

Sustaining Gains in Poverty Reduction
and Human Development in the
Middle East and North Africa

ORIENTATIONS IN DEVELOPMENT

Sustaining Gains in Poverty Reduction and Human Development in the Middle East and North Africa

Farrukh Iqbal



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Preface

The Middle East and North Africa Regional Vice Presidency of the World Bank has published a number of studies in recent years that describe and analyze key aspects of the social and economic development experience of the region as a whole. This effort has so far covered studies of growth, employment, trade, governance, gender, pensions, HIV/AIDS, and social protection. This book is the latest output of this ongoing analytic enterprise. It focuses on the experience of the Middle East and North Africa with poverty and human development. It deals mostly with the period since the mid-1980s, a period that has seen significant changes in the region's economic, political, and demographic context.

The focus on poverty is a natural one for the World Bank. However, some may not think poverty a prominent enough issue in the Middle East and North Africa, given the region's association with oil wealth. This book shows that this image is a misleading one. Although the Middle East and North Africa has a low rate of poverty when compared with other developing regions, the fact remains that one of every five persons there can be considered poor (at the \$2 PPP international poverty line) and that this situation has not improved much since the late 1980s. This may be thought of as the social cost of the low rates of economic growth that have prevailed in the region over this period and it justifies the abiding concern of the World Bank and many of the region's governments with promoting growth as a means to reducing poverty.

The book also draws attention to a paradox. While income poverty did not improve in the last decade, human development indicators for the region improved tremendously, at a rate that surpassed even that of lower middle income comparators. The analysis presented in the book suggests that, among other factors, improvements in the delivery of public health and education services are likely to have played a part in this remarkable achievement. This is an encouraging finding. It suggests that, even in the absence of income growth, the health and education aspects of the living standards of the poor can be enhanced through attention to service deliv-

ery. It is a finding that provides a strong empirical justification for the World Bank's operational focus on health, education and social safety net issues in the Middle East and North Africa Region.

So the twin challenges for the region in the future are that of obtaining higher growth while building on human development achievements. Now that growth rates have begun to pick up in the region, the prospects for poverty reduction in the future have improved as well. But we have to be mindful of the sustainability of the growth path. If growth in the region is based largely on favorable terms of trade shifts for hydrocarbons, the sustainability of such growth may be questioned. We saw a demonstration of this after 1985 when a terms-of-trade shift against hydrocarbons led to economic stagnation for the next fifteen years. But if growth comes from a broader economic base and is led by the private sector, it is more likely to be durable.

Sustaining gains in human development will require tackling new challenges. In education, the focus must now shift from quantity to quality. In health, attention must continue to be paid to the access needs of the poor and to the new diseases arising from changing demographics and shifts in diets and other lifestyle choices. In social protection, more emphasis must be placed on efficiency and insurance objectives than has hitherto been the case in the region.

But this is not all that needs to be done. Economic, political and social inequalities tend to trap disadvantaged people at the bottom of society for generation after generation. This is not only unfortunate for those at the bottom; it is also an impediment to higher economic growth over the long run. When those with ability are denied the opportunity to contribute fully to the economy, the economy suffers. Most Middle Eastern and North African countries have taken big strides toward equalizing opportunities through providing better health and education to their citizens. But meaningful opportunities do not flow from better education and health alone. They are affected as well by the scope for voice, inclusion, and accountability at all levels of decision making. This remains a challenge for the region—one that must be tackled more comprehensively in the future if we are to give full meaning to the term “human development.”

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Abbreviations and Acronyms

BAJ	Barnamaj Al Aoulaouiyat Ijtimaiya
DHS	Demographic and Health Survey
EEP	Education Enhancement Program
GDP	gross domestic product
LPG	liquefied petroleum gas
MENA	Middle East and North Africa
MENA7	Algeria, the Arab Republic of Egypt, the Islamic Republic of Iran, Jordan, Morocco, Tunisia, and the Republic of Yemen
MENA10	Algeria, the Arab Republic of Egypt, the Islamic Republic of Iran, Jordan, Lebanon, Libya, Morocco, Syria, Tunisia, and the Republic of Yemen
MFI	microfinance institution
MOSAI	Ministry of Social Affairs and Insurance
NA	national accounts
NAF	National Aid Fund
PHC	primary health care
PN	<i>Promotion Nationale</i>
PPP	purchasing power parity
PPP\$	purchasing power parity dollars
SWF	Social Welfare Fund

Executive Summary

The main objective of this book is to review and learn from the Middle East and North Africa Region's experience with poverty reduction and human development. A capsule version of the modern economic history of this region would divide the past 40 years or so into two periods—a statist period that prevailed until the mid-1980s and a transition period from then to the present. The *statist period* was characterized, as the name suggests, by state domination of the economic system, an inward-looking economic strategy, and heavy reliance on plan-based public investments as the main engine of growth. The *transition period*, now approximately two decades old, has been marked in different countries by efforts of varying intensity and resolve to move toward more open and market-oriented economic regimes, with a corresponding enhancement in the role of the private sector. It is convenient to frame the region's experience with poverty reduction and human development in terms of these two periods as well.

The coverage of this book is limited by the availability of data. Some countries in the Middle East and North Africa do not collect systematic data on poverty, and have only rudimentary information on health and education inputs and outcomes. Many others collect adequate data but restrict public access to it. This report focuses on a subset of countries from the Middle East and North Africa Region for which relevant data on poverty and human development are available to the World Bank.

Poverty data in aggregate form are available in the World Bank for seven Middle Eastern and North African countries, namely, Algeria, the Arab Republic of Egypt, the Islamic Republic of Iran, Jordan, Morocco, Tunisia, and the Republic of Yemen. Adequate data related to spending and outcomes for human development are available for an additional three countries, namely, Lebanon, Libya, and the Syrian Arab Republic. Thus the term *MENA* is used in this report to refer to the set of 7 countries when poverty is being discussed and to the larger set of 10 countries when human development is being discussed. In neither case does the re-

port cover Bahrain, Djibouti, Kuwait, Oman, Saudi Arabia, and the United Arab Emirates, nor, except briefly, Iraq and West Bank/Gaza. The 10 included countries account for approximately 85 percent of the total population of the region.

Available data show the following features of the statist period:

- *Rapid economic growth occurred.* Average per capita gross domestic product (GDP) for the region rose more than sevenfold, from \$1.6 a day in 1965 (in constant 1993 purchasing power parity [PPP] dollars) to \$11.7 a day by 1985. For much of this period, growth was driven by high rates of investment made possible for some countries by high prices for hydrocarbons and for other countries by high levels of borrowing.
- *Poverty declined.* Pre-1985 household surveys are only available for Tunisia and Egypt, and these clearly show declining poverty rates during 1965–85. In Tunisia, poverty fell from 51 percent in 1965 to only 16 percent in 1985. Egypt’s achievement was also impressive, with poverty declining from 82 percent to 53 percent between 1975 and 1985. An aggregate picture of regional poverty shows a poverty incidence rate of only 25 percent for MENA by 1987, the lowest among all developing regions at that time.
- *Remarkable progress took place with respect to human development indicators.* Between 1965 and 1985, adult literacy almost doubled, going from 24 percent to 47 percent; average schooling completed by those over 15 years of age rose more than fourfold, from 0.8 to 3.4 years; mortality rates for children less than 5 years old fell from 233 per thousand live births to 108; and life expectancy rose from approximately 50 years to 61 years. In comparative terms, the region easily kept pace with the performance of middle-income countries in East Asia and Latin America.
- *The archetypal social policy model of the region came into full effect.* This model comprised three main components: an education and health component in which free education and primary health care services were promised to all citizens; a consumption-subsidy component in which key consumption items, such as food and energy, were provided at subsidized rates to most citizens; and a public employment component through which permanent jobs (and associated old-age pension benefits) were provided to many citizens.

The transition period featured not only meager growth in per capita GDP and little change in poverty but also, remarkably, continued rapid improvements in human development. Attempts to transition from the

statist to a market-oriented economic regime gathered momentum in the mid-1980s as growth collapsed following a decline in the price of hydrocarbons—a key resource for many countries in the region—and debt burdens became unsustainable in a context of low productivity growth. Over the next 15 years or so, the following features were evident:

- *Per capita output stagnated.* By 2000, the region's average per capita output had only reached \$11.3 per day (PPP\$) and had not fully recovered to its 1985 level. The slow growth was due in part to low prices for hydrocarbons, in part to declining remittances and aid flows, and in part to the limited extent of structural reforms undertaken in the region as well as a low payoff to the reforms that were implemented.
- *Very little progress was made on the poverty front.* The region's average poverty rate fluctuated between 20 and 25 percent during the entire decade of the 1990s. By 2001, approximately 52 million people were poor, an increase in absolute numbers of approximately 11.5 million people, compared with the situation in 1987.
- *The Gini measure of inequality fluctuated between 0.32 and 0.44 for most MENA countries,* although it was lower in the 1990s than in the 1970s for the three countries (Egypt, Iran, and Tunisia) for which an adequate time series is available. On the whole, the lack of any systematic deterioration in inequality after 1985 suggests that structural reforms adopted in this period did not have an adverse impact on inequality.
- *Human development indicators continued to improve.* Between 1985 and 2000, literacy spread to 69 percent of the population, average years of schooling (for those above age 15) rose to 5.2, child mortality rates plunged to approximately 46 deaths per thousand children in the first five years of life, and life expectancy climbed to 68 years. Remarkably, the region improved its human indicators faster than did middle-income comparators over this period, and it did so despite a considerably slower rate of output growth and a decline in levels of public spending.
- *The region's social safety nets came under stress as fiscal resources tightened.* In response to fiscal tightening, safety nets were modified in several countries to reduce budget outlays on certain subsidies, tighten eligibility for others, replace in-kind subsidies with cash transfers, reduce public sector employment, and provide temporary jobs through public works programs and longer-term help through microfinance schemes.

The fact that little growth or poverty reduction was achieved during the 1990s despite impressive gains in human development suggests that the region had difficulties in translating rising human capital into higher

productivity. This is supported by two pieces of evidence: the region exhibits low rates of return on education (ranging from 2.5 to 10.0 percent for different levels of schooling); and it has experienced high rates of unemployment (currently just above 13 percent), especially among educated people. Low growth, occasioned in part by macroeconomic policy and structural factors, is an important determinant of both unemployment and low rates of return on education. Among structural factors, recent academic research suggests that the impact of education on income is strongly conditioned by an economy's degree of openness. Insufficient openness to trade and investment has likely constrained returns on education in the Middle East and North Africa Region.

There is reason to believe that the strong gains in education and health since the mid-1980s were due in part to greater efficiency in the delivery of such services. There is a more encouraging aspect as well to the MENA experience with human development in the transition period. Econometric analysis conducted for this report shows that most MENA countries had gains higher than can be explained by initial incomes, initial levels of education and health, income growth during 1980–2000, and average public spending on education (used as a proxy for spending on social services). In part, such gains may have come from a better targeting of spending to deliver services to underserved groups. In part also, such gains may have resulted from positive cross-sector externalities. For example, statistical analysis shows a strong link between child mortality improvements during 1980–2000 and the level of female education achieved by 1980. In other words, investments in female education during the pre-1980 period had an important impact on health gains in the period thereafter.

Opportunities to make social safety nets more efficient instruments for poverty reduction and human development have largely been missed. The parts of the region's safety nets 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 a lot of resource leakage to the nonpoor populace. The benefit transfers from energy subsidies, in particular, are heavily tilted toward the nonpoor: as much as 93 percent of gasoline subsidies in Egypt go to the richest quintile of consumers. At the same time, although cash transfers are relatively better targeted to the poor and the vulnerable, they are funded at such low levels (often less than 1 percent of GDP) that they are not very effective in improving the conditions of the poor. And whereas some improvements in efficiency have taken place in the past with respect to the design of food subsidies, especially in Egypt and Tunisia, opportunities to make a sub-

stantial difference through reforming energy subsidies, involving a much greater fiscal payoff, have largely been missed.

Accelerating the pace of poverty reduction in the future requires an acceleration of growth. The strategy for higher growth in the region comprises three key elements, namely, an enlargement of the role of the private sector, a shift from import-substitution strategies to greater global integration, and a move away from excessive reliance on hydrocarbons to a more diversified base of economic activities. Most countries in the region are already embarked on these three realignments, but more vigorous steps need to be taken in the future to complete the desired transitions. In recent reports the World Bank has calculated that an acceleration of the three realignments noted above, combined with better governance and efforts to increase female labor force participation, could increase the annual average output per capita by 3 percent or three times the actual rate experienced since 1985. Such a difference in growth can make a tremendous difference in poverty outcomes within a decade or so. For example, such a difference in growth rates can mean a difference of 8 percentage points in poverty for the region as a whole by 2015. Translated into numbers, this means that the higher growth rate will help lift an additional 22 million people out of poverty. A higher growth rate also will enable the countries in the region to tackle the more resource-intensive challenge of providing good health care and education in the future.

Growth policies also must be accompanied by policies to increase labor absorption in the private sector. In the short run, the new growth paradigm may be associated with greater volatility in jobs and incomes. Such churning is healthy and helps reallocate capital, labor, and entrepreneurial talent in accordance with changes in comparative advantage brought about by changes in the global economic environment and by domestic policy reforms. But it also could generate adverse short-run changes in employment and incomes among the poor and the near-poor (that is, those living just above the poverty line). For example, trade liberalization may cause some people to lose jobs in sectors that were previously protected, even though the liberalizing measure might be poverty reducing and welfare improving for poor people as a whole. The impact of transitional job losses can be mitigated by measures to increase the private sector's demand for labor in general, and measures to improve the employability of workers through more flexible labor market laws and procedures in particular. Although more flexibility has been introduced in some countries in recent years, rigidities with respect to dismissals and layoffs continue to affect the levels and types of employment offered by the private sector. Many countries continue to ban dismissal for business reasons or make it administratively difficult and expensive. As a result, formal private sector employment is lower than it needs to be; and informal sector

employment, with its attendant vulnerabilities, is higher than necessary. Similar but gender-based rigidities have prevented female labor force participation from rising to levels more compatible with the impressive gains made in female education in the region.

Sustaining gains in human development will require paying attention to new challenges. The good historical performance of the region may not necessarily ensure similar performance in the future. The education and health challenges of the future are likely to be different from those in the past, and they will require different responses. In particular, these responses must factor in the effects of the ongoing demographic transition, the need to compete globally, and the need to become more efficient in the use of available resources.

Sustaining gains in education requires shifting the focus from quantity to quality. As noted earlier, most countries in the region have a strong record of improving the quantity of education provided. The challenge of the future, however, will be more in the area of education quality and labor market relevance. As Middle Eastern and North African economies move toward producing more goods and services 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 these countries will be to compete internationally. Improving the quality of education in public schools is important 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.

Sustaining gains in health requires continued attention to the needs of the poor and the consequences of the ongoing demographic transition. 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. Despite progress in the past four decades, significant disparities continue to exist between rich and poor people with regard to health outcomes such as child mortality and malnutrition. For the most part, removing these disparities will require adequate funding of public health budgets, a continued special focus on maternal and child health services, and specific 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 interven-

tions, it will be important to continue addressing issues such as the supply of safe water and sanitation to underserved groups and to provide nutrition and preventive health education.

Coping with the disease patterns arising from the region's ongoing demographic and epidemiologic transition, however, will require the development of new approaches to health care financing. Because treatment of the emerging noncommunicable disease patterns is likely to be individual oriented and technology intensive, it will be more costly. 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 is to develop insurance mechanisms to spread the financial cost of treatment across a diversified pool of users and establish 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 populations, it will be important to develop a system that provides them with low-cost access to treatment services. Also relevant would be the redesign of existing subsidies (for example, on pharmaceuticals in Iran) so as to minimize leakage to those who are not poor.

Social safety nets should be made more important instruments of the poverty-reduction strategy in the future through a focus on efficiency and insurance objectives. Although measures directed at increasing growth and enhancing the access of the poor to health care and education will remain the two principal pillars of the region's poverty-reduction strategy, attention also must be paid to the third pillar, namely, social safety nets. These have to be reformed with two objectives in mind: increasing the efficiency with which limited resources are directed to the needs of poor and vulnerable people, and improving their ability to cope with adverse income shocks that may occur as regional economies become more private sector, trade, and market oriented. Improved efficiency would imply a greater impact on poverty reduction for any given level of economic growth and volume of fiscal resources devoted to the task. It also could release resources to help those who need safety net assistance and to increase pro-poor spending in other areas, such as public health, improved water supply, and better rural infrastructure.

Safety nets can be made more efficient through better targeting, but this is presently constrained by political economy considerations and by deficiencies in data access and quality and related technical and administrative concerns. Politically, the adoption of pro-poor targeting as a policy objective may provoke discontent and resistance among better-off, more vocal, and politically stronger groups who might stand to lose from such a move. Factors like that have come into play in the region in the past—during attempts to reform food subsidies, for example. In some

cases they led to the abandonment of targeting, but in others they led to more sophisticated program design and flexibility in implementation.

The technical and administrative dimensions relate to the design and cost of targeting mechanisms as well as to the availability and use of appropriate data. Although narrower targeting can improve the efficiency of subsidy programs, this has to be balanced against the cost of implementing appropriate targeting schemes. In countries with weak administrative and governance structures, this may be a big challenge. Efficient targeting also requires good data to identify and locate the poor, good analysis to calibrate the connection between policy and poverty outcomes, and organizational arrangements to learn from experience and modify policies as needed. The Middle East and North Africa presently suffer from deficiencies in all these areas. Data that would allow distinguishing between the chronically poor and the temporarily poor are not collected anywhere in the region except the Islamic Republic of Iran. And the household data that are collected are typically not made public, thereby preventing the breadth and depth of analysis that can substantially strengthen the knowledge base for antipoverty policy formulation. By and large, in most Middle Eastern and North African countries, access to data is not considered a matter of public right but of bureaucratic discretion.

Finally, the effectiveness of antipoverty programs is often hampered by the lack of internal systems to collect and analyze relevant data and to link program design to lessons of experience. In many Middle Eastern and North African countries, the issue is not so much the lack of programs to help the poor as it is the lack of information about whether existing efforts are helping the poor in a cost-effective manner. This can best be remedied through an effort to foster more of an “evaluation culture” within government agencies. Such a culture could be encouraged, for example, by making rigorous baseline surveys and periodic evaluations mandatory in all publicly funded antipoverty programs.

Safety nets also can be strengthened through measures that help ensure against the risks of job and income loss. For example, unemployment insurance schemes, paid for by contributions from firms and workers, can help cushion the transition from one job to another. To date, there is not much experience with such schemes in the region, and care will have to be exercised to keep programs consistent with financial sustainability, equity, and incentives for workers to move out of unemployment. Temporary employment programs also can help. There is much more experience with these programs in the region, and this experience can be used to make the programs both more effective, through a focus on the labor intensity of projects, and more efficient, through an emphasis on targeting to the poor through appropriate wage setting.

Last, the ability to cope with unanticipated shocks is often eased by access to finance. In the case of entrepreneurs from among the poor and near-poor, the relevant resource is microfinance because, without collateral, they rarely have access to loans from commercial banks. In recent years the scale and reach of microfinance schemes have been growing in the Middle East and North Africa. Most governments there have progressively reduced policy impediments to the growth of microfinance institutions, and approximately 19 percent of the potential client base is now being served, up from 3 percent only a decade or so ago.

This survey of poverty and human development trends in the Middle East and North Africa suggests reasons for both concern and optimism. The concern arises from the fact that the growth performance of the region was weak during the last two decades and this exacted a social cost in terms of lack of progress in poverty reduction. Almost 11.5 million people were added to the ranks of the poor between 1987 and 2001 because the region's population continued to grow while its economies did not. Optimism arises from the facts that, despite stagnant growth, human development in the region continued to progress at an impressive pace and that some of this was likely due to gains in the efficiency with which health and education services are delivered. If the region builds on these human development achievements and implements macroeconomic and structural reform measures to climb to a higher growth trajectory, it could well become the first developing region to make poverty history.

