenue for the government.

External sources of revenue

As is the case in Jordan, Egypt also benefited from the economic boom in oil-rich countries, mainly through the remittances from Egyptian workers abroad. However, unlike Jordan which received direct subsidies, Egypt was deprived of Arab aid because of the Camp David Agreement. Thus Egypt received only a few grants — mainly from the USA — but one cannot ignore the positive role of the remittances from about 2 million Egyptian workers in stimulating the economy and hence indirectly increasing government revenues.

Foreign grants are insignificant. For 1975 and 1976 foreign grants accounted for 16 and 11 per cent, respectively, of total government revenues. But for the following years, these accounted for less than 1 per cent of total revenues. Most of the

foreign grants received by Egypt are of a military nature and come from one major source, the United States.

The lack of foreign grants was compensated by heavy borrowing from local and international sources. The amount of debt (most of it concessional) has reached a very high level lately.

Internal sources of revenue

Major internal sources of revenue are classified according to the source: tax or non-tax revenues, as detailed in the following sections.

Tax revenue. Tax revenue constitutes the dominat source of revenue in Egypt accounting on average for 90 per cent of total government revenue and 60 per cent of total public sector revenue (Ahmed, 1984: 16). Tax revenue grew at a fast rate which averaged 28 per cent in nominal terms for the period from 1974 to 1983. The rate of growth varied as between different types of taxes as described below.

Indirect taxes. Indirect taxes are the major source of domestic revenue, accounting on the average for 63 per cent of total tax revenue. For the period under study, indirect taxes increased at an average rate of 22 per cent (see Table 9.3).

Custom duties are the major source of indirect tax revenue. They increased at an average rate of 18 per cent per year in the period from 1975 to 1983, reflecting a slower growth rate in total indirect taxes. Consumption taxes are the second most important source of indirect tax revenue and have also increased at an average of 24 per cent over the same period.

Table 9.3: Indirect tax revenues (millions of LE)

Year	Consumption	Custom duties	Stamps	Others	Total	% Change
1975	231.2	502.2	44.7	51.7	829.8	
1976	283.6	537.8	61.2	55.5	938.1	13.1
1977	339.7	979.4	89.8	71.4	1480.3	57.7
1978	360.3	919.8	126.2	96.5	1502.8	1.5
1979	566.8	905.0	154.8	150.3	1776.6	18.2
1980	699.7	1329.4	167.9	174.6	2371.6	33.4
1981	812.6	1573.2	239.3	230.5	2855.6	20.4
1982	1217.0	1651.0	254.4	222.5	3344.9	17.1
1983	1713.3	1719.0	222.6	247.8	3902.7	16.7

Source: Ministry of Finance of Egypt.

The strong reliance of the government on consumption and custom duties is obvious. The main problem with these types of taxes is their passive nature and the difficulty associated with increasing the rate of taxation.

Direct Taxes. Direct taxes are the second most important source of revenue in Egypt, their average contribution to total revenue exceeding 36 per cent for the period from 1975 to 1983. Direct taxes are gaining importance over indirect taxes, and grew at an average rate of 45 per cent annually for the period under study (Table 9.4).

Table 9.4: Direct tax revenues, Egypt (millions of LE)

Year	Personal income	Business profit	Other taxes	Total direct	% Change
1975	42.3	161.8	94.4	300.4	–
1976	47.7	277.6	90.3	415.6	38.3
1977	54.9	387.2	109.2	551.3	32.6
1978	51.9	538.4	135.5	725.8	31.6
1979	55.1	655.7	159.3	870.1	19.8
1980	73.2	1506.3	244.4	1824.0	209.6
1981	85.4	1577.7	281.6	1944.7	6.6
1982	110.0	1554.3	419.0	1983.3	7.1
1983	127.3	1893.6	502.2	2523.1	21.1

Personal income tax achieved a moderate growth rate of 12 per cent annually. The introduction of the new tax law offering generous tax exemptions in addition to the relatively low income contributed to the moderate increase of revenue derived from it.

The tax on business profits contributed significantly to the growth of total direct tax revenues, increasing at an annual average rate of 45 per cent. However, much of the growth in the yield of this tax is attributed to the oil sector and to the Suez Canal, justifying the phenomenal jumps in certain years. Thus in fact the classification adopted by the Egyptian government, although formally correct, introduces an element of confusion in as much as part of the rent accruing to the government from foreign sources is added to direct taxation on the domestic economy.

Other taxes listed in table 9.4 include taxes on property, estate duties, taxes on land and real estate and local government tax

revenues. The most important tax under this group is the property tax to which most of growth is attributed.

Non-tax revenues

Non-tax revenues rank third in terms of importance after indirect and direct taxes. Non-tax revenues contribute on the average about 8 per cent of total government revenues and increased at an average rate of 30 per cent annually for the period from 1975 to 1983.

Non-tax revenues consist of fees, local government non-tax revenues and other revenues.

Government revenues in Kuwait

Government revenues in Kuwait differ greatly in sources and magnitude when compared to Jordan and Egypt. While Jordan and Egypt suffer from a lack of financial resources, large budget deficit and mounting external debt, Kuwait, thanks to its oil exports, is far from encountering such problems. For the period from 1971 to 1983, Kuwait never had a deficit in the budget. Therefore, government budgeting is primarily concerned with distribution rather than redistribution of wealth (Khouja and Sadler, 1979: 112). Tools necessary for redistribution of wealth are either non-existent or too weak to have any significant influence.

Table 9.5 lists all sources of revenues for Kuwait. Personal and corporate taxes are non-existent; figures listed under corporate tax in column (2) are actually taxes imposed on foreign oil companies operating in Kuwait. Other industrial or commercial activities are tax exempt. Corporate taxes were significant in the first few years and then dropped to a very low level after the nationalisation of foreign oil companies.

Property and fees listed in column (3) include property transfer fees, fines and administrative fees, revenue from this item has grown at a very low rate. Revenue from property taxes and fees has never exceeded 0.5 per cent of total revenue. Excise taxes are imposed on domestic goods and services. This item was relatively significant before the first oil price increase, but was lowered after the oil wealth started to flow; its average contribution is also less than 1 per cent of total revenue.

Investment income is derived from the huge financial assets

Table 9.5: Government revenues, Kuwait (million KD)

	Income from taxes					Non-tax income			
(1) Year	(2) Corporate	(3) Property and fees	(4) Excise	(5) Custom duties	(6) Oil revenues	(7) Investment income	(8) Other non-tax	(9) Total revenue	(10) % Change
1971/72	418	5	120	9	500	42	5	1099	10
1972/73	452	5	132	11	537	50	4	1191	8.0
1973/74	928	6	298	17	584	89	14	1936	62.5
1974/75	398	6	16	21	2534	152	12	3130	61.6
1975/76	430	7	45	32	2793	328	10	3645	16.4
1976/77	109	8	33	38	2598	329	10	3135	(13.9)
1977/78	258	14	18	41	2575	384	23	3313	5.6
1978/79	80	18	19	45	3036	522	16	3736	88.9
1980/81	154	32	30	68	4434	1744	38	6500	(7.9)
1981/82	91	33	25	86	2764	1363	7	4361	11,4
1982/83	92	42	16	79	2967	1657	8	4861	11.4

Sources: Calculated from Central Bank of Kuwait, *Economic Report 1982* and *IMF Government Finance Statistics Yearbook 1984.*

held by the Kuwaiti government as a placement for surplus oil revenue, as well as in the so-called Reserve Fund for Future Generations.

Other non-tax revenues listed in column (8) consist of work permit fees, forfeits and other non-tax revenues.

CONCLUSION

From the preceding analysis it is clear that the type and relative importance of domestic sources of revenue greatly depend on the availability to the government of other financial resources. A direct implication is that taxes are imposed mainly for a revenue purpose; the redistribution or reallocation effect is secondary, and does not on its own warrant the creation of a taxation system. Countries which lack sources of revenue from the rest of the world have no choice but to depend on domestic sources and resort to taxes, whereas countries with large non-tax financial resources, like Kuwait, do not impose taxes simply because revenue is not needed.

It has also been noted that the level of taxation is correlated to the surplus or the deficit in the government budget. This point again emphasises the primary purpose of taxation as a source of revenue rather than a redistributive tool.

Table 9.6 shows the budget surplus or deficit for Jordan, Egypt and Kuwait. It is evident that Jordan and Egypt have had constant budget deficits, while Kuwait enjoyed a significant surplus every year. The surplus in Kuwait's budget made it unnecessary to raise additional revenue through taxation or any other means, while Jordan and Egypt developed their own tax

Table 9.6: Budget surplus of deficit (millions of local currency)

Year	Jordan	Egypt	Kuwait
1975	− 18.8	− 1388.0	1887.0
1976	− 81.5	− 1264.7	1513.8
1977	− 61.1	− 1270.0	1134.2
1978	− 110.8	− 2139.0	1753.9
1979	− 104.0	− 2907.0	4544.6
1980	− 110.5	− 2567.0	3025.3
1981	− 100.8	− 4441.0	566.2
1982	− 108.6	− 4164.0	92.5

Source: Arab Monetary Fund, *Statistical and Economic Data, 1975–1982.*

Table 9.7: Tax burden (tax revenues/GDP) (GDP in millions of local currency)

	Jordan			Egypt			Kuwait		
Year	GDP	Tax revenue	Tax burden %	GDP	Tax revenue	Tax burden %	GDP	Tax revenue	Tax burden %
1974	312.1	58.1	18.6	4197	1130.2	26.9	3487	432	12.3
1976	421.6	89.0	21.1	50.6	1353.7	26.7	3839	514	13.3
1977	514.2	117.7	22.8	6165	2931.6	32.1	4049	187	4.6
1978	632.2	123.2	19.4	7534	2227.8	29.5	4264	324	7.5
1979	753.0	151.0	20.0	9021	2646.7	29.3	6743	149	2.2
1980	979.5	176.6	17.8	12101	4195.6	34.6	7451	209	2.8
1981	1182.5	232.9	17.3	16552	4799.6	28.9	6764	261	3.8
1982	1343.2	263.1	19.5	19402	5428.2	27.9	5727	214	3.7
1983	1487.3	292.8	19.6	21324	6425.8	30.1	6218	196	3.1

Source: Calculated from *International Financial Statistics*, and Tables 10.4, 10.5, 10.8, 10.9, and 10.12.

structure to provide the government with the much needed revenue. However, revenue accruing to the states from both internal and external sources have failed to match the rapidly increasing expenditure.

Table 9.7 shows the ratio of total tax revenues to gross domestic product (GDP), commonly referred to as tax burden ratio. It gives a clear indication of the tax efforts in Jordan. Egypt and Kuwait. Because of the heavy reliance on foreign grants, Jordan's tax burden ratio is less than Egypt's. The ratio fluctuated narrowly and kept apace of changes in GDP. Egypt seems to have a relatively high tax burden which averaged 29.5 per cent for the period from 1975 to 1983. However, as we indicated earlier, 'tax revenue' in Egypt also includes some of the rent accruing from the rest of the world. If this were subtracted, the tax burden would be reduced by almost 30 per cent and appear much closer to that of Jordan. Kuwait is considered an extreme case. But after the sharp decrease in oil prices the Kuwaiti government may be obliged to think about introducing taxes, especially on corporate income. Obviously, Kuwait could easily raise additional revenue if it only tried.

10

Depoliticisation of a Rentier State: The Case of Pahlavi Iran

Afsaneh Najmabadi

A surprising feature of the 1979 Iranian revolution was the speed with which the state collapsed. A mere 13 months elapsed between the first street demonstration in Qum on 9 January 1978, and the final change of the regime on 9–10 February 1979.

In January 1978, the Iranian state looked solid, stable enough at least for the Shah to let up some non-political repression. Roughly one-third of the total budget was regularly allocated to military expenditure. By 1977 this amounted to nearly 10 billion dollars. The army was well-equipped and intact. It had some 454,000 men, with 3000 modern tanks, the largest hovercraft fleet in the world, 290 Phantom bombers, 80 F-14s and 160 F-16s (Halliday, 1979; Oney, 1976). The army had not been weakened by external wars or internal campaigns. The state did not suffer from a financial crisis. Although the increase in oil revenues had slowed down by the late 1970s, Iran's foreign reserves stood at over 20 billion dollars. There were problems arising from the accelerated development spending after the 1974 oil price rises: widespread corruption, economic and infrastructural bottlenecks of various sorts, and by 1977, rampant inflation and unemployment in some sectors. But none of these had produced the sort of social crisis associated with similar situations in other well-known Third World cases. In other words, with huge oil revenues at hand, and a strong army, there was no compelling reason for the Pahlavi state to collapse so completely and so rapidly.

A second feature of the collapse of the Pahlavi state was that the process produced no splits within the 'ruling class'.[1] Compared to all other revolutionary situations, this lack of political differentiation amongst the social elite was new. Certainly, an important section of the commercial bourgeoisie, the traditional *bazaaris*, backed the revolution. But this class had been bypassed politically under the Shah and had become less significant in relative economic terms as a result of the economic and social developments of the preceding two decades; it no longer constituted a part of the political elite of the country. In sociological terms one could say that Iranian society split only horizontally, rather than vertically as well as horizontally. Moreover, there was no political attempt on the part of this economic and social elite to 'save' the situation. The only political figure to put himself forward as a champion for reforming the system rather than working to overthrow it was Bakhtiar, an old opposition politician of the National Front with no ties to the Iranian propertied classes. Such a situation is in sharp contrast to conditions in other Third World countries, notably Latin America. Not only does it not conform to the general pattern of what happens within ruling classes when they face this kind of revolutionary upheaval, it also stands in sharp contrast to previous periods of modern Iranian history.

In late nineteenth-century Iran, a whole layer of political thinkers emerged from both the reforming elements within the Qajar bureaucracy, and those critical of it who were outside government. These men were deeply concerned with the social and political problems of their time. They produced a rich political culture that shaped public opinion. With the political demoralisation that marked post-Constitutional Iran, and the establishment of the Pahlavi state in 1926, there was a break in the continuity of the reform-oriented politics of the elite; there was a rupture with a political culture in which the idea of reform from within remained a viable option.

The 1940s witnessed a new rise of nationalist, reform-oriented politics, symbolised by Mosaddiq, with a strong social base in the bazaar and the traditional middle classes. If the elite had withdrawn from reform politics, the same was still not true of the middle classes.

By contrast, post-1953 Iran was notable for the absence of such politics. With the virtual disintegration of the National Front, the traditional middle classes also seemed to have given up all independent political claims. Moreover, the newly emerging rich, the new industrialists and capitalists of the 1960s, did not exhibit the slightest desire to shape the state. They displayed no political and social concerns, no desire to have any say

in the fate of the society they were sitting on top of. They produced no politicians or political thinkers and seemed to be concerned only with getting richer. This was best demonstrated by the remarkable ease with which they packed their bags and left the country when the chips were down. Wealth was transferred, along with the physical presence of the majority of those who had most benefited under the Shah. No other class in history has behaved quite like that at a time of revolution. What accounts for this total political abdication of the upper classes in Iranian society?

REPRESSION VS REVENUE

At first sight, it may be tempting to attribute this depoliticisation to political repression under the Shah. However, repression by itself cannot result in depoliticisation, as the example of many other Third World countries was well as Iran's previous experience illustrates. Repression affects the type of responses that emerge. Depoliticisation is a different phenomenon altogether. It suggests that civil society has given up any claim on the state, that it does not see it within its power to affect politics, and that the state has somehow succeeded in 'ridding' itself of its civil connections. As Beblawi points out, for the case of Kuwaiti society (see Chapter 2), politics fades away, not merely as a subject for serious discussion, but even as a favourite topic of gossip.

This autonomy of the state from civil society is linked to the huge oil revenues accruing directly to the state. These revenues originating outside the society structure affect the socio-economic development of the country as well as the political behaviour of the state in very particular ways.

Terry Karl, in her very interesting forthcoming book, *Oil Booms and Petro-States: Democracy Over a Barrel in Venezuela*, has compared this 'oil effect' to that of the flow of American silver and gold into the Spanish economy in the sixteenth century. As she points out, that inflow of capital occurred at a time when the Spanish state lacked a fundamental distinction between its economic and political role and was the central economic actor, like its counterparts today in the oil-exporting developing countries. The result of that externally-fuelled boom was a Spanish state that had a strong outward appearance, but was extremely fragile internally. It had few checks on its authority, it earned the political passivity of the aristocracy in return for exempting them from any fiscal responsibility. Through sale of titles it dramatically expanded the size of a parasitic noble class, with bankers and industrialists accumulating capital in order to become part of a leisure class. Unlike the rest of Europe in this period, there was little incentive to increase productivity either in agriculture or in the manufacturing sector. As a result, Spain could neither feed itself nor produce many of its necessary items. It simply grew more dependent on importing them from the expanding economies of Europe, paying with its silver and gold until the latter ceased to flow.

Oil revenues have had similar effects on the political economy of the oil-exporting countries. In the case of Iran under the Shah, for instance, economic observers have pointed repeatedly to a policy of 'neglect' of the agricultural sector. This was intimately linked to the fact that the state was not dependent on surplus extracted from agriculture for its capital accumulation functions. Even more, a catastrophic agricultural policy could be weathered by spending oil revenue on importing agricultural produce.

This autonomy of the state from a taxation base, on the other hand, resulted in a progressive narrowing of the politically relevant body of decision-makers, which ultimately was reduced to the person of the Shah.

We can start examining this process by looking at the Iranian economy and politics at the time when oil revenues first began to have a substantial impact on Iranian society.

THE RISE OF OIL REVENUES AND THE DECLINE OF POLITICS

The significant date for this purpose is the mid-1950s, when a secular rise in oil revenues began, making possible the autonomy of the state from all indigenous social classes. This is also a politically significant period, because Mosaddiq's challenge to the authority of the Shah was the last of its sort and his defeat settled the shape of political authority in Iran for the whole subsequent period. Both Mosaddiq's successes and failures went into the making of the state in the post-1953 period. His success was the nationalisation of the oil industry. This made growing state oil revenues possible. He failed in his challenge to the

structure of power, when he tried to dislodge the Shah from his position as the commander-in-chief of the armed forces. Mosaddiq realised that the Pahlavi state was an army-based state, and therefore any claim on the legitimacy of his own power and any long-term vision of political reform in Iran depended on who controlled the army. The 1953 army *coup* brought this challenge to an end and, through it, the Shah was established as the supreme head of the state — a position that put him in charge of dispensing rising oil revenues and thus shaping the social, economic and political life of the country.

The first big jump in revenues came with the nationalisation of the oil industry in 1950. Whereas in 1948 oil revenues comprised only 11 per cent of total government revenues, in 1960 the percentage reached over 41 per cent (Mahdavi, 1970: 430). Despite the unfavourable agreement reached with the oil consortium in 1954, increased production and more favourable contracts negotiated in the late 1960s resulted in a steady growth of state revenues from oil, as indicated in Table 10.1.

Table 10.1: Major sources of government revenue as percentages of total revenue

Revenues	1954	1955	1960	1965	1970	1971	1973	1974	1975	1976
Oil and gas	11	37	42	54	49	60	67	86	80	76
Direct taxes	5	5	8	10	15	12	12	5	10	11
Indirect taxes	35	28	25	23	26	20	17	6	7	9

Sources: For 1954–60, Mahdavi, p. 455, Table 18. For 1965–76, Central Bank of Iran, *Annual Reports*.

It is important to note that even among the figures comprising direct taxation, the highest contribution came from state corporations, as in shown in Table 10.2.

The next big jump in oil revenues came in 1974 with the fourfold increase in oil prices, increasing the share of oil revenues in the state budget yet again (see Table 10.1).

This increasing independence from reliance on a tax base made it possible for various economic and social policies to be followed without much regard for social consent. A curious inversion of the classical formula 'no taxation without representation' occurred; the Iranian state felt no compulsion to be representative since it was effectively not taxing the population. The population itself gave up political claims on the state, since

Table 10.2: Major sources of direct taxation as the percentage of total direct taxes

Source of tax	1968	1969	1970	1971	1972	1973	1974	1975	1976
Taxes on salaries	21.2	22.6	22.0	22.0	21.0	19.1	13.3	10.1	14.0
Land and real estate taxes	8.1	7.0	8.6	7.8	7.2	7.4	7.7	2.8	3.2
Taxes on state corporations	34.5	31.4	29.6	27.0	27.2	30.3	37.5	61.4	52.9
Taxes on private corporations	16.0	18.2	19.1	20.2	21.5	20.7	21.0	13.2	15.7

Source: Central Bank of Iran, *Annual Reports*.

it was not being taxed; the Pahlavi state was not 'its' state in more ways than one. Rather than the state representing and insuring the interests of certain privileged strata, social classes were adapting themselves to state policies that were beyond their power to influence. When they did come into conflict with state, opposition took the form of rejecting the state in its totality, rather than first pressing it for meaningful reforms.

One might have expected the new industrial entrepreneurs, the new men of wealth, to fill the place of the traditional elites by providing the state with social support and political participation. However, the new upper classes were economic beneficiaries of state policies in the 1960s and the 1970s at the same time as they were becoming politically redundant. They had no organic ties to the edifice that had been their benefactor. Their attitude to the state was expected to be one of gratitude and subservience, and this they obligingly gave. A climate of cynicism prevailed amongst the upper classes of Iran by the 1970s. Zonis, writing in 1971, comments on this phenomenon as follows:

> Where we expected that the older Iranians would have become cynical from their participation in the political system, we find the opposite. The younger elites manifest higher levels of cynicism than their older counterparts. Where we looked for higher levels of manifest insecurity among those of the elite who had fewer institutional ties and thus fewer bases of support, we found the opposite. The more active the elite — the more occupations they have and the more organisations they have joined — the higher their levels of insecurity. Where we had expected the more politically powerful to be more involved and thus more committed to the political system and its objectives, we were again surprised. The more powerful manifested the highest levels of cynicism. The younger elite, then are more cynical; the active more insecure; and the powerful, the least committed (Zonis, 1971: 14–5).

The experience of the older generation of politicians left them with a feeling that they still had a say in politics; the new generation only saw itself in a perfunctory technocratic role. Zonis astutely asks at the end of his book:

> With such intense feelings of hostility to politics by such a large segment of the most politically powerful actors, we may well ask why the political system has been immune from collapse. With these general orientations of insecurity, cynicism, and mistrust and the political attitudes of xenophobia, social disdain, family disdain, and government disdain, why has Iran not emulated so many of its Middle Eastern neighbours? Why has Iran been immune from the *coups d'état* and revolutions that seem to characterise so many developing nations? Why has the *shahanshah* been able to boast so correctly that Iran is a 'sea of tranqillity and stability' in the midst of the world's political chaos?
>
> Fundamentally, the answer lies in the success of the monarch in creating a consensus among the political elite. Contrary to his efforts, however, the consensus revolves neither about his person nor about his policies. The consensus is rooted in a pervasive sense of personal inefficacy on the part of the vast majority of the elite. Beset by personal insecurities, mistrustful of themselves and their fellows, and cynical about the motives of all persons and the outcome of all programs, the elite responds by coping with the system, not by attempting to alter it in fundamental ways. And the process of coping consists, basically, of learning to operate within its norms while maximising the benefits that can be derived from it (Zonis, 1971: 328–9).

Such a system can last only so long as the state continues to be all powerful, and all resourceful. But there is no mechanism for repairing even the slightest fissures. The political vacuum that the state has created leaves it with no capacity for self-reform. Late attempts at reform only exacerbate the problem, as the traditional methods of functioning are given up. Curiously not only were the upper classes cynical and apolitical, but even the Shah at the end felt powerless and paralysed, once it became clear that the old method of rule had ceased working. In the final months of his rule, he was looking to the American administration to save the situation. Later, he became convinced that his fall had been engineered by the CIA (Sullivan, 1981).

EROSION OF THE SOCIAL BASE OF THE IRANIAN STATE

In discussing the rentier character of the Iranian state and its political repercussions several points need emphasising. First, unlike many Middle Eastern oil-exporting states, Iran started with a substantial agricultural and commercial economy, and the beginnings of an indigenous industrialisation before the oil economy took root and began to structure development. For this reason, the process of transformation of the Iranian state into a rentier state may have involved a more painful and prolonged experience of alienation for the society from its immediate past, compared to similar processes in some of the Gulf states, for example. In the latter cases, the new rentier states emerged on the basis of certain traditional structures, that is, tribal/kinship networks. These networks provided the new economic and political elite, the backbone of the new state bureaucracies, and to a large extent they also provided a ready-made distribution network for the new wealth. Iran was quite different: the establishment of an oil state meant a progressive erosion of the traditional linkages between the state and civil society. This went back to the earlier Pahlavi monarch.

Reza Shah took power in a military *coup* in February 1921 and by 1926 he had a Constituent Assembly which deposed the last Qajar Shah and declared him the Shah of a new dynasty. Reza Shah rose to power in an atmosphere of demoralisation. Despite the military victory of the constitutionalists in July 1909, the following decade witnessed such a deep disillusionment with constitutionalism, that by the 1920s we see Iranian reformers talking of the necessity for a 'revolutionary dictator'. Some accounts have attributed the impotence of the early constitutional governments (1909–20) to foreign intervention and

indeed there were foreign pressures and interventions by both Russia and Britain. But more than foreign pressure went into the failure of the constitutional experiment.

The constitutional movement had created a strong legislative body without challenging the form of executive power. Nominally the monarch, and through him the prime minister, headed the government. To combat the royalist stronghold in government, the constitutionalists relegated many former royal prerogatives to the Majlis, without concrete means of producing a functioning executive. Indeed, to render the royalists powerless they produced a powerless executive. Thus the subsequent years witnessed numerous legislative experiments and reform blueprints, with no means for implementing these projects. A series of cabinet crises led to demoralisation. The provinces, impatient with central government, began to form their own local administrations. Eventually localist movements surfaced in several important provinces. The weakness of central government was seen to be responsible for all ills. By the early 1920s, important constitutionalists were advocating a strong state orientation. The terms of political discourse had drastically changed. While the early generation of reformers saw progress as possible only through a democratic constitutional regime, the reformers of the 1920s saw democracy as an impediment to progress. The apparent dichotomy between democracy and progress haunted the country for the next half a century.

With Reza Shah rose a new path to modernisation: perhaps the army could succeed where administrative, educational and constitutional civil reformers had failed; perhaps military discipline, and organising and centralising ability could force through the changes that bureaucrats and politicians had failed to achieve. In effect, in the Reza Shah years a new nation-state was forged through the building up of a modern army, ruling over a multi-national and multi-ethnic society.

The supportive social base of the Qajar state had consisted of merchants, landlords (in parts overlapping with merchants), and clerics.

The creation of the Pahlavi state resulted in important shifts in the class structure of the society, particularly in the relation of these three important social groups to the state.

Merchants provided the state with financial backing (the wealthiest were court bankers) and in return expected it to enforce a measure of internal security and protection of their interests against foreign encroachment.

Landlords owed their rise to the Qajar period, when successive fiscal crises led the monarchs to replace the *toyuldari* system of tenure, which entailed selling a right to the revenue of the land for a fixed period, with permanent land sales. Land was now sold as private property to the highest bidder. Indeed, one of the achievements of the first Majlis was to outlaw *toyuldari* for good.

The clergy had a very special place in Qajari society. They ran the only schools which were religious (*maktabs*). They administered the legal affairs of the Muslim community, in matters of marriage, divorce, custody, endowments and criminal punishment. The more powerful and prestigious among them had their private 'law-enforcers', and of course, through the *khums* and *zakat* religious taxes, paid to them directly, they had their own independent fiscal base.

Reza Shah's policies brought about significant changes in the relation between each of these social groups and the new state.

The merchants benefited enormously from the centralisation policies of the state, introduction of military security, the building of new communication networks, roads, railroads, expansion of the telegraph lines, etc. They also benefited from the protective policies of the new state towards foreign concerns and international trade. On the other hand, the merchants lost the independent political voice they had gained through the Constitutional Revolution. Their own business activities also came under partial state supervision and intervention, through the introduction of certain state monopolies, pricing policies and taxation laws. Moreover, with the gradual expansion of alternative trading outlets (for example, modern shops on new urban boulevards), the bazaar — the traditional bastion of commerce — lost its monopoly over retail trade.

As for the landlords, they became a fully-developed and well-established class during this period. A series of property laws consolidated and formally registered the appropriations and holdings of agricultural land by big landlords. Ownership of whole villages, rather than one's status in the world of commerce, became a source of local power and national prestige in this period. Reza Shah himself confiscated some of the best agricultural land around the southern and eastern coasts of the Caspian Sea and in the Khuzistan province, becoming, by the end of his reign, the single largest landlord in the country.

Although landlords, as much as anyone else, were politically subdued under Reza Shah, they none the less enjoyed a local power base which they later (1941–61) manipulated to influence national politics, primarily through influencing the outcome of elections to the Majlis. Between 1926 and 1963, landed interests made up the largest single block of parliamentary seats in the Majlis.

The group most drastically affected by Reza Shah's policies were the clergy. Introduction of modern schools, new taxation and civil codes, and the setting up of a judicial system independent from the traditional *shariah* courts, undercut all the important traditional social functions of the clergy (Fischer, 1980). *Maktabs* were closed, *mahakim-i shar* (religious courts) were eliminated, and in order to pay government taxes, fewer people could afford the traditional *zakat* and *khums* for the clergy. Even social functions, such as performing marriage and divorce ceremonies, had to go through the offices of public registrars to become legally valid. Moreover, many of Reza Shah's measures were seen as direct attacks against Islamic teachings, such as the forced unveiling of women, decreed in 1936, and the creation of a standing army based on conscription. Reza Shah was seen as emulating Ataturk of Turkey, who was, in the eyes of the clergy, the embodiment of anti-Islamic secularisation.

This change in the relative status of the three social groups is reflected in the occupation of Majlis representatives in the various legislative sessions. In the first Majlis, elected in 1906 in the heat of constitutional politics, landlords had 21 per cent of the seats, merchants 41 per cent, and the clergy 20 per cent. In the twelfth Majlis (1941), the last under Reza Shah, landlords held 58 per cent of the seats, merchants 18 per cent, and the clergy only 6 per cent. It is also interesting to note that in the same period the percentage of Majlis representatives from professional technical occupations increased from 7 per cent to 21 per cent, and that of government employees from 23 per cent to 32 per cent (Bill, 1972).

The final erosion of the traditional social base of the state occurred from the early 1960s when the Shah's developmental policies, in particular the land reform, undermined the landlords as a socially important and politically significant class and bypassed the bazaar and the traditional commercial interests in its attempts to foster a new economic elite with no political voice.

Individually, the landlords became industrialists, commercial agriculturalists or investors in urban real estate and commerce. As a social group, they ceased to exist and have a political voice in the affairs of the country (Del Vecchio Good, 1981).

Previously, they could (and did) use their local power base to affect local as well as national politics: to get representatives elected to the Majlis, to provide the cadres for top governmental positions. In the aftermath of land reform, particularly under the influence of policies designed to bring into government a new layer of technocrats and professionals, they lost these privileges. The percentage of landlords in the twenty-first Majlis (1963) was only 35 per cent, compared to 58 per cent in the previous session; that of government employees rose from 48 per cent to 69 per cent, with private industrialists getting 16 per cent compared to 2 per cent in the previous session (Bill, 1972). The shift was also reflected in the choice of cabinet. With the resignation of the Alam government in early 1964 and appointment of Mansour as the new prime minister, a new layer of state functionaries came to the fore. These were men drawn from the families of the traditional elite, but they brought with them a different technocratic, managerial and apolitical view of government (Bill, 1972: 46–7; Zonis, 1971: 89–90, 223–35).

SHIFTS IN POLITICAL PERCEPTIONS

Another observation regarding the changes in the Iranian state from the 1920s to the 1970s is that this process represented a rupture with the previous relation between state and civil society. For Reza Shah the new state consisted, above all, of a modern army. It is symbolic of the importance of the army in Reza Shah's mind that he appeared on all public occasions in military uniform. Patriotism, for him, was loyalty to the state, not to the country conceived as a definite territorial entity. Citizens were expected to contribute to the building of a new society by becoming part of the growing state and in particular through obedience to the army. An attitude was cultivated that looked down upon those not inside the state, as if working for the state was now the ultimate expression or test of good citizenship.

These attitudes changed drastically by the 1970s. Citizens were no longer expected to contribute to the building of a state, but to

be grateful beneficiaries of state handouts. Loyalty to the person of the Shah, the Great Benefactor, replaced loyalty to the state as the test of citizenship. The population itself became complacent in abiding by the rules of gratitude. Welfare benefits were perceived not as rights, but as gracious handouts from the Shah. This is different from the development of a welfare consciousness that accompanied the rise of welfare states in postwar Western Europe. The contrast is probably linked to two interrelated phenomena: first, the European welfare state was seen to be subsidised from taxes paid by citizens, not from external revenues accruing to the state. Second, it was the struggles of working-class organisations that led in large part to the establishment of welfare measures after World War II, and not the initiative of the head of the state who charitably disposed of state revenues and was not under any pressure to spend it on welfare at all.

For these kinds of reasons the legitimacy of the late Pahlavi state became linked to whether it was dispensing its favours in a just and fair manner. In a society with a strong work ethic, the state is often criticised for being unproductive, parasitic and wasteful of social resources. In a rentier state, the distinction between a productive civil society and a parasitic state becomes irrelevant, since the source of national wealth is largely external rent, not domestic labour. Thus in the 1970s in Iran, politics became polarised around questions of wealth distribution, not control over production; around moral decadence and conspicuous consumption, not political participation and rational decision-making.

The fact that the Iranian government opted for a policy of industrialisation, rather than of investment abroad — as in Kuwait, for instance — suggests that we cannot characterise the state as purely 'distributive' (as do other factors, such as the size of the population and the weight of the traditional agricultural and commerial sectors). To an extent, the Pahlavi state employed resources productively. None the less, as Delacroix, (1980: 3–21) has argued, 'Logically prior to the question of who extracts what from whom in a given society is the question of how that society makes its living'. With huge and growing oil revenues concentrated in the hands of the state, the population became more concerned with how the revenue was distributed, rather than with who owns and controls domestic production. It was not always clear, for instance, whether industrialists became wealthy from state handouts (interest-free loans and subsidies), or from the profits generated by workers in their factories. In the eyes of the workers themselves, the source of social inequality seemed, with good reason, to be an outcome of state favouritism towards the rich, rather than owners exploiting the profits of their labour. Oil revenues derived primarily from a natural resource, not capital investments and productive employment of labour. Therefore, they seemed to be a God-given blessing that should belong to all equally. That the benefits distributed themselves in such a skewed and inegalitarian pattern under the Shah was attributed to conscious state policies, acting against God's intentions and depriving the people of their 'natural' rights. In such a context, corruption, precisely because it is one of the primary distributive levers, becomes the explosive issue.

The elimination of corruption, and new priorities for the distribution of national wealth (whose main source is not domestic labour), produces a Levellers-type of puritanism in politics. As Delacroix has noted:

> First, challengers (to the old regime) will not be able to claim a monopoly of rationality. They will not be able to present themselves as representatives of the progressive forces of history, bent on freeing production from the shackles of a mode of production that has become mired in its own contradictions. Hence it will be difficult for them credibly to draw their inspiration from scientific socialism. Instead, they will have to find their legitimising ideology in strictly moral considerations. Such considerations tend to find their strongest support in Golden Age myths, usually of religious origin. Revolutionary movements in distributive states will thus have strong reactionary ideological components. In their purest forms, they will be completely reactionary.
>
> Secondly, the organisation base of challengers in a distributive state cannot be class. Therefore, other structures of social solidarity will have to be activated.
>
> Alternative structures are, by default, traditional structures. The more recently incorporated into the world economy a society, the more available are its traditional social structures. Hence, a distributive state ruling a recently incorporated society will experience a maximum of tribal, ethnic, and religious challenges (Delacroix, 1980: 11).

The hybrid character of the Iranian state and economy under the Shah — an economy based on oil revenues utilised in part towards an accelerated development of indigenous capitalism — explains the hybrid character of the anti-Shah movement: an Islamic movement with its social base in the traditional lower middle-classes and the millions of urban declassed poor, matched by more classical forms of class-based activities (such as the trends towards unionisation, formation of workers' committees, use of strikes and take-overs in industries and in part amongst public sector employees). Until this very day, both sides of the dichotomy have an objective base in the social structure of society. And this fact will remain a source of future conflicts and exploitations, unless the Islamic regime adopts a systematic policy of destroying the modern and productive sector of the Iranian economy.

THE ISLAMIC STATE AS A DISTRIBUTIVE STATE

This brings us to another important question: is there an affinity between Islamic politics and the rentier character of the state? Are the policies of the present regime working towards strengthening its rentier character or are they undermining it?

In the immediate aftermath of the change in regime, the government's dependence on oil revenues increased, as the productive sectors of the economy became paralysed for a period — first through prolonged strikes, then because the owners and managers just packed and left. Factory committees took over, but the struggles within these committees overshadowed any management decisions, and it took a while before Islamic associations consolidated their hold over these work committees and made the incorporation of these bodies into government structures possible.

To this very day, the economic direction and policy of the Islamic Republic have not been clear. Economics is simply not a top priority of the new regime. However, it is projecting the long-term goal of 'independence', or self-sufficiency as a target, and aiming at a reduced dependency on oil revenues. The Iran-Iraq war, the allocation of much of the oil revenues to war budget and the damages to the oil installations have made this more urgent. Also the state seems to have become more efficient in tax collection. Consequently over the past several years there

Table 10.3: Major sources of government revenue as percentages of total revenue

Revenue	1983	1984	1986
Oil	56.6	49.1	48.7
Taxes	28.4	24.9	35.3

Sources: *Keyhan*, Airmail edition, 11 December 1985 and 25 December 1985.

has been a steady rise of the share of taxes and a decline in the share of oil revenues in total state revenues (see Table 10.3).

On the other hand, however, even with a reduction in the contribution of oil revenues to state finances, important political and ideological considerations have contributed to the strengthening of the distributive character of the state. In the first place, loyalty to the Islamic state has replaced loyalty to a person, notwithstanding the prestige of Khomeini. The new state has a number of advantages: It enjoys a political legitimacy that the old did not; it embodies a revolution that was truly national in scope; and it proclaims the implementation of the ideals of that revolution. Amongst those ideals is the task of redistribution of social resources away from the *mustakberin* (the arrogant and powerful rich) and towards the *mustazefin* (the downtrodden). Note that these Islamic categories resonate better in a rentier society than class categories: you can be rich but not a *mustakbir*, if you pay proper alms and follow Islamic social and individual norms of behaviour. The Islamic state's legitimacy is now in part based on its being the grand collector and redistributor of all alms (*zakat*, *khums*, etc). The Islamic attitude towards receiving of alms as a legitimate means of social welfare — rather than condemning them as unproductive and parasitic — is reinforced as well. The state has thus acquired a permanent legitimacy for its distributive functions — so long as it is seen to be a just dispenser of social wealth.

This new legitimacy cushions the state, for a period at least, even against tax-originated challenges of representation or class politics. Since taxes are projected as one's mandatory religious duty, their payment no longer entitles one to to a say in the affairs of the state: it is not your taxes that the state is spending, but the *imam*'s share and the Islamic community's proper alms that the state collects and that the state alone — as the embodiment of the Islamic community — has the right to decide upon how to dispense. In this sense the new distributive state is more

vulnerable at the level of its actual practice (Is it a fair distributor? Is it behaving according to Islamic precepts?), but less vulnerable at the level of its political legitimacy. It has acquired for itself a legitimacy that can, in theory, mesh better with a rentier state.

NOTE

1. I am putting the expression 'ruling classes' in quotation marks, because, as the argument will shortly indicate, it is not clear in what sense one can speak of a ruling class in the latter days of the Shah.

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About the Authors

Hamid Ait Amara is Professor at the Institut des Sciences Economique, Université d'Alger. He is the author of 'Le développement urbain et industriel en Algérie et mutations de la societé rurale' (*Revue Algérienne*, (1983); 'Blocage de la productivité du sol et crise agricole' (Alger, 1983); 'De la division coloniale à la division internationale du travail en agriculture' (*Revue Algérienne*, (1983).

Hazem Beblawi is presently Chairman of the Export Development Bank of Egypt. He is the author of *The Arab Gulf economy in the turbulent age* (Croom Helm, London, 1984) and of *L'interdépendance agriculture-industrie et le développement économique en Egypte* (Cujas, Paris, 1968).

Michel Chatelus is Professor of Economics at the Université des Sciences Sociales de Grenoble and head of GRESMO. He is the author of 'Towards a new political economy of state industrialization in the Arab Middle East' (with Yves Schmeil, *International Journal of Middle Eastern Studies*, 1984, No. 2); 'Le monde arabe vingt ans après: les défis économiques', *Revue Monde Arabe Maghreb-Machrek*, 1983, p. 101; and edited *L'industrialisation du bassin mediterranéen* (PUG, 1983).

Mahmoud Abdel Fadil is Professor of Economics at Cairo University and the American University in Cairo. He is the author of *Development, income distribution and social change in rural Egypt 1952–70* (Cambridge University Press, 1975) and *The political economy of Nasserism* (Cambridge University Press, 1980), and other books in Arabic.

Hesham Garaibeh is Acting Dean of the Faculty of Economics and Administration of Yarmouk University. He is the author of a texbook on financial management, and of 'Main trends and developments in the Jordanian economy' and 'OPEC investment abroad, evaluation of a specialized institution: the case of the Industrial Bank'.

Larbi Jaidi is Maitre de Conference at the Faculté de Droit, Mohammed V University in Rabat. He is the author of *L'industrie textile et la processus de l'industrialisation au Maroc* (Editions Faculté de Droit de Rabat, 1975); *La* *formation des ensembles regionaux: Issue a la crise dans le Tiers Monde* (Collectif Editions Maghrebines, 1981); 'Chroniques économiques du Maroc' in *Annuaire de l'Afrique du Nord* (1976–80, CRESM, CNRS, Paris).

Giacomo Luciani is Director of Studies at the Istituto Affari Internazionali. He is the author of *International oil companies and Arab countries* (Croom Helm, 1984); *Egypt's economic potential* (with others; Croom Helm, 1985); *L'Opec nell'economia internazionale* (Einaudi, 1975); and editor and co-author of *The Mediterranean region* (Croom Helm, 1984).

Fathallah Oulalou is member of the National Assembly in Morocco and Professor of Economics at Mohammed V University, Rabat. He is the President of the Association of Moroccan Economists and former President of the Union of Arab Economists. He is the author of *Le Maroc face a la BIRD et le FMI* (Editions PubliSud, 1986); *Propos d'économie marocaine* (SMER, Rabat, 1980); *Le monde Arabe et la communauté Européenne* (in Arabic, Maghrebine (ed.), Dar Haddatha, 1981); *Economie politique* (in Arabic, Dar Haddatha 1970–85 (5 editions)).

Afsaneh Najmabadi is associated with the Center for Middle Eastern Studies at Harvard University. She is editor of *In the Shadow of Islam: the women's movement in Iran*; also contributed to *Religion and society in Iran* (ed. by Nikki Keddie) and to *The Iranian revolution and the Islamic Republic* (ed. by Eric Hooglund and Nikki Keddie).

Thomas Stauffer is Professor of Economics at the Center for Contemporary Arab Studies of Georgetown University. He is the author of numerous articles on the economics of Arab countries.

Dirk Vandewalle is a Fellow of the Institute of Current World Affairs, based in Cairo. He is the author of articles on Libya and Tunisia.

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