1. Introduction

1.1 BACKGROUND

Over the past 30 years, after writing three books on economic development in the Middle East, a book on Islamic taxation and numerous articles and popular opinion pieces on the economic performance of the region, it is clear to me that the reasons for economic and social failure in the Middle East are far deeper than simple shortcomings in the quality of economic policies adopted, availability of financial resources and governance. Political, legal, social, cultural and religious factors, regional conflicts and instability, and external meddling in the region have also shaped the economic landscape. In the past, I relied too heavily on economic policies and paid lip-service to some of these other important factors.

The reasons for the disaster that is the Middle East of today are interrelated and straddle these and other disciplines. There is no simple economic policy explanation for the failure of the region. I believe that the explanation lies in what has happened in the region since World War II and especially over the past 30 to 35 years. In brief, my simple conclusion is that there can be no sustained economic growth, development and prosperity in the Middle East without peace and stability. But there can be no stability without economic prosperity. The major powers, instead of supporting social, political and economic progress, have made matters worse by focusing on their own narrow short-term interests and at times even fueling conflicts.

The reasons for the turmoil in the region are multifaceted. From the economic perspective, policies have been misguided, shortsighted and inconsistent, and have been adopted in order to 'buy' local loyalty and thus support the regimes in power. Politically, most governments have lacked legitimacy. The rule of law has not been respected and nurtured. Revolutions, civil wars, regional conflicts and wars have drained the economic lifeblood of the area. In the case of the oil-exporting countries in the region, the focus of my studies, oil has been more of a curse than a blessing; it has become the crutch to avoid policy reform and to keep unpopular governments in power.[1] Oil has destroyed the work ethic of the region, fueled corruption and poisoned the cultural and social fabric of society. Islam has been invoked to garner legitimacy for illegitimate regimes and to gain support where support has not been earned. Islamic teachings have been perverted and conveniently adapted and adopted to support the dictator of the day, with concessions to the religious establishment to gain their backing.

The great powers, especially those in the West, have supported and exploited illegitimate, dictatorial and economically bankrupt regimes to promote their own short-term interests. FDR said more than half a century ago that similar rulers in Latin America were ‘sons of bitches’ but they were America’s ‘sons of bitches’! For the West it might have been easier to deal with little dictators or sons of bitches than with legitimate and nationalistic regimes with checks and balances. Unfortunately, there is now a price to pay: miserable economic growth (even declining real per capita economic output), high unemployment and a dejected, desperate and radicalized new generation of Muslims; Osama bin Laden on the loose, with potentially many more Osamas to follow; Afghanistan and Iraq rife with internal conflict; and much more to come unless the reasons for failure are acknowledged and new policy directions are adopted both within the region and toward the region. If change is simply imposed from the outside, it will fail. Yet under existing circumstances change will not readily come from the inside of its own accord. Effective change will come about only if the disparate reasons for failure are seen as a whole. Change will only be effective if it comes from the inside and is encouraged and supported by the West in word as well as in deed. The West’s principled rhetoric has been trumped and buried by its own selfish deeds. Western credibility, especially that of the United States, is at an all-time low in the region. Middle Eastern cynicism must now be bested by Western actions that are, in deed as well as in talk, supportive of pluralism, rule of law, economic development and social and economic justice. Such an enlightened approach toward the region is in the long-term interest of the West and of the United States.

1.2 AN ACCOUNT OF HOW WE GOT HERE

Whenever a topic becomes of general interest, the public and people from all walks of life become overnight experts. In the case of the stock market boom of the 1990s everyone, from hairdressers in Los Angeles to cab drivers in New York, had advice on what stocks to buy – with New York cab drivers probably more qualified than most. Since the tragic events of September 11, 2001, Islam and the Muslim countries of the Middle East have become a topic of great interest. The first Arab Human Development Report received widespread attention in the media.[2] Americans are interested in Al-Qaeda, know where Iraq is and are aware that there are Sunni and Shia Muslims. But in the process of acquiring this superficial knowledge, there has been a rush to judgement. In their quest to satisfy the public's thirst for more information and simple solutions, pundits and the media have become specialists on the Middle East, from politics to religion to economic development. They have generally blamed Islam, the Middle Eastern character and corruption, most often in that order, as the reasons for dictatorships, economic backwardness, social malaise and terrorism.

During 1974–75, I wrote my first book on economic prospects for the Middle East and North Africa.[3] This was a time of great hope for the region. Oil prices had increased significantly after the Teheran Agreement of 1971 and had started to shoot through the roof after the Arab oil embargo in 1973–74. This was also a time when economists generally believed that economic development and growth could be readily achieved by government investments in infrastructure and in key industries that embodied and supported areas of long-term comparative advantage. The difficulty was seen as the dearth of financing, especially the availability of foreign exchange, giving rise to the then famous Two-Gap Model (the gaps being savings and foreign exchange). With dramatically higher oil revenues, it looked as if the Middle East and much of North Africa had overcome any and all financing problems and that, as far as economic development was concerned, the sky was the limit. Oil exporters with their surplus capital were expected to invest in infrastructure, education, manufacturing and more; economies would grow rapidly, and their growth and surplus capital would in turn fuel growth in the rest of the region. It was a plausible story then and one that I generally espoused in the above-mentioned book. Sadly, it was just naive and wishful thinking, with little factual basis. What happened, what went wrong and what can be done to turn things around are what I endeavor to explore in this book.

It was not long after 1976 that it became obvious that the optimistic expectations were way off the mark and were nothing more than a simple fairy tale. Leaders (dictators or at best autocratic rulers) in the oil-exporting countries of the region became drunk on the vast transfer of wealth. Some embarked on showcase projects and extravagant celebrations to impress the world. Most increased military expenditures dramatically and imported the most sophisticated arms that money could buy, but that nobody knew how to maintain. Some sent their brightest and best to get a Western education even before they had finished high school in their own country. In many countries there was a rush to modernize, which became translated into emulating everything Western.

In most cases, subsidies for food, fuel and electricity became the overnight birthright of citizens. Oil was gushing from the ground and everyone wanted a share, with the powerful taking more than their share. Corruption took off at an even faster rate than did oil revenues, with everyone who could do so grabbing as much as possible, quickly and with little or no productive output. Economic disparity among the citizenry grew. It was a period that could easily be compared to the gold-rush era in the US but it was not clear whether its aftermath would turn out to be more like that of California or that of the Yukon.[4] In the Middle East it was oil that made all of this possible, while Middle Eastern governments seemed to forget that oil was a depleting resource, and a resource whose price could fluctuate wildly.

In 1978, I had the rare opportunity to see some of the policies and practices first-hand as Advisor to the Saudi Arabian Executive Director at the IMF and as Special Advisor to the Minister of Finance of Saudi Arabia. The IMF was preaching responsible fiscal and monetary practices, open trade policies and market reforms to the non-oil exporters of the region, but was quite mute when it came to the oil exporters, especially those who were oil rich and were lending money to the IMF (Saudi Arabia). In 1980, I collaborated with Martin Weitzman, who wrote a seminal paper on economic management in a depletable resource-based economy.[5] The results are quite intuitive. An oil-exporting country should save a higher percentage (than countries that do not rely heavily on a depletable resource) of its net national product (NNP) in order to compensate for the depletion of oil resources over time; the required savings rate depends on the size of oil reserves and their rate of depletion (that is, the expected number of years to the depletion of reserves), on the rate of return on non-oil investments and on where the country wants to be economically when oil runs out. In other words, oil exporters should see themselves as being in the asset transformation business; the asset, oil, belongs to the current and all future generations; oil exporters have to transform oil reserves into non-oil sources of economic output as efficiently as possible to benefit current and future generations in an equitable manner.

During the mid-1980s, I wrote a second book outlining the policy shortfalls of oil exporters and what had gone wrong since 1975.[6] However, in order not to offend a number of individuals and especially the government of Saudi Arabia, regrettably I did not publish this book until 1990. Its message was that delay in economic policy reforms (reduction in subsidies and the need for a policy environment to encourage private sector growth) would only make matters more difficult, both politically and practically, especially in the face of explosive population growth. This was followed by another book in 1997, with essentially the same message but with an examination of a broader range of oil-exporting countries.[7] So why another book now, on what seems to be generally the same topic?

The need for sustained and equitable economic growth (and for social and political change) in the region is ever more urgent. Experts preach the pressing need for democracy in the Middle East and North Africa and invariably recommend that this come from the outside, and quickly. Yet they ignore the economic history of the past 50 years, especially since 1970: the role of oil, economic rape and pillage by autocratic rulers, governments, their relatives and close associates, economic mismanagement on the grandest of scales, the impact of internal and regional conflicts, and the resulting dissolution and despair of the region's general population, especially among its youth. The West has been a party to the region's economic decline. To address the prevailing malaise in the region, political change must be accompanied by radical economic change. The two must go hand in hand. A solution has to incorporate more than economic reforms, the message in my previous books. It is time to give this broader message in blunt terms so as to have a prayer of a chance of avoiding catastrophic social and political disaster in the future.

The message is simple enough. The Middle East (along with Sub-Saharan Africa) has been the worst economic performing region of the world over the past 25 to 30 years.[8] This is all the more surprising because a number of countries in the region have received a vast transfer of wealth in the form of oil revenues. While political instability, an unfavorable business climate, shortsighted and inconsistent economic policies and ineffective institutions have contributed significantly to the dismal performance of the countries in the Middle East, military expenditures, regional disruptions, conflicts, wars, contempt for the rule of law and pervasive corruption have also played a decisive role. All of this has been nurtured under oppressive political regimes that have had their own selfish survival as their primary goal. The Middle Eastern landscape of today is devoid of economic and social justice and is plagued by high levels of unemployment, lack of educational opportunities and little hope for economic advancement through determined hard work. In most cases, a bloated government sector is seen as the best source of employment opportunities. Generally speaking, the governments in the region are reluctant to make the difficult policy choices that would put them on the path of sustained economic growth but that might endanger their short-run survival. But the longer they wait, the more difficult their policy dilemma and the less likely their political survival will become.

1.3 PRESCRIPTION FOR A TURNAROUND

The major beneficiaries of the boom in oil revenues have been a few countries in the Middle East and North Africa. In this book, we take a detailed look at the performance of these countries relative to other countries in

Table 1.1 The examined countries

Selected Middle East oil-exporting countries (MEOE)	The comparison countries in the region	The comparison countries outside the region	Comparison country groups
Iran	Egypt	Chile	All developing countries
Iraq	Jordan	Malaysia	Sub-groups as available in World Bank data
Kuwait	Morocco	Singapore	High income
Qatar	Syria	South Korea	Middle and low income
Saudi Arabia	Tunisia		Middle East & North Africa
United Arab Emirates (UAE)			East Asia & Pacific
			World

the region and outside the region. Our aim is to present a broad picture of how the Middle East oil exporters (referred to as MEOE, see Table 1.1 for list of countries) have performed and where they stand today relative to other country groups (the world, all developing countries, other developing-country groupings) and to select countries, both in and outside the region. The comparison countries are used to provide a benchmark for assessing progress in the major oil-exporting countries; thus the basis for selecting these countries incorporates country size, oil exports, Muslim and non-Muslim countries, and economically high-performing countries. Has Islam indeed been followed in formulating economic and social policies? We hope to draw useful lessons and policy conclusions for reversing the region's dismal economic trend of the past 25 to 30 years and to emphasize why it is ever more important to achieve success as soon as possible. While we will generally refer to the post World War II era, our data and our detailed examination of facts will be focused on the period after 1975.[9]

The world is truly at a crossroads. The leaders of the Middle East and the West have to exhibit unprecedented statesmanship if we are to avoid even more pronounced turmoil in the future. A principled approach in a number of areas has to be sustained for many years before there can be a successful turnaround. There is no spigot that can be turned on and off, when it suits rulers in the region and their supporters in the West, to instill the rule of law, justice, stability and sustained economic growth and development.

NOTES

1. Those readers who have visited Abu Dhabi, Dubai and Qatar will think the author mad for saying that oil has been a curse. The depiction of oil as a curse here relates to the Persian Gulf region as a whole: a region where Iran's population is larger than the combined population of all the other countries bordering the Persian Gulf, and where the combined population of Iran, Iraq and Saudi Arabia represents over 95 percent of the region's population. As we will see, some of these small countries and sheikdoms are so rich in oil or gas that they would really have to try very hard not to be prosperous. At the same time, we should note that economic development is not synonymous with shiny buildings and malls. If you have the money, one of the large international engineering firms can build you a palace out of ice in the middle of the desert, or an indoor ski resort, if that's what you want. Again, this could hardly be called economic development.
2. The United Nations Development Program and the Arab Fund for Economic and Social Development, *Arab Human Development Report 2002: Creating Opportunities for Future Generations*.
3. Askari, Hossein and John T. Cummings, *The Economies of the Middle East in the 1970s: A Comparative Approach*. There are numerous definitions of what countries constitute the Middle East. We define the Middle East as Afghanistan, Iran, Iraq, Kuwait, Bahrain, the UAE, Saudi Arabia, Oman, Qatar, Jordan, Syria, Lebanon, Israel and the Palestinian Territories; and North Africa as Egypt, Libya, Tunisia, Algeria and Morocco.
4. Askari, Hossein, John T. Cummings and H. Reed, 'The Gulf: Gold Rush or Economic Development?'
5. This is contained in an appendix in Askari, Hossein, *Saudi Arabia: Oil and the Search for Economic Development*.
6. Askari, Hossein, *Saudi Arabia: Oil and the Search for Economic Development*.
7. Askari, Hossein, Vahid Nowshirvani and Mohamed Jaber, *Economic Development in the Countries of the GCC: The Curse and Blessing of Oil*.
8. Because the Middle East oil exporters rely so heavily on oil (for exports, government revenues and GDP), economic performance, such as GDP growth, fluctuates dramatically when oil prices change sharply. Oil prices moved significantly upwards during 2004–2005. Thus some of the calculations and conclusions in this volume do not capture this upward surge, which also occurred in 1973–74 and 1979–80. Such sharp annual movements in economic growth or per capita income underscore the fact that the economies of these countries are still significantly affected by oil prices and oil revenues.
9. To avoid data inconsistencies, our data is drawn largely from the World Bank's *World Development Indicators* and *Global Financial Indicators*, and from the United Nation's *Human Development Report*.