

Sustaining the Gains in Poverty Reduction and Human Development

Growth Strategy and Poverty Reduction

To recapitulate, since the mid-1980s the incidence of poverty in the Middle East and North Africa Region has fluctuated between 20 percent and 25 percent of the population (measured at the \$2 line). Although it is low relative to that of other developing regions, the level of poverty in the Middle East and North Africa is substantial. On average, one of every four or five people in this region is poor. Moreover, vulnerability to poverty is quite high. Raising the level of the poverty line from \$2 to \$3 results in a near-doubling of the number of people who are poor from around 52 million to approximately 95 million (see table 1.5). This shows that a large number of people live so close to the poverty line that they can easily drop below it as a result of economic shocks. Therefore, the reduction of poverty should continue to be a major policy objective.

Stagnation in the rate of poverty reduction since the mid-1980s has accompanied stagnation in the rate of growth in per capita output (at around 1 percent annually) and shows that the region is not an exception to the general finding from within- and cross-country data that growth and poverty are strongly linked. Clearly the region's slow growth has exacted a social cost in the form of a lack of progress on the poverty front. Getting onto a higher growth trajectory will be critical to reducing the number and proportion of poor people in the region in the future. It also will be critical to reducing the number of unemployed people from its current level of around 13.4 percent—a level that surely could increase under the demographic pressures that the region now faces.

How is higher growth to be achieved? In a series of recent publications, the World Bank has presented a comprehensive analysis of the growth challenge for the region (World Bank 2004c, h, i). According to this analysis, to achieve higher growth on a sustainable basis, economies in the Middle East and North Africa must complete three fundamental realignments: (a) from public to private sector dominance, (b) from rel-

actively closed to more open to international trade and investment, and (c) from excessive reliance on oil to more diversification.¹ Most countries in the region are already embarked on these realignments but more vigorous steps need to be taken in the future to complete the transition. In addition, countries in the region need to pay greater attention to issues of governance because each transition implies deep changes in the role of government and improvements in its performance. The World Bank has calculated that an acceleration of the three realignments combined with measures to improve governance and increase the rate of female labor force participation will increase average output per capita by 3 percent annually or three times the actual rate experienced since the mid-1980s.

The quantitative importance of such a growth strategy to poverty reduction is illustrated in table 6.1. This table shows how poverty rates would move under two different growth scenarios: a 1 percent per capita annual growth path similar to that experienced during the last decade or so, and a 3 percent per capita annual path that is achievable under the strategy described above. Assuming no changes in the distribution of income, it is clear that the alternative growth paths imply very different poverty paths with significantly different outcomes within 10 to 12 years. For example, such a difference in growth will mean a 15 percentage point difference in poverty in the Republic of Yemen (29.2 percent versus 44.3 percent) by 2015 and in Egypt (10.4 percent versus 25.4 percent). For the region as a whole, the anticipated difference in poverty by 2015 is about 8 percentage points. Translated into numbers, this implies that the higher growth rate should lift an additional 22 million people out of poverty.

Although the growth strategy described above remains the most promising way to deal with the poverty and unemployment challenge faced by the region, it is useful to consider also the vulnerabilities that may be generated in the process. For example, whereas increased openness to trade and investment is likely to propel the region's economies onto a higher growth path, it also may create some adjustment challenges for certain groups in the short run. At the conceptual level, the link between openness and poverty is ambiguous.² On one hand, there are good reasons to expect the position of many poor groups to improve through the expansion of labor-intensive export sectors following trade liberalization. This has been the experience, for example, in many parts of East Asia where export-led economic growth has occurred. On the other hand, it is possible that the position of some groups among the poor could deteriorate. For example, some of those who lose jobs in the import-substituting sectors may be members of the poor population or may slide into poverty as a result.³ Similarly, the price changes that accompany trade liberalization may have an adverse impact on some self-employed

TABLE 6.1

Poverty Forecasts at Alternative Economic Growth Rates

(Percent poor at the \$2 line)

Country	Poverty Incidence at 1% Growth Rate			Poverty Incidence at 3% Growth Rate		
	2005	2010	2015	2005	2010	2015
Algeria	12.9	11.1	9.5	11.4	7.0	3.6
Egypt	33.5	29.4	25.4	30.3	19.2	10.4
Islamic Republic of Iran	4.5	3.5	2.3	3.5	2.5	1.5
Jordan	7.7	6.4	5.2	6.6	4.5	2.5
Morocco	11.3	9.5	7.8	9.9	5.0	2.5
Tunisia	5.2	4.1	3.2	4.4	2.5	1.5
Republic of Yemen	51.2	47.4	44.3	48.3	38.3	29.2
MENA7	19.1	16.9	14.8	17.2	11.6	7.1
MENA7 (millions)	45.6	44.3	42.5	41.1	30.3	20.6

Source: Staff calculations.*Note:* MENA7 includes Algeria, Egypt, the Islamic Republic of Iran, Jordan, Morocco, Tunisia, and the Republic of Yemen.

poor people who may be net producers of commodities whose import is liberalized. A recent study done for Morocco suggested that removing protections from cereal could worsen the economic situation of some poor farmers who happen to be net producers of wheat (Ravallion and Lokshin 2004), even though it would be poverty reducing and welfare improving for the country as a whole.

The impact of transitional job losses can be mitigated by steps to improve the employability of workers through more flexible labor market laws and procedures. The socialist orientation of many Middle Eastern and North African governments in the post-independence period saw the introduction of labor laws that were, on balance, more concerned with job security and minimum incomes for the employed than with the business needs of private sector employers and the employment needs of potential workers. Although more flexibility with respect to regulations governing hiring has been introduced in some countries in recent years, rigidities in dismissals and layoffs continue to affect the levels and type of employment offered by the private sector. Many countries continue to ban dismissal for business reasons or make it administratively difficult and expensive.⁴ As a result, formal private sector employment is lower than it needs to be.

Steps also can be taken to improve the employability of women in the private sector. As noted earlier, female labor force participation in the region is lower than what may be expected on the basis of achieved levels of female education and fertility. This outcome arises from a combination of social and economic factors, including a range of gender-based regulations that restrict the flexibility of female employment. Modifying such

regulations to suit the needs of a modern economy and allow women greater flexibility to play multiple roles as both homemakers and workers would help in generating greater private sector employment opportunities for them.⁵ Furthermore, the adoption of a more market-determined system of production is likely to lead to an increase in the demand for female labor, in contrast to the capital- and male-intensive patterns favored under public sector regimes (often involving infrastructure, construction, and energy projects). In recent decades Morocco and Tunisia have experienced significant increases in female employment in the textiles and garment industries operated by the private sector.

Finally, private sector and market orientation may increase inequality relative to a situation where public sector control of the economy compresses income and wage differences. This may affect poverty through one or both of two channels. First, it is commonly observed that higher levels of inequality lower the poverty-reduction impact of a given level of growth. Second, inequalities of income and wealth tend to lead to political maneuvering by the better-off groups to design institutions and policies to preserve their relative advantage (see World Bank 2006). Is inequality likely to increase under the trade- and market-oriented growth strategy? Recent experience is ambiguous on this point. In China and countries of the Former Soviet Union, the reduction of state control over the economy has allowed wage and income differentials to expand, leading to rising inequality. The same has happened in some countries of Latin America, although the mechanism there has involved greater dispersal of wage differentials by education levels as a consequence of trade liberalization. On the other hand, most studies of long-term trends in growth and inequality fail to show any systematic correlation between the two. And the experience of the high-performing East Asian countries (other than China) since the 1970s certainly has not followed the Latin American trend. In part this may have been because of a sustained effort in the East Asian countries to increase the supply of education and skills at a pace equal to evolving demand. This is an area in which the Middle Eastern and North African countries have done well in the past but still must continue to improve in the future.

Challenges for Human Development

Earlier chapters have shown that the Middle East and North Africa Region has performed well with regard to improvements in education and health indicators, generally considered to be important aspects of the non-income dimensions of poverty. Not only have such indicators improved over the past four decades, but also they have done so at a rate

faster than the rate in comparator countries. And during the 1990s these improvements were achieved despite fiscal stringency and lower per capita spending on social services, thus suggesting both a greater role for private spending and gains in the efficiency of public spending. Nevertheless, good historical performance may not ensure similar performance in the future. The education and health challenges of the future are likely to be different from those of the past and will require different responses.

Challenges in Education

Although the region has a strong record of improving the *quantity* of education provided, the challenge of the future will be more in the area of education *quality* and labor-market relevance. As Middle Eastern and North African economies move toward producing more for world markets, they will need to compete with other countries to secure market share and obtain larger flows of foreign investment. The higher the level of skills in their workforces, the better placed the countries will be to compete internationally.

Improving the quality of education in public schools is of importance for poverty reduction and equity as well. Low quality in public schools is a special problem for poor children because they rarely have alternative higher-quality options in the form of private schools or private tutoring. Moreover, receiving a low-quality education at the primary and secondary levels effectively prevents children from poor backgrounds from passing the competitive examinations typically required for entrance to tertiary institutions.

Similarly, as Middle Eastern and North African economies become more private sector oriented, their respective education systems will need to produce skills that are in demand in the private sector. To achieve this, more attention will need to be paid to enhancing the *relevance* of education curricula. In most countries of the region, curricula were designed originally with a view to preparing graduates for public sector employment. Practical skills that are highly valued in the private sector are less prominent in the curricula and there exist few mechanisms for allowing private sector requirements to influence the content and standards of national curricula. Given the prospective importance of the private sector in future growth strategies for the region, it is important that education systems and curricula (including technical and vocational education) be reformed so as to support the private sector in this task.

The appropriate response to the education challenge of the future will involve going beyond the “engineering” approaches of the past that relied primarily on changing the quantity and mix of inputs (such as new buildings and equipment for schools) in the hope that this would deliver

the necessary outputs. This was fine as long as the output was thought of in quantitative terms as the number of children enrolled in school or the number of computers per classroom and so on. However, when the definition of output changes to one in which quality is the most important dimension, new approaches must be developed. The challenges of the future will require the use of incentive mechanisms to motivate service providers to improve their performance, and accountability mechanisms to equip service receivers (students or their parents) to better enforce agreed-on standards of service delivery.⁶

Challenges in Health

Although the region has performed well in improving the access of the average citizen to primary care facilities and public health interventions, more needs to be done in the future on two fronts: further improving access for the poor and coping with an emerging disease pattern that is linked to lifestyle choices and an aging population. As noted earlier, despite substantial progress in the past four decades, significant disparities continue to exist between rich people and poor people with regard to health outcomes such as child mortality and malnutrition. For the most part, the removal of these disparities will require adequate funding of public health budgets, a continued special focus on maternal and child health services, and special efforts to target regions and neighborhoods with a preponderance of poor residents (such as most rural areas and urban slums). In addition to direct health interventions, it will be important to continue to address issues such as the supply of safe water and sanitation to underserved groups as well as to provide nutrition and preventive health education.

Coping with the disease patterns emerging from the demographic and epidemiologic transition, however, will require the development of new approaches to health care financing. Because the treatment of the emerging noncommunicable disease patterns is likely to be individual oriented and technology intensive, it will be costlier. Accordingly, there will be more pressure on budgetary resources, pressure that may take away funds that presently address the public health needs of the poor. Among ways to relieve such pressure are developing insurance mechanisms to spread the financial cost of treatment across a diversified pool of contributors and establishing charges for the use of university or highly specialized hospital services for those who can afford to pay. Because the new disease patterns also are spreading among the poor, it will be important to develop a system that provides them with low-cost access to treatment services as well. Also of relevance would be the redesign of existing subsidies (for example, on pharmaceuticals in the Islamic Republic of Iran) so as to mini-

mize leakage to the nonpoor populace. This point is taken up in the next section.

Strengthening Social Safety Nets

Although measures directed at increasing growth and enhancing the access of the poor to health and education must remain the two principal pillars of the region's poverty reduction strategy, attention also will have to be paid to the third pillar— social safety nets. These must be reformed with two objectives in mind: (a) increasing the efficiency with which limited resources are directed to the needs of the poor and the vulnerable; and (b) improving their ability to cope with adverse, though temporary, income shocks that may occur as the economies become more private sector, trade, and market oriented. Indeed, improved efficiency can release resources not only to help those who need safety net assistance but also to increase pro-poor spending in other areas, such as public health, improved water supply, and better rural infrastructure. Finally, higher efficiency in reaching the poor through targeted assistance will have a greater impact on poverty reduction for any given level of growth of the economy and volume of fiscal resources devoted to the task.

Targeting Assistance to the Poor

Countries in the Middle East and North Africa Region have an extensive system of publicly funded social safety nets in addition to private arrangements linked to the tradition of *zakat* and other charitable activities. With respect to poverty reduction, the dilemma of the region's public safety nets may be baldly stated: the parts of the safety net that are effective are not efficient, and the parts that are relatively efficient are not effective. For example, food and energy subsidies reach a large number of people and are effective in the sense that they also reach the poor. However, both food and energy subsidies are inefficient in that they involve substantial leakage of benefits to nonpoor people. The benefits of energy subsidies, in particular, are heavily tilted toward the nonpoor. For example, as much as 93 percent of gasoline subsidies in Egypt go to the richest quintile. And the fiscal outlays are huge: energy subsidies in Egypt cost approximately 8.4 percent of GDP (in 2005), and they are thought to be even higher in the Islamic Republic of Iran. At the same time, other safety net components, such as cash transfers, are relatively better targeted to the poor and the vulnerable, but they are funded at such low levels (typically less than 1 percent of GDP) that they are not very effective in improving the conditions of the poor. The challenge for the future is to redesign social safe-

ty nets to focus the bulk of the available resources on the poor and the vulnerable populations.

There is both a political and a technical dimension to improving targeting. The political dimension arises from the resistance to be expected from those who stand to lose if subsidies are cut. Past attempts to reform subsidies have encountered such resistance in several Middle Eastern and North African countries, usually from the urban middle classes who feel squeezed between rising prices and stagnant incomes. The response to such resistance has varied across countries and over time. On some occasions, targeting efforts were abandoned and the subsidies were partially or fully restored. On others, the need to circumvent resistance led to more sophisticated program design (included self-targeting methods) and to flexibility in the pace and scope of the reform effort.

The technical dimension involves developing a cost-effective targeting mechanism. Because individual means-testing is costly in administrative terms, alternative approaches must be considered, including the use of such characteristics as literacy status, size of household, and location, or through inducing self-targeting. As discussed in an earlier chapter, reforms in Egypt and Tunisia have improved the targeting of food subsidies partly by introducing innovations that make it more likely that only the truly poor will seek to avail themselves of the subsidies. As a consequence, overall outlays on food subsidies have been reduced without notably affecting benefits to the poor. Geographic targeting also can be a cost-effective way to cover certain poverty groups that are relatively homogeneous, such as groups in rural or remote areas.

In the Middle East and North Africa Region, however, the ability to develop cost-effective targeting mechanisms is hampered by considerations of data access, quality, and use.

In order to target, public agencies must have good information about the location and other characteristics of the poor. They can be helped in identifying the poor if they share available data with nongovernment agencies and academic researchers with a professional interest in the subject. However, such data sharing is not common in the region. In some countries, household and labor market survey data are considered confidential. In others, they may not be considered confidential but are still made available only on a discretionary basis. Because such data are directly relevant to poverty and employment analysis, wider and easier access would be beneficial in formulating antipoverty policies.

Poverty analysis also can be improved if the underlying data are of relevance to the issues at hand. For example, it is useful to be able to distinguish between those who are chronically poor and those who are only temporarily poor. Regular mechanisms of economic growth may be an adequate way to help the latter group, but other assistance strategies may

need to be devised for the former group. Identifying the chronically poor and understanding poverty dynamics require panel data (that is, data on the same families over time), and survey authorities in the Middle East and North Africa (with the exception of the Islamic Republic of Iran) do not typically collect such data.

Finally, effective antipoverty programs require monitoring and evaluation mechanisms so that results may be tracked and program design changed in accordance with the lessons of experience. This, in turn, requires an “evaluation culture” to prevail within government agencies dealing with poverty. Such a culture presently is lacking in most of the countries in the region.

Promoting Better Risk-Coping Mechanisms

As discussed above, a market-oriented development strategy can increase the risk of income shocks for some groups, leading to the need to find new jobs and set up new lines of business. Social policy in the Middle East and North Africa Region must develop better mechanisms to cope with this situation. The following instruments are especially relevant: unemployment insurance, temporary employment programs, and microfinance programs.

Having an unemployment benefits program in place can help workers transition from one job to another. This region features few programs of this nature. Formal unemployment insurance schemes paid for by contributions from firms and workers are rare. Where they exist, as in Algeria, Egypt, and the Islamic Republic of Iran, there are concerns about financial sustainability, incentives, and equity. Reserves in the insurance pool often are not allocated with a sufficient concern for long-run financial sustainability (see World Bank 2002d, pp. 73–74). Benefit periods tend to be on the long side, thus discouraging job search; and costs to employers are often on the high side, thus discouraging hiring. These aspects will have to be studied carefully to design unemployment insurance schemes that achieve social policy objectives at an affordable social cost.⁷

As discussed in the previous chapter, public works programs are commonly used to provide temporary employment in several Middle Eastern and North African countries. However, they differ widely in terms of program design, funding levels, and outcomes. In some cases jobs created through such programs have amounted to a significant proportion of the labor force (for example, 2.3 percent in Algeria and 2.7 percent in Tunisia), but it is not easy to assess whether these jobs have been created in an efficient manner (that is, at low cost) or even in an effective manner (that is, covering many of the poor). International experience suggests that cost-effective public works programs normally have high wage shares in total costs, and well-targeted programs normally offer wages below the

prevailing market rate for unskilled labor and focus on geographic regions where poverty is high. These characteristics should be more systematically incorporated in public works programs in the Middle East and North Africa.

Having access to finance also helps people respond to business shocks. Because commercial banks rarely lend to the poor and the near-poor, the relevant issue for them is access to microfinance. In this region, microfinance is limited in scope and reach: almost 3 million entrepreneurial poor and vulnerable people still lack access to even the small amounts of finance that could help them run a microenterprise. However, the concept is growing in popularity and reach. Market penetration, or the number of people reached in relation to the number of potential clients (defined as 40 percent of those at or below 1.2 times the poverty line), was recently estimated at 19 percent and growing. Governments have been progressively lifting policy impediments to the growth and spread of microfinance, recognizing its potential to become a more important aspect of future social policy in the region.

Notes

1. Our concern is with trend growth over the long term. In the short run, such exogenous factors as increases in the price of oil can bring about growth spurts, as has been the case in 2003–05.
2. For a recent conceptual and empirical treatment of the subject of trade liberalization and poverty, see Winters, McCulloch, and McKay (2004). They concluded the following: “In the long run and on average, trade liberalization is likely to be strongly poverty alleviating, and there is no convincing evidence that it will generally increase overall poverty or vulnerability. But there is evidence that the poor may be less well placed in the short run to protect themselves against adverse effects and take advantage of favorable opportunities” (p. 72).
3. This may be an especially important consideration in economies where state-owned enterprises are prominent and especially in import-substituting sectors. In some cases the social challenge is compounded if a large proportion of employees in such companies is women.
4. Opportunities and constraints with respect to labor market reforms are discussed in World Bank (2004c).
5. Specific restrictions on women’s work and mobility in the Middle East and North Africa Region are discussed in World Bank (2004b).
6. The scope, content, and limitations of various incentive and accountability mechanisms are being reviewed in an ongoing World Bank study of education reform in the region.
7. International experience shows that no unemployment income support program dominates other options in terms of performance. All have pros and cons, with different effects on labor market incentives and degrees of income insurance.