



Brandeis University

Crown Center
for Middle East Studies

Mailstop 010
Waltham, Massachusetts
02454-9110

781-736-5320
781-736-5324 Fax
www.brandeis.edu/crown

Middle East Brief

Judith and Sidney Swartz Director
Prof. Shai Feldman

Associate Director
Kristina Cherniahivsky

Assistant Director for Research
Naghmeb Sohrabi, PhD

Senior Fellows
Abdel Monem Said Aly, PhD
Khalil Shikaki, PhD
Yezid Sayigh, PhD

*Henry J. Leir Professor of the
Economics of the Middle East*
Nader Habibi

*Sylvia K. Hassenfeld Professor
of Islamic and Middle Eastern Studies*
Kanan Makiya

*Senior Fellow on the Myra and
Robert Kraft Chair in Arab Politics*
Asher Susser, PhD

President of Brandeis University
Jehuda Reinharz, PhD

The Impact of the Global Economic Crisis on Arab Countries: A Year-End Assessment

Prof. Nader Habibi

This Middle East Brief explores how Arab countries have been impacted by the global economic crisis that began in the summer of 2008. In terms of integration into global financial markets, the Middle East falls behind all other emerging-market regions other than Africa; but although a lower level of financial integration is a disadvantage under normal circumstances, it can protect an emerging region when the global economy sinks into a severe financial crisis. In this case, however, the Middle East and North Africa (MENA) region is affected by global economic conditions through fluctuations in the oil market—and some MENA countries have developed strong economic linkages with the global economy that go beyond oil. North African nations maintain strong trade and investment relations with Europe, while the oil-rich countries of the Gulf Cooperation Council (GCC) have accumulated a large portfolio of financial and equity investments in advanced economies. All these factors increase these economies' exposure to global economic downturns.

The global crisis began with a financial meltdown in the United States and Europe in early 2008; within a short period of time it had spread to the rest of the world. In the early stages of the crisis, large international banks that had overinvested in risky real estate mortgages suffered severe losses as real estate prices declined in 2007. The insolvency of major financial institutions

and the erosion of household wealth in real estate and equity markets in turn led to a sharp decline in investor and consumer confidence. While the quick interventions of Western governments prevented their economies from plunging into depression, the sharp decline in consumer and corporate spending pushed the U.S. and European economies into the worst recession since World War II. This worldwide economic slowdown led to a sharp decline in the demand for oil, food, and other commodities.

The Effects of the Crisis: Channels of Transmission to Arab Countries

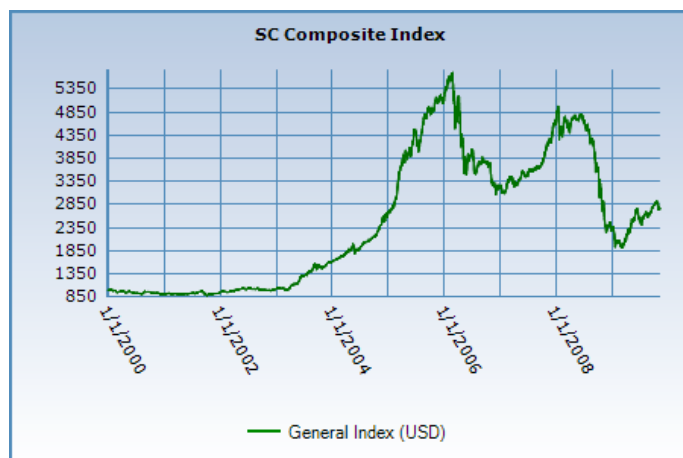
The global crisis was transmitted to Arab economies through several distinct channels: the financial markets, the crude oil market, Arab investments in global asset markets, tourism, the remittance income of Arab workers, and the region's non-oil exports, originating primarily in North Africa and destined for Europe.

Financial Markets

The financial sector was the initial pathway. The first financial shock wave was felt in regional stock markets, which had traditionally suffered from high degrees of volatility. These markets received large volumes of new investment during 2004–7 as a result of the inflow of record-high oil revenues and the repatriation of their foreign investments by some Arab private investors after the September 2001 attacks. Some countries such as Egypt and Jordan, which had previously liberalized their financial markets, experienced especially sizeable foreign investment inflows. In the meantime, Arab stock markets remained highly volatile.

Financial institutions and real estate developers are among the largest publicly listed companies in Arab markets, and both were adversely affected by the global financial crisis. The global crisis sharply reduced the flow of foreign investment into real estate; as a result, the uptrend in real estate prices in the Middle East, which had lasted for several years, came to an end in 2008. This development put severe pressure on real estate construction firms and encouraged sell-offs in regional stock markets. In turn, the end of real estate speculation sharply increased mortgage defaults, and as a result many listed commercial banks came under financial distress. These developments, along with the decline in the price of oil, led to a sharp decrease in stock prices after June 2008, as demonstrated in Chart 1 below.

Chart 1. Composite index of Arab stock markets



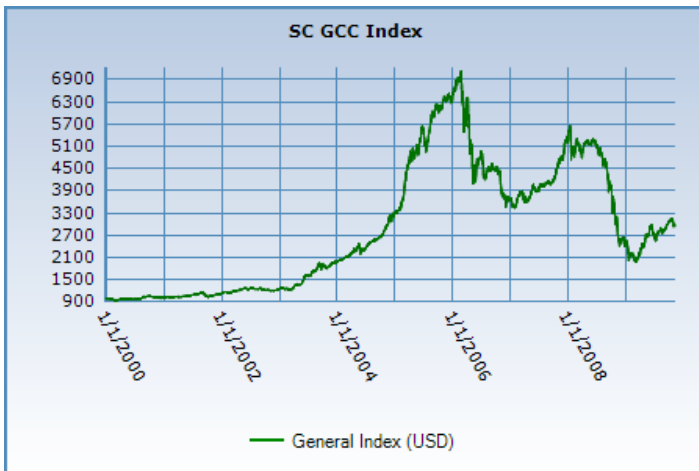
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Nader Habibi is the Henry J. Leir Professor of the Economics of the Middle East at Brandeis University.

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Stock price volatility was even more severe in GCC countries as compared with other Arab countries, as demonstrated in Chart 2. Between January 2008 and March 2009 all GCC stock indexes suffered sharp declines (in the range of 40% to 65%). These declines, which were partly caused by the troubles of banks and financial institutions, caused additional financial losses for the banks and led to a vicious cycle. Although these banks had limited exposure to global financial markets, they maintained large investments in local stock markets and loaned large sums to private entities for investment in these markets. Consequently, when stock prices fell, many banks suffered a large number of loan defaults and asset value losses. These losses were more severe in GCC countries and forced GCC governments to take various measures to support their stock markets and banking systems.

Chart 2. Composite index of GCC Stock Markets



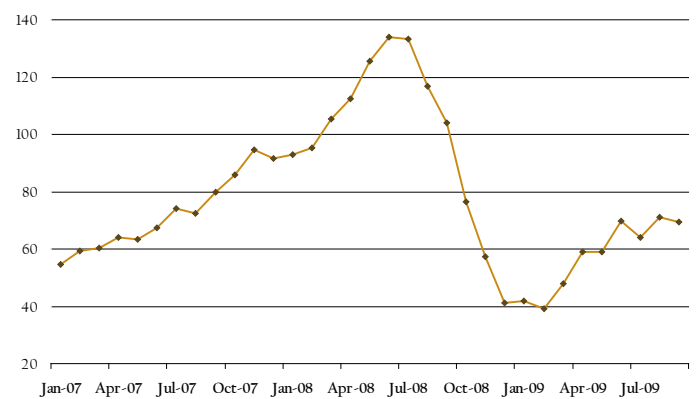
Source: SHUAA Capital psc, www.shuaacapital.com. Reproduced with permission.

Nowhere in the Arab world was the real estate boom as large or as rapid as in Dubai (one of the seven Emirates that constitute the United Arab Emirates). Dubai's massive real estate market was dominated by speculators and international investors; many of these investors took advantage of the attractive mortgages offered by regional banks. In most cases, investors were able to finance a real estate purchase with as little as a 5% down payment (95% financing), and the prices kept rising. By 2008, Dubai's real estate market had become highly speculative, and when real estate prices in the United States and Europe began to fall, the demand for real estate in Dubai diminished. In 2009, real estate prices in Dubai suffered a large decline, and the inventory of unsold properties grew sharply. As a result, many construction projects were abandoned as the developers and their financial backers suffered heavy losses. Dubai's crisis attracted worldwide attention in November 2009 when the state-owned conglomerate Dubai World, which owns several construction firms, announced that it was unable to service its debt.

Oil

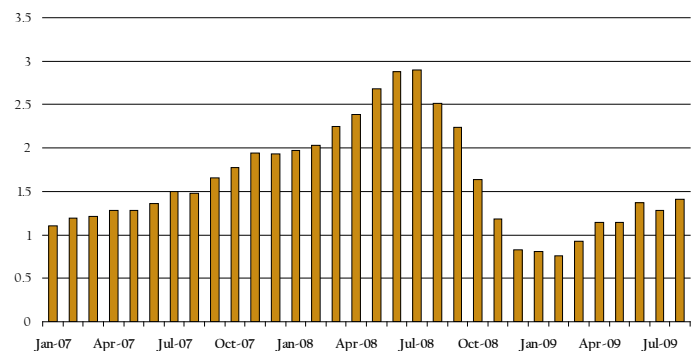
The second channel for transmission of the global economic crisis to MENA Arab countries was the oil market. The global recession led to a decline in the demand for crude oil, which triggered a sharp decline in its price. After reaching a peak of \$133 per barrel in July 2008, the price of oil fell more than 70%, to an average of \$39 per barrel in February 2009. (See Chart 3.) During this period, OPEC members also implemented a production cut (effective January 1, 2009) to stabilize the price. The combination of lower price and reduced output in Arab oil-exporting countries led to a significant loss of oil revenues for those countries, as demonstrated in Chart 4.

Chart 3. Price of crude oil in arab oil-exporting countries (West Texas Intermediate, monthly average \$/barrel)



Source of data: U.S. Energy Information Administration, www.eia.doe.gov.

Chart 4. Arab Oil-exporting Countries: Daily value of oil output (in billions of \$)



Source of data: U.S. Energy Information Administration, www.eia.doe.gov. Author's calculations based on monthly average price of crude oil (WTI) and aggregate daily oil output of Arab oil exporting countries (excluding Iraq).

The sharp decline in oil revenues reduced the fiscal revenues of oil-exporting Arab countries, but it did not lead to a significant reduction in fiscal spending. According to a recent study by the International Monetary Fund (IMF), the relative size of central government revenues as a percentage of gross domestic product (GDP) in MENA

oil exporters reached a record high of 43.2% in 2008 but is projected to decline to 35.5% in 2009; central government expenditures, on the other hand, are expected to grow from 29% of GDP in 2008 to 33.6% of GDP in 2009.¹

Furthermore, the data reported in the same IMF study reveal that while the fiscal revenues of Arab oil exporters (excluding Iraq) are expected to decline by an average of 38% in 2009, fiscal expenditures will be only 2.4% smaller than in 2008.² In five oil-exporting countries (Algeria, Oman, Qatar, Saudi Arabia, and UAE), fiscal spending is expected to be larger in 2009 compared with 2008, despite lower oil revenues. In most cases this increase results from deliberate expansionary fiscal policies initiated in response to the economic crisis. Saudi Arabia, for example, has tried to offset the decline in private spending by increasing fiscal expenditures from 29.6% of GDP in 2008 to a projected 40% in 2009.³ In addition, Arab oil exporters accumulated large oil revenue surpluses during 2005–7 and were able to tap into these surpluses to cover oil revenue shortfalls in 2008 and 2009.

The falling price of oil during 2008–9 was a mixed blessing for oil-importing MENA countries. The lower prices reduced their energy import bill and helped them improve their trade imbalance; but the lower oil revenues of oil-exporting countries reduced those countries' investments and tourism expenditures in other Arab countries. Oil-importing Arab countries such as Morocco, Egypt, and Jordan, which enjoyed increasing flows of GCC investment during the three years up to the first half of 2008, experienced a noticeable decline in these investments during the second half of 2008 and the first half of 2009.

Foreign Assets of Arab Investors

A third channel for the transmission of the global crisis to the Middle East was the decline in value of the foreign assets of GCC countries and Libya. The sharp increase in these countries' oil revenues during 2003–8 caught their governments by surprise. Mindful of the volatile nature of oil revenues in the previous three decades, they did not increase their fiscal spending at a fast pace; instead, they transferred a sizeable portion of their windfall oil revenues into their Sovereign Wealth Funds (SWF), which in turn invested them in global markets. As the size of these funds grew over time, however, SWF managers concluded that investing these large sums in bank deposits and U.S. government bonds was no longer a sound long-term strategy, because low-risk assets offered very low rates of return. Beginning in 2007, Arab SWFs, along with their Asian counterparts, increased their investments in equities and real estate. Some invested in U.S. and European financial institutions, such as Citigroup and Merrill Lynch, which subsequently suffered heavy losses. As a result, the sharp decline in the stock markets and real estate prices

in the U.S. and Europe resulted in large losses for the Arab SWFs.

The exact size of these losses is unknown, but it is likely that Arab SWFs lost approximately 15% of their asset values by March 2009.⁴ These funds still hold sizeable assets, however, in excess of \$1,500 billion, and the decline in their value did not cause financial difficulties for their respective governments.⁵ Indeed some GCC governments, such as Qatar, tapped into these funds earlier this year to support their stock markets and financial institutions. Nevertheless the declining value of their SWFs has forced these governments to be more cautious about their ambitious and expensive development projects.

Tourism

Several MENA countries—especially Egypt, Morocco, Tunisia, Jordan, and Lebanon—rely heavily on tourism as an important source of service sector jobs and foreign exchange revenue, and the global recession of the past two years has reduced the number of foreign tourists in the Middle East. Egypt reported a 9.5% decline in revenue from tourism in the first half of 2009 as compared with the first half of 2008.⁶ Hotel occupancy rates in Dubai and Abu Dhabi (capital of the UAE) declined by 16% and 7%, respectively, in the first four months of 2009 vis-à-vis the same interval in 2008.⁷ During the summer however, while the flow of Western and Asian tourists remained below normal, Arab tourist arrivals increased. This was also owing to the global economic crisis, as many Arab families who usually vacationed in Europe or North America were forced to choose less expensive destinations, within the region. This increase in intraregional tourism has partially offset the decline in international tourism for many Middle Eastern destinations; but at the aggregate level, all Middle East countries have experienced a decline in tourist arrivals and tourism revenue in the first half of 2009.

Remittances

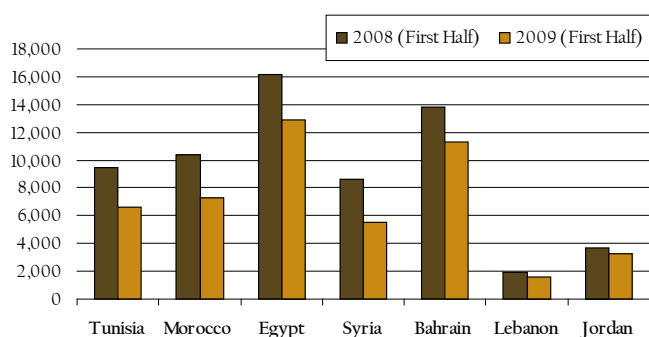
For several Arab countries, remittances are an important source of income. Worker remittances in Jordan, Morocco, Egypt, and Tunisia accounted in 2007 for 22.7%, 9%, 6%, and 5%, respectively, of their GDP.⁸ The remittance incomes of Arab countries enjoyed positive growth in 2008 before being adversely impacted by the global crisis in 2009: The economic downturn in Europe has reduced job opportunities for North African workers, and as a result, the volume of remittances has diminished. Morocco, for example, reported a 12.5% decline in its remittances between June 2008 and June 2009.⁹ Though the experience of most MENA countries is similar to Morocco's, Tunisia reported an 8% increase in its remittance revenue over the same period¹⁰—owing mainly to the higher skill level of Tunisian migrant workers as compared with workers from other Arab countries.

Another Arab country that has enjoyed strong remittances in 2009 despite the global economic crisis is Lebanon. Contrary to IMF and World Bank projections for a 12.5% decline in remittances in 2009, the latest World Bank projection shows that Lebanon's remittances are expected to decline by only 2.5%. Overall, however, for the twelve MENA countries included in the World Bank analysis, 2009 remittances are expected to be 7.2% lower than in 2008.¹¹ For Lebanon, Egypt, Jordan, and Yemen, the GCC countries are a major source of remittance income; slowdowns in tourism and real estate construction in GCC countries have reduced job opportunities for migrant workers, and many have returned home.

Non-oil Exports

The relatively closed financial systems of most MENA countries shielded them from the financial crisis—the first wave of the global crisis. However, these countries were unable to escape the adverse impact of the severe worldwide economic recession that followed—the second wave. The impact of the global slowdown on tourism, oil revenues, and remittances has already been noted. For the North African countries, which have strong economic links with Europe, the economic recession in that region led to a noticeable decline in their merchandise exports. Thus Egypt, Morocco, and Tunisia have reported sharp declines in their exports of agricultural and manufactured products in 2009. (More than 70% of Morocco's total exports go to Europe; the comparable figure for Tunisia is 80%.) As shown in Chart 5, merchandise exports for five Arab oil-importing countries during the first half of 2009 as compared with the first half of 2008. Chart 5 also demonstrates that the exports of Jordan and Lebanon have been more resilient than those of other Arab oil-importers.

Chart 5. Merchandise exports of MENA countries, 2008 vs. 2009

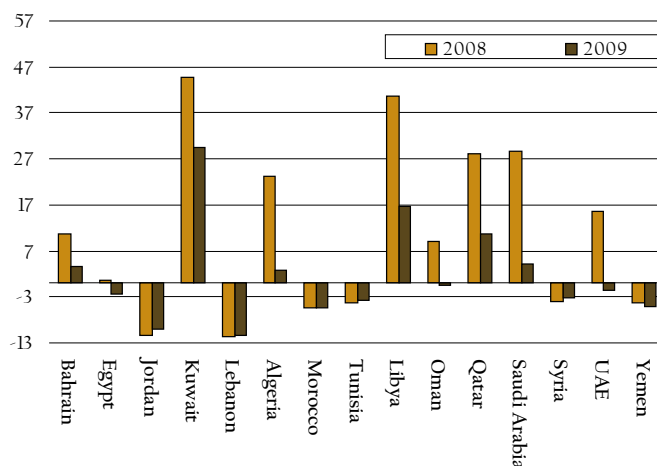


Source of data: Direction of Trade Statistics, IMF

As shown in Chart 6, based on the most recent IMF projections, the decline in exports of merchandise goods has not caused deterioration in the current account balances of Tunisia, Lebanon, Jordan, and Syria in 2009. For these oil-importing Arab countries, the lower cost of

oil imports is expected to have offset the decline in export revenues; as a result, their current account deficits (as a percentage of their GDP) will be moderately smaller in 2009 as compared with 2008. On the other hand, the oil-exporting Arab countries have experienced sharp declines in their current account surpluses in 2009 because of the continued strength of imports. For the United Arab Emirates, for example, the current account imbalance is projected to shift from a surplus equivalent to 15.6% of GDP to a 1.5% deficit. The actual surpluses of oil-exporting Arab countries, however, might be larger than these IMF projections owing to the unexpected strength of oil prices in the second half of 2009.

Chart 6. Current account balances as percentages of GDP



Source of data: IMF, *World Economic Outlook Database* (October 2009, www.imf.org). 2009 values are IMF projections.

The Policy Response of Arab Governments

As the economies of Arab countries were impacted by the global crisis, Arab governments resorted to a variety of measures, similar to those adopted by other governments worldwide, to mitigate the negative consequences. In most countries this involved a mix of monetary and fiscal stimulation along with stricter financial regulations. The relative weight of these measures in each country, however, reflected the unique circumstances of its economy. A recent IMF study offers a detailed breakdown of the financial and monetary policy responses of each MENA country.¹² Since financial institutions and stock markets were among the first institutions to show weakness, the first policy response in many countries was to support their commercial banks by providing credit support and liquidity. Among oil-exporting countries, Kuwait, Saudi Arabia, the UAE, and Libya strengthened their banking systems by offering their commercial banks deposit guarantees. The only oil-importing Arab country to adopt this policy, however, was Jordan. Egypt enhanced its already existing deposit guarantee, and such a policy was also already in place in Morocco.

In addition, the governments of Kuwait, Qatar, and the UAE injected capital directly into financial institutions (by increasing the size of government deposits in commercial banks), while Kuwait, Oman, Qatar, and Libya made similar interventions in their equity markets to support share prices. In the second half of 2008, the Kuwait Investment Authority invested \$4 billion in that country's stock market to support the listed local firms.¹³

These financial measures were complemented in many countries by fiscal stimulus. In general, oil-exporting Arab countries introduced larger fiscal stimulus packages compared with the oil importers. Among GCC countries, the largest fiscal expansion was implemented by Saudi Arabia, which increased its government spending by 9.3%, from \$138.9 billion in 2008 to \$151.8 billion in 2009, despite lower oil revenues. Other oil-exporting countries with substantial fiscal expansion policies in 2009 were Algeria (6.6%), Qatar (4.8%), and UAE (4.9%).¹⁴ Fiscal expansion was also noticeable in Egypt and Syria, which maintain smaller daily oil outputs: Egypt's 2009 budget grew by 14.6%, while Syria's rose by 7%. Egypt launched its first fiscal stimulus package, worth \$2.7 billion (1.5% of GDP), in September 2008. This money was spent on accelerated investments in public utilities and infrastructure projects.¹⁵

Among oil-importing countries, Lebanon experienced significant fiscal growth in 2009 (up 19.7%)¹⁶. Jordan, Morocco, and Tunisia, on the other hand, have adopted smaller fiscal budgets for 2009 in comparison with 2008. This is partly owing to revenue constraints and high sovereign debt, which has discouraged additional borrowing. In general, fiscal stimulus programs result in budget deficits—which, in oil-importing countries, must be financed by additional borrowing. According to IMF estimates, Morocco's 1.8% fiscal surplus in 2008 will be replaced by 2.3% and 2.2% fiscal deficits in 2009 and 2010, respectively.¹⁷

The Impact of the Crisis on Economic Performance

Economic Growth

While the global economic crisis has led to recession and negative economic growth in many parts of the world, its impact on the Middle East has been relatively mild. For all MENA countries with the exception of Kuwait, the impact in 2009 has been limited to growth slowdown rather than economic decline. (While some MENA countries experienced negative growth for one or two quarters in early 2009, for the year as a whole their economic growth rate is estimated by the IMF to have been positive.) For the oil-exporting MENA countries, the slower economic

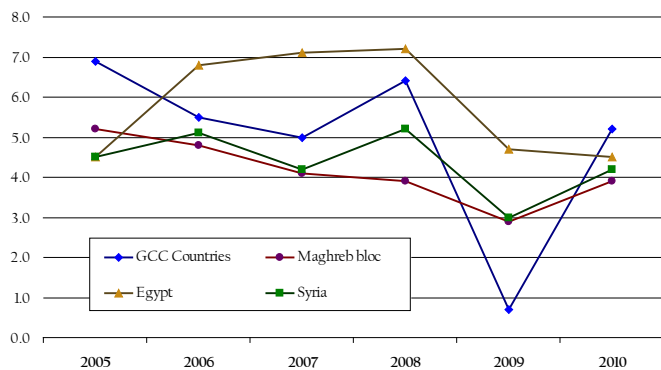
growth is partly due to a decision by OPEC to reduce its oil output by 2.2 million barrels per day (7.5% of the cartel's total oil output in December 2008), effective January 2009. Implementation of this decision led to a reduction in the value of Arab oil exporters' oil sector GDP in real terms. For GCC countries, for example, oil sector output is projected to have suffered a 5.2% decline in 2009.

Economic activity in the non-oil sector of the GCC countries has been adversely affected by a slowdown in real estate activity (the extent of which varies from country to country) but has benefited from the fiscal and monetary stimulus that was discussed above and is expected to show moderate positive growth in both 2009 and 2010. This growth, however, will be partially offset by weak performance in the oil sector.¹⁸ In the case of Saudi Arabia, which is the largest oil producer in the Middle East, the non-oil sector is expected to have grown by 3.3% in 2009, but this will be more than offset by an estimated 10.3% decline in oil sector GDP, and the Saudi economy as a whole is expected to suffer an 0.9% decline. For GCC countries as a group, economic growth is projected to have slowed down from 6.4% in 2008 to 0.7% in 2009, but it is projected that this will be followed by a strong recovery, to 5.2% growth, in 2010.

In the oil-importing countries, the tourism and export sectors have suffered as a result of the weakness in global demand, but government stimulus programs have partly made up for this decline. As shown in Chart 7, after enjoying solid economic growth during 2005–8, the Arab economies have grown at a much smaller pace in 2009. Chart 7 also reveals that the projected slowdown in oil-importing MENA countries in 2009 is not as severe as in oil-exporting countries—however, while all Arab countries are projected to enjoy higher growth rates in 2010, the oil exporters are expected to recover at a moderately faster rate than the oil-importers.

The slowdown in MENA economies as a group is not significantly different from that in other emerging market economies. The economic growth rate for the emerging market and developing market economies as a group fell from 6% in 2008 to a projected 1.9% in 2009.¹⁹ The MENA oil importers fared better than this: All of them enjoyed 3% or more growth rates in 2009. The MENA oil exporters, on the other hand, grew by only 1.4%.

Chart 7. Real GDP growth in the Middle East and North Africa (Annual growth in %)



Source of data: IMF, World Economic Outlook, 2009. 2009 and 2010 values are IMF projections. Note: The Maghreb bloc in this chart comprises Algeria, Morocco, and Tunisia.

Unemployment and Poverty

Although the adverse impact of the global economic crisis has been moderate in most Arab countries, the impact on employment and household incomes has been significant in some countries. The International Labor Organization (ILO) has estimated that the unemployment rate in the Middle East and North Africa has increased by 25% and 13%, respectively, in the period from 2007 to 2009.²⁰ A mid-October assessment by the ILO put the 2009 unemployment rate in the Arab world in the 9%–11% range.²¹ Yet the Arab Labor Organization has estimated the unemployment rate in the Arab world at a much higher rate of 17% as of December 2009 and has blamed the current global crisis for the loss of hundreds of thousands of jobs in Arab countries.²²

The decline in manufacturing and in tourism—which is a labor-intensive industry in Morocco, Tunisia, and Egypt—has taken a toll on low-income workers. According to a recent study by the Center for Trade Union and Workers Services in Egypt, more than 347,000 job opportunities in that country were lost during the second half of 2008 as a result of the economic crisis²³: The total unemployment rate in Egypt rose from 8.4% in the fourth quarter of 2008 to 9.4% in the first and second quarters of 2009. The latest official data, however, show a decline to 9.3 in the third quarter, which could point to a gradual improvement in the labor market in the second half of 2008.²⁴

In Morocco, the unemployment rate rose in 2008 and in early 2009, but a moderate improvement has since been reported in 2009—owing mainly to favorable climate conditions, which have led to increased agricultural activity; employment in the industrial sector is still weak and contributes to high urban unemployment (12.6%). Despite increased government support for the export-oriented industries, some 7,000 industrial and handicrafts jobs disappeared in the second quarter of 2009 as a result of

declining exports.²⁵ In Tunisia, which has a larger industrial base, the overall unemployment rate remained high at 14% in 2009²⁶.

The decline of real estate construction and industrial activity in oil-rich Arab countries has forced tens of thousands of Arab migrant workers to return home, and their return has put added pressure on labor markets in Egypt, Jordan, Morocco, and Yemen. The decline in remittance income, along with rising unemployment, has increased the incidence of poverty in many Arab countries. Based on available household income statistics in developing countries, the World Bank uses two thresholds to measure extreme poverty, which are periodically revised. According to the most recent revisions, these thresholds are \$1.25 and \$2.00 per capita income per day when measured in internationally comparable prices.²⁷

While the incidence of extreme poverty (per capita income under \$1.25 per day) in the Arab world is very small (less than 5%), nearly one-fifth of the population in Arab countries earn less than \$2 per day. The economic slowdown has put this segment of the population at risk of falling into extreme poverty.²⁸ Furthermore, the number of people earning between \$2 and \$3 per day is also substantial, and the income level of this group is also at risk on account of the global economic crisis. World Bank poverty statistics reveal that among the combined population of Algeria, Egypt, Jordan, Morocco, Tunisia, and Yemen, 48.1 million people earned less than \$2 per day in 2001, while 37.1 million earned between \$2 and \$3 per day.²⁹

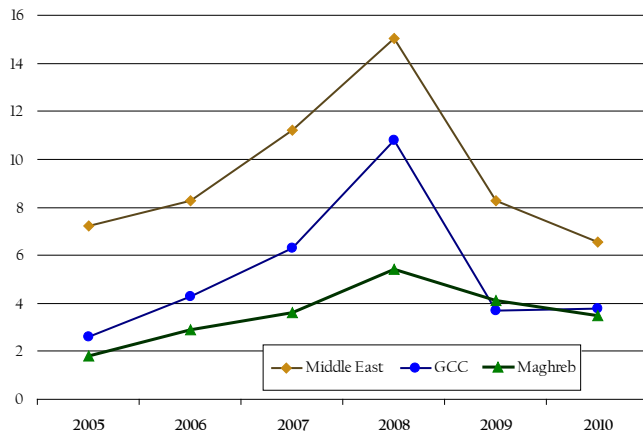
In Arab countries with the highest percentages of the population under the poverty line (the Palestinian territories, Yemen, Algeria, and Egypt), economic stimulus programs alone will not be enough to create an adequate number of new jobs and prevent an increase in poverty in the short run. If current economic stagnation continues or the economic recovery proceeds at a slow pace, a large number of households in these countries will be at risk. To relieve the economic hardship of these at-risk households, the governments involved would have to implement direct anti-poverty programs.

Inflation

One positive outcome of the global economic crisis for the Middle East is the reversal of rising inflationary trends. Fiscal expansion and the rapid injection of record-high oil revenues during 2005–8 had put upward pressure on prices in many MENA countries. This upward pressure was most visible in oil-exporting GCC countries, which had traditionally enjoyed low inflation rates. Their economies were clearly heating up, and most employees were concerned that their wages were not keeping up with the prices of consumer goods. (See Chart 8.) Qatar, which had enjoyed a moderate 2.5% average annual inflation rate from 2000 to 2004, saw

inflation rise to 15% by 2008. Saudi Arabia's annual inflation rate rose from an average -0.2% *negative* rate during 2000–2004 to a record 9.9% by 2008.

Chart 8. Annual inflation rate, 2005–10)



Source of data: IMF, *World Economic Outlook Database*, October 2009. 2009 and 2010 values are IMF projections.

In GCC countries, the cost of industrial goods, and of professional services in the oil sector, was also rising rapidly. The sudden increase in oil and gas sector investments worldwide resulted in a shortage of oil- and gas-related engineering equipment and services, which led to noticeable cost overruns and delays in related projects as of early 2008. The global economic recession has reduced the demand for such equipment and services, thereby eroding these shortages, and as a result, prices have become more affordable. A similar development has emerged with respect to construction costs in the real estate sector. The average inflation rate in GCC countries is estimated to have declined from 10.8% in 2008 to 3.7% in 2009.

For oil-importing Arab countries, the decline in the price of oil in late 2008 and early 2009 has been a blessing in disguise. A decline in the cost of energy, along with the overall economic slowdown, has helped moderate the inflation rate in these countries. In Lebanon, the inflation rate rose to a record 14.9% in 2008 before declining to a negligible 0.2% in 2009—and significantly lower inflation rates are also estimated for other Arab oil-importing countries in 2009. Furthermore, the IMF expects inflationary pressures to remain subdued during 2010 as Arab economies gradually recover.

Conclusion

The global economic crisis which began in the second half of 2008 impacted Arab economies through several transmission channels. The flow of foreign investment into the region diminished; the crude oil market experienced

a significant price correction after having reached record-high levels as of mid-2008; international tourism to Middle Eastern destinations declined; and there was a reduction in global demand for the region's non-oil exports. Depending on their exposure to each of these transmission channels, different Arab countries were impacted differently by the crisis.

Oil-exporting countries suffered from a reduction in oil revenues and had to adjust their ambitious development projects accordingly. The GCC countries, however, were able to sustain their government-supported development projects by tapping into their large Sovereign Wealth Funds. They also intervened proactively to protect their financial markets, which were hit hard because of the decline in real estate prices.

The North African countries were hurt most by the severe recession in Europe, which reduced their export, tourism, and remittance revenues. These governments introduced economic stimulus measures to beef up domestic demand. While these steps helped reduce the adverse impact of the global crisis on economic growth, thousands of jobs in tourism- and export-related industries were lost, and poverty has increased. One of the important challenges facing the governments of many Arab countries is to carefully monitor the condition of vulnerable low-income households and provide them with more economic assistance in these difficult times.

While no Arab country has escaped the adverse effects of the global economic crisis, the impact on most countries has been only a slowdown in economic growth rather than an actual economic decline. There are three reasons why the impact remained mild: The region's relatively low integration into global financial markets protected its economies from some of the downturn; economic stimulus policies implemented by the region's governments offset some of the negative consequences of the crisis; and strong economic growth in most Arab countries during 2007–8, prior to the crisis, afforded them a cushion against the subsequent contraction. Alongside its adverse effects, the global recession had at least one positive impact on MENA economies: It reduced the inflationary pressures that had built up in 2008 in most Arab countries, particularly in GCC countries.

The controversy revolving around Dubai World's unexpected debt service default led to fears that it might snowball into a regional financial crisis, with adverse implications for many Arab countries. Yet it is now clear that the impact of Dubai World is confined to the economy of Dubai and, to a lesser extent, that of the United Arab Emirates; there is no evidence that it has had a significant direct impact on other Arab countries. This is in part

owing to Dubai's unique development strategy. In Dubai the government tolerated excessive speculation in the real estate sector, with high levels of foreign participation and financing. When the global crisis sharply reduced the flow of foreign investment, Dubai property values declined, and large real estate firms, such as the giant real estate developer Nakheel (which is owned by Dubai World), faced heavy losses.

Other GCC countries have also experienced some volatility in their real estate markets in the past two years, but since they limit property ownership to their own citizens (plus, in some cases, the citizens of other GCC countries), they have not experienced a large sell-off by foreign investors. Furthermore, in some GCC countries, such as Qatar, the government has stepped in to purchase the bad assets of domestic banks so as to avoid a financial crisis. What affords these economies more stability than Dubai is their large oil revenues and government reserves, which can be used to stabilize their domestic asset markets and protect their financial institutions.

Endnotes

Two students at Brandeis University, Dan Roffman and Georges Fadel, have provided valuable research assistance for this study.

1 International Monetary Fund, "Regional Economic Outlook: Middle East and Central Asia," October 2009, Statistical Appendix Tables 8 and 11.*

2 Ibid.; author's calculations based on Statistical Appendix Tables 2, 8, and 11 in this report.

3 Ibid., Statistical Appendix Table 11.

4 I base this estimate on the assumption that Arab funds maintained approximately one-third of their assets in equity stock and real estate in Western countries. Equity assets lost nearly 50% of their value during the twelve-month period ending in March 2009; accordingly, the losses incurred by Arab SWFs amounted to one-sixth (approximately 15%) of their entire total assets. In a recent report, the financial losses of the Kuwait Investment Authority and the Abu Dhabi Investment Authority were estimated to be \$31 billion and \$125 billion, respectively ("Post-Financial Crisis Outlook: What's Ahead for Sovereign Wealth Funds?" *The Capital Express*, September 18, 2009.)* Given that the value of these funds' assets immediately before the crisis was estimated at \$200 billion and \$850 billion, respectively, their relative losses amounted to approximately 15%, which is in line with my estimate for Arab funds.

5 For a recent review of the asset value of GCC foreign assets, see Nader Habibi, "Managing the Oil Wealth: Foreign Assets of GCC Countries" (*Crown Paper 1*, June 2008), Crown Center for Middle East Studies, Brandeis University.*

6 "Egypt Tourism Revenue Fell 9.5% in First Half," *AMEinfo.com*, July 15, 2009.*

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Brandeis University Crown Center
for Middle East Studies

Mailstop 010
Waltham, Massachusetts
02454-9110

781-736-5320
781-736-5324 Fax
www.brandeis.edu/crown

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