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Public Finance in the Arab Countries

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IDRC-MR135e

PUBLIC FINANCE IN THE ARAB COUNTRIES

edited by Giacomo Luciani

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FOREWORD

The structure of public finance in the Arab countries has certain peculiar characteristics that deeply affect the conduct of economic policy and prospects for development.

Oil revenue is by far the most important source of government finance in many countries. Non-oil producing countries also benefit from it in various forms: direct subsidies, transit tolls for passage through the Suez Canal or pipeline transportation, migrants' remittances. The latter do not accrue directly to the state treasury, but are indirectly taxed mainly through customs duties, as they cause an increase in the demand for imports.

There is little doubt that the complex mechanism of oil rent circulation in the region has increased the financial means available to practically all Arab states, the only exceptions possibly being Morocco, Mauritania, Somalia and Djibuti. At the same time, it has discouraged the development of a modern taxation system again with the possible exception of Morocco.

As Oualalou and Jaidi clearly show in their chapter, the taxation systems have only marginally been modified since independence, and different systems found in each Arab country still mostly reflect different colonial experiences. Certain countries inherited an income taxation system pre-dating the oil era, in others there is no direct income tax worth speaking of, although, as Gharaibeh points out for Jordan, attempts are being made to reducing dependence on subsidies, custom revenue and indirect taxes.

The lack of a well developed income tax has momentous consequences for the conduct of economic policy. Income taxation is a fundamental tool to control liquidity and contrast inflation; it is also an effective and visible redistributive tool. When governments are deprived of this tool, income redistribution can be pursued only through the expenditure side, leading to uncontrollable deficit spending, of which the consumption subsidies that are common to all Arab countries are the clearest example. Thus calls for greater financial orthodoxy necessarily come to mean that real income distribution should be allowed to worsen.

Under the present structure of state revenue, economic growth often leads to a worsening of the state deficit, as expenditure tends to increase more rapidly than revenue. Growth is also almost inevitably accompanied by income polarisation, leading to social and political protest. The evolution in the pattern of state expenditure is discussed in the chapters by Mona El Baradei and Khaled El Manoubi, pointing to strong similarities and common dilemmas that Arab states face.

Fiscal constraints are the immediate and prosaic cause of many an ideological turnaround, as 'socialist' production units commonly fail to generate a surplus and become constant drains for public resources. This point is well documented in the chapter by Oualalou and Jaidi, and is further discussed in the case of agriculture in the chapter by Hamid Ait Amara. Faced with a growing deficit in their agricultural balance, Arab governments have ceased to view agriculture as a sector that should be squeezed to sustain the industrialisation effort.

The limited yield of Arab taxation systems, coupled with the decline in oil prices that has been evident for much of the 1980s, and has now become a full-scale rout, is one of the causes of increasing indebtedness of the Arab countries. Azzam Mahjoub clearly documents a negative trend, which could lead some Arab countries to face problems of a magnitude comparable to that of the Latin American debtors.

In view of the importance of migrants' remittances, a chapter (written by Ibrahim Saadeddin Abdallah) was specifically devoted to their influence on economic policies of the countries of origin and on the possibility of taxing this important source of income.

Finally, two chapters by Hazem El Beblawi and Mahmoud Abdel Fadil are devoted to an analysis of rentier economies at the micro and macro level respectively. The dominant role played by the oil rent has in fact multiple consequences alongside the underdevelopment of taxation systems, that affect the very possibility of redressing the situation, and reducing the reliance of the state on sources of revenue from outside the national economy.

It is hoped that this collection of essays will serve the purpose of underlying the importance of developing modern taxation systems, and in particular direct income taxation, and reduce dependence on an unstable oil rent.

Research for the papers in this collection was made possible by a generous IDRC grant to the Istituto Affari Internazionali of Rome, which came to complement an existing interdisciplinary research program on the foundations and nature of Arab states.

Although the latter dealt with ideological, historical, social and political considerations as well, it was clear from the beginning that economic variables, and in particular public finance structures, are of paramount importance to an overall understanding of Arab states. The broader research program will lead to the publication of four collective volumes (The Arab State: 1. Foundations, edited by G.Salamè; 2. The Rentier State edited by H.Beblawi and G.Luciani; 3. Beyond Coercion, edited by A.Dawisha and I.W.Zartman; 4. Integration and Arab Politics, edited by R.Aliboni and A.Cudsi; Croom & Helm, 1987, London) in which some of the IDRC supported papers will also appear. Readers who have an interest in such interdisciplinary approach are referred to those.

In order to allow for mutual criticism and discussion, the authors of these papers were invited to participate in three international gatherings, which took place respectively in Corfu in September 1984, Alexandria in April 1985, and again in Corfu in September 1985. The meetings in Corfu were organised in cooperation with the Pantios School of Political Science.

Andrew Watson encouraged this project and provided precious criticism and suggestions. I am grateful to him for all of them, but I am even more grateful to him for his friendship. The latter was very appreciated in countering the frustrations of organising collective research under sometimes difficult conditions.

The shortcomings of this work are my responsibility. I only wish that, in accordance with IDRC's main purpose, participation into this effort will have been instrumental in improving the understanding on the part of my Arab friends of the problems of their beautiful countries.

Giacomo Luciani
Istituto Affari Internazionali
May 1986

Chapter 1

FISCAL RESOURCES AND BUDGET FINANCING IN THE COUNTRIES OF THE MAGHREB (ALGERIA, MOROCCO, TUNISIA, LIBYA AND MAURITANIA)

Fathallah Oualalou and Larbi Jaidi

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

The failure of policies aimed at mobilising the economic surplus is shown by the quantitative and qualitative limits of domestic tax revenue, and obliges all Maghrebi countries, with the exception of Libya, to look for international credit. Debt accumulated by Morocco, Mauritania, and to a lesser extent Tunisia, provoked a gradual worsening of international and domestic financial equilibria, and led the states to follow restrictive policies on consumption and public investment, following the classical recipe of the IMF. In Algeria as well as in Libya, oil revenue still allows a situation of relative financial ease, although it has fallen very considerably since 1982.

Notwithstanding attempts at fiscal reform presently underway in Morocco, it is correct to conclude that in all five countries it is the oil rent and/or foreign credits that determine the way in which the budget is financed, and the state has no incentive to reform and reinforce its fiscal instruments.

It is impossible to study fiscal resources in the Maghreb countries without considering other financial sources of support, mostly from abroad. In this context, we shall analyse the role of fiscal resources in the financing of the budget in Algeria, Morocco, Tunisia, Libya and Mauritania; a general comparative synthesis will be offered at the end of the chapter.

ALGERIA

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

In a dynamic perspective, the ratio of oil revenue relative to other sources fluctuated as a function of the level of economic activity and of adjustments that were made in the fiscal system. On the other hand, economic policy, while it is still centered around the role of the state, was modified because of changes in economic orientation as well as in the political superstructure. The fiscal instrument was affected by these changes but not profoundly.

First Period: from Reappropriation of Resources to the Build-up of the State, 1962-70

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

This phase was however not uniform. Two sub-periods may be distinguished, one characterised by uncertainty and a deficit in public finance, the other by the elimination of the disequilibrium and a clear orientation towards the economic policies that were to characterise the development strategy of Algeria in the seventies.

a) Sub-period 1962-65. Immediately after independence, Algeria had a predominantly agricultural economy, with a fragmented and extroverted industrial sector. Income generation was concentrated in the large land holdings devoted to export agriculture. Colonial capital paid little attention to industry, but oil concessions that had been granted in the early 50s represented a growing share of domestic production.

The restructuring of the Algerian economy in order to break dependence on France was based on nationalisation of former colonial capital, an attempt at financial sovereignty and the search for an autonomous development strategy (Jacquemot 1977: 65-70).

The goals of reconstruction and development postulated the mobilisation and centralisation of financial resources. However, on one side, the 'surplus' that the agricultural sector generated was too small and fragile to satisfy the financial needs of the economy; on the other hand, the mismanagement of recently nationalised public enterprises ruled out a transfer of resources to benefit the state budget. Finally, the revenue yielded by the fiscal system was limited because of the poor economic environment and in particular the economic and social displacement caused by the departure of the French. The fiscal system was not adapted to development conditions and its effectiveness was limited by the collapse of the tax base. It was foreign public aid which permitted to pay for investment and part of current expenditure.

The fiscal legislation was only marginally modified (Kandil 1970: 120-35). Because direct taxes could not be levied on a sufficiently wide base, indirect taxes remained more important (table 1).

Table 1: Structure of the fiscal system (percentages) 1961-66

Year	61	62	63	64	65	66	63-66 average
Direct taxes	29	30.7	29.4	29.2	26.5	32.3	29.7
Indirect taxes	71	69.3	70.6	70.8	73.5	67.7	70.3

Source: Ministère des finances, quoted by Kandil, 1970, p. 120

The fiscal system was at work in the midst of disorganisation and economic depression. Revenue considerably decreased after independence and did not begin recovering until

1966. Because revenue was derived mostly from activities with an important foreign participation, it was severely curtailed by the liquidation and departure of the French. The revenue decrease was amortised through a reinforcement of fiscal pressure. The self-managed and the public sectors were mostly in the red and many enterprises did not contribute to the state budget.

State budgets for 1963-65 were characterised by the weakness of budget revenue when compared to its level before independence; by the increasing weight of current expenditure over the total, due to the growth in the administrative apparatus; by the limited size of investment expenditure compared to the total. Foreign public aid played a key role in the financing of the deficit, covering all investment and part of current expenditure.

b) The 1966-70 sub-period. In the years 1966-73 the Algerian economy changed course. The phase of experimentation and learning by doing was abandoned and a new political context precipitated crucial decisions for the Algerian productive system. The state apparatus was reinforced and the national economy restructured.

The new orientation was manifested by the creation of a system of planning and the implementation of structural reforms.

With respect to public finance, the reorganisation effort allowed to gradually reequilibrate the state budget. The budget laws in the latter years of this period introduced few changes, but the yield of existing taxes increased. Revenue passed from 4 to 6.4 billion Algerian dinars. Half of this increase was due to taxes on income and expenditure. Oil revenue increased in connection with increased production and came to be almost one quarter of the total. The contribution of the socialist sector had a tenfold increase following the introduction of compulsory contribuions to the Treasury on the part of State enterprises. Foreign aid played a more limited role.

The budget closed with a surplus at the end of the period. This was made possible by an increase in revenue and strict control over current expenditure, thus allowing to increase investment and public saving.

Second Phase: Oil Revenue and the Algerian Development Strategy

During this period (1971-77) an industrialisation strategy was implemented aiming at breaking away from dependence bonds. The essential components of the strategy were the enlargement of the state sector, industrialisation, agrarian reform and reinforcement of the planning system. State intervention in the economy was largely financed by oil revenue. The latter grew very fast because of increases in both price and government take; it came to play a dominant role over the total revenue of the state passing from 23.0 per cent in 1971 to 37.2 per cent in 1974. At the same time, the heavy commitments of the state, and in particular the Treasury loans and anticipations to finance public investment, also greatly increased. Foreign credit was tapped to meet part of these needs, but Algerian debt service remained modest.

Industrialisation was expected to integrate the economy and reduce dependence from abroad. Capital intensive industries were preferred, because of their ability to transform the economy. The allocation of investment funds to individual industrial sectors confirmed the bias in favour of the investment goods producing sector, and of the oil and gas sector. The strategy was based on the intensification of the valorisation of hydrocarbons; iron and steel and mechanical engineering were to be the key sectors of the industrialisation effort. This strategy had a very high cost for the state.

The industrialisation effort could not be pursued in the long run if the agricultural sector was not reformed as well. Algerian agricultural policy after independence was characterised by 'weakness and inefficiency of structures' (Destanne de Bernis 1971: 30). Production and exports were declining, and agriculture did not generate the surplus needed to finance its own investments and modernisation. Agrarian reform was expected to solve this problem as well as to redistribute land. Its implementation led to modest production increases and did not allow for a transfer of financial resources to the rest of the economy.

Direct public control over production activity and the inflow of oil revenue allowed the funding of the projects included in the two four-year plans in this period (1970-73 and 1974-77). The first plan had put the total of public investment at 27.7 billion Algerian dinars, as against 9.4 billion in the 67-69 plan. The second plan envisaged total public investment of 110 billion Algerian dinars, more than three times the figure in the previous plan. The increase in the total level of investment is attributable to the increase in oil revenue following the oil price increase of 1973. The largest share of investment under the two plans went to industry and energy (54 per cent in 70-73, and 43.6 per cent in 74-77).

The rapid growth of public investment was financed primarily through an increase in the State investment budget, that registered yearly growth rates of 14.9 per cent in 1971 and 32.4

per cent in 1973. Out of a total of approximately 41.2 billion Algerian dinars of public investment spent during the 71-74 period, almost a third (12.9 billion) was accounted for by State capital expenditure (IMF 1977: 13). The rest was financed by public enterprises, mostly in the industrial sector. The primary source of funds for public investment was oil revenue. Mobilisation of financial resouces from domestic sources remained minimal, and the largest part came from abroad. Domestic savings contributed only 25 per cent of funds utilised under the 70-73 plan, while oil revenue accounted for 31 per cent, revenue of migrants for 16 per cent and foreign aid for 28 per cent (Jacquemot 1977: 155). Thus the State involvement in the economy is closely linked to oil revenue, as table 2 shows.

A radical change in the structure of revenue took place in 1974/75. Taxes on the oil sector became the most important item (59.1%), because of the increase in posted oil prices and in the income tax rates applied to oil companies. This structural change was maintained in the period 75-77, as the data in table 3 show. Total revenue in 1975-77 grew by nearly a third and the two main components, oil revenue and ordinary tax revenue, grew at the same pace (36 and 34 per cent respectively).

Table 2: Summary of the Ordinary Revenue of the State 1971-74

	1971	%	1972	1973	1974	%
TAX REVENUE	4,264	61,1	5,050	5,701	7,976	34,1
Taxes on income and profits	1,198	(28.1)	1,400	1,653	2,117	(26.5)
Taxes on international trade	565	(13.3)	641	759	1,286	(16.2)
Taxes on production	2,501	(58.6)	3,009	3,289	4,573	(57.3)
OIL TAX REVENUE	1,648	23.6	3,188	4,116	13402	57.2
NON-TAX REVENUE	1,071	15.3	967	1,495	3,039	8.7
Contribution of state enterprises	683		609	742	1,524	
Of which: SONATRACH				(300)	(1,000)	
Other non-tax revenue	388		358	453	515	
TOTAL REVENUE	6,983	100	10,205	11,312	24,417	100

Source: Data submitted from the Algerian government, IMF, 1977, p. 71

Table 3: Algeria, Survey of Ordinary State Revenue Forecasts 1975-77 (millions of AD)

	1975	%	1976	1977	%
ORDINARY TAX REVENUE	7,265	33	8,280	10,260	36,7
Direct taxes			1,800	2,150	(21)
Customs duties			1,020	1,800	(17.5)
Indirect taxes			5,300	6,150	(61.5)
Registration and stamp			160	160	
OIL TAX REVENUE	13,000	59.1	15,000	16,500	59.1
NON TAX REVENUE	1,730	7.9	910	1,150	4.2
TOTAL REVENUE	21,995	100	24,190	27,910	100

Source: Data derived from various reports on the Algerian economy. Discrepancies with respect to Table 2 should be attributed to the classification standards adopted by the IMF, which differ from those currently used at the national level.

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

A reform was introduced that embodied a new fiscal philosophy with respect to the role of public enterprises in the national economy, based on four main principles (Boussoumah 1982: 645): a) the socialist enterprises that manage the domain of the state are not ordinary taxpayers; b) the state, being the sole owner, has the right and obligation to define the tasks that public enterprises must fulfill in the development process; c) a unified contribution is introduced as the form of taxation on socialist enterprises; d) this contribution is divided between the state and the local community. Thus the state became more demanding both in terms of economic efficiency and in terms of fiscal revenue.

Table 4: Algeria, General Budget of the State (millions of AD)

REVENUE AND EXPEND.	71	72	73	74	75	76	77
Total revenue	6,982.6	9,205.2	11,011.7	23,400.4	25,053	25,660	33,479
of which:							
Oil revenue	1,648	3,188	4,115	13,462	14,237	18,019	
Ordinary expenditure	-4541.5	-4920.7	-6,193.6	-8,336.3	-13,659	-14,410	-15,281
Balance on ordinary budget	2,441.1	4,284.5	4,818.1	15,064.1	11,394	11,250	18,198
Investment expend.	-2254.2	-2808.7	-3,719.3	-4,158.5	-5,480	-7,870	-10,191
Balance on total Budget	186.9	1,475.8	1,098.8	10,905.6	5,914	3,380	8,007

Source: for 71-74: IMF, 1977, for 75-77, Annuaire de l'Afrique du Nord, various issues

The situation of the Algerian budget considerably improved over this period (table 4), as the surplus went from 187 billion Algerian dinars in 1971 to 8,007 billion in 1977. This improvement was mostly due to the increase in oil revenue, while current expenditure increased but slowly until 1973, but at a very accelerated rate in the following years. The growing surplus in the budget is however not indicative of the situation of the Treasury, as a large part of it was absorbed by loans and advances extended by the Treasury itself. In principle, loans from the Treasury should be used to finance industrial investment or redress the financial situation of public enterprises. Overall, however, the increase in Treasury credit led to a decrease of outstanding debt to the banking sector, a decrease in financement from the domestic non-banking financial sector, and limited amortisation of foreign indebtedness.

On the latter aspect, the number and total value of loans arranged on the international financial market rapidly increased after the beginning of the first four-year plan, and even more so during the years 1976 and 77. Since independence, Algeria has always had an important foreign debt both when her trade balance was in deficit and when it was in surplus. Foreign credit was extended in the years 1962-66 mostly under form of bilateral loans granted from France, and then also by other countries (USA, URSS, Arab countries). Sellers credit had become the preferred form of aid at the end of the 60s. But since the inception of the strategy based on large industrial projects, funds were increasingly provided by loans underwritten by international banking consortia and by the Euromarkets. Total outstanding debt became quite important in 1977 (14.9 billion US dollars) but debt service remained moderate during this period (absorbing 15.3 per cent of exports in 1977).

Third period: change in development policy and continuity in fiscal policy

During the period (1978-84) the development policy was redefined: the industrialisation effort was slowed down, the public sector was restructured, the role of private initiative was redefined, and planning showed a greater degree of pragmatism. While these changes were introduced, the revenue of the state continued to be generated mostly by the oil sector, following the second wave of oil price increases. The turnaround in the oil market in the 1980s had a considerable impact on the ability of the state to meet its financial needs.

In the industrial sector, a critical assessment underlined the excessive development of the hydrocarbons sector and numerous structural deficiencies. On a total public investment of almost 400 billion Algerian dinars that was expected to be realised between 1980 and 1984, almost half was allocated to the completion of projects undertaken under previous plans. The oil sector maintained a dominant position in the allocation of funds under the plan for 80-84 (40.8 per cent) but a considerable share was also allocated to intermediate goods (28.1 per cent).

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

At the same time, the rehabilitation of private enterprise was the most evident sign of the change in the conduct of economic policy. The state tried to define the role of the private sector both more precisely and more broadly.

The change in economic orientation took place at a time when the oil market was characterised by slackness of demand, and at the end of 1981 the price of Algerian oil was lowered 2 dollars per barrel. Oil revenue was correspondingly reduced, even more so as Algerian production is constantly decreasing (52 million tons in 79, 47 in 80, 44 in 81). At the same time the strategy of valorisation of natural gas resources, that were expected to produce a considerable revenue, suffered because of the difficulties that were encountered in the renegotiation of prices with European and American customers.

The negative evolution in the international environment had an impact on the revenue of the state. Oil revenue further increased to reach 68 per cent of total revenue in 1981, but subsequently declined to 57.7 per cent in 1984. Oil revenue increased 3.1 times between 1978 and 84 (table 5). The tax rate was increased to 85 per cent (from 70 per cent) and uniformly applied to all hydrocarbon-related activities (production, transport, commercialisation).

Ordinary fiscal revenue grew from a minimum of 32.1 per cent of the total in 1981 to 46.3 per cent in 1984. While in absolute numbers the various components of ordinary taxation grew unevenly depending on the year and the tax, the overall rate of increase was high. The budget laws introduced numerous changes that had social, economic and technical objectives: taxation on consumption goods was reduced to preserve the real value of wages; modifications were introduced in the fiscal treatment of enterprises in the social sector, of handicraft enterprises as well as of agricultural and hydraulic activities; technical measures were adopted which aimed at simplifying fiscal procedures. None of these measures had a structural character: aside from the 1977 reform of taxation on public enterprises, the Algerian taxation system suffered no major changes in the period.

Direct taxation in the Algerian Fiscal System

The primary distinction is between the contribution of the oil sector and other ordinary fiscal revenue.

Taxation on the oil sector is the most important source of budget revenue. Corporations operating in the sector pay a royalty which is a fixed percentage of the posted price, and an income tax at an established rate, imposed on the estimate of net income based on posted prices after deduction of the royalty

Table 5: Algeria, Ordinary budget revenue forecasts and allocations 1978-84 in millions of Algerian dinars

Year	78	79	80	81	82	83	84
Ordinary taxation	14.329	17.2	19.0	22.2	25.4	41.1	49.0
Direct taxes		2.6		3.8		7.6	8.6
Turnover tax		5.4		7.4		14.0	15.9
Contributions*		5.0		5.2		6.5	7.6
Customs		2.6		3.9		7.6	8.7
Other taxes		1.4		1.7		5.3	8.0
Oil taxation	18.2	19.6	31.7	46.1	47.6	57.5	56.7
TOTAL REVENUE	32.6	36.9	50.8	68.4	73.1	98.6	105.7
Current expenditure	18.1	20.6	27.8	36.2	42.2	50.4	59.7
Balance on current budget	14.4	16.3	23.0	32.2	30.9	48.2	46.0
Investment expenditure	14.3	16.2	23.1	31.6	42.6	48.2	46.0
Balance on total budget	0.1	0.1	-0.1	-0.6	-11.7	-	-

Sources: Maghreb developpement, various issues.
* Contributions: excises, profits of fiscal monopoly, taxes on specific services, taxes to use goods, etc.)

and of estimated production costs (IMF 1977: 60). Both the royalty and the income tax rate have been repeatedly increased since 1973. In 1980 the income tax rate reached 85 per cent, while it was but 55 per cent in 1974. This rate, which initially applied to oil activities only, was later extended to pipeline transportation and to all liquid hydrocarbons (70 per cent previously).

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

Direct taxation is composed of:

a) a tax on industrial and commercial income: this is paid by both individuals and entities (including cooperatives and state enterprises) as a function of profits derived from commercial, industrial, craft or banking activity. It is characterised by a multiplicity of regimes: thus private corporations pay a higher rate than public enterprises; self-managed enterprises benefit from a reduced rate; new enterprises benefit from a temporary exemption.

b) taxation on non-commercial income: this tax applies to income earned by individuals or entities in the exercise of a liberal profession. The State tried to improve evaluation of professional income while at the same time offering special reductions and deductions.

c) taxation on salaries and fixed earnings: it imposes a monthly withholding on salaries, fixed earnings, pensions and other emoluments, based on net revenue after deductions, and witheld at the source.

d) a tax on higher salaries: this is a complementary yearly tax on the higher salaries. It is also deducted at the source and benefits the central administration.

e) a tax on financial assets: it affects the gross revenue of individuals and entities coming from financial assets and deposits. The tax is geared to discourage the distribution of benefits and favours long-term savings. It has more of an economic than a financial purpose, as its revenue is negligible. Interest on Treasury bonds and other paper is also taxed.

f) a tax on property revenue: it is composed of a tax on inheritance and a tax on donations. The former is calculated on the net inherited assets, the rates being a function of the total value of transferred assets and the degree of parentage; the latter is calculated on the net value of the donation.

g) a complementary tax on total revenue: it is added to the individual taxes, with the exception of the tax on salaries, and is progressive; it has but limited yield.

h) registration rights: they apply to many legal acts as well as to certain contracts; the rates are fixed or progressive depending on the nature of the act.

Indirect taxation, is also characterised by the simultaneous presence of numerous taxes:

a) taxes on goods and services: including a unified global tax on production, a unified global tax on services and duties on certain products. The unified global tax on production is levied once only on merchandise sold in the country or imported. It is not applied to agricultural products and to certain goods that

pay consumption taxes. Rates are diversified (reduced, normal and increased). This is the tax that has the highest yield among indirect taxes. The tax on services is also not applied to the agricultural sector. Its rates are considerably higher, and the revenue goes to local communities.
b) excises: imposed on certain basic consumption goods (sugar, gasoline, wine, tobacco...) are composed of a specific duty which can be frequently changed and of a tax ad valorem. The most productive products are gasoline and tobacco, followed by sugar, coffee and tea.
c) custom duties: these were initially low and were revised only in 1968, a fact that explains their limited contribution to the total yield of indirect taxes. A new tariff was introduced in 1973. A regular tariff is applied to merchandise coming from countries that grant to Algeria the MFN treatment. A special tariff may be applied if the merchandise is included in specific commercial agreements. Rates are differentiated between primary need products, secondary need products and luxury products. Investment goods and raw materials are exempted from duties.
d) other taxes, such as the one on road transportation and stamp rights on certain legal acts, make a very minor contribution to the total revenue derived from indirect taxation.

TUNISIA

The Evolution of Tunisian Fiscal Policy in the First and Second Development Decades 1960-70

Following independence and until the end of the decade of the 60s two subperiods may be distinguished in the evolution of Tunisian fiscal policy. A first transitional period was dominated by the problems of decolonisation and witnessed no change in the structure and conception of the fiscal system as an instrument of economic policy. Financial aid from France continued to dominate investment expenditure. In a second phase, going from 1962 to 69, Tunisia chose planned development, structural reforms and industrialisation led by the state. This phase witnessed certain adjustments in the fiscal instrument, but no effective integration of taxation into the broader framework of development policy. The failure of the dirigiste experience signals the end of this decade, and opens the door to a more liberal orientation.

During the early years of independence, the most urgent problem was to maintain financial equilibrium and establish a budget structure that would permit the transition of power to take place. The massive exodus of foreigners and the withdrawal of capital invested by financial intermediaries considerably weakened the financial possibilities of Tunisia.

The fiscal system inherited from the protectorate was maintained, no new taxes were created and rates were not significantly increased. The fiscal system included taxes that can be grouped under two main headings: taxes on revenue and taxes on expenditure. A tax on capital, with a low yield, completed the structure. Taxes on the income of individuals and entities were and still are schedular (specific vs. general). They include: a) a patent tax which applies to industrial and commercial activities; b) a tax on non-commercial professions including liberal professions; c) a tax on fixed earnings and salaries (ITS); d) taxes on real estate; e) taxes on financial assets; f) the so-called personal contribution to the State (CPE). Taxes on expenditure include a tax on turnover, composed of three elements, a tax on production, a tax on consumption, a tax on services and specific taxes on certain individual products. The fiscal system was unbalanced and its yield was low: the largest share of the revenue came from indirect taxes (in excess of 80 per cent) (Ayadi 1980) while within direct taxes 90 per cent of the revenue was derived from the patent tax, the ITS and the CPE. Fiscal pressure was well within tolerable limits (17% in 1956).

The increase in public expenditure following the new, expensive tasks undertaken by the state made it necessary to drain a maximum of financial resources from the economy. The state proceeded to increase rates without touching the structure of the system.

Notwithstanding increased taxation, increased indebtedness and an obligation imposed on banks to participate in investments guaranteed by the state, the financial needs of the Treasury could not be met. To obtain the needed financial means the new state was obliged to seek foreign aid (Poucet 1971: 92).

Starting in 1962 a policy of reforms and more active encouragement to development was initiated. The emphasis on structural reform implied a new orientation in economic policy. A fiscal reform approved in 1961 was expected to mobilise revenue to meet the rapid increase in public expenditure.

The fiscal reform was inspired by the following objectives: maximise mobilisation of potential domestic resources, contribute to social justice, fashion an instrument to pursue economic equilibrium and provide an orientation to development. The reform modified the characteristics of certain taxes and improved the collection techniques for direct taxes. Almost all taxes saw their field of application redefined, so as to reduce the importance of defiscalised sections of the economy (Ayadi 1980). Agricultural taxes were completely changed, to increase the contribution of agriculture to the revenue-raising effort.

The reform had positive effects on revenue, but indirect taxes continued to prevail as a source of revenue, accounting for 75.4 per cent of total revenue on average. The main components of indirect taxation were the turnover tax (45 per cent), fiscal monopolies (17 per cent), customs duties (16 per cent) and consumption duties (11 per cent). Direct taxes did not account for more than 21.9 per cent of total revenue and stagnated after 1965. Revenue from a few oil fields generated a marginal contribution to the total (4.7 per cent of revenue). Fiscal revenue was 15.6 per cent of GDP on average. Because of the dominant role of indirect taxation, one may conclude that the reform failed to mobilise in full potentially available fiscal resources.

Considerable financial tensions and difficulties were the result. Increasing reliance was made on external financing, and onerous loans were gradually substituted for grants in aid. Already in 1964 the service of the Tunisian foreign debt came to 7.6 million dinars, as against 1.1 million in 1962 (Poucet 1971: 97).

The Financing of the Budget in the Second Development Decade

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

The second development decade had two constrasting phases. In a first phase (1970-76), fiscal policy introduced further technical changes in the determination of certain taxes (creation of a proportional advance and of a forfeit system in the determination of the patent tax as a function of the nature of the activity and of turnover; modification of turnover taxes to improve the system of deductions). Thus, fiscal measures included in the various budget laws were mostly aimed at improving the methodology of determination and collection of direct taxes. The base of the tax on individual revenue was enlarged to take into account various elements of the standard of living (ownership of land, real estate, automobiles, etc.). Special measures were adopted to ensure a more equitable distribution of the fiscal load among salaried personnel. Legislation called for the determination of salaries to include the totality of revenue for the year (bonuses, fringe benefits, etc.).

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

These changes in economic strategy and in fiscal policy brought about a considerable increase in the ordinary revenue of the state (table 6). It should also be said that during this period economic activity expanded rapidly in the wake of a favourable international situation. The increase in total budget revenue reflects primarily the remarkable increase in tax revenue, which increased 15.7 per cent between 1972 and 73, further accelerated to 27.4 per cent in 74 and 30 per cent in 75, then slowed down to 10 per cent in 1978. However, the relative share of tax over total revenue has not changed during this period (passing from 84 per cent in 1970 to 84.2 per cent in 1976). The burden of taxation over GDP increased slightly (passing from 22.8 per cent in 1972 to 27.2 per cent in 1976).

The overall increase in tax revenue was accompanied by a limited modification in its structure. The relative importance of indirect taxes was reduced from 77.8 per cent in 1970 to 75 per cent in 1976. Among indirect taxes, taxes on international trade played a growing role. Another important factor is the increase in non-tax revenue from the oil sector, which contributed 56.6 per cent of total non-tax revenue in 1976, up from 45 per cent in 1970. Public sector enterprises did not at all contribute to the budget, as the rest of ownership revenue came from financial assets in the hands of the Treasury.

Notwithstanding the positive evolution of tax revenue, public finance suffered a negative turn after 1970. Table 6 shows that current expenditure of the consolidated central administration grew at an accelerating pace after 1972. Its annual rate of increase, which had been 14.7 per cent in 1972/73, shot to 27 per cent in 1974/75 before slowing down to 9.7 per cent. The ratio between current expenditure and nominal GDP reached 21 per cent in 1976, while it was 18.3 per cent in 1972. The increase in current expenditure was primarily due to increased subventions and transfers to the Caisse générale de compensation and to public enterprises. The total amount of these outlays passed from 54.3 million dinars in 1972 to 144.1 million dinars in 1976. Personnel expenditure also increased from 98 to 172 million dinars), essentially because of increases in the pay of civil servants. Interest on foreign public debt (17.7 million dinars in 1976) was only 4.6 per cent current expenditure.

Following a decrease in 1971 and 1972, investment expenditure increased more than fourfold and reached 4.8 million in 1976. Net state loans also considerably increased in this period. As a consequence of these movements, the balance onoperations of the central public administration, following an improvement in 1972, worsened again because of the acceleration in capital expenditure, and reached a deficit of 4 million dinars in 1976, equal to 10.3 per cent of total expenditure (including net loans to the econoy).

The financial needs of the central administration continued to be met predominantly by domestic sources (state drawings from deposit banks, drawings from the public sector, public sector deposits with the Treasury, net Treasury drawings from the central bank). The net utilisation of foreign resources financed more than a third of the deficit, but total outstanding foreign debt increased considerably.

In a second phase, going from 1977 to 1980, the relatively high rate of growth resulting from a favourable international environment decreased dramatically. Tensions on prices of imported goods and in domestic financial resources began to have negative effects on domestic as well as external equilibria.

The state aimed at supporting economic activity and limiting bankruptcies in the private sector. Public investment, including both investment of the state and of public enterprises, accounted for two-thirds of total investment during the period. Economic stagnation limited the possibility to finance investment with domestic savings and reliance on foreign loans increased. On top of official loans and other forms of aid from abroad, the state tapped the international capital market for the first time in 1977. This tendency was maintained until 1980.

Table 6: Tunisia, structure of revenue and summary of accounts of the consolidated central administration 1970-76 (millions of TD)

	1970 (1)	1972	1974	1976
Fiscal revenue	143.7	207.3	305.06	436.6
Taxes on income and net profits	31.9	39.2	55.9	82.6
Taxes on property		5.7	8.6	13.8
Taxes on goods and services	48.3	77.8	100.6	138
Taxes on foreign trade and international transactions	40	53.6	90.9	126.3
Social security contributions	23.5	13.6	20.5	24.9
Other tax revenue		17.4	29.1	51
Non-tax revenue	27.1	38.7	80.3	81.9
Revenue on property	15.4	22.4	65.6	67.7
of which: oil revenue	(13.3)	(16.5)	(5.7)	(51.1)
Other non-tax revenue	11.7	16.3	14.7	14.2
Total ordinary receipts	170.8	246.0	385.9	518.5
Grants	20.7	16.5	18.4	15.3
Other revenue	0.4	0.3	2.2	8.4
TOTAL REVENUE AND GRANTS	191.9	262.8	406.5	542.2
TOTAL EXPENDITURE & NET LOANS	213.9	272.3	421.9	604.7
Current expenditure	151.9	197.2	276.8	385.4
Investment expend.	57.5	43.9	119.3	191.8
Net loans to the economy	4.5	31.2	25.8	27.5
CURRENT PUBLIC SAVINGS	-19.5	48.8	109.1	133.1
OVERALL DEFICIT	-22	-9.5	-15.4	-62.5
SOURCES OF FINANCE	18	9.5	15.4	62.4
Foreign	18	2.1	6.4	20.2
Domestic		7.4	9.0	42.2
of which: monetary authority		(-28.2)	(8.3)	(25.0)
GDP (current prices)	759	1,078	1,534	1,908

Sources: IMF, 1977 and 1983

Reliance on foreign credit is partly explained by the fact that the fiscal system was not able to mobilise sufficient domestic resources. As was said, the fiscal system was but marginally changed in the first development decade, and changes introduced in the second decade, although more important, did not amount to an organic reform. New measures introduced between 1977 and 1980 aimed essentially at reinforcing mechanisms of control, combatting fraud, rationalising fiscal incentives. The only important innovations were the introduction of a tax on real estate appreciation and an extra tax on certain luxury products to finance expenditure on the part of the Caisse de compensation. Lastly, certain rates were increased to foster revenue (the maximum rate of the CPE went from 45 to 55 per cent, and customs duties were raised).

These measures allowed a certain improvement in fiscal revenue (see table 7), which increased by a factor of 1.6 between 1977 and 1980, but the rate of increase decelerated at the end of period (going from 23.4 per cent between 77 and 78 to 14.4 per cent in 78/79 and 15.1 per cent in 79-80). The slowdown is even more marked if social security contributions are included. Consequently the share of total expenditure covered by fiscal revenue practically did not change (69.7 per cent in 1980 as against 67.6 per cent in 1977), notwithstanding the reduction in capital expenditure. The structure of fiscal revenue was improved and the role of direct taxation increased (passing from 22 per cent in 1977 to 26.2 per cent in 1980) but indirect taxes continued to play a dominant role.

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

Table 7: Tunisia, Summary of Accounts of the Consolidated Central Administration (millions of TD)

	1977	1978	1979	1980
Current revenues	616.2	779.0	939.1	1.108.5
Fiscal revenues	522.3	644.6	735.0	846.1
Direct taxes	102.6	132.3	149.6	194.4
Taxes on goods and services	176.3	203.8	243.0	264.5
Taxes on foreign trade and international transactions	158.5	193.7	234.1	273.3
Other indirect fiscal revenues	28.8	32.0	10.2	11.0
Social security contributions	56.1	82.8	98.1	102.9
Non-fiscal revenues	94.9	134.4	196.1	243.4
Revenue on property	78.5	111.2	175.4	214.4
- of which oil revenue	(53.7)	(69.0)	(129.8)	(173.3)
Other non-fiscal revenues	16.4	23.2	20.7	29.0
Other administration revenues	22.6	8.5	12.9	22.7
Capital revenues	9.2	0.8	2.1	0.7
Of which	13.4	7.7	10.8	22.0
Current expenditures	463.4	559.9	728.2	784.1
Expenditures on goods & services	269.9	308.3	389.3	471.3
Interest on public debt	21.4	29.9	48.1	50.4
Subsidies and other transfers	172.1	221.7	300.2	267.4
IV Surplus or Deficit on Current Account	152.8	219.1	210.9	324.4
V. Capital expenditure	266.4	285.6	265.4	333.3
VI. Net Loans	42.2	43.2	38.0	112.7
VII Financial Deficit	-132.2	101.2	-139.6	- 98.9
VIII Sources of Funds	132.2	101.2	139.6	98.9
Foreign	95.8	75.5	136.8	80.4
Domestic	36.4	25.7	2.8	18.5
Non banking	46.0	14.9	18.6	26.8
Commercial banks	2.7	17.1	-21.5	26.2
Monetary authority	-12.3	-6.3	5.7	-34.5

Source: Government Finance Statistics Yearbook IMF, 1983: p. 754-57.

In fact, current expenditure increased rapidly in those two years (20.8 per cent and 30 per cent respectively) because of increases in the pay of civil servants and in subventions and transfers to the Caisse de compensation. In this phase Tunisia followed an active policy of subsidisation, and the outlays of the Caisse for the containment of prices of basic necessities went from 50.4 million dinars in 1975 to 157 million in 1981. Progressive price readjustments met with considerable social resistance.

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

The Structure of Tunisian Fiscal Revenue

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

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

-a set of schedular taxes (specific income tax vs. general) with proportional rates that separately affect each type of revenue (revenue from financial assets, industrial and commercial profits, non-commercial profits, fixed earnings and salaries) with no distinction being made between individuals and entities;

-an additional tax with progressive rates, called contribution personelle d'état or personal state contribution (CPE), that affects the overall revenue of individuals (Magnet 1969).

The schedular taxes are as follows:

-a tax on industrial and commercial profits, which is levied on partnerships, corporations and individuals. It is composed of a right of activity and a proportional right. The former replaced, in 1968, a fixed right that was a forfeit tax on small artisanal and traditional activities; it is equal to 1 per cent of total sales of the tax paying body. The proportional right is levyied with a differential rate depending on the nature of the taxpayer and on the sector of activity, be it industry, handicraft or tourism (40.1 per cent for societies and 29 per cent for individuals) or commerce (46.5 per cent for companies and for individuals).

-a tax on the profit of non-commercial activities which is levied on individuals and entities that are active in a liberal profession or any other profession which is not included in the previous tax; it is composed of a uniform right of 0.5 per cent or 1 per cent of sales and of a proportional right with a uniform rate of 30 per cent of net revenue.

-agricultural taxes again comprise two categories: on the one hand, specific taxes on consumption products (cereals, wine, olives), each affecting a specific product and being applied to the income from domestic or foreign sales; on the other hand, a general agricultural tax instituted in 1962 following the suppression of preexisting land taxes and applied to the annual gross income of the farm.

-taxes on capital include a tax on financial assets and a tax on real estate. The former goes back to the colonial period and has been repeatedly modified, while the second was introduced in 1979. The tax on financial assets affects dividends and interest paid on bonds and other financial instruments. Rates vary according to the nature of the revenue and the individual concerned .

-a tax on fixed earnings and salaries: the law of 30 December 1967 introduced progressiveness in this tax. The rates range from 5 per cent for income up to 2500 dinars, to 8.9 per cent for income above 6001 dinars. The system of determination of the tax takes into account various salary complements (bonuses, fringe benefits, pensions, etc.) and allows for various deductions.

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

2. Indirect taxes: these are divided into three categories:
a) taxes on domestic expenditure, which are further divided in general turnover taxes (production tax, consumption tax, tax on services), excises on consumption and revenue of fiscal monopolies;

b) taxes on trade and international transactions;
c) rights on legal acts and services.

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

Taxes on turnover were modified repeatedly. They are:
- a production tax, imposed on producers' prices at a rate of 14.40 per cent, and applied to goods made in Tunisia or imported from abroad;
- a consumption tax, which is generally added to the production tax to increase the fiscal load on goods which are not basic necessities;
- a tax on services, which is imposed on all commercial operations except merchandise sales, including sales of services from self-employed individuals; the general rate for this tax is 5.8 per cent.

Excises are levyied on particular products (alcohol, tea, coffee, oil products) and are different for each product. The contribution of hydrocarbons to this category has become dominant in recent years (76 per cent in 1981).

Finally, products whose manufacture, import or sale are the object of a state monopoly (tobacco, matches) include in their sales price an important consumption tax which accrues to the state. Furthermore, units that produce or distribute these products transfer a part of their profits to the general budget, where it is registered as revenue from indirect taxation.

Taxes on international trade and transactions gave to the state budget a revenue of 338.2 million dinars in 1981, equal to 50.8 per cent of indirect tax revenue. Rates applied to the majority of import products varied between 20 and 40 per cent. The tariff of 1973 aimed at encouraging certain industrial lines of production (mechanical industries, automobile contracting...). Higher rates were imposed on luxury items to increase the revenue derived from these products. Agricultural production generally receives 'greater protection than industry does, that includes also products whose domestic production is insufficient to meet demand in the country' (IMF 1977: 33).

Imports must also pay the turnover tax and a tax for custom processing, imposed at a fixed rate per gross ton of merchandise, with a minimum of 2.5 per cent of declared value. Taxation on imports accounts for almost all taxes on international trade and transactions, reaching 335.4 million in 1981 (157.6 million for the customs rights and 167.8 for the other import levies).

Taxes on exports affect only a limited number of products (pepper, peanuts). The tax is fixed per gross ton of exported produce with a minimum of 1.5 of the value of merchandise. The revenue from this tax accrues directly to the Caisse de compensation.

The custom tariff that was in use at the time of independence was left unchanged until 1973. The tariff on investment goods, raw materials and intermediate products was lowered in an attempt to encourage investment and production in the industrial and agricultural sectors. On the other hand, duties on products competing with domestic production were increased.

3. Categories of revenue generate only marginal resources. They are generally levied on the occasion of certain legal acts or occurrences. The total of these rights reached 16.4 million dinars in 1981 (of which 4.2 million were stamp rights).

B. Non-tax revenue is essentially derived from state properties. Reaching a total of 316.8 million dinars in 1981, it represents almost a third of total fiscal revenue (31.2 per cent) and are far more important than indirect taxation. In the total of budget resources (i.e. the total of current revenue and gifts) it accounts for a share of 23.7 per cent. This important contribution is derived primarily from the oil sector.

In Tunisia, the public and semi-public sector is also greatly developed. The state is the sole owner of numerous enterprises and jointly owns the capital of other enterprises, thus realising an association of private and public capital under its control. In this way, the state owns 'a huge portfolio whose total size is difficult to estimate' (Ben Achour 1981: 134). State participation occurs in all economic sectors, such as transportation, energy, mechanical industries, banking. The primary goal of this participation is to command levers in strategic sectors of the economy whose huge capital needs and low rates of return discouraged private capital; at the same time the state also has an interest in potentially profitable activities that may add to the revenue of the Treasury. However, management problems afflict the public sector and oil revenue is almost the only form of revenue which the state derives from its holdings.

MOROCCO

General Framework

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

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

The Structure of the Moroccan Budget

Table 8 depicts the evolution of the Moroccan budget in 1978-84 and highlights the growing constraints since 1978.

As the table shows, current consumption expenditure on the part of the State grew but after since 1978. However, transfers to the Caisse de compensation administering price subsidies grew regularly from 1978 (389 million dirhams) to 1985 (2,375 million), notwithstanding the repeated price increases. At the same time, the service charge on public debt to foreign creditors continuously increased and passed from 1,047 million dirhams in 1978 to 4,118 million in 1984, after rescheduling. Such a continuous increase is due to the accumulation of foreign loans on the international financial market between 1974 and 1980.

Budget revenue was insufficient to cover working expenditure (dépenses de fonctionnement) and amortisation of public debt in 1984. Fiscal revenue reached a total of 21,545 million dirhams, of which 5,300 came from direct taxes, 4,885 million from custom duties, 9,100 million from indirect taxes and 2,260 million from registration and stamp rights. In 1984 fiscal revenue covered 69% of actual State expenditure: a relatively high percentage which can be explained with the reduction in investment expenditure that was financed with foreign credit. In 1982 the same ratio stood at 55 percent.

Revenue from the public sector supplies but a small contribution to the budget. In 1984 public enterprises contributed 1,608 million dirhams to the Treasury, of which 1,100 million came from the Office Chérifien des Phosphates (OCP). Thus, public enterprises contributed less than 4 percent of the total state budget.

Table 8: Morocco, Evolution of the Structure of the Budget 1978-84 (millions of MD)

	1978	1979	1980	1981	1982	1983	1984
Ordinary revenue	11,693	13,802	15,193	17,838	20,480	21,094	23,815
Direct taxes	2,625	3,202	3,231	3,650	4,120	4,599	5,300
Customs duties	2,568	2,897	3,530	4,208	4,943	4,452	4,885
Indirect taxes	4,168	4,659	5,487	5,784	7,376	8,290	9,100
Registration and stamp	832	1,186	1,338	1,396	1,702	1,756	2,260
Monopolies	295	215	167	546	1,015	570	500
Public domain	56	50	57	56	55	57	50
Other revenue	349	893	583	901	729	620	620
Office Chérifien des Phosphates	800	700	800	1,297	540	750	1,100
Current expenditure	10,420	12,073	15,310	18,898	20,475	21,525	23,644
Public debt service	1,047	1,360	1759	2,924	3,144	3,526	4,118
Working expenditure	8,984	10,102	12,124	13,872	15,331	16,367	17,151
Subsidies	389	611	1,427	2,102	2,000	1,632	2,375
Current deficit or surplus	+1273	+1,729	- 117	-1,060	+5	-431	+171
Investment expenditure	-6629	-9,016	-8,565	-9,612	-12,481	-7,979	-7,410
Extra-budgetary expenditure	- 739	+1,018	+1,172	- 426	+1,368	+ 407	
Financial deficit	-6,095	-6,269	-7,510	-11098	-11108	-8,003	-7,239
Funding	+6,095	+6,269	+7,510	+11098	+11108	+8,003	+7,239
Foreign credit	3,364	4,016	3,911	7,116	6,471	3,392	4,769
Bank loans	2,287	1,319	2,888	3,788	2,197	6,703	2,170
Bank of Morocco	(1,007)	(715)	(1,259)	(1,648)	(1,342)	(2,543)	
IMF	(-)	(-)	(781)	(821)	(2,885)	(839)	
Deposit banks	(1,280)	(604)	(848)	(1,319)	(654)	(3,321)	
Non-bank loans	569	959	447	325	379	190	600
Reserves	-125	-25	264	-131	2,061	-2,282	-300

Source: Government of Morocco, Ministry of the Treasury

Investment expenditure was mainly financed from resources from abroad. Its growth has considerably abated since 1978, contrasting with the fast growth in previous years: from 6,229 million dirhams in 1978 to only 7,410 million in 1984, with a peak of 12,481 in 1982. Investment was the first to be reduced in the successive restrictions of 1978 and 1983.

Public debt as a source of revenue became more and more important, both to cover investment expenditure and to service preexisting outstanding debt. Foreign long term indebtedness grew from 3,364 million dirhams in 1978 to 7,116 million in 1981. It stood at 4,769 million in 1984.

The structure of budget revenue

Budget revenue is made up of tax revenue, tranfers from public enterprises and public debt. The budget law for 1985 includes the following breakdown of fiscal resources: 6,710 million dirhams from direct taxes, 4,749 million dirhams from custom duties, 10,275 million dirhams from indirect taxes and 2,326 million dirhams from registration and stamp rights. The tax revenuetotal thus comes to 24,060 million dirhams, equal to 63 percent of total budget revenue.

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

There are ten direct taxes; agricultural revenue, that was traditionally undertaxed, was totally exempted in 1982. The two most important taxes are the tax on professional revenue (3.160 million dirhams according to the 1985 budget law) and the witholding tax on salaries (2,180 million). The national solidarity tax, created in 1979 as a complementary direct tax to finance the defense effort imposed by the war in the sahara, is third with 551 million; the three together account for 88 percent of total revenue from direct taxes.

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

In May 1985, the government introduced in parliament a fiscal reform project which replaces schedular income taxes with a general income tax, which would increase equity, improve the determination of the tax base and collection procedures and unify deductions. The general income tax is to be applied to professional income, agricultural income, salaries, income from real estate and from financial assets.

Indirect taxation is composed of taxes on domestic consumption, a tax on turnover, custom duties and registration and stamp rights.

Taxes on domestic consumption yielded 2,430 million dirhams, i.e. 25 percent of the total raised through indirect taxes. These consumption taxes are mostly excises imposed on 13 products whose prices are fixed directly by the state, the most important being tobacco (1,421 million, or 58 percent of the total) and oil products (500 million, or 20 percent of the total).

The tax on turnover was created in 1962 to replace a tax on transactions, and as a prelude to a tax on value added. It is a cornerstone of fiscal revenue, yielding 7,845 million dirhams. It is composed of two taxes:

a) a tax on merchandise, yielding 5,613 million dirhams, of which 64 percent comes from imported products. It is levied on all products, either as they are imported or as they are sold, and has an array of 8 different rates, from a maximum of 30 percent on luxury products to a minimum of 6.38 percent, basic necessities are exempted altogether.

b) a tax on services, yielding 948 million dirhams, with three rates of 4.17, 7.50 and 12 percent respectively. This tax is entirely cumulative.

In the framework of the proposed fiscal reform, a tax on value added should be introduced, taxation extended to wholesale trade, deductions generalised to guarantee the neutrality of the price structure, the two existing taxes unified and the rates reduced to four, with a standard rate of 19 percent, a high rate of 30 percent and two reduced rates of 14 and 7 percent.

Custom duties generate significant resources (more than 4,749 million dirhams). They are based on two essential elements: import duties (2,184 million dirhams) and the special import tax (2,290 million). Custom duties on exports are insignificant, contrary to the Arab oil producing countries. For a long time the Moroccan government was inclined to increase taxation on imports to protect local production as well as to increase state revenue. More than ever before, this was the case between 1978 and 82 to reduce disequilibria in the Treasury and in the balance of trade. But the liberalist tendencies that have prevailed since 1983 have led the government to reduce import duties as well as the rate of the special import tax. This new policy gives priority to competition and may negatively affect the effort to overcome domestic financial disequilibria, as well as the small and medium enterprises that cater to the local market.

Registration and stamp rights yielded 2,326 million dirhams, of which 686 million from registration rights, 1,510 from stamp rights (of which, in turn, 1,005 million were received from the customs authority), and 130 million from a special tax on automobiles.

Thus indirect taxation plays a dominant role on total tax revenue and some 45 percent of the revenue it yields is levied directly or indirectly (duties, turnover tax, stamps) on imports.

Transfers from public and semi-public enterprises are but 4.5 percent of total budget revenue and 64 percent of the revenue under this category comes from the OCP. The rest is transferred from the Bank of Morocco (250 million), the postal authority (120 million), the Caisse de depôt et de gestion (85 million) and the National Office for Transportation (50 million).

Thus, 700 public and semi-public enterprises contribute only marginally to the financing of the budget. The weakness of their transferable surplus is largely linked to the stagnation in the sales of unprocessed phosphates, partly offset by increased sales of derivatives such as phosphoric acid. It is also due to the failure of public enterprises, most of which receive subventions to cover current and investment expenditure and to finance deficits that are caused by faulty management, to the excessively low prices motivated by social considerations, and to constraints imposed on exporting enterprises by international markets conditions.

The difficulties of the public sector are heatedly discussed in the country. The prevailing orientation envisages a reduction of subventions, greater attention to costs in the determination of prices, and the conclusion of special agreements between the state and the most important enterprises to improve their management and to transfer some of their lines of activity from the public to the private sector, in particular, in agriculture.

Public debt has played an important role in the financing of the budget, particularly since 1975. The decline in phosphate demand and prices caused a considerable decrease in financial resources, which had increased in 1973 during a period of passing euphoria and caused a significant jump in the level of public investment. To compensate for the decrease, the government massively resorted to foreign borrowing, encouraged by international financial operators who were suffering from an excess of liquidity in the 70s. Thus external financing became the prime mover in the undertaking of investment projects on the part of the government, public enterprises or financial intermediaries.

While investment expenditure was soon reduced, the limits of domestic sources of revenue caused a further accumulation of external debt between 1978 and 1982. As a consequence, the debt service load continuously increased from 1.7 million dirhams in 1978 to 5.7 million in 1983, bringing the debt service ratio (debt service exports + migrants remittances) to 45 percent in 1983. The evolution of total outstanding debt is represented in table 9. A first rescheduling was agreed upon in 1983 in cooperation with the IMF, affecting the years 1983-85.

Table 9: Morocco, Outstanding Debt of the State and of the Public Sector 1980-84 (million Us$)

	1980	1981	1982	1983	1984
Budgetary outstanding debt(1)	4813 (2)	5,733	8,048	8,361	8,516
IMF	153	308	704	841	864
Debt of the public sector	2224	2,435	2,713	2,505	2,844
TOTAL	7,190	8,476	11,465	11,680	12,224

(1) Excluding short-term aid
(2) Excluding military debt

Source: Morocco, Ministry of Finances

Domestic debt has a limited role because of the weakness of local savings. It is expected that revenue from domestic loans will reach 1 billion dirhams in 1985, while the level of discounted external loans would be over 6 billion. Revenue from domestic loans is composed of two categories:
a) the first, revenue from the sale of Treasury bonds, essentially to financial institutions and the Caisse de dêpot. In February 1985 the Treasury for the first time issued bonds directly to the public. This issue was a total success because of the high rate offered (14 percent) over a three year period.
b) the second, the receipts of a compulsory investment reserve, imposed on corporations paying taxes on profits and yielding 200 million dirhams. This form of forced loan is due to disappear under the proposed fiscal reform.

LIBYA

Following independence and until the beginning of the 70s Libya was a country under the control of external forces and was unable to mobilise the financial resources that were necessary for its development. In the 50s, the Libyan state was one of the poorest in the world. Sparse agricultural resources spread over a huge territory with few natural endowments could not offer to the state sufficient means to engage in the building of a country. Foreign aid, a fluctuating and self-interested source of income, was geared to keep the Libyan economy in a condition of mere survivability. The discovery of the first oilfield in 1957 was the beginning of a process of assured and continuous growth in the state financial resources. Nevertheless, the oil cartel's domination of the exploitation of oil, distortions and bottlenecks introduced in economic structures by the hegemony of the oil sector, and the uprooting of traditional social structures contributed to creating a favourable environment for institutional change, which took place in 1969. This was the beginning of a process of policy redefinition, starting with the reappropriation of national resources, which with the help of increases in oil prices, led to a substantial increase the revenue of the state. Taxation on the oil sector became the most important, indeed almost exclusive source of budget revenue, and the total revenue it generated increased enormously. An exogenous source of revenue fueling the intervention capacity of a state keen on spending, it pushed the endogenous sources of government revenue to a mere complementary role. The growth in absolute terms of non-oil taxation is partly connected with economic activities or income redistribution indirectly supported by the oil sector.

Knowing full well that establishing control over its future requires not only centralisation of financial resources and freedom from the limits imposed by the oil companies, but also the overcoming export of concentration exports on a single commodity, albeit a strategically important one, Libya espoused an active but incoherent policy of diversification of its economic structures.

The unfavourable turnaround in the oil market, together with domestic obstacles to development, frustrated its ambitions. This, again is a manifestation of the precarious financial condition of a state which depends on the sale of one raw material on the international market. The precarity is relative, however, when compared to the situation in other Third World countries.

<u>From independence to the revolution of 1969: royalties substitute for external aid as a source of budget revenue</u>

In the first decade after independence, Libyan economic structures remained very fragile and could not offer a base for taxation and revenue for the state. Personal income and consumption generated but modest sources of revenue. The Treasury was as the same time called on to pay for an expanding administrative structure, and foreign aid was required to fill the resulting gap.

Between 1954 and 1961 total expenditure increased three times and domestic revenue equalled an average 63 percent of expenditure. This level was reached thanks to revenue from custom duties. Foreign creditors supervised the utilisation of aid. The Libyan Public Development stabilisation Agency (LPDSA), created in 1952 and staffed by nationals of the donor countries, managed the funds made available. A second commission, the Libyan-American Reconstruction Commission (LARC) created in 1956, was in charge of controlling the projects funded by the Us at a time when American aid began to overtake both English and multilateral aid. The Libyan government was rarely consulted on the utilisation of funds (First 1974: 142).

In 1959 Esso standard discovered the famous Zelten oilfield and was soon followed by a rush of other companies.

Oil production expanded at a rate of almost 45 percent per year between 1963 and 1969 (Talha 1981: 205). The Libyan state was able to increase its revenue from oil, but this was still a modest fraction of the turnover of the oil companies. The companies themselves imposed their rules in the definition of relations with the Libyan state. The oil revenue of the Libyan state came from royalties of 12.5 percent of oil sales and from a tax on profits of corporations at a rate of 50 percent. These parameters being rigidly fixed, the state could only increase its revenue through an increase in production and/or prices. But the index for prices of Libyan crude went from 100 in 1961 to 71 in 1966, then to back to the level of departure by the end of the decade. The state lost revenue, and the loss was aggravated by the manipulations of the oil companies.

The state introduced certain modifications in legislation, and as a consequence, while between 1961 and 1966 it received only 20 percent of the value of gross exports, starting in 1965 this ratio rose to over 40 percent.

Royalties and taxes on the oil companies reached 75 percent of budget revenue, and state expenditure was essentially paid by oil money (table 10). The contribution of other taxes was almost negligible.

The growth in oil revenue pushed the government to increase expenditure. Working expenditure increased four times between 1963 and 1969, and notwithstanding the contribution of oil revenue budget equilibrium was reached only after two years. (65/66 and 66/67).

<u>From the Revolution of 1969 to the Beginning of the 80s: the Dominant Role of Oil Revenue</u>

The revolution of 1 September 1969 was more than a simple change in political institutions. A new policy was inaugurated, especially in relations with oil companies. The government pursued a development policy based on diversification of the productive base of the economy, and taxation was an important instrument to this end. Taxation other than on the oil sector was reformed to comply with the new official doctrine, but its economic and social effectiveness remained limited.

After the revolution, two phases may be distinguished in the Libyan economic policy in general and taxation policy in particular. A first phase (1970-75) was centered around the recovery of national resources and characterised by an abundance of financial resources. A second phase (1977-82) was characterised by the effort to diversify the economy and create an economic and social infrastructure, but also by the reversal in international oil conditions and the emergence of domestic bottlenecks.

Legislation regulating the oil sector was repeatedly modified (in April 1971, July 1973, January 1975) providing a framework allowing the state to rationally control this sector as well as to improve its capability to tap oil revenue. In 1975, the state received 75 percent of the national production of oil.

Direct control of the state was not limited to the oil sector. Banks and insurance companies were restructured and their assets concentrated in the hands of the state. A variety of public enterprises were created in various sectors to be the instruments of sectorial policies of the government. The policy of reappropriation of national resources allowed the state to maximise benefits from oil price increases. Oil revenue accruing to the state went from 447 million dinars in 1969 to 1741 million dinars in 1975 (table 11), almost a fourfold increase. The relative contribution of non-oil revenue correspondingly decreased from 18.7 percent in 1969 to 12.1 percent in 1974. Its growing importance in 1975 is simply a consequence of decreasing oil exports in that year. Modifications in the fiscal legislation affecting the non-oil sector, and in particular, the increased pressure brought by laws in 1964 and 1973 affecting the tax on income and economic activity, certainly improved the efficiency of ordinary direct taxation, but they had no effect on the relative role of this type of taxation on the total resources of the state.

Oil revenue permitted an increase in budget expenditure, in particular in 1974. Current expenditure was affected primarily by the increase in civil servant pay. Special expenditures, which absorb a third of the budget, were concentrated in the stabilisation of the price of certain basic necessities (flour, wheat, rice, sugar, tea, coffee...) and in aid to foreign countries. The law of 26 October 1970 reserved a minimum of 70 percent of oil revenue to financing development projects, explaining the strong increase in the investment budget in 1974 and 1975. In 1973-75, 2,571.2 million dinars were destined to investment, and of this total the contribution of the private sector was 370 million, i.e. 14.4 percent of public investment. The state pursued such interventionist policies that the government was obliged to go to the banks three times (in 1972, 73 and 75) to finance a deficit in the budget.

Table 10: Libya, Evolution of Budget Revenues (millions of LD)

	63/64	64/65	65/66	66/67	67/68
- Customs	15,000	15,500	15,000	20,000	24,000
- Monopolies	1,900	2,250	3,200	3,200	3,307- -
- Charges	4,788	6,500	7,150	9,275	10,430
- Taxes	1,650	1,810	3,250	3,750	4,450
- P.T.T.	1,250	1,350	2,000	2,100	2,250
- Ports	1,125	1,350	3,600	4,000	4,067
- Civil aviation	300	280	1,000	1,000	1,000
- Agriculture, wood	70	100	100	100	175
- Public services	1,000.5	1,200	1,300	1,400	1,436
- Others	728	650	800	1,465	1,521
- Miscellaneous	1,600	1,490	2,000	2,610	3,364
- Total receipts	29,411.5	32,480	39,400	48,900	56,000
- Oil revenues	29,411.5	32,480	39,400	48,900	56,000
- Petrol reserves	23,000	46,500	116,000	138,800	170,000
- General reserves	1,457.4				
- Revenue surplus			8,000		
- charges, taxes			1,600		
- Temporary investments			835		165
- Foreign assistance	9,500	6,821.4			
TOTAL	63,368.9	85,801.4	165,835	187,865	226,000

Source: Annual Report 66/67 et 67/68, Bank of Libya, Chronique économique, AAN, 1967

From 1976 to 1982
While oil revenues continued to increase until 1980, Libyan oil production systematically declined. Decrease in world demand and political tensions with the United States, over and above the Libyan preoccupation for exhaustion of reserves, are the main causes of the decline. Exports plummeted in 1981 and 82, while

Table 11: Libya, Revenue and State Budget 1969-75 (millions of LD)

	1969	1970	1971	1972	1973[1]	1974	1975	1976
STATE REVENUE	447.1	535.9	737.2	753.9	548.2	1,863.8	1,741	2,584
Oil revenue	363.5	453.2	651.3	646.4	429.5	1,638.0	1,283	2,093
Non-oil revenue	83.6	82.7	85.9	107.5	118.7	225.8	458	491
of which: customs duties	37.7	35.2	41.6	55.8				
ORDINARY BUDGET	291.9	288.9	361.9	437.1	223.5	430.9	460.0	564
SAVINGS BUDGET	155.2	247.5	376.3	316.8	324.7	1,432.9	1,281	2,020
EQUIPMENT BUDGET	113.1	146.1	247.6	397.3	413.7	866.0	941	1,190
SPECIAL BUDGET (2)				59.8	189.6	549.7	746	849
DEFICIT	+42.1	+101.4	+128.7	-140.3	-278.6	+17.2	- 406	-19

Source: 69-72: Y. Gazzo, Pétrole et développement: Le cas Libyen, p. 70 and 89
73-74:IMF,: Libyan Arab Republic: Recent Economie Development, August 1976
75-76: FMA: Principaux aspects des économies des Etats Arabes, FMA April 1980, p. 104.

(1) As of 1 Jan. 1974, the budget goes with the calendar year (from 1 Jan to 31 Dec) and not the fiscal year (from 1 April to 31 March). Therefore, 1973 is reduced to nine months (April to December).
(2) The special budget inclused subventions to basic products, aid to foreign countries and military equipment expenditures.

prices, which had increased until 1981, started to decline in 1982. Oil revenues increased until 1980, reaching 23,200 million dollars, from 7,500 million in 1976. (see Table 12). Thus, budget revenue increased until the end of 70s and started to decline in the 80s, in 1981 it was 31 percent off the previous year (Talha 1981).

This turnaround took place at a time when the Libyan government had a pressing need for funds to finance its development projects. Under the 1976-80 five-year plan, a costly policy of diversification was begun, whose benefits could only come in the longer term, and which needed to be sustained by the plan for 1981-85. But the ordinary fiscal system, parcellised in a multiplicity of low-yield taxes, contributes only to a limited extent to the mobilisation of domestic resources. While the revenue derived from it has increased, a large part of it is still directly or indirectly linked to oil activity: state expenditure on salaries to domestic and foreign workers broadens the base of personal income tax; consumption induced from distribution of the oil revenue increases the yield of excises and custom duties, etc. At the same time, the policy of the government has led to a shrinking of the private sector, and consequently to a loss of budget revenue.

Nevertheless, one has the impression that the potential for raising revenue domestically has not been fully exploited.

Table 12: Libya: Oil revenue and state budget 1976-80
(million Libyan dinars)

	1976 (1)	1977	1978	1979	1980 (2)
state revenue	2,468.6	3,098.3	2,714.8	4,262.2	-
- of which:					
oil revenue	2,093.6	2,702.3	2,253.4	3,762.2	4,144.7
state budget					
(total expenditure)	2,582.8	2,818.3	3,278.5	4,101.8	3,138.1
- of which:					
current expenditure	564.0	669.3	796.5	770.0	1,273
Contribution of oil revenue to budget resources (percent)	84.8	87.2	83.0	88.3	

Source: Gazzo, Y (1980)

(1) Data for 1976 do not correspond with data for the same year in the preceding table because of accounting differences.
(2) Data for 1980 are from Talha 1980

MAURITANIA

The components and final equilibrium of the Mauritanian budget are intimately linked to those of the balance of payments. Revenue is essentially derived from the tax affecting the exploitation of iron resources, from royalties paid by foreign fishing vessels operating along the Mauritanian coast and by official gifts and transfers or loans from abroad.

Immediately after independence, and until MIFERMA began exploiting iron ore in 1964, tax resources did not suffice to pay for operating expenditures, notwithstanding the latter's paucity. For four years in a row, France funded the budget deficit in view of the special ties between Mauritania and Paris.

In the second half of the 60s revenue from exports of iron ore constituted between 23 and 27 percent of the total current revenue. One should also add customs duties, which generated 36 percent of the revenue: it is evident that public consumption was strictly linked to foreign trade. Table 13 pictures the evolution of the current revenue of the Mauritanian state.

Table 13: Mauritania, Financement of Current Expenditure (millions of MO)

Year	Current expenditure	French aid	Iron ore revenue	Customs duties
1960	626	57 %	0	19.5 %
1962	909	11 %	11.8 %	38.5 %
1964	806	0	16.8 %	40.7 %
1967	1.222	0	28.5 %	28.9 %
1970	1,498	0	23.1 %	25.8 %
1975	4,061	0	19.7 %	35.5 %
1977	7,008	0	0	39.5 %

Source: Vergala, <u>L'économie Mauritanienne et son développement</u>

The remaining revenue came from taxation.

a) the contribution to support the national defence effort, which reached 745 million oukiyas in 1977 when Mauritania intervened with Morocco in the Western saharan conflict.

b) direct taxation, composed of a tax on fixed earnings and salaries (yielding 675 million oukiyas in 1979); an income tax (300 million oukiyas); a tax on profits (475 million oukiyas)

c) indirect taxation, including: a tax on the export of copper, which yielded some 40 million oukiyas in 1974, when mining of copper was ended; an excise on consumption of hydrocarbons (200 million oukiyas); a consumption tax (69 million); a tax on tobacco (39 million).

These figures show the stringent limits of tax revenue, both direct and indirect, due to the small dimension of the Mauritanian economy. At the same time, the operating budget increased rapidly after 1974 because of the abandonment of the policy of austerity which had continued since 1960, the exodus of nomads from the desert following the drought of the 70s, and the national defence needs between 1976 and 77.

The investment budget is funded from three sources of revenue: fishing royalties, transfers from the public sector and the surplus on the current budget (table 14). Four observations deserve to be made regarding these figures: a) the investment budget has considerably increased; b) royalties paid by foreign fishing vessels has become the main source of income; c) transfers from the public sector reflect the nationalisation of MIFERMA. They ceased in 1977 because war in the Sahara brought iron ore production to a halt. The surplus in the current budget disappeared in 1974, because of the increase in current expenditure.

In Mauritania, government investment projects are also financed out of special accounts of the Treasury and resources of public or semi-public enterprises. Gifts and loans from abroad are credited to the special accounts. They totalled some 5 billion oukiyas in 1975, 77 percent of which came from the Arab oil producing countries and were intended to fund industrial projects whose profitability was later questioned (an oil refinery, a sugar refinery at Nouadhibou, etc.).

Fiscal policy since 1979

The deterioration in the economic situation, the worsening of domestic and foreign financial equilibria and constraints brought on by Mauritanian intervention in the saharan conflict led to the fall of President Moktar Ouldada. Since then, despite

Table 14: Mauritania, State Investment Budget (millions of MO)

Years	Total investment expenditures	Fishing royalties	Transfers from public sector	surplus of the current budget
1970	159	-	-	-
1972	282	40	0	200
1974	335	215	120	0
1977	600	400	200	0
1978	-	600		
1979	-	2,000		

Source: Vergala, L'économie Mauritanienne et son développement

almost permanent political instability, all governments have been obliged to follow a policy of restrictions on expenditure. The budget for 1982 aimed at equilibrium: custom duties and direct taxes were increased and the minimum personal revenue exempted from taxation passed from 45,000 to 80,000 oukiyas. Taxation on houses was reduced to encourage building activity.

However, stagnation of iron ore exports, not entirely compensated by the increase in the value of the dollar, and insufficient agricultural production led to a widening of the financial gap and obliged the government to tighten its austerity policy, in accordance with the IMF.

Foreign debt reached an intolerable level because the revenue of many projects funded from abroad was very limited: the oil refinery, the sugar refinery, the power generating complex, the Nouadhibou harbour, the road from Nouakchott to Noumia. Debt service was more than 3 billion oukiyas in 1978, i.e. 39 percent of exports, while foreign outstanding debt was estimated at 711 million Us dollars.

The economic policy followed since 1979 can be summarised as follows: rescheduling of the foreign debt; financing of the budget deficit in the budget thanks to funds from the EEC, the IMF, Iraq and France; realisation of projects with an assured capacity of generating revenue (in particular the iron enrichment plant in Guelbs) and postponement of others; priority to the agricultural sector; creation of joint ventures in fishing activities with countries whose ships are active in Mauritanian waters (Spain, USSR, Japan, South Korea).

Following the accession to power of Lt. Maaouya Sid Ahmed Ould Taya in December 1984 the policy of financial restriction was further reinforced. With a total outstanding debt of 1.7 billion dollars, equal to twice its GDP, Mauritania bowed to IMF recommendations. The price of basic necessities, such as rice, was increased 10 to 20 percent, and the price paid to producers was also increased. Parallelly, Mauritania allowed the oukiya to float and lose about 15 percent of its value. This facilitated negotiations for a new rescheduling of foreign debt.

COMPARATIVE ANALYSIS OF MAGHREBI TAXATION SYSTEMS

The fiscal systems of the Maghrebi states have a common origin. Modern taxes were created during the colonial period. The old taxes, based on religion, sovereignty or customs, lost importance after the disgregation of pre-capitalist modes of production, in spite of numerous attempts at reform which preceded colonial intervention. The colonial administrations pursued an increase in fiscal revenue by, on the one hand, modernising some old taxes, particularly those on agriculture, and, on the other hand, creating new taxes, modelled on those of the colonising power. Progressively new taxation systems, including direct and indirect taxes, were introduced in the Maghreb. Most of the present-day taxes date from this period.

The second World War had an important influence on the revenue of these taxes, linked to international economic conditions. Because of restrictions on international trade, customs duties and domestic consumption taxes yielded decreasing revenue. At the same time expenditure was growing, thus necessitating the creation of further direct taxes. Thus, a tax on fixed earnings and salaries was imposed in Tunisia (1937) and Morocco (1939), while taxes on corporations were sharpened (in Morocco, Tunisia and Algeria).

Created by the colonial powers to serve their own purposes, taxation systems in the Maghreb are not functional to the development needs of the countries. Following independence, the social and economic turmoil brought by decolonisation and economic development requirements underlined the need to restructure these systems. Yet, more than two decades later, these systems are still essentially the same. Governments have only increased rates, made a few technical adjustments, and implemented partial reforms to substitute new taxes for old ones (e.g. substituting taxes on products and services for taxes on transactions, the agricultural tax for tertib, etc...). These partial measures have not greatly affected state revenue or the economy of the Maghrebi countries. Countries which had the most pressing revenue needs (Morocco, Tunisia, Mauritania) enacted the most important changes, at least quantitatively speaking. All the same, the need for in-depth fiscal reform is on the agenda in all the states of the Maghreb.

Even while sharing a common historical origin, the Maghrebi fiscal systems reflect the realities of the individual economies in which they are applied. Yet certain common constituent elements can be found.

Thus, schedularity is a fundamental characteristic of all Maghrebi fiscal systems. Taxation of income may be diversified, but it certainly is also excessively fragmented. schedules are approximately the same, with similar elements of progressiveness: taxes on industrial and commercial profits, on professional income, on income from real estate and financial assets, on fixed earnings and salaries. To these is added complementary taxation. On the other hand, taxation on capital is but partial: it affects capital only occasionally, as with the inheritance tax (in Algeria) and taxes on transfers.

Taxation on consumption also occurs under similar conditions. Custom tariffs are diversified and pursue the objective of providing effective protection to domestic production. Excises are imposed on the consumption of specific products such as tobacco and alcohol. Finally, taxes on transactions affect both tangible products and services at differentiated rates.

This extreme schedularity may have the advantage of spreading taxation over numerous sources of revenue and expenditure, but it also leads to a lack of homogeneity and simplicity, which in turn may generate distortions and inequalities, while favouring evasion.

In all Maghrebi countries a disproportionate share of the fiscal revenue comes from indirect taxation. Taxes on products and services and custom duties generate between 45 and 50 percent of ordinary budget revenue (excluding oil revenue in the oil exporting countries). A characteristic of underdeveloped countries, the predominant importance of indirect taxation is that it serves to restrict consumption in accordance with the need to save and invest and also reflects the fact that direct taxes are less flexible.

Direct taxation is gaining importance, but is nevertheless relatively slight (see table 15). This reflects the limits of the contribution of the productive sectors and economic entities. This limit becomes even clearer when it is recalled that an important part of the income base is made up of the revenue of state-controlled enterprises (OCP, Sonatrach) and of budget expenditure under the form of fixed earnings and salaries.

Although taxation rates on the profit of enterprises, be they private or public, are progressive and relatively high, production units give but a small contribution to state revenue. Development policies based on the creation of development poles (such as in Algeria and Libya) generate large units, financed by slowly maturing investment, operating in an environment with no economic rationality and offering little potential for growth. It is, then, to be expected that enterprises will not generate a financial surplus that may be a base for state taxation. Alternatively, the policies based on light industry (Morocco and Tunisia) and export-oriented small and medium enterprises are accompanied by taxation policies favouring international competitiveness. In this context they benefit from important fiscal advantages which translate into revenue lost to the government.

The weakness of direct taxation in Maghreb public finance is, more generally, a consequence of the pattern of growth in the respective economies. Growth is unbalanced, the industrial sector is weak and disintegrated, the agricultural sector archaic, the services sector plethoric. Deficiencies in productive structures explain the peculiar behaviour of the elasticity of direct fiscal revenue with respect to GDP. This elasticity is strongly linked to exogenous factors (oil and mining) and to modifications in fiscal legislation.

The tendency to introduce numerous minor changes in legislation each year (especially in non-oil countries) manifests the need of the states to regularly increase their revenue to fund their growing commitments, and implicitly, also the lack of a direct link between economic growth and fiscal revenue. In other words, this elasticity is neither automatic nor endogenous; it is an input from the rest of the world or follows legal and/or technical changes.

Consequently, governments have but little control of their tax revenue and cannot use fiscal policy as an efficient instrument of short-term economic policy or long-term planning of revenue and expenditure. Foreign demand determines a large part of fiscal revenue, both directly and indirectly. Because

Table 15: Maghreb, Comparative Structure of Current Budget Revenue

	Morocco 1981	Tunisia 1981	Mauritania 1985	Libya 1981	Algeria
Income taxes	18.20	15.28	23.93	13.98	5.60
of which: on individuals	8.34	6.68	19.81	7.58	-
on enterprises	8.77	7.88	3.55	6.38	-
Property taxes	2.04	1.97	0.77	-	-
social security contributions	5.31	8.79	6.57	2.39	-
Taxes on goods and services	31.06	23.38	18.16	36.82	18.58
Taxes on trade and international transactions	20.5	25.45	26.46	6.38	5.73
Oil revenues	4.86	1.23	0.25	19.48	67.20
Non-oil revenue	18.03	23.90	23.86	10.24	2.59
of which: property revenue	8.89	21.89	2.72	10.24	0.07

Source: for Morocco, Mauritania and Tunisia, IMF, 1984 (GFs): for Libya and Algeria our elaborations on data from budget laws.

fiscal variables cannot be controlled, formulation of long-term objectives is a myth, rather than an exercise in rational planning. Fiscal constraint and the absence of alternative fiscal policies nullifies all attempts at autonomous development.

Despite similarities in their ordinary systems of taxation, the countries of the Maghreb finance their budgets in quite different ways. This differentiation originates in the role of oil revenue (Libya and Algeria) or of external debt (Mauritania, Morocco, Tunisia, Algeria). Thus, the tendency for public savings to disappear emerged in certain countries (Morocco and Mauritania) making current expenditure partly dependent on foreign loans or advances from the central bank (Morocco) or even on foreign aid (Mauritania). On the other hand, the allocation of oil revenue to current expenditure allows the oil countries (Algeria and Libya) to bridge the gap between ordinary revenue and current expenditure, while the remaining surplus is devoted to capital expenditure. Tunisia still is in an intermediate position, as current revenue and expenditure are basically kept in line.

While Libya managed to invest a considerable financial surplus abroad in the good years and limited her dependence to a few insignificant loans, Algeria and the other countries regularly tapped international financial markets to acquire the funds needed to speed up economic development. Nevertheless, the debt situation is different in each country of the Maghreb.

Morocco, which relied more than others on this source of financing, was brutally confronted with the problem of managing its international debt, with the usual consequences in relations with creditors (debt rescheduling, structural adjustment program). Algeria and Tunisia have avoided coming under pressure from international financial institutions, and keep their level of debt within proportions that are compatible with their ability to repay.

The interplay of the three main sources of state financing (domestic taxation, international taxation - mostly related to exports of hydrocarbons - and foreign debt) may serve as the base for a taxonomy of the five countries of the Maghreb.

Oil or extrative rent.

Since the beginning of the 70s, oil rent has become the most important source of funds for the budget in Libya, which may be compared to the countries of the Gulf, and in Algeria, where oil and gas replaced the other productive sectors in supporting the state Treasury. In these two countries the enormous increase in public expenditure is the direct consequence of the rapid increase of resources linked to hydrocarbons.

In Mauritania budget financing is also fundamentally linked to iron exports, but the rent is more fragile and fluctuating because of unfavourable conditions in the international markets.

Tunisia also benefitted from the hydrocarbon boom, because its oil resources, albeit limited, contributed to creating a certain financial ease in the last 15 years. In Morocco, on the other hand, hydrocarbons are totally lacking and the extractive sector does not significantly contribute to the Treasury, as the period of increasing phosphate prices was very short-lived.

It is clear that the importance of rent is inversely proportional to that of domestic taxation.

Domestic taxation

Morocco is the only country in the Maghreb that finances a substantial part of its current expenditure from taxation. But the weakness of individual income and the importance of exemptions extended to investors under the investment codes, or to entire sectors such as agriculture and real estate, lead to a differentiation of fiscal pressure which weighs mostly on consumers and salary earners. The importance of taxation in Morocco explains the initiation of a reform aimed at simplifying, modernising and rationalising the fiscal system.

similarly to Morocco, Algeria and Tunisia inherited from the colonial period a taxation system which is outdated but still operational, although its importance has been diminished in Algeria through the predominance of oil revenue.

In Mauritania and in Libya, on the contrary, there is no a fiscal tradition. This does not bother the Libyan state, but certainly is one of the structural disequilibria in Mauritanian public finances.

Foreign Debt

In this respect, Libya is the exception, as it has seldom tapped foreign sources of credit. The other four countries have all linked their investment budgets to credit from international financial institutions, from the developed or oil exporting countries, or from international financial markets.

The level of indebtedness of the four countries is relatively high. In absolute terms, Algeria is first, followed by Morocco, Tunisia and Mauritania. But Morocco and Mauritania face the most critical situation, if their outstanding debt is measured against their GNP, total public expenditure or export capacity. Since 1981 the IMF has intervened in both countries to recommend reductions in public consumption and investment and to help in rescheduling their debt.

Tunisia is in a precarious position, while Algeria risks being driven into one by the decrease in oil revenue.

In the second half of the 1980s the situation of public finance in the five countries appears far from brilliant.

Morocco will face the need for austerity at least until 1990. While external resources stagnate and import costs increase from one year to the next, the Moroccan state must tighten restrictions on consumption and investment and cut subsidies while liberalising foreign trade.

Mauritania is in total disarray. Revenues from iron exports and royalties on fishing are insufficient to cope with drought and exodus, and the state must drastically restrict expenditure and accept IMF recipes to obtain a rescheduling of debt.

The financial situation in Tunisia is also critical at times. Government attempts at reducing subsidies on food items are politically unacceptable.

In Algeria, oil rent permitted a twenty-year period of abundance, with important subsidies being extended to consumers and nationalised enterprises. But a growing foreign debt, continuing technological dependence and the decrease in hydrocarbons revenue may lead to unexpected disequilibria.

Finally, in Libya the ratio of oil revenue to population still allows for a relaxed fiscal management but the times of surpluses are clearly gone.

Overcoming disequilibria calls for a reorientation of the means of financing and greater reliance on the domestic economy. Fiscal systems must be revised and enriched to mobilise a maximum of the national surplus and reduce reliance on funding from abroad.

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Chapter 2

GOVERNMENT INCOME SOURCES AND THE DEVELOPMENT OF THE TAXATION SYSTEM - THE CASE OF JORDAN, EGYPT AND KUWAIT

Hesham Gharaibeh

INTRODUCTION

It is a well established fact that governments in less developed countries assume a major economic role, especially when compared to the developed countries. This situation is dictated by the ideological inclinations of the governments and the socioeconomic composition of the population.

The importance of governments in economic life is even greater in the Arab world. Regardless of the political and economic ideology of any country in the Arab world, the economic role of governments remains central and vital.

Until recently all Arab countries were classified as poor countries with varying degrees of poverty. The massive and consecutive increases in oil prices created a clear distinction among Arab countries. For those that produce oil, the massive flow of oil revenues moved them from the poor or middle income group and placed them among the wealthiest countries in the world, while the rest of the Arab countries which are deprived of oil wealth struggle to maintain and sustain their economic growth with varying degrees of success. Thus, the flow of oil revenues created a 'wealth gap' in the Arab world with social and Political consequences.

As a result, one can classify government revenues as being dependent on oil income finoil producing countries, coupled with meagre or non-existent tax systems. For non-oil producing countries, one can expect the existence and importance of tax systems to generate revenues to compensate the lack of sizeable oil income generated elsewhere in the region. Taking into consideration the spill-over effect and linkages among Arab countries represented by the financial flows among them through financial aid and workers' remittances, it becomes clear that the massive revenues of some Arab countries have widened the gap between those who have oil wealth and those who do not. This matter has resulted in free tax societies as opposed to heavily taxed ones.

As the oil sector in the Arab world is entirely controlled by governments, it is expected that those particular governments are the direct and primary recipients, of oil revenues. This in turn, dictates and necessitates that governments should be the biggest employers, spenders and investors. Thus, one can feel the role of governments in all aspects of economic life. This fact is even more relevant in Arab countries since, in addition to governments controlling revenues and expenditures, the newly existing private sector is underdeveloped and there is a lack of entrepreneurial spirit in the sector.

It is the purpose of this paper to analyse and compare the sources of revenues in a sample of Arab countries, and in general to answer the following questions:

1. How important are the sources accruing to the state budget, and how have they grown in the last 15 years?

2. How important are the financial revenues accruing from taxation versus other sources?

3. If taxation is an important financial source, what part of it is from personal income tax, corporate income tax and other direct and indirect taxes?

4. How is the taxation system structured: what taxes are levied, what segments of the population are effected and how important is tax evasion?

5. How important is the non-tax income, its nature and sources?

A sample of three Arab countries will be under focus to analyse the relative importance of the different sources of revenues. The sample includes the following countries: Jordan, Egypt and Kuwait. The sample is thought to be representative as it includes an oil-rich country - Kuwait, a semi oil-rich country - Egypt and a non-oil rich country - Jordan.

SOURCES OF GOVERNMENT REVENUES

As mentioned earlier, higher oil prices and the consequent large oil revenues for oil exporting countries created a clear distinction between Arab countries. For oil wealthy countries, revenues generated from oil exports considerably exceeded domestic needs and encouraged governments to engage in extensive internal and external transfers. Governments of oil exporting countries transfered wealth to the private sector by providing free services and subsidies, and developing societies in which taxation is absent. The accumulation of oil wealth also induced oil exporting countries to engage in large unilateral transfers to other Arab and foreign countries. The non-oil exporting Arab countries had to rely on their domestic revenues requiring the development of a taxation system, in addition to external aid received from oil exporting countries. In other words, oil revenues induced oil countries not to impose any significant taxes and remain with an underdeveloped domestic taxation system, while the rest of the Arab countries were obliged to impose different types of taxes to partly finance their development programs. This, in turn, led to the establishment of a relatively modern taxation system.

Recent developments in the oil market, which resulted in a sharp decline in prices and volume of oil exports, caused some Arab oil exporting countries to start thinking about establishing a taxation system to generate more revenues to offset the deficit in external revenues. However, these efforts are inadequate for replacing the significant loss in external revenues. The development of a taxation system is needed not only to raise revenues, but also for its redistributional effect, as wealth is concentrated among a relatively small number of people.

TAXATION STRUCTURES

A general look at Kuwait, Egypt and Jordan provides an accurate classification of their revenues. While Kuwait is considered a major oil country as most, if not all, of its revenues are generated from oil exports, Egypt is a semi-oil country meaning that some revenues are generarted from oil and the rest are generated from other tax and non-tax sources. Jordan is a non-oil country: sources of revenues are confined to internal sources of income such as taxes and fees, in addition to foreign aid. For the purpose of detailing sources of revenues, we will point out the major sources of tax revenues and the structure of the taxation systems in the three countries. Of the three countries, only two, namely Jordan and Egypt, have a comprehensive taxation system. Oil and external sources of revenues are self explanatory.

Sources of Tax Revenues

Among the three countries in the sample, only two, namely Jordan and Egypt, have a comprehensive taxation system. The following is a brief description of taxation structures in the sample countries.

Taxation structures

When a taxation structure is carefully designed and organised, it is likely that such a structure will be highly influential in generating revenue for the government. In general, experts agree that a good taxation system should have as its fundamental criteria: equity, consistency, economic effectiveness, elasticity and feasibility. The equity pertains to the ability to pay taxes in a fair way; consistency refers to the taxation being in harmony with overall economic policies; economic effectiveness refers to the positive effect taxation should have on economic development; elasticity is the degree to which the taxation system will increase revenues in response to the growth in income; and feasibility is the extent to which an equitable and efficient tax system can be implemented (Enthoven 1973: 210). Because of some differences in the tax structure in the sample countries, a brief description will be given for each country.

Tax Structure in Jordan

After the economic boom in Jordan which covered the period from 1974 to 1982, the government found it very necessary to change, amend, and up-date the taxation structure in response to the changes in income, cost of living and other economic variations. The most significant changes in the tax structure were introduced and became effective in 1982. The new tax law featured many important changes such as:

- Self-assessment: where each person is responsible for reporting his income from different sources to the tax department by the end of April each year. Where before the new law was introduced, income used to be estimated by tax department employees based on whatever documents they may have had. Under the new law, a tax return is still not unless it is approved by the tax department, but in general, taxpayers have much more freedom in estimating their income.

- Tax exemptions: the new law gives somewhat generous exemptions when compared to the law that existed before. These changes include more exemptions for families, education, house rent and some sources of income such as agriculture.

- Larger tax brackets: under the new law, a progressive tax is imposed on net income according to the following rates.(Jordan Tax Department 1982: 10)

from	0	to	1000	J.D. pays	5 %
from	1001	to	2000	J.D.	10 %
from	2001	to	4000		15 %
from	4001	to	6000		20 %
from	6001	to	9000		25 %
from	9001	to	12000		30 %
from	12001	to	16000		35 %
from	16001	to	20000		38 %
from	20001	to	25000		40 %
from	25001	to	30000		45 %
from	30001	to	36000		50 %
Any additional taxable income pays					55 %

The tax rate reaches the maximum at 45 per cent for personal tax. Under the previous law the width of tax brackets was 400 dinars. In other words, the new tax law introduced more exemptions and wider brackets to the effect that if a taxpayer earns a taxable income of 200 dinars per month, he is not required to pay income tax. In addition to that, income is taxable only when consistent and renewable (Khasawneh, Saleh 1981: 25) Income from agriculture and interest earned from government bonds is totally exempted.

<u>Tax deductions</u> The following deductions from taxable income are allowed for all income earners residing in Jordan:

- 400 dinars for singles and 600 dinars for married taxpayers
- 200 dinars for each child
- 100 dinars for each other spouse
- 500 dinars per person to cover higher education expenses
- 50 per cent of the income of government employees is exempted from taxes and 25 per cent of the income earned by employees in the private sector
- interest charges can be deducted from income
- income derived from agriculture is entirely tax free

Corporate tax is also important in Jordan, especially after the economic boom in which many new corporations were created and realised sizeable profits. The Jordanian corporate tax law distinguishes between corporations according to types of business, with a clear inclination to treat industrial corporations favourably.

According to the new tax law, corporations are taxed at the following rates:

- industrial, health and educational corporations: 35 per cent; private and non-resident companies: 40 per cent; finance and banking corporations: 50 per cent; limited ownership finance companies: 55 per cent

Taxes on building and real estate This type of tax is imposed on the rent value of the building which is often underestimated. Tax on buildings is charged at the rate of 17 per cent of rent value. A new amendment to this law was introduced in which 25 per cent of rent value is exempted in Amman and 50 per cent in other cities outside the area of the capital to encourage construction outside the heavily populated capital.

Indirect taxes Indirect taxes in Jordan - as in the case in other countries - are not directly levied on taxpayers as much as on their economic activities. Thus indirect taxes can be avoided and transferred to others.

Indirect taxes are the most important source of income for less developed countries -are not directly levied on taxpayers as much as on their economic activities.

Indirect taxes are the most important source of income for less developed countries. The importance of this type of taxtation for government stems from the general advantages of indirect versus direct taxation: indirect taxes are easy to collect and cannot be evaded. Therefore, the collection from this type of tax is sizeable. However, there are some important disadvantages to indirect taxations such as social inequity, bacause .it is imposed on all people regardless of their income. Moreover, indirect taxes tend to be unstable and vary according to economic cycles.

Below are the most important indirect taxes used in Jordan:

- Customs duties: a type of tax imposed on goods imported or exported. This type of tax is the most important in Jordan in terms of revenues. The rate varies according to the goods imported, luxury goods are heavily taxed, also imports with local substitutes are taxed differently to protect local production.

Taxes on exports are also used in Jordan at a flat rate of 1 per cent of the value of exported goods.

- Excise tax: this tax is usually imposed to restrict demand on certain goods in addition to generating revenue (Buchanan 1975: 307). Accordingly, this type of tax is imposed on goods such as tobacco, cigarettes and alcoholic beverages. The tax ranges from 175 per cent at its highest levels on alcoholic beverages to 2 fills per liter of gasoline.

- Stamp tax: is an indirect tax collected on documents obtained from the government and on checks by means of a stamp - of a certain value - affixed on each document.

Taxation Structure in Egypt:

The introduction of taxes in Egypt dates back to the 1930s, thus making Egypt the first country in the Middle East to introduce a complete taxation system. Tax structure and rates changed from time to time according to inflation, economic development and government budget. It has also been noted that the increase in taxation rates is largely used to finance the increase in public consumption rather than to reduce the share of aggregate consumption in the economy (Mabro 1974: 183-4). In other words, taxes are imposed mostly for their revenue effect rather than for distributional or consumption purposes. Following are the major types of taxes used in Egypt:

Income Tax. Egypt, like Jordan, employs a progressive income tax rate. Iincome tax rates according to law 157 which was introduced in 1981 and is still valid (Egyptian Ministry of Finance) are given below:

2%	on the first	LE	480
5%	on the next	LE	480
10%	on the next	LE	960
15%	on the next	LE	960
18%	on the next	LE	960
22%	on any amounts in excess thereof		

Income up to LE 960 is exempted from income tax. The tax law No 157 featured some changes when compared to law No 199 and other laws introduced in 1974 and 1978. These changes are reflected in greater income exemptions, wider taxable income brackets and the degree of progression.

For schedular taxes, the highest tax rate is 50 per cent. According to law No 157, schedular taxes are paid on four types of income, dividends and interest, profits, professional income, wages and salaries. Income brackets under schedular taxes are different from general income tax in that they starting with LE 1000 for income reaching LE 9000 and with LE 5000 or more for higher income.

Corporate Income Tax. A tax imposed on the net profit of all establishments on an annual basis. Before the new law of 1981, corporate income tax was a flat 40 per cent of net profit earned by corporations. The new law 157 makes a distinction between public sector companies and other individual and partnership companies. Public sector companies pay 32 per cent of their net profit as tax, while individual and partnership companies pay progressive tax rates according to the following:

20 % on first LE 1000
23% on the next LE 1500
27% on the next LE 2000
32% on the remaining profits.

The above tax rates represent a reduction of taxes levied on partnerships and individual companies from a flat 40 per cent to a progressive rate with a maximum of 32 per cent.

Taxes on Property. These taxes are levied on property of agricultural land or buildings. Taxes levied on arable land were abolished in 1981, but local taxes imposed by governorates are still in existence at the rate of 14 per cent of the annual rent value of arable lands.

The tax on buildings is assessed on the actual rental value, or imputed rents if building is occupied by owner. The 1981 tax law also abolished taxation on buildings, but local governorates impose building tax at the rate of 10 per cent for non-residential buildings and a progressive tax from 10 to 40 per cent for residential buildings.

Indirect Taxes. As is the case in Jordan and indeed most less-developed countries, indirect taxes are the most significant source of revenue in Egypt. There are many types of indirect taxes used in Egypt. The following are the most important types:

Custom Duties

The most important source of tax revenue in Egypt. Custom duties range widely from 0 to 3000 percent depending on the type of imports. Favourable tax treatment is given to capital goods with no or very little import tariffs, whereas consumer and luxury items are highly taxed to a rate which can reach 3000 percent on alcoholic beverages.

Custom duties are levied on imports based on their CIF import prices. Foreign exchange is translated into Egyptian pounds according to the Central Bank exchange rate.

Development tax: a tax levied on most imports in addition to custom duties to finance economic development. The current development tax is about 5 per cent levied on most imports.

Export custom duties: A selective tax imposed on a few goods when exported. These goods include raw hides and skins, metal scraps and wastes and antiques. This type of tax ranges according to the product exported The highest rate is 5 per cent imposed on antiques of an age exceeding 100 years.

Consumption tax: A selective tax imposed on a list of 53 commodities regardless of their origin (local or imported) such as coffee, tea, cigarettes and beverages.

Stamp Tax: tax levied on a wide range of documents, requiring users to affix a stamp of a certain value on the document.

Some attempts were made to analyse the tax efforts in selected developing countries. The most important and comprehensive study was done by Alan Tait in which he ranked the efforts in Egypt as eleventh in a sample consisting of 44 developing countries (Tait 1979; IMF Staff Papers 1979). However, the rapid changes in tax rate and structure make it difficult to analyse the tax capacity or efforts in Egypt.

Taxation Structure in Kuwait

Owing to the abundance of oil revenues, Kuwait has never used taxation as a source of income, nor a fiscal tool to influence levels of production, employment, prices or the distribution of income (Central Bank of Kuwait 1981: 49). The government of Kuwait levies no income, corporate or direct taxes. The main source of tax revenue comes from indirect taxes. A relatively low custom duty is levied on certain imported luxury items imported. Custom duties were originally about 4 per cent of imported goods. The rate was increased to 10 per cent in 1971. Foodstuffs and raw materials, in addition to many commodities needed for local industry are duty free.

GOVERNMENT REVENUES : JORDAN, EGYPT AND KUWAIT

In this section, we will try to shed some light on the major sources of government revenues, how they have grown in recent years and will compare the importance of domestic versus external revenues for the sample countries.

Government Revenues in Jordan

Jordan is considered a small country in terms of size and population, with an area of 91,000 square kilometers and a population of 2.7 million (in 1985). In addition to a limited area of land suitable for agriculture, Jordan is not endowed with any significant natural resources. But in spite of the lack of natural and financial resources, Jordan has managed to be one of the most prosperous among the less-developed countries.

The fact that Jordan lacks both natural and financial resources is clearly reflected in government revenues. Except for a few years, external revenues have always exceeded domestic revenues both in volume and relative importance.

The recent economic growth achieved by Jordan is mainly attributed to the oil wealth generated in neighbouring Arab countries. Accumulation of oil revenues triggered massive development plans implemented by oil-rich Arab countries. As a consequence, demand for skilled labour, administrators, engineers and other professionals soared to run the newly created facilities. Jordan stands as a major supplier of educated and skilled manpower. New job opportunities and higher pay induced Jordanians to migrate in a massive scale to the oil-rich countries. It is estimated that about 300,000 Jordanians are currently working abroad, a number which is equal to the labour force in Jordan itself.

Government revenues in Jordan are classified according to their source, external and internal. Internal or local sources are also classified into two major groups: tax and non-tax revenues. Following is a detailed analysis of all sources of revenues.

External Sources of Revenues

As a result of the influx of Jordanian workers to the Gulf region, remittances to Jordan started to increase as the economic situation in oil-rich countries blossomed. Increasing remittances, coupled with other factors, caused an economic boom in Jordan itself, which led to increased tax and other revenues for the government.

In addition to the remittances from abroad, Jordan was also a major recipient of foreign and Arab aid, which reached its highest absolute level in 1978 when total foreign and Arab aid reached 289.9 million Jordanian dinars, or 24.4 per cent of GDP for that year. It then started to decline.

Table 1 shows the magnitude and importance of foreign aid relative to GDP.

Table 1: External revenues, Jordan (in million JD)

Year	GDP	External revenues	% of GDP
1970	134.4	37.3	21.5
1975	312.4	116.7	37.4
1976	421.6	86.1	20.4
1977	514.2	180.7	35.1
1978	632.2	172.4	27.2
1979	753.0	247.9	32.9
1980	979.5	280.9	28.6
1981	1182.5	289.2	24.4
1982	1343.2	246.4	18.3
1983	1487.6	233.5	15.7
1984	1529.5	252.5	16.5

Source : Central Bank of Jordan, Annual Report, several issues

Clearly, Jordan is among the very few countries in the world which heavily depends on foreign aid and grants. This situation was created as a result of lack of internal resources, which obliged Jordan to look for external revenues to compensate the shortage of domestic revenue.

Following are the major items included under foreign revenues:

Budget Support The most significant source of foreign revenues. Budget support mainly comes from Arab oil-rich countries, which under the agreements signed in more than one Arab Summit conference, have pledged to financially support Jordan and other 'confrontation line countries' to enable Jordan to defend itself and to have a sound economy. Thus, this kind of support takes the shape of financial grants that Jordan will not have to repay.

The main problem facing the government of Jordan is the sharp fluctuations in Arab aid listed under budget support. Recently, most Arab oil-rich countries ceased their contribution, with the exception of Saudi Arabia, leaving no choice for the government but to increase local revenues.

Economic and Technical Assistance is the second source of foreign grants. Economic and technical assistance is mainly constituted by of equipment, studies and other services rendered to Jordan without obligation. The main countries providing this type of foreign aid are the USA., Japan and some European countries.

Development Loans Jordan is increasingly depending on foreign loans to finance its development plans. Total development loans contributed about 44 per cent of all foreign receipts in 1983. Major suppliers of loans to Jordan are the USA., Germany, the United Kingdom and Japan. In the mid 70s, Arab oil-rich countries started to provide Jordan with loans through the 'development funds established in Saudi Arabia, Kuwait, UAE and other countries.

Table 2 shows the magnitude and relative importance of foreign revenues and the share of foreign revenues in government expenditure.

The dependence on foreign revenues proved to be risky for the government of Jordan. We can notice from table 3 the instability of foreign aid, which makes it difficult for the government to plan ahead. Furthermore, foreign aid is usually cut without advance notice, such as the stoppage of aid by USA, Libya, Iraq and Kuwait, thus leaving the government no choice but to increase local revenues to compensate for the decrease in foreign revenues.

Internal Revenues

Internal revenues have gained significance in recent years after several countries halted their financial aid to Jordan. Increasing internal revenues is the only choice left to the government to offset the decline in foreign aid.

In the following sections, different types of internal revenues will be discussed:

Tax Revenues Tax revenues constitute, on average, more than 75 per cent of total local revenues. Tax revenues include both indirect and direct taxes:

Table 2: Relative importance of domestic and foreign revenues (in JD millions)

Year	Domestic Revenues	Foreign grants	Foreign borrowing	Other foreign	Total foreign	Total revenues	Total expenditure	% of foreign grants on total
1967	25.49	40.29	44.29	.22	44.92	70.41	68.15	65.91%
1968	26.27	40.11	5.43	.10	45.64	71.92	80.52	56.68
1969	32.52	38.37	4?72	.65	43.74	76.27	88.41	49.47
1970	30.26	2.07	2.07	. 41	37.90	68.10	80.70	46.96
1971	35.75	35.39	3.55	3.50	42.44	78.19	83.14	51.04
1972	42.86	44.47	10.20	1.18	55.85	98.73	101.535	55.00
1973	46.18	43.60	11.44	2.00	57.04	103.23	119.51	47.73
1974	65.74	57.65	15.21	1.33	74.19	139.93	146.62	50.60
1975	82.63	100.61	16.15		116.76	199.391	2048	656.99
1976	107.53	66.24	19.88		86.12	193.71	262.48	32.81
1977	142.25	122.20	58.51		180.71	322.46	337.84	53.49
1978	158.49	81.69	90.69		172.38	330.88	361.51	47.68
1979	187.89	210.30	37.62		247.92	435.82	515.66	48.07
1980	226.15	202.83	71.56	6.46	280.85	507.01	563.14	55.39
1981	309.19	206.31	75.73	7.22	289.26	598.47	647.10	44.70
1982	360.22	184.50	61.50	.40	246.40	606.61	656.27	40.62
1983	396.00	130.00	101.54	2.00	233.54	629.54	717.65	32.54
1984	437.7	124.00	128.54		252.54	705.26	746.15	33.84

Source: Calculated from the Central Bank of Jordan, Annual Report, different issues.

Indirect Taxes Indirect taxes are the most important source of local revenue constituting more than 80 per cent of total tax revenues and one third of local revenues. Total indirect tax revenues have been increasing at a steady pace. Table 4 shows the magnitude and types of indirect taxes used in Jordan. It is clear that custom duties are the biggest source of local revenue. Custom duties often change in Jordan to increase revenues or to protect local industry. There has also been a positive relationship between increasing indirect taxes and the decrease in foreign aid.

Table 3: Sources of aid to Jordan

Year	Arab aid	US aid	Other aid	Total aid
1967	37.57	7.62	6.39	51.58
1968	46.25	1.19	5.63	53.07
1969	41.15	1.23	3.41	45.79
1970	33.07	1.38	4.63	39.08
1971	19.11	12.82	3.56	35.49
1972	23.19	35.95	6.82	65.96
1973	23.66	30.83	6.60	61.09
1974	46.60	25.31	12.52	84.43
1975	105.65	22.44	9.92	138.01
1976	77.59	26.13	19.03	122.75
1977	132.31	15.62	19.01	166.94
1978	66.26	18.56	17.81	102.63
1979	299.66	4.59	13.80	318.05
1980	370.43	6.15	14.27	390.85
1981	394.92	--	20.41	415.33
1982	335.83	--	27.89	363.72
1983	258.31	--	31.25	289.56
TOTAL	2311.56	209.82	222.95	2744.33
PERCENT	84.2	7.6	8.2	100.0

Source : Central Bank of Jordan, Monthly Statistical Bulletin, several issues

Excise tax has been on the increase in recent years with most of the revenues coming from tobacco and cigarettes. Licences also generated a good amount of revenue mostly from vehicle licences, by which each car owner is supposed to pay a fixed licence fee on an annual basis. An additional tax is imposed on imports over and above custom duties. Fees are also charged on imports over mainly transoportation equipment -in addition to custom duties. In spite of the steady increase in total indirect tax revenues has slightly decreased in recent years due to the rapid increase in direct taxes. Reasons for the growth in direct taxe will be explained in the following section.

Direct Taxes Direct taxes rank as the third most important source domestic revenues after idirect and non-tax revenues. As explained earlier, direct taxes are composed of income and corporate taxes in adition to other direct taxes imposed for different reasons.

Table 5 shows revenues generated from all types of direct taxes. Government statistics do not separate between income and corporate tax. However, most of the revenues generated from income tax are generated from corporate income tax. Low salaries and generous tax exemptions mentioned in the previous section, have decreased the share of personal income tax in total direct tax revenues. Meanwhile, heavy corporate taxes and the significance of corporate profits realised during the economic boom have caused the share of corporate income tax to increase. Table 5 also shows the steady increase in direct tax revenues and the increasing share of direct taxes in total revenues. But in spite of the increase in direct tax revenues, the contribution of direct tax revenues never exceeded 20 per cent of total tax revenues.

Table 4: Indirect tax revenue, Jordan (in JD millions)

Year	Customs	Exise	Licenses	Fees	Additional tax	Total indirect tax	%Change	%of total tax revenue
1967	8.19	5.05	1.01	1.85		16.10	1.2	88.1%
1968	8.84	5.52	1.41	1.49		17.27	6.8	90.0
1969	10.65	6.08	2.17	1.80		20.70	20.3	90.0
1970	9.10	5.09	1.87	1.54	1.35	18.96	10.7	88.0
1971	7.68	6.87	2.13	2.21	1.50	20.40	7.9	87.5
1972	9.54	7.78	2.55	2.69	1.92	24.48	20.0	88.2
1973	12.19	7.77	3.90	3.95	2.39	30.22	23.8	88.5
1974	16.85	8.98	4.97	4.12	2.90	37.83	25.1	86.7
1975	20.90	10.65	5.91	7.66	3.64	48.78	28.8	83.8
1976	39.98	9.09	10.60	12.66	5.28	77.63	59.3	87.2
1977	63.99	9.87	13.10	8.36	6.40	102.70	32.3	86.4
1978	61.35	6.99	13.29	13.40	6.17	101.23	(1.5)	82.1
1979	72.06	10.56	16.59	17.06	8.00	123.28	21.7	81.5
1980	78.03	13.21	18.90	19.54	10.11	139.89	13.4	80.0
1981	94.07	16.88	25.17	36.54	11.52	184.28	31.7	79.0
1982	109.75	24.11	24.81	38.00	12.69	209.36	13.6	79.4
1983	121.61	35.38	25.70	40.26	13.89	236.84	13.1	80.1
1984	126.50	37.00	28.50	43.47	16.00	251.47	6.2	79.6

Source: Ministry of Finance and Central Bank of Jordan, Annual Report, several issues

In addition to personal and corporate income tax, direct taxes also include types of taxes such as property tax, departure tax and social services tax. Among these taxes, departure tax is gaining importance after the imposition of 10 JD on every Jordanian leaving the country through the airport. The government expects to collect 10 million JD from this tax alone in 1985.

Non-Tax Revenues Non-tax revenues rank second after indirect taxes in terms of importance in revenue generation. Non-tax revenues are mostly generated from government services or investments. Table 6 shows the major sources of non-tax revenues. As can be noticed, non-tax revenues have increased about 27 per cent annually in the last five years, surpassing in growth rate both direct and indirect taxes.

Table 5: Direct tax revenues, Jordan

Year	Income tax	Other taxes	Total direct taxes	% Change	%of total tax revenue
1967	2.05	.10	2.15	7.5%	11.5%
1968	1.77	.44	2.21	2.7	9.4
1969	2.24	.38	2.62	18?1	9.8
1970	2.47	.23	2.70	3.8	11.2
1971	2.84	.53	3.37	24.8	12.4
1972	3.20	.60	3.80	15.1	11.7
1973	3.84	.55	4.39	15.5	11.4
1974	5.32	.36	5.68	29.3	13.2
1975	9.27	.85	10.12	77.8	16.0
1976	9.34	2.09	11.43	12.9	12.8
1977	12.24	2.75	15.99	39.8	13.5
1978	18.56	3.50	22.06	38.3	17.8
1979	22.42	5.42	27.85	26.3	18.4
1980	27.88	6.97	34.84	25.1	19.9
1981	39.98	8.79	48.77	39.9	20.9
1982	43.54	10.10	53.64	10.0	20.5
1983	45.92	10.11	56.03	4.4	19.3
1984	49.00	15.10	64.1	1.1	20.4

Source: Ministry of Finance and Central Bank of Jordan, Annual Reports, several issues

The major item included under non-tax revenue is the interest and profits generated by the government, most of which come from the profit of the Central Bank of Jordan whose net profit for 1984 was 45 million dinars, or 91.8 per cent of the total interest and profits item for that year (Central Bank of Jordan 1984: 47).

Table 6: Non-tax revenues, Jordan (in JD millions)

Year	Post, tlgr. and teleph.	Interest and profits	Miscell aneous	Total non tax revenue	% Change	% of dom. revenues
1967	1.28	2.05	3.88	7.22	35.8%	30.7%
1968	1.00	2.88	3.28	7.16	(1.4)	27.0
1969	1.06	4.64	3.82	9.52	33.8	29.2
1970	1.01	4.82	2.97	8.80	9.2	29.9
1971	1.15	5.12	6.17	12.44	40.9	34.7
1972	1.10	3.82	9.87	14.79	18.8	34.8
1973	1.30	5.33	5.43	12.06	8.1	26.0
1974	1.56	8.47	12.13	22.16	84.1	33.4
1975	2.23	10.83	11.41	24.47	10.4	29.5
1976	2.27	10.10	6.14	18.51	(24.2)	17.2
1977	3.45	12.42	8.63	24.50	32.4	17.2
1978	7.59	14.35	13.25	35.19	43.3	22.2
1979	8.86	15.68	12.68	37.22	5.7	19.5
1980	11.98	21.17	18.33	51.48	38.1	22.7
1981	12.67	45.02	18.54	76.23	48.2	24.6
1982	20.72	53.01	25.18	98.91	29.7	27.5
1983	23.33	55.42	31.86	110.61	11.8	26.8
1984	33.00	49.00	40.15	122.15	10.3	27.9

Source: Ministry of Finance and Central Bank of Jordan, Annual Reports, several issues

Revenues from post, telegraph and telephones have also increased at a steady rate. But the growth rate has accelerated in the last few years after the installation of a new telephone network which now covers the entire country.

Total non-tax revenues are greater than revenues from direct taxation. This is partly due to low income and tax evasion. Non-tax revenues are not a function of income in most cases and more important, cannot be evaded. In addition to that, non-tax revenues are usually paid for a visible service, which people tend to be willing to pay.

Government Revenues in Egypt

The Egyptian economy witnessed many drastic changes after the Second World War. These changes swung the economy from one system to another. Thus the economy operated under a liberal system until 1952, then was transformed to a socialist system. In 1974 liberalisation measures were introduced. Under all economic systems, the dominant role of government was kept. Government now accounts for 54 per cent of GDP, 40 per cent of total employment and 70 per cent of total investment (Ahmed 1984). The increasing role of government in the economy have caused public expenditure to increase at a faster rate than government revenues. The wide gap betweeen government expenditures and revenues is a major problem facing Egypt and will likely remain as a challenge for years to come. Total tax revenues finance about 38 per cent of public expenditure, while non-tax sources cover about 20 per cent of total expenditure, thus leaving a budget deficit of more than 4 billion pounds in 1982. Dependence on foreign and local borrowing seems inevitable to bridge the gap between expenditure and revenues. In the next sections we will discuss major sources of revenues for the government.

External Sources of Revenues

As is the case in Jordan, Egypt also benefited from the economic boom in oil-rich countries. But, unlike Jordan, the main benefit was the remittances from Egyptian workers abroad. Egypt was deprived of Arab aid because of the Camp David Agreement. Thus, Egypt received only little financial aid -mainly from the USA- but one cannot ignore the positive role of the remittances from about 2 million Egyptian workers in stimulating the economy and hence, indirectly increasing government revenues.

Table 7 shows the amounts of aid that Egypt received in millions of LE.

Table 7: Foreign Grants (in millions of LE)

Year	1975	1976	1977	1978	1979	1980	1981	1982	1983
Grants	250.0	223.0	60.0	61.9	20.3	18.2	9.1	16.0	100.1

Source: International Monetary Fund, <u>Government Finance Statistics Yearbook</u> Vol. VIII, 1984

As can be seen from the table, foreign aid is insignificant. For 1975 and 1976 foreign aid accounted for 16 and 11 percent respectively of total government revenues. But for the following years foreign aid accounted for less than 1 per cent of total revenues. It is believed that most of the foreign aid received by Egypt is of a military nature and comes from one major source, the United States.

The lack of foreign aid was compensated by heavy borrowing from local and international sources. The amount of debt has reached a very high level lately. Total debt currently is about 31 billion dollars.

Internal Sources of Revenues

Major internal sources of revenues are classified according to the source: tax or non-tax revenues, as detailed in the following section.

Tax revenues Tax revenues constitute the most dominant source of revenues in Egypt accounting on average for 90 per cent of total government revenues and 60 per cent of total public sector revenues (Ahmed 1984: 16). Tax revenues grew at a fast rate which averaged 28 per cent in nominal terms for the period from 1974 to 1983. Rate of growth varied between different types of taxes as described below.

Indirect Taxes

Indirect taxes are the major source of local revenue, accounting on the average for 63 per cent of total tax revenues. For the period under study, indirect taxes increased at an average rate of 22 per cent.

Table 8 shows the types and magnitude of indirect taxes.

It is evident from table 8 that custom duties are the major source of indirect tax revenues. Custom duties increased at an average rate of 18 per cent per year in the period from 1975 to 83, reflecting a slower growth rate in total indirect taxes. Consumption taxes are the second most important source of indirect tax revenues and have also increased at an average of 24 per cent over the same period.

Stamp tax is gaining importance and is increasing at a fast rate which has averaged 26 per cent per year. Other indirect taxes increased at an annual rate of 9 per cent for the same period and surpassing stamp tax in importance. The strong reliance of the government on consumption and custom duties is obvious. The main problem with those types is their passive nature and the difficulty associated with increasing the rate of taxation. However, one may argue that setting different exchange rates for imports may serve as an additional duty on imports, as long as exchange rates do not prove advantageons to imports.

Table 8: Indirect Tax Revenues (in millions of LE)

Year	Consump tion	Custom duties	Stamps	Others	Total	% Change
1975	231.2	502.2	44.7	51.7	829.8	
1976	283.6	537.8	61.2	55.5	938.1	13.1%
1977	339.7	979.4	89.8	71.4	1480.3	57.7
1978	360.3	919.8	126.2	96.5	1502.8	1.5
1979	566.8	905.0	154.8	150.3	1776.6	18.2
1980	699.7	1329.4	167.9	174.6	2371.6	33.4
1981	812.6	1573.2	239.3	230.5	2855.6	20.4
1982	1217.0	1651.0	254.4	222.5	3344.9	17.1
1983	1713.3	1719.0	222.6	247.8	3902.7	16.7

Source: Ministry of Finance of Egypt

Direct Taxes Direct taxes represent the second most important source of revenues in Egypt. The average contribution of direct taxes to total revenues exceeded 36 percent for the period from 1975 to 1983. Direct taxes are also increasingly assuming an important role at the expense of indirect taxes. Recent years have show a fast growth rate for direct taxes.

Table 9 shows types and magnitude of direct taxes. One can notice the fast growth in revenues from indirect taxes which averaged 45 per cent annually for the period under study.

Personal income tax achieved a moderate growth rate of 12 per cent annually. The introduction of the new tax law which offered generous tax exemptions in addition to the relatively low income contributed to the moderate increase on personal income tax.

Business profits contributed significantly to the growth of direct tax revenues by increasing at an annual average of 45 per cent. Much of the growth in business profits is attributed to Suez Canal dues which started to come in very rapidly since it was re-opened in 1975. Table 10 shows the revenues from Suez which are included under business profits.

Table 9: Direct Tax Revenues Egypt (in millions of LE)

Year	Personal Income	Business Profit	Other Taxes	Total Direct	% Change
1975	42.3	161.8	94.4	300.4	----
1976	47.7	277.6	90.3	415.6	38.3%
1977	54.9	387.2	109.2	551.3	32.6
1978	51.9	538.4	135.5	725.8	31.6
1979	55.1	655.7	159.3	870.1	19.8
1980	73.2	1506.3	244.4	1824.0	209.6
1981	85.4	1577.7	281.6	1944.7	6.6
1982	110.0	1554.3	419.0	1983.3	7.1
1983	127.3	1893.6	502.2	2523.1	21.1

Table 10: Dues from Suez Canal (in millions of LE)

Year	1975	1976	1977	1978	1979	1980	1981	1982
Revenues	33.2	121.7	167.4	201.1	412.1	464.3	621.8	657.8

Source: International Financial Statistics Yearbook 1983

Revenues from the Canal contributed on the average more than 40 per cent of the business profits item.

Another major factor the led to the rapid increase in business profits is the surplus transferred from the petroleum sector, and to a lesser degree, growth in taxes collected from private industrial and commercial activities.

Other taxes listed in table 9 include taxes on property, estate duties, taxes on immovable property and local government tax revenues. The most important tax under this group is the property tax to which most of growth is attibuted.

Non-Tax Revenues

Non-tax revenues rank third in terms of importance after indirect and direct taxes. Non-tax revenues contribute on the average to about 8 per cent of total government revenues and increased at an average rate of 30 per cent annually for the period from 1975 to 1983.

Non-tax revenues consist of fees, local government non-tax revenues and other revenues.

Table 11 shows major sources of non-tax revenues. Fees are growing steadily but at a slower rate when compared to other non-tax items. Local government revenues are also limited in scope, but growing at a slow rate. Miscellaneous revenues are the most significant because they incorporate many items.

Table 11: Non-tax Revenues, Egypt (in millions of LE)

Year	Fees	Local Government	Miscellaneous	Total	% Change
1975	32.4	16.2	62.8	11.4	----
1976	38.2	17.5	63.1	118.8	6.6%
1977	46.8	23.0	65.9	135.7	14.6
1978	53.8	28.2	65.2	147.2	8.4
1979	81.3	32.5	153.4	267.2	81.5
1980	123.9	50.4	319.7	494.0	84.8
1981	127.2	60.9	398.9	587.0	18.8
1982	248.3	71.3	472.4	792.0	34.9
1983	272.4	87.9	581.3	941.6	18.8
1984	297.6	98.6	693.4	1089.6	15.7

Source: Ministry of Finance of Egypt

The state budget for 1984 anticipated an increase in total revenues by 14 per cent but a budget deficits of LE 2425 was also anticipated (Central Bank of Egypt 1983: 12). Deficits are largely financed by additional debt, thus increasing the debt burden, which will remain as a challenge to government in the future.

Government Revenues in Kuwait

Government revenues in Kuwait differ greatly in sources and magnitude was compared to Jordan and Egypt. While Jordan and Egypt suffer from a lack of financial resources, large budget deficit and mounting external debt, Kuwait, thanks to its oil exports, is far from encountering such problems. The increase in oil revenues in Kuwait is more than the increase in public expenditure. For the period from 1971 to 1983, Kuwait never had a deficit in the budget. Therefore, government budgeting is primarily concerned with distribution rather than redistribution of wealth (Khouja 1979: 112). Tools necessary for redistribution of wealth are either non-existent or too weak to have any significant influence.

The classical division of revenue, sources may not apply to Kuwait because this country has one major source of revenue namely oil exports. Revenues from the oil sector are so signficant that it is unncecessary to impose taxes to increase revenues.

Table 12 lists all sources of revenues for Kuwait. Personal and corporate taxes are non-existent, figures listed under corporate tax in column (2) are actually taxes imposed on foreign oil companies operating in Kuwait. Other industrial or commercial activities are tax exempted. Corporate taxes were significant in the first few years and then dropped to a very low level after the nationalisation of foreign oil companies.

Property and fees listed in column 3 include property transfer fees, fines and administrative fees. Total revenues from this item have grown at a very low rate. Total revenues from property taxes and fees have never exceeded 0.5 per cent of total revenues. Excise taxes are imposed on domestic goods and services. This item was relatively significant before the first oil price increase, but was lowered after the oil wealth started to flow. The average contribution of this item is also less than 1 per cent of total revenues.

Kuwait does not impose heavy custom duties on imports but duties that do apply to certain types of imports usually are not more than 4 per cent of import value. Total contribution of custom duties averaged 1.2. per cent of total revenues for the period under study.

Oil revenues listed in column 6 in the table, should be taken together with investment income because both items belong to the oil sector. Both oil revenues and investment income contributed 95 per cent of total revenues. In spite of

Table 12: Government Revenues, Kuwait (in million KD)

Year (1)	Corporate (2)	Property and fees (3)	Excise (4)	Custom duties (5)	Oil revenues (6)	Investment income (7)	Other non-tax(8) (9)	Total revenues	% Change (10)
1971/72	418	5	120	9	500	42	5	1099	10%
1072/73	452	5	132	11	537	50	4	1191	8.0
1973/74	928	6	298	17	584	89	14	1936	62.5
1974/75	398	6	16	21	2534	152	12	3130	61.6
1975/76	430	7	45	32	2793	328	10	3645	16.4
1976/77	109	8	33	38	2598	329	10	3135	(13.9)
1977/78	258	14	18	41	2575	384	23	3313	5.6
1978/79	80	18	19	45	3036	522	16	3736	12.7
1979/80	133	25	16	53	5940	880	12	7059	88.9
1980/81	154	32	30	68	4434	1744	38	6500	(7.9)
1981/82	91	33	25	86	2764	1364	7	4361	11.4
1982/83	92	42	16	79	2967	1657	8	4861	11.4

Sources: Calculated from Central Bank of Kuwait, Economic Report 1982 and Government Financial Statistics Yearbook 1984

government efforts to diversify sources of revenues, the oil sector is still dominating the whole economy. Oil revenues increased drastically after 1973 when oil prices started to leap.

As shown in table 12 oil revenues reached their maximum in 1979/80 when oil prices reached 34 dollars/barrel and the demand for oil was high.

Investment income is derived from the huge financial assets held by the Kuwaiti government as a surplus from oil exports. Kuwait invests the surplus in industrial countries and mostly in the United States and the United Kingdom. Investment income matches oil revenues simply because investment income is a portion of oil revenues.

Other non-tax revenues listed in column 8 consist of work permit fees, forfeits and other non-tax revenues.

Total revenues fluctuated along with oil revenues, as the latter contributed 95 per cent of total revenues. However, in spite of the decline in oil revenues for some years, total revenues increased at an average annual rate of 19.3 per cent, thus exceeding the growth rate in public expenditure. The net result of this was a surplus in the budget for most of the period under study.

CONCLUSION

From the preceding analysis, we have noticed that types and relative importance of local revenues depend vastly on other financial resources available to government. A direct implication is that taxes are imposed mainly for their revenues in the first place; the redistribution or reallocation effect of taxes comes in second place in terms of importance and policy. It has been proven that countries which lack financial resources have no choice but to depend on other local revenues, taxes being the most effective tool, whereas countries with huge non-tax financial resources, like Kuwait, do not impose any significant taxes simply because tax revenues are not needed.

It has also been noted that the level of taxation matches the surplus or the deficit in government budget. This point again emphasises the primary purpose of taxation as a source of revenue rather than an effective fiscal tool.

Table 13 shows budget surplus or deficit for Jordan, Egypt and Kuwait. It is evident that Jordan and Egypt have had constant budget deficits, while Kuwait enjoyed a significant surplus every year. The surplus in Kuwait's budget made it unnecessary to raise additional revenues through taxation or any other means, while Jordan and Egypt developed their own tax structure to provide government with the much needed revenues. However, those revenues accruing to the states from internal and external sources have failed to match the rapidly increasing expenditure. In this case the governments, of Jordan and Egypt hade three choices to solve the problem of budget deficit:

1 Increase total revenues and in particular internal revenues, because countries can do very little to increase external revenues.

2 Decrease expenditure, which may lead to economic slow-down and other social and economic problems.

3 Increase borrowing to offset the deficit in the budget, inevitably leading to more complicated problems.

Both Jordan and Egypt, whose total revenues covered 80 and 81 percent, respectively, of total expenditure in 1982, tried the first and third options with a trong recent inclination to cut down expenditures.

Table 14 shows the ratio of total tax revenues to gross domestic product (GDP) for the three countries. This ratio is also known as tax burden ratio which measures the significance of tax revenues as a percentage of GDP.

Table 14 gives a clear indication of tax efforts in Jordan, Egypt and Kuwait. Because of the heavy reliance on foreign aid, Jordan's tax burden ratio is less than Egypt's. The ratio fluctuated narrowly and kept a pace of changes in GDP. Egypt seems to have a relatively high tax burden which averaged 29.5 per cent for the period from 1975 to 1983. Kuwait is considered an extreme case in tax burden, due to the non-existence of many taxes. But after the anticipated sharp decrease in oil prices, the Kuwaiti government should think about introducing taxes, especially on income, corporate. In fact, Kuwait could easily raise additional revenues of more than one billion dinars if the tax burden were increased to 20 per cent based on 1983 figures.

Table 13: Budget Surplus of Deficit
(in millions of local currency)

Year	Jordan	Egypt	Kuwait
1975	- 18.8	-1388.0	1887.0
1976	- 81.5	-1264.7	1513.8
1977	- 61.1	-1270.0	1134.2
1978	-110.8	-2139.0	1753.9
1979	-104.0	-2907.0	4544.6
1980	-110.5	-2567.0	3025.3
1981	-100.8	-4441.0	566.2
1982	-108.6	-4164.0	92.5

Source: Arab Monetary Fund, Statistical and Economic Data 1975-1982

Table 14: Tax Burden (Tax revenues GDP) (GDP in millions of local currency)

	JORDAN			EGYPT			KUWAIT		
Year	GDP	TAX REV.	TAX BURDEN	GDP	TAX REV.	TAX BURDEN	GDP	TAX REV.	TAX BURDEN
1974	312.1	58.1	18.6	4197	1130.2	26.9%	3487	432	12.3%
1976	421.6	89.0	21.1	50.6	1353.7	26.7	3839	514	13.3
1977	514.2	117.7	22.8	6165	2931.6	32.1	4049	187	4.6
1978	632.2	123.2	19.4	7534	2227.8	29.5	4264	324	7.5
1979	753.0	151.0	20.0	9021	2646.7	29.3	6743	149	2.2
1980	979.5	176.6	17.8	12101	4195.6	34.6	7451	209	2.8
1981	1182.5	232.9	17.3	16552	4799.6	28.9	6764	261	3.8
1982	1343.2	263.1	19.5	19402	5428.2	27.9	5727	214	3.7
1983	1487.3	292.8	19.6	21324	6425.8	30.1	6218	196	3.1

Source: calculated from International Financial Statistics and tables 4, 5, 8, 9, and 12.

In the long run, Jordan will have to develop internal revenues to decrease the reliance on foreign aid. Due to low income and limited business opportunities, the development and increase of local revenues will not be an easy task. Jordan can still borrow from local and international capital markets, but this is acceptable as a short term solution. Developing export-oriented activities may be a good solution in the long run. As for Egypt, Suez Canal dues are likely to increase but this increase will be absorbed by decreasing surpluses from the oil sector.

Kuwait is not likely to face any financial problems in the future, but imposing taxes may become a necessary action at least for their redistributional effect, which will be necessary in the future.

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Chapter 3

MIGRATION AS A FACTOR CONDITIONING STATE ECONOMIC CONTROL AND FINANCIAL POLICY OPTIONS

Ibrahim S.E. Abdallah

Inter-Arab migration has become one of the most important phenomena in the Arab region, especially after the increase of oil prices during 1973 /74. The correction of oil prices after 1973 widened the already existing gap in per capita income between the scarsely populated Arab oil exporting countries in the Gulf area and North Africa and other Arab countries.

The policies of accelerated growth and rapid modernisation adopted by almost all of the oil exporting countries, necessitated increasing dependence on expatriate workers. Demand increased rapidly for both Arabs and non Arabs. Demand included all levels of skills and types of professions. The wage and income differentials between the oil and non oil-Arab countries was so great that it attracted larger and larger numbers of workers and professionals, ready to try their chances through migration. A large exodus of manpower and of temporary immigrants took place from the non-oil to the oil exporting states in the Gulf and North Africa.

Without going into detailed figure about the expatriate labourers working in the area and the increase in their number during the seventies and early eighties, it is enough here to mention that more than 2.2 million Arab workers were working in Gulf countries and Libya in 1980. Almost half of these came from Egypt. More than 80 per cent of total Arab expatriate workers in the Gulf and North Africa are citizens of only three countries, namely Egypt, Jordan and the Yemen Arab Republic. Migrants from these countries constituted an important proportion of their total manpower. In Egypt the segment of manpower working abroad was about 8.5 per cent of total manpower in 1980. For YAR and

Jordan, the segment reached 20 per cent and 28 per cent in the same year.

THE ECONOMIC IMPACT OF MIGRATION

Such large migration from non-oil to oil Arab countries, resulted in major and deep changes in the structure of economies and in economic relations in the 'sending' countries.

Remittances from migrant workers became one of the most important, if not the most important, component of disposable income in the labour exporting countries. Value of remittances bypassed traditional exports in many countries and became the main source of saving. They helped finance personal consumption, investments and exports.

Data concerning recorded remittances show more than a ten-fold increase during the period 1973/80 in YAR. The increase in Jordan and Egypt during the same period was by a factor of about 14 and 30. Actual remittances were much higher. Recorded remittances are estimated to be only 50 per cent of total remittances that actually flow into the Arab labour exporting countries. Researchers in Jordan estimated transfers through the banking system and official exchange bureaus to be only 40-50 per cent of the total transfers from migrant workers. The same is true about Egypt and Sudan, where an important part of migrant savings is exchanged through the black market to finance what is termed 'own-exchange imports'. The banking system in YAR serves only about 8 per cent of the population, leaving most of the transfers in the hands of non official agents. The following table gives an estimate of the growth of remittances of migrant workers in the most important Arab countries from 1973 to 1980.

The fact that migration has resulted in large transfers of remittances, has not prevented heated discussions among economists concerning the net effect of migration on economic and social conditions in the countries of origin. Certain economists, especially in the early stages of labour migration, looked positively to the new phenomenon and considered the availability of surplus labour in a group of Arab countries and surplus funds in others, reciprocally advantageous to both groups, as each group can gain from exchange of its surplus factor of production with the factor it lacks (al-Sherbini 1977). Later, while more and more economists doubted the reciprocal advantages to both groups of countries, they still considered that migration had both positive and negative effects

Table 1: Evolution of Remittances of Migrant Workers, 1973 - 1980 (in millions of dollars)

	1973	1974	1975	1976	1977	1978	1979	1980
<u>First Group</u>								
Jordan	45	75	172	388	408	438	510	630
Sudan	4.2	2.5	140	160	130	240	270	--
Syria	5	62	99	140	234	231	290	--
Egypt	85	189	366	755	896	1761	2282	2625
YPDR	33	41	58	119	188	257	314	342
YAR	135	--	270	676	987	946	1025	--
Total	353.2	--	1105	2238	2852	3873	4691	--
<u>Second Group</u>								
Tunisia	98	118	161	364	311	538	589	--
Algeria	371	390	423	456	388	436	453	--
Morocco	249	359	489	499	574	657	944	--
Total	718	864	1073	1319	1473	1631	1986	--

Source: Adopted from Ibrahim Saad el-Din and Mahmoud Abdel-Fadil, <u>The Movement of Arab Workers, Problems, Effects and Policies</u>, Table 2-1, p.78.

Note: The first group include countries exporting workers mainly to Arab oil exporting. The second group includes North African countries exporting mainly to Europe.

on the economies of the sending countries. While it is difficult to measure in an exact way the net result and to determine its nature, the fact that migration cannot be prevented or eliminated makes the best policy on aimed at minimising the negative effects while maximising the positive ones (Abdel Fadil 1979, 1980; el-Din and Abdel Fadil 1963; el-Din 1979; Anani and

ABdel-Jaber 1981). Few economists and social scientists, however, emphasised that migration of manpower and population in the present social context can only lead to a complete waste of resources and to the spread of negative attitudes and values that will adverselly affect development in both the sending and receiving countries (Fergani 1980).

Whether the net effects of migration to the sending countries are negative or not, it is nevertheless, useful to summarise the main effects of large scale migration on the economies of the sending countries.

(a) It is an accepted fact by almost all economists that large scale migration from Arab countries with surplus labour has helped lessen both disguised and open unemployment in the countries of origin. It is also agreed that the phenomenon has not disappeared completely. Migration does not necessarily draw upon the excess available labour. Demand for migrant workers is highly selective and biased toward higher skills. Figures concerning migrant workers in the Arab world show that outward flows of workers include all levels of skills and all types of professions, but the proportion of professionals and skilled workers to the total of migrant workers is much higher than the proportion of other categories to total manpower. Most of the sending countries, which originally suffered from shortages of professional and skilled workers, have suffered more as a result of migration. This is particularly true in the case of Sudan, Jordan and YAR. But it is also the case of Egypt. Large scale migration from Jordan has led to acute shortages in professional and skilled workers which has adversely affected the implementation of development programs, especially the creation of new industrial projects enlargement of the port of Aqaba and irrigation projects in the Jordan Valley, etc. (Anani and Abdel-Faber 1981).

In the case of YAR, even though most of the migrant workers are non-skilled, a great number and a higher percentage of skilled and professional Yemenis leave their country to look for better employment possibilities in the oil countries, causing considerable shortages of skilled workers (Fergani, ?). The 1976/80 development plan expected a shortage of manpower supply of about 38 per cent of total demand, mainly in skilled workers and technicians.

In Egypt, the large increase in demand of construction workers by the Arab oil countries led to a very high increase in wages construction due to shortages in trained construction workers caused by migration. This led to recruitment of increasing numbers from the agricultural sector. Both migration of farm workers to both the Arab countries and the construction sector led to a scarcity of labour in certain agricultural areas. These negative effects were strengthened by the weak occupational mobility in the local market (Choucri, Ekarns and el-Din 1978). Shortages in professional and skilled workers in other occupations led to the deterioration of many services. University education suffered greatly from migration of professors (el-Din 1980).

Besides the shortage of labour in the labour exporting countries, and because of it, is a high worker turnover, an increase of absenteeism and lack of discipline. Studies in Jordan, YAR and Egypt indicate a deterioration in work discipline in all three countries due to migration.

(b) Increasing remittances are supposed to help finance development and cover deficit in the balance of payment of the countries of migrating workers' origin. The fact is that such a positive effect of remittances has been limited by the way large scale migration of Arab workers to oil countries influences the consumption patterns in sending countries. The high income oil producing and exporting countries in the Gulf and North Africa are affluent societies, enjoying a very high standard of living and consuming mainly imported non-durable and durable goods. Workers who move to these countries are affected by the consumption patterns and the widespread consumerism in most countries. This 'demonstration effect' has a great influence on consumption in the labour exporting countries, because of the temporary nature of migration and the high turnover of migrants. Migrants returning during vacations or after they have finished their work, bring with them new modern imported goods that they demonstrate among their friends and neighbours, arousing their envy and pushing them to try to acquire similar goods either through migration or directly from the local market, if they can achieve a higher income locally. The new consumption patterns that have spread in the last ten years in Arab labour exporting countries include many imported durable and non-durable goods or commodites that have a very large import component. During the period 1971/79 the number of electric refrigerators consumed in Egypt increased by 26 per cent annually, washing machines by 25 per cent, television sets by 37 per cent, private cars by 26 per cent and metal furniture by 24 per cent (el-Din and Abdel Fadil 1963).

In Jordan, expenditure on personal consumption increased from 161.1 million dinars in 1971 to 520.5 million dinars in 1979 at current prices while Jordanian imports of consumer goods increased in the same period from 33.44 million dinars to 215.21

million. Thus, while total expenditure on personal consumption increased little over three times, importation of consumer goods increased by nearly seven times (el-Din and Abdel Fadil 1963). The same trend is true for the YAR and Sudan. Various studies in a number of Arab labour exporting countries have shown high correlation between migration remittances and importation of durable consumer goods.

Such preferences for fancy imported goods or commodities with a high import content lead to the loss of an important part of the financial resources and savings that would otherwise have been available because of migration. The net beneficial effect, especially in the long run, of migration on facing balance of payments is now doubted by more and more economists.

(c) Remittances add to personal income. Decisions concerning their allocation to consumption or savings depend on individual decisions, within the context and general rules and conditions governing the economy as a whole. The saved part of remittances plays an increasingly major role in determining the size of aggregate national savings of the labour exporting societies. Decisions of migrant workers concerning investment of their funds to a large extent determine the pattern and size of investment. Few studies have investigated the actual behaviour of migrant workers concerning the use of their saved funds. A survey by the Royal Jordanian Society in the summer of 1980 showed that more than 50 per cent of families included in the survey did not make any investiment, while 22 per cent invested in real estate, especially in the ownership of small apartaments (al-Saket 1981). Table 2 is a summary of the findings of the survey mentioned above.

Studies by the central bank of Jordan confirm the fact that only a minor part of migrant's remittances were directly invested during the period 1965/79, and that only a small part of these invested funds were channelled to productive projects (al-Nabawi and al-Shaar 1982).

In Egypt, sample surveys conducted on construction workers (Al-Ahram 1978), school teachers (Messeiha 1980) and university professors (el-Din and Omar 1980) showed that the greatest part of the savings of migrant workers is invested in real estate. While school teachers and university professors tend to invest in bank deposits, construction workers invest the largest part of their savings in private self-operated business (especially in the purchasing of taxis and partnerships in small shops). Table 3 is a summary of the results of the abovementioned surveys concerning the patterns of investment.

Table 2: Patterns of Investment of Remittances by Migrant Workers, 1980 (per cent)

Type of investment	High income group	Groups with less than high income	Palestinian Camps 1948	1967	Villages	Total
Returning migrants						
- Purchase of non-agricultural land	1.5	0.2	-	0.3	0.5	2.5
- Purchase of non-agriculture and non-industrial buildings	3.4	4.6	2.3	3.6	4.0	19.9
- Investment in ag. projects	-	0.2	-	-	0.2	0.4
- Investment in ind. projects	1.0	0.2	0.2	0.3	0.3	2.0
- Investment in govt. bonds	-	0.2	0.2	-	-	0.4
- Investment in stocks	0.5	0.2	-	-	-	0.7
- Others	8.8	15.5	8.7	12.9	6.5	52.4
not mentioned	4.2	5.6	3.3	4.9	3.7	21.7
Present migrants						
- Purchase of non-agricultural land	3.2	1.2	0.6	0.8	2.1	7.8
- Purchase of non-gricultural non-industrial bldg.	4.2	2.3	2.8	4.9	5.4	19.6
- Investment in agric. project	0.9	0.4	-	0.5	0.9	2.7
- Investment in ind. project	1.4	0.2	-	0.9	0.7	3.2
- Investment in govt. bonds	1.4	0.2	-	0.5	0.5	2.3
- Investment in stocks	1.9	0.9	-	0.5	0.7	4.0
- Others	2.4	4.0	1.9	4.2	3.7	16.2
- Not mentioned	9.5	17.2	9.7	3.0	4.7	44.2

Computed from al-Saket "Remittances by migrant workers and their uses" p. 116 and published in Ibrahim Saad El-Din and Mahmoud Abdel-Fadil (1981) Movement of Arab Manpower, Problems, Effects and Policies, Royal Scientific Society, Amman, p. 96.

Table 3: Investment Patterns of Remittance of Selected Occupational Groups in Egypt, 1978

Fields of investment	frequency % among construction workers	frequency % among school teachers	frequency % among university academic staff
Buildings	12		55
Purchase of agricultural land	4	25	6
Participation in initiation of new private projects	38		33
Purchase of productive equipment including transportation vehicles)	8		
Bank deposits	6	31	55

Source: Ibrahim Saad el-Din and Mahmoud Abdel Fadil (1963) Movement of Arab Manpower, Centre of Arab Unity, Beirut Table 2-11, p. 98 based on studies by Egyptian authors.

In Sudan, the result of a sample study by Dr. A. Awad (1) and Galal el-Din indicates that the major part of the savings of migrants to the oil countries were invested in the following fields:

- Purchase of apartment houses already constructed and land for contruction in big cities, especially Khartoum
- Construction and improvement of houses
- Purchase of taxis and other transportation vehicles
- Opening of small shops and cafeterias, etc.

Moreover a number of observations indicate that migrants from the rural areas in Egypt, Jordan, YAR and Sudan invest part of their savings in the purchase of tractors, agricultural machinery and electric motors.

Generally speaking, the portion of savings that is invested in the productive sectors (especially agriculture and industry) is very limited. The largest part is absorbed by the real estate sector, fuelling speculation which pushes the prices of land and buildings higher and higher.

(d) If the net beneficial impact of large-scale migration and remittances on the balance of payments deficit of the labour exporting countries is a matter of controversy between different economists, it is an accepted fact that remittances from migrant workers contribute to inflation in the sending countries during the seventies and early eighties. Inflationary pressure increases through the following processes all related to migration:

- migrant worker remittances lead to an increase of money supply and increased of demand by migrants and their families for goods and services. Such increased purchasing power is not paralleled by an increase in productive activity, as it is generated outside the local economy. Remittances are mainly spent in markets for durable consumer goods and non durable, business and personal services and on land and buildings. The inelasticity of supply in these markets means that increasing purchasing power creates demand surplus which leads to increasing prices.

- Inelasticity of internal supply leads to an attempt to import to face additional demand. Increasing imports lead to increasing demand for foreign currency which is purchased from the black market at high exchange rates. This is compensated by higher margins and higher prices by importers.

- Migration of technical and skilled workers and increasing demand on labour internally to meet the demand of migrants for more goods and services, especially apartments and buildings, lead to wage increases that affect costs in the productive firms, thus contributing to cost push inflation as well.

- The large difference of wages and incomes between migrants and workers in the local market, leads to a lack of work discipline and ethics, and thus to lower productivity, which also contributes to the inflationary pressure in the labour exporting countries.

e) Studies about the effect of large-scale migration of manpower on distribution of income in the sending countries gave no conclusive results as to whether it leads to more or less equitable distribution.

Migration also affects distribution of income through various channels. First, there is the effect of higher wages and income abroad on remittances and the ability to support and raise the standard of living of the dependents of migrants in the sending countries. Secondly, migration affects the wage structure in the sending countries. Wages in certain sectors and in certain occupations increase greatly in comparison to others. Inflationary pressures also lead to redistribution of income in favour of the non-fixed income groups. Remittances may also affect the distribution of ownership of assets. Migrants, especially in high income groups, use an important part of their incomes to acquire new assets They are encouraged to do so through facilitations and tax exemptions.

While all such factors indicate that migration has caused unproportional changes in the income of different social groups and strata within the countries of origin, there is no proof as to whether this has led to a more or less equitable income distribution.

While it is generally accepted that remittances have increased the money income of some of the lower income groups, it is doubtful whether it has really succeeded in eradicating poverty. Inflationary pressures through the seventies and deterioration of services, especially government services, eroded the effect of income increases.

While transfer by higher income groups may increase their share of ownership through new investment, remittances by lower income groups are usually used to support their families, satisfy their demand for basic goods and meet part of the newly created demand for durables. The degree of variance of the new income generated abroad, thus, also affects the general degree of variance of future income patterns in the country of origin.

An important aspect that should be taken into consideration, however, is that migration has led to the expansion of the strata of small owners and 'own-account' operators in the countries of origin.

IMPACT ON STATE ECONOMIC CONTROLS

While it is now commonly recognised that large-scale migration of Arab workers to the Arab oil exporting countries in the Gulf and North Africa has both negative and positive effects, it is still argued whether the costs of migration exceed the benefits or vice versa. Whatever may be the case, it is an accepted fact that the tide of migration has become too strong for anyone to prevent or control it from the source. Besides, labour sending countries have become too dependent on income generated abroad and remittances transferred by their workers to take any measures that may reduce it. The now prevailing consumption patterns with high import content can hardly be changed in case of a reduction of income inflow. The expected results, if this were to occur, would be deeper balance of payment deficits and lower rate of growth of GDP.

This dependency on migration, together with the stiffer and stiffer competition that Arab workers now meet in the Arab labour importing countries from other expatriates, especially from the south and south-east Asia, lead to unwillingness of policymakers to take any steps that might harm the goose that provides them with golden eggs.

Interviews with a number of policy makers and top officials in the labour sending countries show refusal to take any steps to control the
flow of workers. Most of the officials of the sending countries consider it unwise to negotiate on behalf of their fellow migrant workers to guarantee better working conditions to ask for non-discriminatory treatment or to protect their legal rights, etc... The idea of demanding compensation for losses caused by shortages of skilled manpower or for investment in education and training is not accepted. Policymakers are also very reluctant to accept suggestions that migrant workers should be compelled in any way to contribute to the financing of their country budget or to face the burden of a negative balance of payments. Taxation of migrant income is always refused as apolicy options. It is also considered unpractical to require migrants to transfer a certain minimum percentage of their income through official banking channels.

Transfers of remittances are considered too sensitive for any measure of control. The only sensible policy option under such conditions is to provide more and more incentives as well as guarantees against possible adverse action by their own governments. Only economic levers can motivate workers-beyond the control of their government-to send back a larger part of their income generated abroad (World Bank Mission 1977).

Even in the context of a tightly controlled system, some allowances and exemptions have to be provided to the owners of income generated abroad. As far back as 1968, Egypt which had a complete government monopoly of imports, adopted what was called own-exchange imports. Through that system, private importers were permitted to import certain specific items if they needed no allocation from the foreign exchange budget. The goods which were thus imported were mainly raw materials, capital and intermediate goods needed especially by the small commodity producers. Funds needed to finance this trade were for the most part purchased from migrant workers at a higher rate than the official exchange rate. After 1970, Syria, also provided a number of outlets to the private sector to import goods financed from foreign exchange holdings abroad, or through arrangements with migrant Syrian workers abroad. Non-residents were authorised to open foreign exchange accounts in Syria and to transfer funds without clearance from the exchange office. Within the context of the overall state control system of foreign trade, a system of extraordinary permits allowed the private sectors to import raw materials, intermediate goods and even some consumer goods on a restricted list. These measures increased the share of private sector imports from 29 per cent in 1971 to about 40 per cent in 1976 (World Bank Mission 1977).

Even PDYR which is still following a socialist road of development and is closely allied to the Soviet Union, introduced some measures to encourage its migrant citizens in the Arab countries to transfer part of their income either in monetary form or in needed goods to their home country.

From 1973 award, during the same period of large-scale migration of workers, a transformation of economic systems took place in a number of Arab countries. Certain countries that used to adopt a more or less centrally planned and controlled system during the sixties and or the early seventies, went through a process of liberalisation.

Egypt, Syria, Iraq, Algeria, Sudan, Libya and PDRY, all depended on the public sector as the locomotive of development during the sixties and or the early seventies. Internal resources were mobilised and brought under control of the central government which became responsible for allocation of resources and the use of funds and the implementation of the social and economic development plans.

Most of these countries depended on administrative control devices to run the economy and ensure fulfillment of plans. Such controls were widespread in cases where resources are scarce compared with the goals sought. Policymakers and planners were, in such cases, compelled to adopt more and more administrative control devices to achieve some kind of equilibirum that could not be attained via market mechanisms except at a very high price of social injustice and deterioration of the standard of living of the masses.

In most cases, investment, were centrally directed and controlled. Foreign, as well as local capital was blockedd from investment in certain sectors or areas. Some kind of import controls, including of state or public sector monopoly of all imports, or importation of certain goods, and/or import permits were widely used. Foreign exchange was allocated by the central banks or other government organs according to priorities set the central development plans. Movement of workers to other countries needed special permission and exit visas.

The second half of the seventies was an era of liberalisation and releasing of certain control devices in a number of Arab countries. While in most countries it meant an easing of controls, the liberalisation process went as far as transforming the whole system in the case of Egypt and Sudan.

While availability of Arab investible funds and the need to encourage the transfer of remittances are among the factors that led to a certain degree of liberalisation, other economic and political reasons could not be excluded, especially in the case of transformation of the system.

(a) <u>The case of Egypt</u>

Considering the case of Egypt, we can observe that attempts to liberalise the economy started during Nasser's rule. The Egyptian economy faced certain difficulties after the mid-sixties. Pressures on the economy were caused by the war in Yemen which started in September 1963, in which Egyptian armies became involved. Besides rigidities of the system, the absence of both positive and negative incentives led to inefficiency. The rate of growth started to decline from the year 1964/65. The war with Israel, the military defeat and the protracted battles that Egypt had to bear thereafter made it very difficult to cope with economic problems. Average annual rate of growth declined to 3.5 per cent during the period 1964/65 - 1971/73, while population growth reached 2.5 per cent. As early as 1967/68 attempts were made from, inside the system to introduce a number of changes that would open the economy to some kind of cooperation with Western countries and to motivate foreign capital to invest in Egypt. It was also suggested to free the public sector from administrative controls and to depend more on the profit motive in directing economic activities. Such suggestions were made by the planning and policy committee of the council of ministers, which was then under the chairmanship of the Vice-president Zakaria Mohie el-Din, but were refused by Nasser.

Soon after his death, however, the first attempts were made to encourage the inflow of foreign and Arab capital. Law No. 65 of 1971 was issued for that purpose. But it was only after the 1973 war and the increase of oil prices that the infitah or "open door" policy was proclaimed as the official policy of the country. The October paper of 1974 declared that such a policy was necessary to benefit from Western technology and Arab funds. The public sector was then still considered as the leading sector in the Egyptian economy. Foreign capital was to be called in to finance projects approved and included in the economic development plan to help accelerate their implementation. Pressures by foreign and Arab capital, together with local capitalists, soon washed away all constraints and restrictions. Many restrictions that were imposed during Nasser's era were officially described as obstacles that deprived Egypt from the benefit of advanced Western technology and available Arab funds.

Law No. 43 of 1974 was issued permitting foreign investments in all sectors of the economy and granting guarantees and privileges to foreign and Arab capital. The law was subsequently changed to accommodate the observations and complaints of would-be investors. All privileges that were granted to foreign capital were soon extended to local capitalists also. To attact foreign capital and encourage local private entrepreneurs, a large amount of legislation was issued during the 1974-77 perid and thereafter to ease restrictions and integrate the economy more and more in the international market.

Government policies towards control of foreign exchange importation of goods and emigration of workers changed entirely after the proclamation of the infitah policy. More and more administrative controls were substituted with incentives and guarantees.

(b) The Case of Sudan

Changes in the economic system of Sudan took place after and as a result of the attempt to overthrow Numeiry in 1971. The support of the communist Party of Sudan to the unsuccessful coup led the president to make a complete change of face and policies. He allied himself with the Western countries and the conservative Arab regimes. This was accompanied by more dependence on the private sector and especially on foreign and Arab assistance and investment. As in the case of Egypt, this necessitated discarding many of the administrative control devices then in use and introducing a set of incentives and guarantees to investors, whether local or foreign.

Such a major change in economic policies is the function of a number of economic, social and political factors. Some are objective constraints while others are subjective, mainly related to the nature and preference of the ruling classes or elite. Mass migration of workers to the oil countries due to income differential is an objective phenomenon that can hardly be controlled by either administrative or economic means. Income generated abroad is very sensitive to changes in the economic climate. It can hardly be controlled by national governments of the sending countries, and cannot be mobilised by any administrative devices. At the same time, the flow of income to the countries makes it less necessary to use administrative devices. While emigration may thus encourage liberalisation of the economic system, a major change in the system is related mainly to the nature of the ruling elite and its political and ideological orientation.

EFFECT OF MASS MIGRATION ON PUBLIC FINANCE

The effects of mass migration on public finance of the Arab labour exporting countries is very hard to trace. The exodus of workers and the resultant large inflow of funds from remittances influenced the structure of the economies of the sending states as well as the relative importance of their various financial resources. While some of the most important direct effects of migration were mentioned in the first part of this paper, these are only the apparently known results.

Some of the multiplier and accelerating effects of inflows are very difficult to ascertain. This is especially so because of the lack of accurate data and because phenomena like migration and large remittances constitute a break in the system rather than a continuation of it. Furthermore, the reactions of the various Arab countries to the large increase of remittances differed because of the differences in the nature of the prevailing economic systems, the structure of the economies and the level of development. Moreover, certain variations were also caused by the choice and adoption of different financial policies. Such choices are hard to relate directly or at least solely to the increase of migration and remittances.

As mentioned earlier, migration and large increases in remittances resulted in a certain activisation of the economies of the labour exporting countries. Especially, they led to an acceleration of dependence on imported goods and very high increase of importation. They also contributed to the revitalisation of the trade, finance, and construction sectors. They caused high inflationary pressures because of both the increase of costs and higher demand. These factors influenced both the revenues of the state budgets and their expenditures.

Domestic revenues kept increasing mainly because of the rise of custom duties and the rise of business profit taxes. In Jordan, for example, total domestic revenues reached 28 per cent of GDP in 1979 compared to 22 per cent in 1972. On the average, 12 per cent of domestic revenues came from income and business taxes and 46 per cent from custom duties (World Bank 1978, 1980). In the YAR, which only established a modern tax system between 1967 and 1972, government revenues showed a dramatic increase in the seventies. Tax revenues which were equivalent to 4 per cent of GDP in 1970/71 increased to 15 per cent by 1979/80, with an average growth rate of 45 per cent per annum. Import duties constituted the single most important source of revenues in YAR. In 1979/80, they accounted for 60 per cent of total budget revenues. During the seventies, their share never fell below 50 per cent and they even exceeded 70 per cent in 1976/77, which reflected dependence on imports as the main supply for goods of all kinds (World Bank 1982).

In Egypt, which has a more complex and developed tax system, revenues from total taxes kept up with the increase of GDP. Total taxes to GDP varied between 20 per cent and 24 per cent during the period 1976 to 1981/82. Tax revenues constituted about 90 per cent of total government revenues during the period. The two most important revenue sources were the business profit tax and custom duties. Business profit tax revenue increased by about 37 per cent annually during the period. Its share in total tax revenue rose from about one-fifth to one-third during the period. This was mainly due to profits from oil and the Suez Canal. Excluding profits from both resources, share of business tax revenues varied from about one-eighth to about one-sixth, with an increasing overall tendency. On the other hand, custom duties which constituted about 40 per cent in 1976 came down to about one-third of total tax revenues by the beginning of the eighties. However, the ratio of revenues from custom duties to GDP remained around 8 per cent during most of the years as nominal revenues from duties increased by about 22 per cent per annum (World Bank 1983, Ahmed 1984).

Despite the nominal rise in revenues and of the ratio of total tax revenues to GDP, current and capital expenditures showed a high rate of increase that led, in most cases, to higher budget deficit. While most of the increase in public expenditures could be traced to inflationary pressures, whether domestic or imported, it was also caused by the ambitious capital investment programs of the governments.

In Jordan, for example, the annual rate of growth of total government expenditures reached 25 per cent during theperiod 1972-75 and about 25.9 per cent during the period 1975/79. This was due to a current expenditures increase of 21.3 per cent and 22.7 per cent in the two periods and a capital expenditures increase of 32.9 and 27.1, respectively. Current and capital expenditures thus reached extremely high levels. They increased from 36 per cent and 18.1 per cent of GDP in 1973 to 47.1 per cent and 29.1 per cent of the GDP by the end of the seventies. The very high level of current expenditures is due to the high level of military expenditures (about 17 per cent of GDP since 1975) and of expenditure on the civil services. Even though the relative importance of the civil service in current expenditures decreased after 1975, its rate of growth was around 18 per cent annually. One of the reasons for the high rate of growth was the need to incrase wages in order to retain valuable personnel in the civil service. Nominal wages and salaries were increased at a rate close to the cost of living index till 1978. A 20 per cent salary increase was also granted in 1979. Government transfers also increased because of consumption subsidies and interest on public debt. Subsidies reached about 5.1 per cent of GDP by the end of the seventies and the beginning of the eighties. Defence expenditures in Jordan have been and are covered by foreign assistance both from foreign and Arab countries. If both foreign assistance and defence expenses were excluded from the budget, the budget would show a small surplus during the seventies. This small surplus turned into deficit by the end of the seventies due to a substantial increase in subsidies and interest on debt. When capital expenditures are added, the budget showed an overall deficit during all the years.

In YAR, budgetary expenditures increased at an average annual rate of around 35 per cent between 1970/71 and 1979/80. This was less than the rate of increase of revenues for the same period which reached almost 45 per cent. However, within this period, there were two sharply constrasting phases. In the mid-seventies, the very rapid growth of imports financed by expatriate remittances increased revenues much more rapidly than expenditures. Between 1974/75 and 1976/78 revenues increased by nearly 85 per cent compared with an increase of expenditures of under 50 per cent. During the period the overall deficit declined from 6 per cent of GDP to 2 per cent. A different pattern has developed since 1977-79 as the growth rate of revenues declined to less that 17 per cent while at the same time expenditures increased by over 40 per cent annually. As a result overall deficit was more that 15 per cent of GDP by the end of the seventies.

One of the main reasons for the increase of current expenditures was the rise of wages and salaries which accounts for about two-thirds of current expenditures. General adjustment of government pay scales had to be made to meet the effects of inflation and wage increases in neighbouring countries. In 1977, salaries became twice their 1971 level. Another increase of about more than 40 per cent took place in 1979.

In Egypt, total expenditure as a percent of GDP has increased from 55 per cent in 1976 to 60 per cent in 1982/83, as compared with an increase in total revenue from 34 per cent to 39 per cent of GDP in the same period. Deficit thus remained around 20 per cent with a wide fluctuation from a low of 17 per cent in 1977 to a high of 27 per cent in 1979.

The high increase of budget expenditures is related to domestic inflationary pressures caused by the large deficit, as well as by the increase of public debt and the burden of serving debts. The deficit itself is susceptible to the influences of exogenous factors on both revenue and expenditures. The exogenous influences on the revenue side are transmitted through the dependence on the petroleum and Suez Canal revenues. The ratio of these revenues to the total reached about 35 per cent in 1980/81 but fell to less that 27 per cent in 1981/82 and less that 25 per cent in 1982/83. The decline was due to lower oil prices and oil trade. The main exogenous influence on expenditure is the magnitude of consumer subsidies which mainly depends on international food prices.

Deterioration of terms of trade causes a reduction in government receipts, raising the budget deficit. As most of the deficit is financed through domestic sources, especially bank financing, it leads to an increasing rate of inflation which then feeds back into higher budget expenditures and deficit in the next stages. An increase of food prices in the international market has the same effect as lower revenues from oil or the Suez Canal.

Exemptions from various taxes and duties are most widely used to attract migrants to bring their remittances back and invest them at home. This becomes more and more important the larger the trade deficit of the country and the larger the role played by migrants' remittances as a source of funding of the balance of payment. Tax exemptions, however, can hardly stop there. As more incentives are offered to migrants, other investors and social groups usualy press for similar treatment. While most of the labour exporting countries complain of large budget deficits, they allow such wide exemption from taxes that their benefit is doubtful at best.

Incentives via tax exemptions are more widely used in cases where the market exchange rate of the local currency differs greatly from the official exchange rate.

Egypt widely uses tax exemptions to attract migrants to transfer their savings back home. Incentives are provided in various forms.

First, under law No 43/1974, amended in 1977, private foreign investments from all taxes for a period of 5 years from the first fiscal year following commencement of production. The period could be extended to eight years. Exemptions are for ten years and can be extended up to fifteen years if investment takes place in the new urban areas. The 1977 amendment provided Egyptian investors with a number of advantages offered to Arab and foreign investors. One of the objectives of the 1977 amendment was to attract Egyptian savings abroad. For this purpose, Egyptians were provided with advantages and exemptions that were included in six acts of the law. Tax exemptions covered industrial and commercial profits, income on bonds, and total personal income.

Revenues from deposits in foreign currencies in Egyptian banks have long been exempted from taxes. However Law No 11/1983 concerning migration and the protection of interests of Egyptians working abroad extended such exemption to all deposits in any of the banks operating in Egypt by migrant Egyptians and Egyptian working abroad. Moreover, capital shares by any migrant or Egyptian working abroad in project operating in Egypt are offered the most advantageous treatment of either foreign or local capital operating in the same field.

As mentioned earlier, tax exemption for the benefit of foreign or Arab investors or for migrant Egyptians could not but be extended to all other Egyptian investors. The new joint stock company act provided Egyptian investors all the exemptions, benefits and guarantees included in law 43/1974. Tax exemptions also cover:

- interest income from bonds issued by joint stock companies and offered for public subscriptions;
- interest on bonds issued by public sector banks as well as interest on bonds issued by banks in which public sector capital accounts for more than 5 per cent if the bond are issued with the aim of financing projects within Egypt.
- profits resulting from revaluation of assets when these assets are used for participation in joint stock companies;
- real estate transactions if used for joint stock companies.

As mentioned earlier in this paper, Arab workers in the Gulf and North African oil producing countries a re not subject to any taxes from either the host countries or the country of origin. Taxation of such income by the countries of origin is refused by the decisionmakers as it may effect negatively the inflow of remittances. While the migrants benefit from all government servies when they go back to their countries, they do not contribute to the financing of these services. While they are working abroad their income from investments in their countryof origin is often exempted from taxes. Less fortunate citizens working in the local market are left to bear the whole burden.

Besides the uneven distribution of the tax burden due to such wide exemptions, their cost and benefit are not studied or known. However, as they become more and more widespread, they become harder to eliminate. We have only to take notice of the very strong reaction against any attempts to change the now prevailing rules of the game. Attempts by the minister of economy in Egypt to organise the import market and to bring the black market in foreign currencies under control in January 1985 were cruelly rebuffed. A campaign was launched against him, supported by actions from those in control of the markets causing deep crisis and a state of stagnation, finally bringing the minister to his knees.

These few remarks concerning effects of migration on public finance, do not thoroughly cover the topic which needs a more in-depth treatment as well as wider coverage. They may, however, be useful to bring to our attention the dilemma now faced by the Arab labour exporting countries. These countries are now faced by a decline or lower growth rate of inflow of oil revenues from abroad. Such a decline or lower rate of growth will influence internal economic activities and lead to the stagnation of budget revenues Expenditures however, are hard to cut down. Better mobilisation of resources through efficient and more equitable tax systems is raising and is expected to raise strong opposition from very powerful and widely spread private interest groups.

FOOTNOTES

1. The author interviewed a number of officials in Egypt, Sudan, Jordan and Yemen Arab Republic in preparation of his and Abdel Fadil's book on the Movement of Arab Workers, Problems, Effects and Policies.

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Chapter 4

STATE EXPENDITURE IN THE MAGHREB (TUNISIA, ALGERIA, MOROCCO)

Khaled el-Manoubi

If it is true that state expenditure reflects the nature of the state itself, an examination of its spending will promote a more precise understanding of the nature of the state.

In this chapter we shall employ the concept of the 'sub-rentier state', which we already introduced in previous writings (Manoubi 1985).

The reader will note as well that the concepts used and conclusions reached in this study benefit from certain commonalities that are evident through a cross-sectional analysis of the three Maghrebi states.

As for the exact definition of state expenditure, in the case of both dependent societies in general and sub-rentier states in particular, state expenditure should be taken to include the whole of the public sector subjected to the authority or control of the state. By limiting oneself solely to central government expenditure *stricto-sensu*, it is impossible on the one hand to account for the total reach of state intervention and moreover, to grasp the underlying logic of spending itself. In the hope of understanding this logic, we shall first attempt to highlight common characteristics of the three states which will provide a means of establishing both spatial (by using a few brief international comparisons) and temporal (providing a perception of underlying historical conditions of the societies being studied) analytical viewpoints. We will also employ the concept of the sub-rentier state as a means of examining the bureaucratic phenomenon on a practical and theoretical level in these societies.

The second part shall be devoted to describing, first, the principles governing public expenditure for the purpose of capital accumulation, and second, the legitimation of the nature and quality of the sub-rentier state.

Table 4.1: The Evolution of Public Expenditure in Maghreb Countries at the Time of Colonialisation as a Percentage (%) of Gross Domestic Product (GOP).

	Algeria			Tunisia			Morocco		
	Current civilian expenditure	Investment expenditure	Total	Current civilian expenditure	Investment expenditure	Total	Current civilian expenditure	Investment expenditure	Total
End of last century or beginning this century Algeria = 1880, Tunisia = 1910, Morocco = 1920	12	4	16	14	3	11	10	3	13
1955 (for the three countries)	18	9	27	17	8	25	12	5	17

Source: Samir Amin, Le développement inégal, Les Editions de Minuit, Paris, 1973, p 210

It is important to stipulate at the outset that this nature clearly manifests itself in all three Maghreb states, despite the differences that distinguish them. Although these differences seem to be diminishing, the case of Algeria stands out. There on the morrow of its independence, official sources spoke of pursuing a 'retreat from the frontiers of capitalism' and of the construction of a self-centered economy.

PUBLIC EXPENDITURE, SPECIFIC FEATURES OF THE STATE AND BUREAUCRACY

The present tendency of capitalism is characterised by a strenghtening of the state's role in coordination with capital markets, aiming at a growing socialisation of the production means, accompanied notably by a continued growth of the portion of social surplus managed by the state. Hence, total public expenditure as a percentage of gross domestic product (GDP) in 1972 ranged between 12.1 per cent and 31.8 per cent in the largest industrialised capitalist countries (Japan: 12.1 per cent; Italy: 22.1 per cent; United Kingdom: 31.8 per cent) and in the smaller European capitalist countries, it reached 21.8 per cent, 33 per cent and 34.4 for Austria, Denmark and Ireland respectively. Moreover with the deepening structural crisis of capitalism, the beginning of the present decade saw this share increase by at least two points in all the countries cited above. For the larger countries, total public expenditure as a percentage of GDP grew in 1980 to 14 per cent in Japan, 38.6 per cent in the United Kingdom and for the second group of countries to 24.2 per cent in Austria and 53.9 per cent in Ireland. In real terms, the share of the social surplus going into public expenditure is higher than the preceding percentages would seem to indicate because virtually all public expenditure is derived from the social surplus which itself is inferior in size to GDP as measured by the national accounts. As such, the percentages of public expenditure cited above must be raised by nearly 10 percentage points on average to be brought in line with the social surplus, and hence may be estimated to oscillate within a range of 20 to 60 per cent.

Independent capitalist countries such as the Maghreb states which are the subject of our study, public expenditure as a percentage of GDP is not inferior to that of the capitalist countries, approximately 25 per cent for the three states at the beginning of the 1970s and rising cautiously afterwards at equal rates within all three states. At the beginning of the 1980s, public expenditure as a percentage of GDP came close to 50 per cent in Algeria, 40 per cent in Tunisia and 40 per cent in Morocco.

Table 4.2: Public Expenditure as a Percentage of Gross Domestic Product (GDP)

Year	1972	1973	1974	1980	1981	1982	1983	GDP per cap. (1980)
Algeria	28.2	30.9	25.8	49.1	38.0	45.9	49.5	2180
Tunisia	23.1	25.6	26.5	35.2	41.6	40.6	40.6	1392
Morocco	26.0	19.0	20.0	36.1	36.4	38.8	28.2	807

Source: League of Arab States, Rapport Economique Arabe Unifil 1984; IMF, International Financial Statistics, annuals

In addition to the quantitive aspects already mentioned, it should also be noted that the portion of local (regional) social surplus spent by the state in the Maghreb grows in direct relation to average income - the size of which is determined principally by the importance of sources of rent (in fact it is rather a subrent, as we shall see) accruing for the most part directly to the state which is left in turn to redistribute them.

Even more significant, qualitatively speaking, is the allocation of public expenditure. Whereas in non-dependent capitalist countries, large and small, the major portion of public spending is destined for consumption, in the Maghrebi states the share of consumption only exceptionally exceeds 50 per cent and hovers almost invariably below this percentage.

Table 4.3: Public Consumption as a Percentage of Public Expenditure.

	1980		1980		1977	1980
Canada	88.3	UK	56.6	Algeria	41.7	43.4
USA	78.2	Italy	47.5	Tunisia	48.6	45.6
France	71.2	Austria	75.4	Morocco	51.5	58.2
Japan (1979)	70.0	Denmark	66.5			
Australia	60.1	Ireland	57.1			

Source: IMF, International Financial Statistics

In other words, more than half of public expenditure is for investment.

State intervention in gross fixed capital formation is a fundamental priority of public policy. The share of the budget allocated to investment over the total gross fixed capital formation demonstrates this, reaching in 1982 43.5 per cent in Tunisia, 59.2 per cent in Algeria and 79.6 per cent in Morocco.

In fact, state intervention in capital formation is not limited to public funds spent directly by the state, as the state totally (in most cases) or partially controls the investments of public or semi-public enterprises. In effect, this type of investment can take legal forms which differ from those of the central public administration. If we add capital formation by the public sector to that by the government, the total reaches particularly high levels: more than 96 per cent in Algeria in 1980 according to Mahnoud Ourabah (1982) (1), 70 per cent in Morocco and nearly 60 per cent in Tunisia. The equivalent figure for the centre of capitalism, the United States, is a mere 14.1 per cent of total fixed capital formation (in 1980). Thus it is clear from a methodoligical point of view that spending on the part of public enterprises must be included in the analysis of public expenditure.

In the discussion of public enterprises however, analysis must be limited to the investment aspect. This is inevitable, given investment's important role in capital formation and because information sources are limited. Many of the sources are contradictory or non-comparable when it comes to data.

Thus, while expenditure of the central government in the Maghrebi countries is in line with that of non-dependent capitalist countries, large or small, when consideration of public enterprises is added, state intervention in Maghreb is clearly more important as the state controls the largest part of the surplus which is devoted to capital accumulation (or its near entirety in Algeria) and thereby occupies a crucial qualitative role. In effect, the state is not only the locus of the polarisation of the social surplus and the centre of its appropriation, but is as well the principal source and promoter of investment. Consequently, in cases of dependent capitalism it is not possible to limit the state's role to the area of surplus circulation - despite the importance of this aspect - but rather, it is necessary to acknowledge the close relationship between the state and its role, and both domestic and foreign production relations. Therefore, and to account for this phenomenon, we have retained the definition of the state as 'sub-rentier'.

The state (and with it the public sector) not only directly underwrites the major share of capital formation, but it also assures conditions allowing national private capital expansion and strengthening providing guidance and continual support. Moreover, the survival of national capital would be threatened in a situation in which these conditions were to cease (Benachenhou 1980, 1984; Malki and Doumou 1984). One should note that public sector intervention in capital formation is not only a quantitatively dominant factor, but also plays a strategic role in determining its sectoral distribution and in guaranteeing capitalist profitability, which allows the private sector to capture a share of the social surplus. In this way, the private national sector emerges as an emanation of the state and the latter can only be conceived as a depository of global capital.

If then the state appears to impose itself on local society in the three Maghrebi countries, this phenomenon is not determined by the socialisation of production, but is an expression of the submission to the logic accumulation of capital, firstly global and then national.

In other words, capital development on the global scale as well as production relations at the national level are reproduced through the national state which, as a result, is necessarily sub-rentier. The development of local factions of the dominant class in particular, can only be sustained on the coattails of the state.

In order to perform this role, the state creates a vast bureaucratic apparatus which can be seen as a connecting link between global capital and local society. Naturally public spending is considerably affected by the existence of a large bureaucracy in terms of both its total level and destinations.

Even if bureaucracy does not in itself constitute a class, in the case of the sub-rentier state it cannot be distinguished, in theory and practice, from other fractions of the dominant capitalist class, despite the very real contradictions that mark theire relations. The phenomenon of the sub-rentier state's domination genuinely expresses one essential consideration: the impossibility of the national capitalist class to assert itself in production relations without state mediation. In dominant capitalist societies, capital (as a form of relations of production), originates social classes (the constituents of these relations) and classes express the state (capitalist). On the contrary, in the case of sub-rentier states, the following sequence holds: capital (as a form of relations of production on the global scale), originates the sub-rentier state in national society, and the state originates social classes.

This leads to the conclusion that state resources (and those of society itself) consist entirely of sub-rent, that they are a rent seemingly of external origin or a portion of the social surplus which global capital consents to leave to local society, entrusting the direct or indirect management of it to the state in conformity with the needs of production relations which generate the sub-rent in the first place. The rent remains qualitatively worn out, because of the inability of local society to control its utilisation. There are two major uses for the sub-rent:

- in support of capital accumulation - taking the lion's share of the social surplus which is returned to society in the form of sub-rent.
- in support of legitimation - receiving a necessarily limited share in most sub-rentier states.

These two categories shall be analysed in two successive paragraphs of this chapter. But first we must clarify the effect of the bureaucratic phenomenon on public expenditure in sub-rentier states.

Bureaucracy is the sum of two components: the state apparatus on the one hand and public sector on the other hand.

The state spends an appreciable amount of the GDP on administrative services. Since the 1960s nearly 9-10 per cent in Algeria and 12-13 per cent in Tunisia has been spent for this purpose. In contrast, while Moroccan spending hovered around 11 per cent till the beginning of the 1970s it has since increased considerably and seems well on the way to reaching 20 per cent.

Table 4.4: Administrative Services as a Percentage of GDP** at Constant Market Prices*.

	68	70	72	73	74	75	78	80	81	82	83
Algeria	10.6		10.2	9.7	9.2		8.8	9.9			
Tunisia	13.7	12.4							11.2	12.2	12.1
Morocco						10.2	11.8	15	17.4		

(*) The 1975 and 1978 figures for Morocco are calculated at current prices.
(**) The year is indicated in brackets

Source: Documents of the Ministry of Planning;
Ligue Arabe, <u>al-Taqrir al-Iqtisudi al Arabi al Mugad</u>;
CNRS, <u>Annuaires de l'Afrique du Nord</u>;
IMF, <u>International Financial Statistics.</u>

In this way, administration services alone absorb nearly 12 per cent of GDP in all of the Maghreb states - nearly one sixth of the national social surplus - and nearly one fourth of total public expenditure. But in order to completely evaluate the cost of the bureacracy, one must consider the purchase of goods and services consumed in large part by the bureaucracy in order to enjoy a lifestyle which often involves a certain degree of waste. The cumulative share of these two categories constitutes then nearly one-third of total state expenditure.

The importance of this portion of public expenditure is due to the growth in the purchase of goods and services (machines, cars, furniture, etc.) this has been particularly rapid in Algeria since the oil price hike (Nancy 1981) and in Tunisia it surpassed the growth of salaries and of the total of public expenditure in recent years.

Table 4.5: Salaries and Acquisition of Goods and Services as a Share of Total Public Expenditure

	(1) Expenditure for salaries		(2) Expenditure in goods & serv.		(3) Total (1+2)	
	1980	1983	1980	1983	1980	1983
Tunisia	26.2	28.3	6.7	6.4	32.9	34.7
Algeria	23.0					
Morocco					25.1	33.3

Source: CNRS, <u>Annuaires de l'Afrique du Nord</u>;
Bank of Morocco, <u>Annual reports</u>;
Central Bank of Tunisia, <u>Annual reports.</u>

Table 4.6: Growth of Administrative Spending on Salaries and Goods and Services (per cent) (annual growth rates for Tunisia only)

	Morocco 1970-1980	Tunisia 1970-1974	1974-1977	1978-1983
Salaries	47.6	12	17	20
Goods and serv.	34.4	11	21	31
Accumulated salaries, goods and services	43.9			22
Total state expenditure	32.7			18

Source: CNRS, <u>Annuaires de l'Afrique du Nord</u>;
Bank of Morocco, <u>Annual reports</u>;
Central Bank of Tunisia, <u>Annual reports.</u>

In Morocco however, expenditure for salaries was the most dynamic component; but purchases of goods and services still grew faster than total expenditure.

At the same time, one must not lose sight of the fact that expenditure for salaries is nearly four times larger than that of goods and services, and consequently constitutes the fundamental source of the hypertrophic administrative costs.

The swelling of salaries can be attributed to two principal factors:

- The need to keep up the purchasing power of at least part of the civil service, including in particular, executives as well as the army, the police and the judiciary.
- The need to meet the personnel requirements of the sub-rentier state, in order that it can play its role with respect to both capital accumulation and legitimation (however restrained), through the supply of free social services and the recruitment of personnel beyond its real needs. The latter practice is due to either apparent or latent - but in any case, chronic - under-employment dictated by the law of absolute overpopulation characteristic of dependent capitalism (Manoubi 1984).

Even if one does not take into account education and health personnel, Table 4.7 indicates that in the three states of the Maghreb, the share of public over total employment far surpasses the equivalent indicator for the industrialised capitalist states, these have an administrative work force equaling 2-3 per cent of total employment, while the Maghreb has almost triple (or more). Although sources fail to concur completely, the table reveals recurrent and pronounced disparities between the Maghreb states. These seem correlated to the level of per capita income, which is to say the amount of sub-rent available to each state, as Algeria has the highest percentage, followed by Tunisia and then Morocco. We do not wish to suggest however that the ordering be attributable solely and unconditionally to the volume of the state's sub-rent.

Table 4.7: Public vs Total Employment.

	64	66	69	70	73	77	79	80
Morocco			6.9		7.3	8.5		9.0
Tunisia	6.6			9.9		11.7		12.4
Algeria		19.5				16.9	16.7	

(1) According to L. Hajane, this percentage was 9 per cent in 1971, see Annuaire de l'Afrique du Nord 1980, Editions du CNRS, Paris 1981, p. 226.
(2) According to M. Bekkali, this percentage was 12.8 per cent in 1976, see preceding reference, p. 66.

Source: For Morocco, Récensement général de la Population et de l'Habitat 197?, Serie "S", Vol. II, 1973, Table III 5; Boutata, M. La Crise... L'Altêrnative, Edition Al Bayane, Casablanca, 1978, p. 252; IBRD, Rapport 1978 sur le Maroc, 1980 quoted by Daouad, Z.
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In effect, the demands of the states' sub-rentier responsibilities on the one hand, and on the other hand the events of history, as seen in the case of Algeria, go a long way in explaining this hierarchy. In addressing the Algerian case, one must take into account the emergence, somewhat unknown in the other two countries, of a large political and military bureaucracy preceding independence, and which the post-colonial state was obliged to absorb entirely.

One should here recall that the Tunisian colonial administration and, to an even greater extent, the protectorate on Morocco had been conceived in such a manner as to limit the occupier's bureaucratic costs. Thus, in the aftermath of independence there did not exist an inordinately swollen bureaucracy.

However one should not fail to note the remarkable convergence of these percentages in all three countries. One notes in Morocco, for instance, a moderate yet clear acceleration in the growth of this rate which could well exceed the 10 per cent mark. In Tunisia a considerable but decelerating rate of growth approaching 13 per cent has emerged, while in Algeria, one sees a considerable decrease which however, has slowed down as it approached the level of 16 per cent.

In summary, these figures seem to suggest that the different rates are moving towards a point of convergence somewhere between 13-15 per cent of total employment (2). This rate could very well constitute a characteristic of the sub-rentier state in dependent capitalist societies in a phase in which it is unable to address the question of industrialisation but, at the same time, it is still capable of preserving its independent existence.

But direct control of the state is not limited to the administrative apparatus. It encompasses the whole of the public sector producing material products and paid services which alone represent between one-quarter (in Morocco) and two-thirds (in Algeria) of total value added in the country. The administration and public sector together employ between one-third and four-fifths of salary earners, between one-fifth and three-fifths of the total work force, and equal more than half of the accumulated sum of wage payments. In Algeria this figure reaches 90 per cent. Comparing columns 3 and 5 of Table 7.8 indicates that the share of the public sector alone in the social surplus slightly but clearly surpasses the share of the administration and the public sector together in total employment. It seems therefore, it should be possible for the state to pay its personnel and those of the public sector more than the average for the total work force, owing simply to the global value added of the public sector and independently of taxation. Thus, it should be of little wonder that state and public sector wage earners enjoy an average revenue which is higher (of more than 100 per cent) than the average revenue of wage earners in the private sector, although the latter are mostly productive.

Table 4.8: The Economic and Social Impact of Government Administration and the Public Sector (in percentages).

	Admin wage earners per total wage earners	Admin. & public sector per total wage earners	Admin & public sector wage earners per total employment	Admin & public sector salaries per total salaries	Part of Public sector (without administration) in value added
Morocco	18% (+) (1971)	1/3 (++)	1/5 (++)	(++) 1/2	25% (1975)
Tunisia	19% (1977)	38% (1977)	24% (1977)	62% (1977)	29% (1977)
Algeria	20% (1976)	80% (1978)	60% (1978)	90% (++) (1978)	65% (1977)

+) L. Hajane sets this figure at 22 per cent.
++) Estimated by the author.

Source: For Tunisia: various documents of the Ministry of Planning, in particular, L'Enquete sur les entreprises publiques, 1969-1979, 1980; for Algeria: A. Benachenhou, Planification et développement en Algérie, 1962-1980, 1980, M. Durabah, Les Transformations économiques de l'Algérie 35; for Morocco: European Year Book. Annuaires de l'Afrique du Nord, H. el-Malki, "Capitalisme d'Etat, Développement de la bougeoisie et problematique de la transaction. Le case du Maroc", Revue Juridique, Politique et Economique du Maroc, No. 8, 1980, p. 219.

The share of value added generated by the public sector is however modest when compared to the role of the state in capital formation. The state accounts for the largest share of investment but receives only a smaller share of the social surplus. Thus it is clear that the state allocates some of its resources from taxation and investment income to uses outside the public sphere. We already pointed at the beneficiaries: global capital first and national private capital second. To them we now turn.

PUBLIC EXPENDITURE AS AN EXPRESSION OF THE SUB-RENTIER STATE

Public Expenditure and Capital Accumulation

Capital formation constitutes the fundamental priority of state expenditure in the three Maghreb states.

In Algeria, investment expenditure alone constitutes two-fifths of total state expenditure, and the total of capital formation, subsidies, loans and participations has represented nearly three-fifths of total expenditure in recent years. The equivalent figure for Tunisia is more than 55 per cent over the period 1980-1983. If the proportion of investment alone (31 per cent) was inferior to that of salaries and current inputs (46 per cent) during the same period, the sum of investment, subsidies, loans and participation taken together, nearly totalled two-fifths (40 per cent).

In Morocco, one can attribute the relative weakness of investment expenditure to efforts made in previous years which engendered a significant debt, and a debt serviceng factor which reached 13 per cent of total state spending in the years 1980-83. As such, the sum of expenditure for capital formation, subsidies, loans, participations and debt service amounted to more than half of total public expenditure. In Tunisia the same aggregate equals two-thirds of all of public spending with a growing part (14 per cent in 1983 against 8 per cent in 1977) reserved for debt service and reimbursement. The same applies to Algeria: in her case, the debt service burden has been multiplied by a factor of 5.25 between 1974 and 1978, and this portion has jumped from 13.9 per cent of export revenue in 1974 to 39 per cent in 1979. According to World Bank sources, the service of the foreign public or publicly guaranteed debt has sharply increased from 0.95 of GNP in 1970 to 9.8 per cent in 1982.

As far as growth rates in various public spending areas are concerned, it is generally found that capital formation is the fastest growing item whenever resources are available. If the administration's participation in and encouragement of capital formation slackens, it is the public sector that compensates at least in part for the absence of resources, even at the cost of growing debt.

Under all circumstances, the share allocated to the economic services, that the state extends to capital, continues to grow, despite the growing burden of debt service or armaments procurement.

The portion of state-funded economic services has in effect gone in Morocco from 25.6 per cent in 1972, to 28 per cent in 1981, and in Tunisia from 23.3 per cent in 1972 to 34 per cent in 1981 (see Table 4.9).

Economic infrastructure represents one of the services which the state or the public sector frequently supplies for free or at least well below cost. This item, for example, absorbs nearly a tenth or more of state investment. Moreover, investment expenditure _per se_ constitutes a huge occasion for profits to the benefit of foreign and national capital. In effect, somewhat less than one-half of capital formation is composed of studies and equipment which are essentially imported. Building and public works constitute the remainder. Here again, foreign public works enterprises play an important role in the realisation of projects, and what is not done by them is done by national enterprises which draw substantial benefits from their work.

We must now show how public expenditure and public sector investment benefit first of all global capital and national capital secondly.

First, one should address the significant decrease of agriculture's share in total capital formation in the 1960s and 70s, passing from nearly one-fourth in the three countries to nearly one-seventh in Tunisia and Morocco and one-fifth in Algeria. These figures clearly illustrate the evolution of the role of Maghrebi agriculture in the international division of labour since the departure of the European colonialists.

In effect, the colonial farmers exported dry agricultural products (cereals, olive oil and wine notably) whereas since that time agriculture seems devoted to 'developing industrial crops for export and transformation by local industry' (4). This requires the mobilisation of important hydraulic resources, which are very limited in Maghreb (5).

In this respect, M.Benhlal, commenting on a IBRD Commission 1964 study of the Moroccan economy, writes,

> Agricultural problems were the subject of the longest chapter. The report argues that agricultural reform is not necessary, but counsels rather a rapid and efficient increase in agricultural production and a concentration of public and private investment in agriculture, particularly in hydraulic infrastructure'(Benhlal 1975).

The role assigned to Morocco (as well as to Tunisia and even Algeria) can be formulated in three essential points:

- Integration into the new international agricultural division of labour.
- development geared to the interests of national capital, i.e. large and medium-sized land owners and agricultural transformation industries, which can be either state or private-owned, national or foreign.
- the opening of profitable markets to the benefits of large foreign capitalist enterprises, particularly those constructing large dams whose development has been under way since the 1940s based on plans drawn up by the colonial administration.

One should point out that 100 percent of large water-works technology and know-how has been imported along with 50 percent of the necessary raw materials, whereas the smaller water-works projects such as surface wells, which are superior to larger projects in terms of employment generation, intensification of cropping and soil protection depends on imports for no more than one-quarter of the required technologies and materials (Elamami 1980). The three countries have increasingly allocated agricultural investment funds for irrigation and large water-works projects. The share of heavy hydraulics is constantly increasing and has reached nearly two-fifths of capital formation in agriculture in Morocco and Tunisia, and one-quarter in Algeria.

Agricultural subsidies in large part tend to go to owners of large and medium-sized farms. In an inquiry conducted in the Gharb, it was learned that small farms of less than 10 hectares (not including cooperatives and breeders) received virtually no state subsidies, whereas large farms (more than 50 hectares) took in 42.2 percent of subsidies for farm materials; 85.5

percent of subsidies for fertilizers; 28.7 percent directed at selective seeding; and finally 40.4 percent of subsidies available for animal production (Libération 20-27 Nov. 1980: p. 8). A World Bank study of the Doukkala project confirmed these results revealing that at the project's termination, 'the average subsidy received by farms ranged from 2554 DH for small farms of less than 2 hectares of land to 41,213 DH for those of over 20 hectares - that is 16 times more for the latter' (Libération, 20-27 Nov. 1980: p. 8).

State and public sector expenditure for industry - in terms of subsidies as well as investments - equally serves the needs firstly of world capital and secondly of national capital.

With respect to global capital, the operations of the state and the public sector assume two distinct but not fundamentally different forms. In Tunisia as well as in Morocco, state and public sector investment is clearly integrated in the international division of labour: valorisation of raw materials (principally the processing of phosphates) for export - an extention of agro-mining activities which began during the first period of the international (and colonial) divison of labour. In Morocco, export industries have been taken over by the public sector whereas, in Tunisia, these export industries have been developed by private Tunisians or foreigners, producing, as in Morocco, in the interests and to the ultimate benefit of no other than the multinational companies.

Algeria, by contrast, has apparently not predisposed industrial development to evident integration into the international division of labour and has even endeavoured, formally at least, to construct an integrated industrial system. In the belief that it has paid the price of this avowed objective, Algeria nevertheless has accepted significant deviations of realisation from the planned goals. We have already mentioned the declining role of agriculture in capital formation - a role that lies well below expectations which themselves are in decline (6).

The share of investment dedicated to basic infrastructure is also modest as for social services. But it is the analysis of the sectorial composition of industrial investment that clarifies the subservience to world capital, which ensures in this way its hydrocarbon supplies, imposes a high cost on 'industrialisation' and causes a high propensity import in the existing industrial structure.

Hydrocarbons have, in effect, received nearly one-half of industrial capital formation instead of two-fifths, as anticipated in successive plans in the 1960s and 70s. Moreover, 90 percent of investment in hydrocarbons was to be allocated for the 'financial functions' of the sector, to the detriment of the genuine 'industrial function' (production of fertilisers, petrochemicals plastics).

It is equally significant that the total return on investment in the hydrocarbon sector only reached 4.3 per cent in 1977 against 18.3 per cent for total investments. Therefore, investment in this sector, serves merely to maintain existing production and export capacity.

As for the rest of industrial investment, nearly one-tenth of the total goes to non durable consumer goods, and an equivalent share goees to equipment goods, which are rightly considered to play a strategic role for capital accumulation.

The local private sector on the one hand receives various incentives, exemptions and direct and indirect subsidies covering financing, realisation and start up of new production capacity. At the same time, and more importantly, the private sector also benefits from low priced inputs and services supplied from the public sector. For example, one notes in this regard, that in Tunisia, for someone starting a business, it sufficed to put down only 3 per cent of the cost to realise a project up to a maximum amount of 30,000 dinars in 1974 and 75,000 in 1977, thanks to multiform state support totally nine-tenths of the costs (Dimassi 1983). As an example of the low pricing of inputs let us recall that in Algeria, the SNS public company sells 30 per cent of its production to the private sector at prices lower than both local production costs and international prices. Similarly, a national construction material company sold 40 per cent of its production to the private sector (2.5 million tons per year) at a loss of 30 dinars per ton produced or imported, generating an annual transfer of value to the private sector amounting to nearly 75 million dinars (Benachenhou 1980:109). Naturally, under such conditions, the state budget is pock-marked with costs arising from public sector losses. These costs reached 4.2 per cent of the GDP in Tunisia in 1983, whereas treasury securities taken out in the name of investment and invigoration of public enterprise reached an amount equal to GDP.

Our discussion of the support offered to private capital could not be complete without mention of the subsidies to productive consumption, which are a form of direct assistance to capital, as well as subsidies for final consumption. The latter constitute, above all, an indirect aid to the enterprises by holding back wage costs. This policy therefore reflects the logic of capital accumulation in a situation of dependence, although it also serves purposes of legitimation, which is discussed in the following paragraph.

These subsidies were instituted as short-term policy and ended up assuming a structural character to the point where they approach today 2 per cent of GDP, 5 per cent of state expenditure and 5-10 per cent of Gross Fixed Capital Formation. Such levels of had already been reached in Tunisia in 1974 while Morocco and Algeria passed them in 1980 and 1982, respectively. By 1984 Tunisia had attained rates of subsidisation twice as high as those registered ten years earlier.

The Expenditure of the Sub-Rentier State: From Restrained Legitimation to Internal Repression and Border Conflicts

Indebtedness in the Maghreb states - certainly not the same for each country - is clearly growing. The situation in Morocco has become critical as debt reached nearly 61 per cent of GDP in 1982. Yet the rate of public or publicly guaranteed debt servicento GDP in Algeria was greater than the corresponding rate in Morocco (9.8 per cent against 9.4 per cent and 5.9 per cent in Tunisia) because of Algeria's higher rates of investment, which are twice those of Morocco and 50 per cent greater than Tunisia's.

One is not surprised then to see that the three states have reduced the share of expenditure devoted to social services to the work-force, and more generally to acquire legitimation. Thus, the share of social services in total investment in Algeria has dropped from 18 per cent before 1974 to 14 per cent afterwards (according to Planning Ministry statistics). In Tunisia, the share of social services in total state spending has fallen from 47 per cent in 1972 to 37 per cent in 1981, while in Morocco, it has also fallen from 32 per cent in 1972 to 25 per cent in 1981 according to World Bank data. Measured against GDP, the growth of state spending in social services seems modest (around two percentage points) in Tunisia and in Morocco, compared to increases in economic services and defence spending, (both doubled during this particular period), and to the growth in demand for social service in connection with their expanding base.

Yet this level of expenditure for legitimation does not assure social peace in the real sense of the term and has led to the growing tendency to resort to forms of internal repression.

Table 4.9: Evolution of Total State Expenditure and its Structure.

	Morocco		Tunisia	
	1972	1981	1972	1981
Total expenditure (% of GDP)	22.4	39.8	22.5	32.4
Surplus/Deficit total (% of GDP)	-3.8	-13.6	-0.9	-2.5
Structure of expenditure (%):				
Economic services	25.6	28	23.3	34.0
Defence	12.3	16.2	4.9	8.3
Social services	32.4	25.1	46.7	36.6
of which:				
- teaching	(19.2)	(16.5)	(30.5)	(15.3)
- housing and welfare	(8.4)	(5.6)	8.8	(13.6)
- health	(4.8)	(3.0)	(7.4)	(7.7)
Other expenditure	29.7	30.7	25.1	21.1

Source: World Bank, World Development Report 1984 (in Arabic), pp. 306-7.

Table 4.10: State Expenditure Structure and Importance (percentage share over GDP)

	Morocco		Tunisia	
	1972	1981	1972	1981
Economic Service	5.7	11.1	5.2	11.0
Defence	2.8	6.4	1.1	2.7
Social services	7.3	10.0	10.5	11.9
Of which:				
- teaching	(4.3)	(6.7)	(6.9)	(5.0)
- housing & welfare	(1.9)	(2.2)	(2.0)	(4.4)
- health	(1.1)	(1.2)	(1.7)	(2.5)
Other expenditure	6.7	12.2	5.6	6.8

Source: World Bank, World Development Report 1984, (in Arabic), pp. 306-7.

However, the latter has proved insufficient to consolidate state authority, the state is forced to seek legitimation by leading the country into border conflicts with neighbouring countries.

Border area conflicts among sub-rentier states have not been a rare occurrance in the Maghreb in the post-colonial period. All five states of the Maghreb, when viewed in terms of the bilateral relationships stipulated by their common borders, have experienced border conflicts, without mentioning clashes, with other neighbouring non-Maghrebi states.

Border area conflicts in a certain way represent the reality of the sub-rentier state and are indeed organically bound to its very nature. They require significant military resources which, although providing some legitimation, are not sufficient to dispense of internal repression. Hence the swelling of the resources allocated to the police. How large exactly are these resources?. It should be noted that important data on military and police spending remain unavailable and are classified as military secrets. This expenditure is only partially accounted for in official statistics. Nevertheless, available information makes it possible to form a rather clear idea of the increasing role of military spending.

Similarly, the three states have taken the course of increasing their acquisition of armaments since the beginning of the 1970s for use in internal repression. This has been particularly true for Tunisia.

In only four years (1972-76) the size of the Tunisian police force doubled from the 1970 figure of one police agent for every 700 inhabitants to one every 500 in 1976. This effort continued in the 1977-81 plan.

In total, domestic and defence spending oscillates between one-third of state personnel expenditure (in Algeria) to two-fifths (in Morocco) (Bank of Morocco 1983). This figure grew more rapidly than those for teachers and health services personnel.

As far as equipment spending is concerned, the share of military spending in this area has risen from a neglible amount in the early 1970s to 26 per cent of direct state investment in 1982 (7). In Morocco, military equipment expenditure, which represented only 3 per cent of all state investment during the period 1968-72 rose to 15 per cent between 1973-77.

The share of defence in total state expenditure has risen in Morocco (from 12.3 per cent in 1972 to 16.2 per cent in 1981) and even more so in Tunisia (from 4.9 per cent in 1972 to 8.3 per cent in 1981). Relative to GDP, the share of defence has similarly grown from 2.8 per cent in 1972 to 6.4 per cent in 1981 in Morocco and from 1.1 per cent in 1972 to 2.7 per cent in 1981 in Tunisia. According to available information, it seems that Algeria, stands in an intermediary position vis-à-vis Tunisia and Morocco. The latter makes the greatest effort in relative terms, with defence allocations equalling 40 per cent of total state spending at the beginning of the 1980s (Bernard 1981).

NOTES.

1. In spite of the underestmation of the portion of private capital in Gross Fixed Capital Formation, it is very low in Algeria, though not negligible. In the three countries, the portions presented otherwise constitute a relatively good approximation of reality.

2. This corresponds closely to the share of administrative salaries in GDP that we have already deduced in comparing the three states.

3. In Tunisia, for example, in terms of average salary; the average income of a salaried worker in the public sector = 62/38 = 1.63. The average salary of the rest of the salaried class = 38/62 = 612. The ratio of the former to the latter = 1.63/0.612=266 or 166 per cent more.

4. See, for example, the Moroccan Plan for 1968-72, Vol 1, p 103.

5. Irrigated land accounts for 11.1 per cent of workable agricultural land in Morocco, 4.5 per cent in Algeria and 2.9 per cent in Tunisia.

6. The portion of capital formation tends to grow and to be oriented towards dry crops in the three states, but their are many doubts about this new policy.

7. According to budget figures published by the Ministry of Planning.

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Chapter 5

GOVERNMENT EXPENDITURE STRUCTURE AND IMPACT: THE CASES OF EGYPT, KUWAIT, SAUDI ARABIA AND JORDAN

Mona El Baradei

INTRODUCTION

There is no doubt that the economic positions of the Arab countries are strikingly different because of oil revenues accruing to some of them and not to others. After 1973 this variance was greatly accentuated, and a sharp economic line divided the Arab world into two groups, the balance of payments surplus countries versus the balance of payments deficit countries (Mabro 1979: 23).

At the same time, the increase in wealth and surplus funds in the rich oil states facilitated the creation of mechanisms of inter-country transfers through which the poor countries of the Arab world could secure for themselves some of the returns of the oil wealth. These transfers affected to a great extent the public budget in the countries examined and created what was called the 'rentier mentality' (El-Beblawi 1982: 214).

PUBLIC EXPENDITURE AT THE AGGREGATE LEVEL

There is generalised evidence that over the post-war period there have been sharp upward movements in government expenditure relative to GNP. There has also been pressure on governments to spend (Prest 1977: 14). The four Arab countries examined are no exception. In this case, besides the other reasons, which are common to most countries, one should mention the greater role of the public sector (Egypt) and the unprecedented increase in government revenues (Kuwait and Saudi Arabia, to a lesser extent, Jordan).

When examining the figures in Table 1, we find that Saudi Arabia has the highest annual growth rate of public expenditure as compared to the other three countries. With an average growth rate of 24.4 per cent per annum, it is followed by Egypt (15.5 per cent) and then Kuwait and Jordan with a similar rate (14.9 per cent).

Fluctuations in the rate of growth of public expenditure are higher in Kuwait and Saudi Arabia than in Egypt. However, the four countries show a big surge in the growth of public expenditure in the period of the oil boom compared to the period prior to the oil boom, and a fall in this growth, even negative growth in the case of Saudi Arabia and Kuwait (1) after this period. The figures below show the difference between annual growth rates of public expenditure in the different periods:

Country and period	% Rate of Growth
Egypt	
1963/4-1973	6.9%
1974-1980/1	31.1%
1981/2-1985/6	11.4%
Saudi Arabia	
1969/70-1972/3	18.9%
1973/4-1981/2	40.5%
1982/3-1985/6	-0.3%
Kuwait	
1963/4-1973	12.4%
1974/5-1980/1	29.5%
1981/2-1985/6	-1.9%
Jordan	
1964/5-1973	11.8%
1974-1981	23.6%
1982-1985	0.07%

Table 1: Annual growth rates of public expenditure and GDP in Egypt, Kuwait, Saudi Arabia and Jordan

	Egypt				Kuwait			
Fiscal year (1)	Total public expenditure in ml LE	Annual growth rate %	Annual growth rate of GDP%	Proportion of public expenditure to GDP	Total public expenditure in ml KD	Annual growth	Annual growth rate % of GDP	Proportion of public expenditure to GDP %
1964	1079.4	-	5.1	53.5	176.1	-	n.a.	n.a.
1965	1184.4	9.7	8.5	50.1	182.2	3.4	n.a.	n.a.
1966	1206.0	1.8	3.2	48.2	241.5	32.5	n.a.	n.a.
1967	1197.7	-0.6	1.1	43.7	274.0	13.4	-	32
1968	1099.1	-8.2	7.4	52.5	324.0	18.2	2.1	37
1969	1416.5	28.8	10.2	53.6	264.0	-18.5	9.0	28
1970	1593.8	12.5	5.9	51.2	299.6	13.4	3.9	30
1971	1612.5	1.2	8.6	50.6	324.2	8.2	9.6	30
1972	1732.3	7.4	7.1	53.7	369.7	14.0	30.7	26
1973	1970.2	13.7	14.5	48.0	436.7	18.1	9.9	28
1974	2073.0	5.2	20.4	58.0	552.9	26.4	35.4	26
1975	3015.0	45.4	22.0	55.0	1162.9	110.3	65.1	33
1976	3280.0	8.7	22.2	50.0	1337.4	15	10.0	34
1977	4169.0	27.1	19.7	57.0	1519.3	13.6	5.4	37
1978	5559.0	33.3	34.1	56.0	1959.2	28.9	5.3	45
1979	7096.7	27.6	36.7	61.0	1943.9	-0.8	58.1	28
1980	-	-	-	-	2423.7	21.6	10.5	32
1981	10555.2	48.7	17.2	63.0	3377.9	39.3	-9.2	49
1982	12887.1	31.0	3.9	73.2	3783.0	12.0	-15.5	66
1983	16896.2	-4.0	7.3	81.0	3732.0	-1.41	8.5	60
1984	16231.6	-4.0	7.3	81.0	3364.3	-9.8	n.a.	n.a.
1985	18277.2	12.6	-	-	3931.2	16.8	n.a.	n.a.
1986	19909.7	3.3	-	-	3761.7	-4.3	n.a.	n.a.
Average	-	15.5	12.8	56.6	-	14.9	13.2	36.5

* Budget

Notes:

(1) years relate to fiscal years which normally do not correspond to solar years, in this case, only the second of the two years is indicated (i.e. 1963/64 = 1964) except for Egypt from 1980 onwards and Jordan in 1964-65, for which only the first year is indicated (i.e. 1980 = 1980/81); also, fiscal years are often based on Hijra calendar years, hence, 1972 corresponds to 1391/2 H and so on.

Table 1 (cont.): Annual growth rates of public expenditure and GDP in Egypt, Kuwait, Saudi Arabia and Jordan

		Saudi Arabia					Jordan	
Fiscal year (1)	Total public expenditure in ML SR	Annual growth rate %	Annual growth rate of GDP%	Proportion of public expenditure to GDP %	Total public expendi-ture in ml JD	Annual growth rate % of GDP	Annual growth	Proportion of public rexpenditure to GDP %
1964					43.6	-	-	29.3
1965					46.9	7.5	12.5	27.9
1966					38.6	-17.7	1.7	22.6
1967					68.1	76.4	-23.0	51.9
1968					80.5	18.2	18.9	51.5
1969					88.4	9.8	17.4	48.2
1970	6028	-	-	35.0				17.4
1971	6293	4.4	31.6	27.8	80.7	-8.7	-4.9	46.3
1972	8130	29.2	23.3	29.0	83.1	2.9	6.7	44.6
1973	10158	24.9	44.0	25.3	101.4	22.0	11.2	48.9
1974	18595	83.1	146.5	18.8	119.5	17.8	5.3	54.7
1975	35039	88.4	40.8	25.0	146.6	22.6	13.2	59.2
1976	81784	133.4	17.7	50.0	204.8	39.6	26.2	56.6
1977	106737	30.5	24.4	52.3	262.4	28.1	35.0	62.2
1978	137110	28.5	9.8	61.2	337.8	28.7	21.9	65.6
1979	146255	6.7	10.6	59.0	361.5	7.0	22.9	57.1
1980	185724	27.0	55.0	48.5	515.6	42.6	19.1	68.4
1981	230416	24.1	35.0	44.5	563.1	9.2	30.0	57.4
1982	283258	22.9	0.8	54.2	647.1	14.9	20.7	54.7
1983	244900	-13.5	n. a.	n. a.	656.2	1.4	13.5	48.8
1984	223200	8.8	n. a.	n. a.	717.6	9.3	10.7	48.2
1985	212900	4.6	n. a.	n. a.	770.2	7.3	-	-
1986	200000	-6.0	n. a.	n. a.	811.2	5.3	-	-
					-	-	-	-
Average	-	24.4	32.9	40.8	-	14.9	12.8	50.6

* Budget

Sources:

Egypt: for 1963/4-1973: Reafat Al Mahgoub, Al-Maleya al-Amma, Dar El Nahda al-Arabiyya, 1973, p. 84 and CAPMAS, Statistical Yearbook, various issues; for 1974-1981/2 : World Bank, Arab Republic of Egypt, Current Economic Situation and Growth Prospects, World Bank Report No. 4498-EGT, Washington D.C., 5 October, 1983, table (2-1) p. 124 and table (5-1) p. 136; for 1982/3: Closing Account Report presented to the People's Assembly; for 1983/4-1985/6: Public Budgets presented to the People's Assembly.

Kuwait: for 1963/4-1968/9: Central Bank of Kuwait, Economic Report, various issues; for 1969/70-1978/9: Central Bank of Kuwait, The Kuwaiti Economy in Ten Years, Economic Report of the Period 1969-1979, pp. 45 and 51; for 1979/80-1982/3: Central Bank of Kuwait, Economic Report, 1983, p. 32; for 1984/5-1985/6: Middle Eastern Economic Digest, 26 April 1985, p. 21.

Saudi Arabia: for 1969/70-1981/2: Ministry of Planning, Haquae wa Arquam, 1390-14-2 H., Tables, 1,2,5, 6; for 1982/3-1985/6: Middle Eastern Economic Survey (MEES), 25 March 1985, p. B1; for GDP from International Monetary Fund, International Financial Statistics, various issues.

Jordan: for 1964/5-1983: Central Bank of Jordan, Yearly Statistical Series (1964-1983) Special Issue, Tables 36, 39 and 45; for 1984 and 1985: MEED, 4 January 1985, p. 13.

Table 2: Composition of public expenditure in Egypt, Kuwait, Saudi Arabia and Jordan (%)

	Egypt		Kuwait (9)		S. Arabia		Jordan	
Year (1)	Current expenditure	Capital expenditure (2)	Current expenditure	Capital expenditure (3)	Current expenditure	Capital expenditure	Current expenditure	Capital expenditure
1964	62.0	38.0						
1965	62.7	37.3					79.0	21.0
1966	71.3	28.7					76.2	23.8
1967	64.4	35.6					73.3	26.7
1968	72.0	28.0					65.5	34.5
1969	70.7	29.3					71.0	29.0
1970	68.6	31.4	57.8	42.2	63.3	36.1	73.8	26.2
1971	74.4	25.6	55.6	44.4	63.4	36.6	73.0	27.0
1972	72.0	28.0	65.8	34.2	58.5	41.5	73.0	27.0
1973	71.5	28.5	63.4	36.6	55.7	44.3	69.0	31.0
1974	75.0	25.0	50.8	49.2	45.5	54.5	65.0	35.0
1975	76.0	24.0	37.1	62.9	43.4	56.6	70.5	29.5
1976	80.0	20.0	49.2	50.8	47.1	52.9	61.5	38.5
1977	77.0	23.0	49.1	50.9	48.8	51.2	70.8	23.2
1978	51.6	48.4	38.8	61.2	51.4	48.6	57.9	42.1
1979	56.0	44.0	45.3	54.7	55.9	44.1	58.8	41.2
1980	53.0	47.0	51.9	48.1	51.8	48.2	62.3	37.7
1981	57.0	43.0	44.0	56.0	36.3	63.7	59.6	41.4
1982	59.9	40.1	46.2	53.8	39.6	60.4	60.5	39.5
1983	59.0	41.0	54.8	45.2	45.5	54.5	66.0	34.0
1984	62.0	38.0	69.5	30.5	n.a	n.a	62.5	37.5
1985	61.0	39.0			50.0	50.0	58.8	41.2
							60.0	40.0
Average	63.8	36.2	51.9	48.1	50.0	49.6	66.7	33.3

Notes:
(1) years relate to fiscal years which normally do not correspond to solar years, in this case, only the second of the two years is indicated (i.e. 1963/64 = 1964) except for Egypt from 1980 onwards and Jordan in 1964-65, for which only the first year is indicated (i.e. 1980 = 1980/81); also, fiscal years are often based on Hijra calendar years, hence, 1972 corresponds to 1391/2 H and so on.
Source:
Egypt: for 1963/4-1973: Reafat Al Mahgoub, Al Maleya El 'Amma, Dar El Nahda Al-Arabiyya 1979, p. 86; for 1973-1977: Mahmoud Abdel Fadil and Reda El-Edel, Mabade al-Maleyya al-'Amma... (Principles of Public Finance with special reference to the Evolution of the Egyptian Fiscal System) Dar al-Nahda al-Arabiyya, Cairo, 1982 p. 189; for 1978-1982/3: Actual spending, in the 1982/3 Closing Account Report presented to the People's Assembly; for 1983/4-1985/6: Public Budget presented to the People's Assembly.

Kuwait for 1973-1979: Central Bank of Kuwait, The Kuwaiti Economy in Ten Years, Economic Report for the period 1969-1979, Table 11, p. 51; for 1979-1983/4: Central Bank of Kuwait, Economic Report, 1983, Table 6, p. 33.

Saudi Arabia: Ministry of Planning, Haqaek wa Arquam, Mongazat Khettat al Tanmeya (Facts and Figures, Achievements of Development Plans, 1390-1402 (Ministry of Planning, Al Riad, 1403), Table 4, p. 72.; 1982/3-1984/5: EIU, Quarterly Economic Review of Saudi Arabia, Annual Supplement, 1984, p. 20.

Jordan for 1964/5-1983: Central Bank of Jordan, Yearly Statistical Series, (1964-1983), Special Issue, Table 39; for 1984, 1985: MEED, 4 January 1985, p. 13.

(2) Includes investment expenditure and capital transfers
(3) Includes investment expenditure, land acquisition and foreign expenditure
(4) Kuwaiti budgets are a curious mixture of capital and current items. The FFG receives a minimum statutory subvention equivalent to 10% of the state's total revenues, while KFAED's capital is increased by a typical KD 30-50 mn per annum. Both these items technically represent investment of reserves, but the income derived from these reserves is excluded from the government's budget calculations. In effect, the FFG and KFAED expenditures represent no more than an accounting gesture, and are best described as an allocation from investment income.

PUBLIC EXPENDITURES DISAGGREGATED

It is impossible to have a common classification of expenditures for the four countries, because on the one hand, each one of them has items that do not correspond to other countries and on the other, there are items which gain great prominence in one country so that they require separately treatament.

Table 2 gives a broad composition of public expenditure in Egypt, Kuwait, Saudi Arabia and Jordan.

The two oil countries (Kuwait and Saudi Arabia) have about the same composition between current and capital expenditures and so do the two 'semi-oil' countries (Egypt and Jordan). However, the four countries show an upward trend in capital expenditures during the period of the oil boom (1974-1981/2) averaging 34.3 per cent in Egypt, 54.8 per cent in Kuwait, 52.1 per cent in Saudi Arabia, and 37.3 in Jordan, compared to 31.0 per cent, 41.3 per cent, 39.6 per cent and 28.1 respectively in the period prior to 1974.

Egypt

The complexity of Egypt's budgetary accounting system makes it difficult to obtain a comprehensive overview of government expenditure.

Economic Classification of Expenditure A partial economic classification of expenditure is available only for current expenditure after 1979 (Table 3 below). It indicates that between 1973 and 1982/3 current expenditure has grown at a higher annual rate (43.2 per cent) than investment expenditure (25.2 per cent) with the consequence of the decline of investment expenditure as a proportion to total expenditure from 38.6 per cent in 1979 to 29.6 per cent in 1982/3.

Table 3: Egypt: Economic classification of current expenditure, 1979-1982/3

	1979		1980/1		1981/2		1982/3		Average annual growth rates (%)
	Value	%	Value	%	Value	%	Value	%	
Current expenditure	4,044.0	61.4	6,080.4	61.8	7,872.7	65.1	11,889.2	70.4	43.2
Wages & salaries	993.0	15.0	1,452.6	14.8	1,947.5	16.1	2,200.8	13.0	30.3
Defence	772.0	11.8	1,039.0	10.6	1,365.8	11.3	3,329.6	19.7	62.7
Domestic interest	208.0	3.2	340.3	3.4	360.7	3.0	890.2	5.3	35.7
Foreign interest	147.7	2.3	116.8	1.2	147.0	1.2			
Other nonsubsidy	200.7	3.0	436.3	4.4	583.6	4.8	1,756.2	10.4	106.0
Subsidies	1,352.2	20.5	2,116.4	22.0	2,199.8	18.2	2,053.6	12.2	14.9
of which: GASC	(1,002.1)[1]	(15.2)	(1,703.0)[2]	(17.3)	(1,473.1)[1,2]	(12.2)	(1,336.5)	(7.9)	10.0
Other	(350.1)	(5.3)	(463.4)	(4.7)	(726.6)[3]	(6.0)	(717.1)	(4.3)	26.9
Public Authorities deficits	234.0	3.6	274.8	2.8	414.7	3.5	127.6	0.7	-18.4
Other current transfers[4]	136.0	2.0	254.2	2.6	853.6	7.0	1,521.2	9.0	123.6
Investment expenditure	2,547.0	38.6	3,765.3	38.2	4,218.1	34.9	5,007.0	29.6	25.2
Total expenditure	6,591.0	100	9,845.7	100	12,090.8	100	16,896.2	100	36.8

NOTES

1. Excludes from current expenditure and subsidies in 1981/2 LE 122.3 million in subsidies incurred in 1979. An equal amount has been added to subsidies in 1979.

2. Excludes from current expenditure and subsidies in 1981/2 LE 595 million which is equal to the debt incurred by GASC to finance losses on its operations in 1980/81. The central government did not provide financing for these losses until January 19, 1982, when it issued a bond in the amount of LE 595 million to the Central Bank and used the proceeds to repay the GASC's obligations to commercial banks. The 1980/81 actuals have been adjusted to include this transaction as expenditure in that year.

3. LE 300 million in construction debt arrears incurred by the government since 1979, budgeted in 1981/82 but disbursed in 1982/83, has been excluded from current transfers in 1981/82. However, an equal upward adjustment has not been made to the earlier years since the allocation of the arrears to the date originally incurred is not possible. Since these were disbursed in 1982/83, they are regarded as payment of arrears in that year rather than an expenditure item.

4. Includes mainly current transfers previously classified as 'expenditure from treasury and investment funds'.

Source: 1979-1981/2: IMF, Arab Republic of Egypt, <u>Recent Economic Development</u> (IMF Document SM/83/116, June 7, 1983), p. 97, appendix I, table 48.

1982/83: Closing Account Report presented to the People's Assembly.

Interest payments experienced a high annual rate of growth (35.7%) reflecting the growth in foreign and domestic debt and consequently debt service obligations. Egypt's foreign debt has increased considerably during the last few years reaching a total of 30.8 billion dollars in 1982/3 (130% of GDP) (World Bank 1983: 40-5). Domestic public debt has also increased sharply since 1979 reaching 240.8 million Egyptian pounds (112.8 per cent% of GDP) (Ministry of Planning, various reports). Defense appropriations have grown at a very rapid rate (62.7 per cent annually) in comparison with subsidies which have only shown a moderate rate of growth (14.9 per cent).

Defence Expenditure From the beginning of the fifties, military spending constituted a heavy burden on the Egyptian budget because of the participation of Egypt in several wars since that date. Although the information on military spending is secret, we still have some indicators of the defense expenditures and their volume.

Egypt has devoted an extremely large percentage of its national resources to defense as can be seen from Table 4 below.

Table 4: Military expenditure and gross national product in Egypt (in billions of US dollars)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980/1	1981/2	1982/3	1983/4	1984/5
1.MILEX	1.3	1.5	1.5	2.8	4.1	6.1	4.9	4.4	4.4	2.2	2.1	2.4	2.4	3.0	3.7
2.GNP	6.7	7.1	7.6	8.9	9.5	11.7	12.9	13.3	n.a	16.2	n.a.	n.a.	31.7	n.a.	n.a.
%	18.9	21.1	19.9	31.0	42.8	52.4	37.0	32.8	n.a	13.1	9.5	8.6	7.5	n.a.	n.a.

Source: International Institute for Strategic Studies, The Military Balance, London, various issues

Another estimation (US ACDA 1983, 35-8) of Egyptian defence expenditures amounts to 47.2 per cent, 47.5 per cent, 47.7 per cent and 47.7 per cent of GDP in 1981/2, 1982/3, 1983/4 and 1984/5 respectively. These are extraordinary levels of expenditures for any country.

The full extent of Egypt's military debt is not known. However it is significant and rising rapidly. Since 1979 total inflows of loans and grants from the USA have been more than $2 billion. At least 75 per cent of this amount has been in the form of long-term loans at commercial US interest rates, currently averaging 12 per cent to 13 per cent. Egypt has also borrowed from several other countries. In addition, there is the overhead of unpaid military debt owed to the East Bloc countries which has not been serviced for several years. According to official statements this could be as much as $3 billion (World Bank 1983: 40).

However, defence expenditure which is the largest economic drain on Egypt's national resources has not always been essential to internal security; rather it was 'the inescapable legacy of choices made decades earlier, of long - standing decisions and policies - both foreign and domestic - whose outcomes had so structured the national condition as to leave little if any room for substantial downward alterations (Jabber 1982: 419)

There were several motives besides the wars behind this high level of defence spending in Egypt. Since 1952, Egypt knew only military leadership which continued to anchor its political base in the military institutions and it was to be expected that military strength was always a matter of high priority to it. Added to this was the desire to build up army morale after years of neglect on the part of the former colonial regime and the need to assure regime security in an unstable political and economic environment (Jabber 1982: 422).

Classification of Expenditures by Main Categories The coverage of the functional classification is seriously incomplete (although recent budgetary reforms have somewhat simplified the picture). Another categorisation of public expenditure in Egypt (World Bank 1983: 44) is based on two main pillars: the importance of expenditure and its autonomy (where expenditure is called autonomous whenever the degree of discretionary decision is very small).

It includes: (a) current expenditures of the central, local and service agencies (which include wage and salary payments and purchases of other goods and services), (b) current deficit of the public economic authorities, (c) net capital transfers, the three constituting autonomous expenditure, (d) subsidies as a major budgetary expenditure since 1974) (e) investment expenditure. The contribution of each category to the overall increase in expenditure has varied substantially in recent years.

Table 5 : Composition and Structure of Public Expenditure in Egypt, 1974-1982/5 (millions of Egyptian Pounds)

	Value	%	Value	%	Value	%	Value	%	Value	%	Value	%	Value	%	Value	%	Value	%	Value	%
Central, local & services agencies current expenditure	949.0	45.8	1352.0	44.8	1670.0	50.9	1701.0	40.8	2623.8	40.6	3686.3	42.0	3900.5	38.0	5237.2	36.6	7945.8	47.0	1017.5	51.8
Public economic authorities Current deficit	37.0	1.8	39.0	1.3	42.0	1.3	55.0	1.3	58.0	0.9	60.0	0.7	67.3	0.6	96.1	0.7	127.6	0.7	264.4	1.2
Subsidies	410.0	19.8	622.0	20.6	434.0	13.2	650.0	15.6	711.0	11.0	1229.9	14.0	1571.0	15.3	2909.2	20.3	2053.7	12.2	1996.1	10.1
Net capital expenditure (a)	80.0	3.9	102.0	3.4	154.0	4.7	214.0	5.1	776.4	12.0	1062.4	12.1	1054.3	38.0	1664.6	11.6	1756.2	10.5	1811.3	9.2
Investment expenditure	597.0	28.7	900.0	29.9	980.0	29.9	1549.0	37.2	2282.3	35.5	2736.6	31.2	3691.8	35.9	4404.1	30.8	5007.2	29.6	5430.0	27.7
Total public expenditure	2073.0	100	3010.0	100	3280.0	100	4169.0	100	6451.5	100	8775.2	100	10284.9	100	14311.2	100	16890.3	100	19659.4	100

Note (a) Includes government debt installments ondomestic and foreigndebt, net capital tranrsfer to public economic authorities and public sector companies and miscellaneous capital expenditure by the government.

Source: 1974-1977: Calculated from World Bank, Arab Republic of Egypt, Current Economic Situatien and Grewth Prospects, World Bank Report No. 4498-EGT, OOctober 5, 1983 (Table 5.1, p. 135.

1978-1982/3: Calculated from the 1982/3 Closing Account Report, presented to the People's Assembly (Acutals)

* Budget, presented to the People's Assembly

The main characteristics of public expenditure during the period from 1974 to 1982/3 are:

1. The large role of autonomous expenditure.
2. The growing importance of subsidies as a major budgetary expenditure.
3. The slowdown in the growth of investment expenditure.

Between 1974 and 1980/1, autonomous expenditure declined relative to subsidy and investment expenditure due to very rapid growth rates in the two categories (22.5 per cent for subsidies and 35.5 per cent for investments), following the favourable resource situation which emerged in Egypt during the 1974-1980/1 period (Ahmed 1984: 44).

The increase in budgetary subsidies is a reflection of the government's policy of protecting the living standards of the poorer sectors of society, against growing concentration of income and rapid inflation. The growth in investment expenditure, on the other hand, indicates both the attempt on the part of the government to ease up the existing infrastructure bottlenecks which had gained prominence with the surge in the level of economic activity in this period, and the attempt to reorganise the industrial base into a more modern and capital intensive structure (Ahmed 1984)

With the emergence of resource tightness since 1981/2, the relative importance of autonomous expenditure has increased, following rapid growth in its components due to high rates of inflation and the government's policy of absorbing a part of the impact of decline in resource availability by limiting growth in investment and subsidy expenditure. The 1982/3 -1985/b experience illustrates this quite dramatically. There is a big jump in the share of autonomous expenditure and significant decline in the shares of subsidy and investment expenditures.

1. Autonomous Expenditure: The largest component of autonomous expenditure is current expenditure. The main reason for the rapid increase in current expenditure is increases in defense appropriations and in the wage bill. The growth in the wage bill has been due more to increase in the level of employment in government services than to wage adjustments (Ahmed 1984) The large increase in government employment reflects the policy of

providing guaranteed employment to graduates. The employment guarantee for graduates was first introduced in 1964 to assure full employment and to be a redistributive tool. This policy has led to excess employment of educated employees. The government sector is thus characterised by considerable surpluses leading to work disincentive and this has contributed to the deterioration of work ethics (Hansen and Radwan 1982: 206-8).

Since 1979 the expenditure on interest payments (domestic and foreign) has assumed significant proportions. The growing burden of the public debt since 1979 has also resulted in increased budgetary expenditure on amortising payments.

The other component of capital transfers expenditure is loans to public economic authorities and public sector companies to cover their capital commitment deficits and also their current deficits.

2. Subsidies: Subsidies first entered as a budgetary item in 1950 but it was not until 1973 that they gained prominence. Since then, subsidy expenditure has increased at a very rapid rate. It increased from 2.8 per cent of total current expenditure in 1969/70 to 24.2 per cent in 1974 and reached 32.3 per cent in 1979, (Ministry of Planning 1981: 40-1) but declined to 20.5 per cent in 1982/3 and declined also from 19.7 per centof total public expenditure in 1974 to 12.2 per cent% in 1982/3 (1982/3 Closing Account Report presented to the People's Assembly). The most important category of direct subsidy is food which alone accounts for about 70 per cent of total subsidy expenditure (World Bank 1983: 61). Other items include transport, agricultural input subsidies on fertiliser and pesticides, interest subsidy on agricultural and housing credits, consumer subsidies on textiles, kerosene, bottled gas, newspapers and various types of industrialised goods produced by nationalised industries. The growth in budgetary expenditure on food subsidies are due to increases in the variety and volume of subsidised goods, as well as to increases in the gap between procurement and sales prices (World Bank 1983: 61).

Budgetary subsidies reflect only explicit subsidy expenditure incurred by the government. Even such subsidies are underestimated because all imported subsidised goods are chanelled through the General Authority for Supply Commodities (GASC) and are evaluated at the Central Bank exchange rate.

Apart from direct food subsidies, the government has attempted to improve the income distribution through two other channels. These are: (a) expenditure on health and education and

(b) subsidies through price controls on transport and on industrial goods, an interest subsidies for housing finance and a guaranteed employment programme for graduates.

While it is true that food subsidies have a favourable effect, on income distribution, they also have negative effects especially on the allocation of resources, by providing erroneos signals.

But in spite of all the negative effects of the subsidy system and of the price control system on efficiency and resource allocation, the regime has chosen to keep it, after the food riots of 1977 that took place in most Egyptian cities, which were to a large extent dominated by the urban proletariat (Ayubi 1982: 419).

3. Investment expenditures: Between 1974 and 1982/3 nominal investment expenditure grew at an annual average rate of 35.5 percent. The growth in investment expenditure was quite uneven. In 1977 the share of public investment expenditure reached 37.2 percent of total expenditure. Since 1979 the share of investment expenditure has been declining. This decline is partly due to the government policy of reducing investment expenditure in response to resource tightness in the economy and partly due to physical absorptive capacity constraints. These physical constraints are inadequate availability of overhead, such as transport, construction materials and skilled workers as well as institutional bottlenecks (World Bank 1983). However, it remains that public investments expenditures are the main element affecting growth and resource allocation in the economy (despite what is often argued about the low levels of efficiency of these investments and the large discrepancies for almost all sectors between financial and economic profitability) (World Bank, 1982) for they account for about 70 percent of total investment in the economy (World Bank 1983: p. ii) (and they accounted for 90 percent of total investment in the period from 1971 to 1976) (Zaki 1981: 11).

The government of Egypt has formulated a five-year development plan for the period from 1982/3 to 1986/7. The need for structural change is explicitly stated in the plan. The plan identifies several constraints which need to be overcome, the first one is the structure of output which is biased towards non-commodity production. Despite an increase in the share of investments in the commodity sectors of about 17.8 per cent in 1981/2 which increased the share of commodity sectors to 44.1 percent compared to 42.6 percent in 1981/2, 55.9 percent of this expenditure went to the services sector with the consequence that the share of commodity sectors is still about 44.1 percent of total investment expenditure compared to 48.1 percent in 1980/1 and 48 percent in 1979 (1982/3 Closing Account Report). However, in the conditions of tight budgetary resources aggravated by the decline in exogenous resoures from the beginning of 1981/2 and economic distortions mainly due to political constraints, public investment expenditures, despites their capital importance in the case of Egypt, are not expected to fully achieve their effects on resource allocation and development.

Further, the high rate of growth of public expenditure with insufficient revenues has caused a growing public deficit. The most important feature underlying the financing of public deficit is the increasing role of bank financing, which increased from 34.5 per cent in 1976 to 47 per cent in 1981/2 of total deficit financing (World Bank 1983: 46) but declined to 23 per cent in 1982/3 (1982/3 Closing Account Report). Increasing reliance on bank financing has caused an expansion in the supply of money in the economy - the average proportion of deficit bank financing to the supply of money during the period from 1974 to 1979 was 29 per cent (Zaki 1981: 122) - a rate faster than the rate of expansion of the demand for money. The imbalance has generated significant inflationary pressure in the economy causing problems for resource allocation as well as income distribution (Abdel Fadil 1982: 68).

Kuwait

The discussion of expenditure composition of the Kuwaiti government may be carried out at two levels: current versus development expenditures, and sectoral distribution of development expenditures. The former serves as an indication of the development orientation of government finance, while the latter may point out the development policy of the government (El-Mallakh and Atta 1981: 42).

Current expenditures Two expenditure categories have been experiencing fluctuations: land purchases and foreign transfers. The program of land acquisition has been criticised for being an indiscriminate and inequitable way of distributing revenues and for failing to invigorate the economy, because the private sector has invested a large amounts of the funds received abroad (Khouja and Sadler 1979: 34) Some have the feeling that the program weakened entrepreneurial ability because of growing dependence on the government as a source of income (Ibrahim, Shihata and Mabro 1978: 1) The second major item is foreign aid, which from the domestic point of view constitutes a drain on development resources. However, Kuwait's awareness of its vulnerability as a mineral rich but militarily weak state was evident from the early beginnings of its emergence as an independent state in 1961 when foreign aid became a political necessity (El-Mallakh and Atta 1981: 174).

The political objective in Kuwait's aid is, however not the only one. It has been indicated that there is a mix of political, sociological and historical motives (Khouja and Sadler 1979: 210). Also, with virtually no other natural resources aside from oil and gas, Kuwait is very constrained in its development potential, so it is in Kuwait's interest that the Arab world develop as a whole (El-Mallakh and Atta 1981: 176).

Wages and salaries were the most important item of current expenditure in almost every year from 1976/77 to 1982/3. This is due to Kuwait's employment policy which aims, on the one hand, at securing employment for all Kuwaiti citizens and on the other hand, at raising wages and salaries to attract foreign skilled labour (Sayigh 1982, 167). Kuwaitis represent around 54 per cent of total government civil servants; around 25 per cent of the total Kuwaiti labour force is in government employment (Central Bank of Kuwait, 1980: 59). Employment thus provides serves as an allocational and redistributional device (El-Sheikh 1972 63) and also encourages pressure from the population for ever increasing expenditures on subsidies and social services. When the alternative use of funds is investment abroad or foreign aid, it is often difficult to resist such pressure' (El-Mallakh 1968).

The consumers in Kuwait has long enjoyed many government subsidies irrespective of their income. These subsidies cover such basic services as water, electricity and gasoline. Due to inflation, the subsidy system has been extended in recent years to cover many of the essential food products (rice, sugar, milk, meat, vegetable oil, etc.). The cost of the food subsidy programme has varied but it is estimated to be in the order of KD 20 million per year (Khouja and Sadler 1979: 34)

Defence expenditure. Defence and security expenditures ranked first on the bill of public expenditure in the seventies with their outlays totalling KD 1595 million or 17.4 percent of the total public expenditure. About 82 percent of the outlays related to this sector were incurred in the second half of the

Table 6: Composition of Public Expenditure inKuwait (KD millions)

	1976/7		1977/8		1978/9		1979/80		1980/1		1981/2		1982/3	
	Value	%	Value	%	Value	%	Value	%	Value	%	Value	%	Value	%
Domestic expenditure (a+b+c+d+e)	1417.8	93.3	1745.5	89.0	1749.9	90.0	2210.7	91.2	3115.8	92.2	3538.2	93.5	3501.3	93.8
a) Domestic current expenditure	746.0	49.1	759.5	38.7	881.4	45.3	1252.6	51.7	1483.4	43.9	1745.0	46.1	2000.9	53.6
Wages & Salaries	368.2	24.3	423.0	21.5	456.6	23.5	621.6	25.6	638.8	18.9	723.0	20.4	858.7	23.0
General Expenses	314.3	20.7	269.8	13.7	345.7	17.8	462.6	19.0	508.7	15.1	775.8	20.5	799.9	21.4
Domestic transfers + Unclassified	63.5	4.1	66.7	3.5	79.1	4.0	168.4	7.1	335.9	9.9	245.7	5.6	388.9	9.2
b) Land Purchases	108.4	7.1	188.4	9.6	107.4	5.5	263.9	10.9	391.8	11.6	449.2	11.9	219.9	5.9
c) Development Expend.	353.1	23.2	493.9	25.2	499.0	25.7	462.9	19.1	492.3	14.6	658.4	17.4	661.9	17.8
d) Local loans	35.2	2.3	6.3	0.3	23.1	1.3	13.5	0.5	98.3	2.9	-29.5	-0.7	-0.1	0.0
e) Participations	175.1	11.5	297.4	15.3	239.0	12.3	217.8	8.9	650.0	19.2	715.1	18.9	574.1	15.4
- share of local companies	(51.6)	(3.4)	(186.0)	(9.5)	(56.3)	(2.8)	(91.9)	(3.8)	(213.8)	(6.3)	(119.8)	(3.2)	(106.4)	(2.8)
- share of financial & Government Institutions	(123.5)	(8.1)	(111.4)	(5.8)	(182.8)	(9.5)	(125.9)	(5.1)	(863.8)	(12.9)	(595.3)	(15.7)	(467.7)	(12.6)
Foreign Transfers	101.5	6.5	213.7	10.9	194.0	9.9	213.0	8.9	262.1	7.8	244.8	6.4	230.7	6.3
Total Public Expend.	1519.3	100	1959.2	100	1943.9	100	2423.7	100	3377.9	100	3783.0	100	3732.0	100

Source: Central Bank of Kuwait, Economic Reports, 1978, 1981, 1983 (calculated) seventies for the construction of military bases, armaments and the institution of compulsory military service (Central Bank of Kuwait 1980: 58)

Defence expenditures accounted for about 5.4 per cent (on average) of GNP in the seventies, as shown by Table 7 below.

Table 7: Military expenditures and GNP in Kuwait, 1971-1980 (billions of US dollars)

	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
1.MILEX	0.185	0.210	0.234	0.568	0.731	1.086	1.043	1.076	1.181	1.315
2.GNP	3.882	3.778	4.032	11.481	13.348	15.509	16.562	17.856	26.663	30.969
%	4.8	5.6	5.8	5.0	5.4	7.0	6.3	6.0	4.4	4.2

Source: USA Arms Control and Disarmament Agency (ACDA), World Military Expenditures and Arms Transfers, 1971-1980, ACDA Publications, Washington D.C., 1983, Table I, p. 44.

Total government expenditure in Kuwait is an injection of liquidity into the economy and it has been proved that a close relationship exists between the domestic balance, liquidity expansion and inflation in oil-rich countries (Morgan 1979). Government domestic expenditure has been rising at a rapid rate in Kuwait which has consequently led to a high rate of inflation (0.6 per cent in the period from 1960 to 1970 and 35.6 per cent in the period from 1970 to 1976) (Mabro 1979: 21). The cost-of-living index rose from 100 in 1972 to 175 in 1979 (Central Bank of Kuwait 1979: 70) and from a base of 100 in 1978 to 138.7 in 1983 (Central Bank of Kuwait 1983: 95). The policies that Kuwait adopted to alleviate inflation (through subsidies, welfare services, elimination of taxes...) did not help much, because as experience demonstrated, 'attacking the symptoms of inflation by means that exacerbated the causes was likely to yield, at best, only temporary results' (Morgan 1979: 76). Hence, price stability has not been achieved.

In recent years Kuwaiti budget forecasts have shown increasing expected deficits. However, the deficit is more apparent than real and in fact, the figures conceal healthy surpluess. The following factors account for the discrepancy.

First, about half the deficit is represented by transfers to the Future Generations Fund and KFAED, which are not expenditures in the real sense. Second, the deficit is usually reduced by the 'scissors effect' of actual expenditures falling below budget, while revenues are higher than planned. The third factor is investment income, which is treated as an off-budget item.

Development expenditures. In the period from 1976/7 to 1982/3, development expenditures decreased as a proportion of total expenditures. Until recently, Kuwait has had no formal development plan although economic guidelines were set for 1967/8-1971/2 and 1975/6-1980/1 and for specific economic sectors such as electricity and water, housing, oil and gas, and public health. Instead Kuwait has tended to rely mainly on annual programmes with only vaguely described long-term objectives. The increasing complexity of the economy, however, together, with the shockwaves induced by the collapse of the unofficial stock market in 1982, prompted the government to elaborate a more comprehensive strategy to be incorporated in a five-year plan covering 1985/6 to 1989/90 (Economist Intelligence Unit 1984:7).

Actual spending has always been less than appropriations, but not much less, (Sayigh 1982: 168).

Table 8 shows a sectoral distribution of public expenditures. The data reflects the infrastructural bias in capital expenditures.

Table 8: Kuwait, Government development expenditures 1978/9-1982/3 (in millions of Kuwait dinars)

	Actuals				
Fiscal years	1978/9	1979/80	1980/1	1981/2	1982/3
General public service	21	17	28	31	33
Education	18	15	18	11	18
Health	21	11	9	9	28
Social affairs	8	6	7	16	10
Housing Facilities	141	134	108	126	157
Economic services	191	234	316	464	458
Electricity, etc.	(117)	(141)	(197)	(319)	(343)
Roads	(51)	(68)	(80)	(97)	(84)
Other	(23)	(25)	(39)	(48)	(31)
Other	2	6	3	6	4
Total	408	423	489	663	708

Source: IMF, Kuwait, Recent Economic Developments, (IMF Document SM/85/2, Washington D.C., 1985) Table 16, p. 37.

Saudi Arabia

The Saudi Ministry of Planning gives a composition of public expenditure which is limited only to wages and salaries, transfers and subsidies (current expenditure) and projects expenditure (Ibrahim 1982:54). Another classification of government expenditure in Saudi Arabia may give a better picture (Table 9).

Table 9: government expenditure estimates in Saudi Arabia

	1981/2 Rls mn	%	1982/3 Rls mn	%	1983/4 Rls mn	%
- Human resource development,	26,248	8.9	31,864	10.1	27,791	10.7
- Transport and communications	35,343	11.9	32,533	10.3	24,950	9.6
- Economic resource development	22,679	7.7	22,045	7.0	13,209	5.0
- Health and social develpment	13,716	4.5	17,010	5.4	13,591	5.2
- Infrastructure development	14,126	4.7	11,075	3.5	9,583	3.7
- Municipal services	26,292	8.8	26,225	8.4	19,070	7,3
- Defence and security	82,533	27.7	92,889	29.6	75,733	29.1
- Public administration and other government spending	43,113	14.5	44,586	14.2	47,053	18.1
- Government lending institution	24,850	8.3	23,382	7.5	20,000	7.7
- Local subsidies	9,100	3.0	11,162	7.0	9,020	3.6
Total expenditure	298,000	100	313,400	100	260,000	100

Source: The Economic Intelligence Unit, Quarterly Economic Review of Saudi Arabia, Annual Supplement, London, 1984, p.20.

The pattern of public expenditure in Saudi Arabia displays clearly the nature of the dilemma which Saudi Arabia faces: growth versus security.

The vast financial resources have placed obligations on the Saudi government to modernise the country, create new institutions, build an elaborate infrastructure, raise the standard of living and diversify the economy. At the same time, these vast financial resources thrust the kingdom into a sudden position of importance and vulnerability (Ibrahim 1982: 55). The concern is with both external (geographical proximity to disputed territories) and internal security (justified in view of repeated attempts at coups d'ètat).

Thus the goal of rapid socio-economic development works in some ways at cross-purposes with the goal of internal security and the political stability of the regime (Ibrahim 1982).

Table 10: Military expenditure and gross national product in Saudi Arabia (in US $ billion)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
MILEX	0.4	0.4	0.9	1.5	1.8	6.8	9.0	7.5	13.2	14.2
GNP	4.0	4.3	5.2	8.3	24.8	37.2	51.1	55.8	87.8	94.6
%	9.8	8.9	18.1	18.3	7.3	18.0	17.7	13.5	15.0	15.0

Source: International Institute for Strategic Studies, The Military Balance, London, annual.

Defense Expenditure The breakdown of Saudi government expenditures in more recent years confirms that defense expenditure ranks first in government spending and by far exceeds all other items. In the three years, 1981/2 to 1983/4, it avrage 28.2 percent of public expenditure. In the 1984/85 budget, defence and Security continues to be the major item (30.7 per cent of total projected expenditure) (MEES 9 April 1984, p. A2).

Estimates indicate that military spending in Saudi Arabia absorbed 14.16 percent of GNP during the period from 1970 to 1979 (Table 10 above).

Public administration and other government spending This ranks second in public expenditure. Together with municipal services itey constitutes an average of 23.7 percent of total expenditure in the period from 1981/2 to 1983/4 (EIU1984: 9).

Developmental expenditures Transport and communications with a priority over all other development expenditure, averaged 10.6 percent of total expenditure in the 1981 to 1984 period (EIU 1984). Economic development policy in Saudi Arabia was articulated into five-year plans, the third and most comprehensive of which started in 1980.

In the first and second plan, both spending and performance targets tended not to be fulfilled as the kingdom's planners overestimated the absorptive capacity of the economy. During the second plan, spending raced ahead as the economy over-heated and inflation took off, but this did not affect the pace of implementation of infrastructural projects many of which have been carried over incomplete into the third plan, which already seems likely, for this reason, to have more of an infrastructural and less of a productive bias than originally planned (EIU 1984) Table 11 shows the apparent shift in development emphasis between the second and third plans.

Table 11: Government expenditure on development in Saudi Arabia

	2nd plan (1975-1980) %	Rls bn	3rd plan (1980-1985) %
Economic resource development	25.1	261.8	37.3
Human resource development	15.9	129.6	18.5
Social development	9.4	61.2	8.7
Physical infrastructure	49.6	249.1	35.5
Total development expenditure	100.0	701.7	100.0
Administration	6.7	31.4	4.5
Reserves and subsidies	15.9	49.6	7.1

Source: The Economist Intelligence Unit, Quarterly Economic Review of Saudi Arabia, Annual Supplement, London, 1984, p. 9 and MEED 25 March 1985, Table 2, p. 33.

The table clearly indicates the high priority of physical infrastructure in development planning. Economic resource development gained importance in the third plan, as did human resource development. The Saudis have usually maintained that they prefer not to duplicate the Kuwaiti experience with its emphasis on a substantial welfare programme. Yet, when the total of social programmes, including subsidisation of food staples is added up, it is difficult to differentiate between the system which seems to be emerging in Saudi Arabia and that which exists in Kuwait.

With education and health care provided by the government at no charge, with housing, transportation, electricity and food subsidised, and with extensive social security programmes to be effected, the Saudi Arabian government is evidently assuming a major role in the economic life of its citizens (Wells 1976: 63)

There is one major omission from the data on expenditure in Saudi Arabia namely, foreign assistance to other countries. For example, Saudi Arabian commitments of bilateral aid were estimated to be over $2 billion. Aid has been extended to a wide range of developing countries. In addition to bilateral aid, Saudi Arabia also pledged funds to the oil facility of the IMF (El-Beblawi 1982: 200)

It was estimated that Saudi Arabia's foreign aid dispersements eualled $2.4 billion in 1977 and $1.5 billion in 1978, or 4.3 percent and 2.3 percent of GNP respectively (El-Beblawi 1982: 200).

From the view point of assessing development strategy, it is important to understand the limits of the planning exercise. 'At one extreme the plan could be the primary determinant for budget decisions; at the other, it might be an ineffectual statement of intentions, ignored in the budget decision-making process' (Wells 1976: 50), for each ministry draws up its own set of objectives, programs, and projects. Each individual ministry has its own political base and not all ministries are equal. Tribal and family loyalties abound throughout the government and power and influence are closely tied to such relationships. These considerations help to explain why two important sectors (defence and oil) are not integral parts of the plan (Wells 1976: 51-2).

<u>Jordan</u>

The striking feature of the Jordanian budget is the great dependence on foreign aid, although military aid does not appear in the budget. In spite of this underestimation, it appears that more than 50 per cent of public expenditures are financed through different forms of foreign aid: budget support, economic and technical assistance and foreign borrowing (Rivier 1980: 62). The Jordanian budget is divided into two autonomous parts:

1. The first part is financed through internal revenues (taxes, profits...) and untied foreign aid (budget support, untied loans). These revenues finance the central government's current expenditures (wages and salaries, subsidies, defence and security) and capital expenditures (foreign debt, development).

Since internal revenue is always insufficient to cover government expenditure, foreign aid is essential for financing both capital and current expenditure (Rivier 1980: 24).

2. The second part of the budget is exclusively financed through tied aid (economic and technical assistance or tied loans for specific projects).

Table 12 gives a composition of public expenditure in Jordan in the period from 1973 to 1983.

Table 12: Composition of public expenditure in Jordan 1973-1983 (%)

Year	General administration	Defence	Internal order & security	International affairs	Finance administration	Economic development services	Social services	Culture & information services	Communication & information services	Total
1973	0.9	35.9	5.4	1.0	20.9	23.4	9.1	2.0	2.2	100
1974	0.7	30.4	5.6	1.1	24.1	21.5	12.6	1.8	2.2	100
1975	0.6	23.6	5.0	1.1	28.1	24.1	11.6	2.0	3.9	100
1976	0.5	35.6	4.4	1.1	22.0	16.8	12.0	1.7	5.9	100
1977	0.4	24.5	4.3	0.9	23.4	28.9	10.6	1.9	4.8	100
1978	0.7	24.7	4.7	0.9	20.6	29.6	11.4	2.1	5.3	100
1979	0.6	22.3	4.8	0.8	30.4	22.6	10.9	1.7	5.9	100
1980	0.5	21.0	4.4	0.8	29.5	25.3	11.5	1.3	5.7	100
1981	0.5	21.3	4.6	0.8	30.6	23.4	12.3	1.7	4.8	100
1982	0.6	23.9	5.3	0.8	27.5	21.0	12.8	1.9	6.2	100
1983	0.6	23.4	5.0	0.8	30.5	21.5	12.3	1.4	4.5	100
Average	0.6	26.0	4.8	0.9	26.2	23.5	11.5	1.8	4.7	100

Source: Calculated from Central Bank of Jordan, Yearly Statistical Series (1964-1983), Special Issues, Table 39.

The first major item in the budget (as for the other three countries examined) is defence expenditure which accounts (together with internal order and security expenditure) for an average of 30.4 per cent throughout the period.

Administration ranks second on the budget with an average of 26.8 per cent (for both general and finance administration). The third item in the budget is economic development expenditure with an average of 23.5 per cent, followed by social services with an average of 11.5 per cent. It must be noted that economic development expenditure showed an upward trend, especially in the years 1978 and 1979, then started to decline.

Defence expenditure has also declined from 35.1 per cent in 1979 to 23.4 per cent in 1983, although those figures do not include military expenditure which constitutes a heavy burden on the national budget as can be seen from Table 13.

Table 13: Jordan, Military expenditures and gross national product 1970-1982 (in US $ billion)

	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
MILEX	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.3	0.4	n.a.	0.4	0.4
GNP	0.7	0.6	0.7	0.9	1.0	1.3	1.3	1.8	n.a.	2.7	n.a.	n.a.	n.a.
%	14.8	14.8	16.0	16.4	14.2	12.2	12.9	10.9	n.a.	14.2	n.a.	24.6	24.8

Source: International Institute for Strategic Studies, The Military Balance, London, annual.

These military expenditures are not only justified on the basis of the fact that Jordan is a 'front line state' but also on the basis of political stability endangered by repeated attempts at 'coups d'état'. It is evident that the result of these heavy military expenditure, together with defence and security expenditure is a continuing drain on Jordan's tight economic resources.

As is the case with Egypt, the growing public deficit in Jordan and the increasing role of bank financing has caused an expansion in the supply of money in the economy. The public deficit accounted for about 25 per cent of the supply of money in 1977 and 1978 (Abdel Fadil 1982: 73) which led to inflationary pressures (the cost-of-living index in Jordan rose from 126.4 in 1972, to 396 in 1983) (Central Bank of Jordan 1972-1983).

CONCLUSION

The structure of public expenditure in Egypt, Kuwait, Saudi Arabia and Jordan in the last decade demonstrates clearly that in spite of many differences between these countries in income and revenues there is homogeneity in the pattern of public expenditure. Defence expenditure is the major item in the budget of each of the four countries in spite of the fact that the two oil countries are not 'confrontation' countries. Although there is no explicit conflict in these two latter countries, there is a growing sense of basic strategic insecurity among them. Wages, salaries and subsidies constitute major items in the budget of both the oil and the semi-oil countries. The latter two items showed an upward trend in the period of the oil boom, which was due, to a great extent, to the rentier mentality which prevailed in this period and to the choice of political stability. Development expenditures, which always rank second to the items cited above, had an infrastructural bias in the four countries. In most cases, the interrelationships between budgetary and planning policies have not been clearly recognised. Further, the high growth rates of public expenditures caused inflationary pressures (increased in the two semi-oil countries by bank financing of the budget deficit) involving disruptions and social tensions which in turn hindered development expenditure from fully achieving its effect on resource allocation and growth.

In spite of large resources devoted to subsidies price stability has not been achieved, because of the high rate of inflation. Subsidies, in turn had other disincentive effects which hampered efficient economic development. Furthermore, inflation pressures affected both income distribution and development efforts.

Thus, the experience of public expenditure in Egypt, Kuwait, Saudi Arabia and Jordan proves that having or not having the money needed for development is not what matters most. 'It is the utilisation of money more than the acquisition of money which determines the developmental path of any society' (Ayubi 1982: 359). The utilisation of money in the four Arab countries examined indicates that there have been many abuses which hampered economic development. In many cases, the main reason for these abuses was that the government had to choose between efficiency and security. The goal of rapid socio-economic development worked, in most cases, at cross-purposes with the goal of internal security and the political stability of the regime.

NOTE

1. The expenditures are autonomous in the sense that the degree of discretionary influence is very small.

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Chapter 6

THE STATE, SOCIAL CLASSES AND AGRICULTURAL POLICIES IN THE ARAB WORLD

Hamid Ait Amara

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

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

In certain cases the new orientations have brought about a significant change in the nature of relations between the state, various peasant groups and the urban working classes. The rise in the price of agricultural products reduces the purchasing power of fixed income earners, and in order to achieve the objectives that were set for the growth of production, the state would like to rely more on market oriented farmers, and reduce the role of the small peasants. Hence, the food crisis, which almost all the Arab countries must confront, threatens the system of class relationships built up during the 1960s and 70s.

THE RETREAT OF AGRICULTURE

Since the seventies, the economy of Arab countries has undergone extensive restructuration, marked by the retreat of agriculture to the benefit of other sectors, and other sources of savings became more important for development.

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

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

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

In Syria, cotton exports which fluctuated between 200 and 250,000 tons per year in 1967/73, fell to 155,000 tons in 1976/77 and 117,000 tons in 1980.

Algeria practically stopped exporting its agricultural products in the middle of the seventies. In 1980/84 hydrocarbons made up 97 per cent of export revenues. In Tunisia oil products and derivatives hold first place - 880 million Tunisian dinars in 1983 - then come textile products - 339 million - and agricultural exports total only 86 million.

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

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

Table 1: Agriculture in GDP, 1981

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

Source: Situation mondiale de l'alimentation et de l'agriculture 1983

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

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

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

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

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

Morocco was estimated to have had losses in the region of 126 million US dollars in 1980/81 because of the enlargement of the EEC; Tunisia lost some 100 million dollars.

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

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

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

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

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

Thus, in Algeria, the guaranteed minimum wage in agriculture was made equal to that of industry and services in 1980. It went from an index of 100 in 1970 to 437 in 1980, progressing much more rapidly than the average non-agricultural wage index. In Tunisia the minimum guaranteed wage more than doubled between 1977 and 1983, but it still only represents 70 per cent of the guaranteed interprofessional wage. In Morocco, the substantial increase - 40 per cent in May 1979, or 10.15 dirhams a day against the previous 7.25 - failed to narrow the gap between agricultural and non-agricultural wages.

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

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

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

An analysis of the agricultural food situation over the period 1973/83 shows that for a majority of the countries in the Arab world food imports grew rapidly while domestic production of basic items declined on a per capita basis. Yet, one can distinguish two groups of countries: a first group, comprising Saudi Arabia, Syria and Libya, in which production per capita has perceptibly increased; and a second in which it decreased by 10 to 15 per cent on average. Thus, the per capita production index in Egypt went from 99.13 in 1974 (1974/77 = 100) to 90.6 in 1984, in Iraq it went from 92 to 76, in Algeria from 93 to 82.8, in Morocco from 106 to 87.8 and in Tunisia from 94 to 86.7 (FAO 1985).

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

Table 2: Cereal Imports of Selected Arab Countries in 1980 - '000 tons

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

Source: Economie et géopolitique des échanges de céréales en Méditerranée, IAM, Montepellier, 1985

Since the beginning of the 1980s the cereal deficit has yet again increased for all Arab countries, except Saudi Arabia and Libya which have partially reduced their foreign deficits. The Maghreb countries and Egypt have the biggest deficits; Algeria and Egypt, in particular, import more than half of their total food requirements (3).

Table 3: Food Self-sufficiency Rate - Wheat, 1977/81

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

Source: FAO, Production Yearbook 1984

In Algeria, with the exception of the excellent harvest of 1985, average cereal production (durum wheat, common wheat, barley) has been stagnating at 1.8 million tons for about fifty years and that of wheat at 1.3 million tons. Total wheat consumption is estimated at 4.5 m. tons. Local production, therefore, covers only about a quarter of national requirements. Egypt assigns only one million feddan to wheat cultivation - less than for cotton which is exported - and the harvest is lower than in 1974-76 (1,960 million tons, as against 1,815 million tons in 1984).

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

A NEW AGRICULTURAL POLICY

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

Investment in agriculture

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

In Morocco the amount of investment in agriculture - including irrigation and agricultural water management - which stood at 5,468 billion dirhams for the period 1973/77, increased to 19,635 billion for the period 1981/85. In the case of Tunisia, this amount went from 197 million dinars in 1972/76 to 1,360 million in 1982/86 and in Algeria from 2,683 billion Algerian dinars in 1970/73, to 5,850 billion in 1974/77, to 10 billion in 1980/84 (4).

While public investment in agriculture declined in the seventies as compared to the previous decade, we witness today a strong recovery of the share of investment going to agriculture. In Tunisia, this share stood at 20 per cent for the decade 1961/70, fell to 13 per cent in 1971/80, then increased again to 17 per cent for the period 1981/86. In Algeria, agricultural investments were below 8 per cent on average in 1970/79, but appropriations went up to 12 per cent in 1980/84 and to 14.4 per cent of total investment in 1985/86. A new situation, indeed, whereby the agricultural sector receives in most Arab countries a share of public finance which is larger than its contributions to the GDP. Privately funded investment remains small when compared to the publc effort, reaching some 13 per cent in Morocco, somewhat less in Tunisia, and 10 per cent in Algeria.

> One can, however, generalise the question posed by Hachmi Alaya (1984) for Tunisia: 'whether the volume of investment allocated to the agricultural sector is not greater than its absorption capacity, especially with respect to that part which is financed by the banks. Necessary conditions - in the organisation and technical training of the farmers, in the farming of state lands, in agricultural prices, in the supply of

> production inputs to the farmers, in the marketing of agricultural products - do not seem to be as yet all met to the extent that would warrant the planned growth of the sector'.

This is especially true in Algeria where, despite a clear improvement, the rates of realisation in comparison to appropriations were only 65 per cent in 1970/73 and 68 per cent in 1974/77.

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

Table 4: Share of Hydraulic Investment over Total Agricultural Investment

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

In Libya, irrigated land has risen to 80,000 ha, and a project being carried out by a South Korean company should, with almost 4,000 kilometers of canalisations, drain the water tables of the southern desert and bring the water to the lands of the north, increasing the irrigated area by 180,000 ha (at a total cost of 10 billion dollars) (Burgat 1985). Saudi Arabia has likewise undertaken vast hydraulic investments to tap the shallower water tables; this allowed her over the last years to turn her wheat deficit into a surplus (5).

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

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

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

Table 5: Egypt, Evolution of the Ratio of Population to Cultivated Land

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

Source: Ministry of Irrigation, Cairo

Hydraulic investment aims at removing natural constraints to production. The Mediterranean climate along the thin littoral belt progressively deteriorates into a semi-arid or arid climate over the much wider farmable land surfaces of the interior. Countries like Egypt, Libya and Saudi Arabia cannot cultivate without irrigation. But in all other regions, the annual rainfall is insufficient as well, and a large part of arable land does not receive enough water for crops (6). This is the case not only of Jordan, Syria and Iraq but, in the western Mediterranean as well, of Tunisia, Algeria and Morocco.

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

Table 6: Agricultural Population per Hectare of Arable Land, 1981

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

Source: FAO, 1983

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

Mechanisation of agriculture

The modernisation of agricultural cultivation methods and equipment is the second aspect of the new agricultural policy. The state wants to achieve growth in agricultural productivity by increasing mechanisation services, introducing fertilisers and other chemical products, and improving the livestock. To this end, tax reductions, credit and subsidies have been introduced. Thus, for example, large subsidies are granted to encourage fertilisers consumption, and aid is given for the use of other production factors; imports of agricultural material are exempted from customs duties and taxes; the purchase of tractors is subsidised, and the state offers free services in fertilisation, veterinary care, plants and seeds, mechanised work. Credits to farmers at improved rates are obtained more easily. In Tunisia for example (but the same could be said of Algeria, Morocco and Syria) the operation of the Fond spécial de dêveloppement agricole (FOSDA) went from 14,000 million in 1974 and 18,000 million in 1977, to 65,000 million in 1982. In 1981, the National Bank of Tunisia doubled the funds allocated to farming loans from 20 million DT to 48 million Tunisian dinars.

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

In Algeria, the number of tractors has more than doubled since the beginning of the seventies - from 26,000 to 58,000 units - with an acceleration of growth in the last five years. In Tunisia, only 18 per cent of farmers used mechanical traction in 1962, whereas in 1976 that percentage had increased to 55 per cent and in 1980 to 58 per cent (Ramdhane 1983). The tractor pool went from 20,000 units in1976 to 28,000 in 1983. The same holds true for Morocco, Egypt and Syria where there has been a quantitative and qualitative increase in mechanical implements, concentrated for the most part in large and medium-sized farming concerns. Correspondingly, small-scale concerns have limited access to mechanisation and run up against growing difficulties in cultivation because of the substantial drop in domestic livestock.

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

Agricultural prices

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

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

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

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

Table 7: Evolution of Cereal Prices -Durum and Common Wheat in National Currency, per 100 kg

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

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

In Algeria, prices have risen more sharply, 60 per cent for durum wheat, 65 per cent for common wheat and dry vegetables, upward of 150 per cent for milk. In Syria, the government increased the purchase price of cotton by 44 per cent in 1981/82 and by 20 per cent in 1982/83 (World Bank 1983). Finally, in Egypt, the price increases which occurred in 1979/80 were more modest. Wheat prices gained 9 per cent, rice 15.4 per cent, sugar 27.6 per cent. The price payed for cotton has remained at a much lower level compared to the world market (World Bank 1980).

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

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

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

Since 1982 (Law 82-67, 6 August 1982) the land belonging to the state (almost 400,000 ha of good land) can be leased for an approved length of time, not to exceed thirty years, to Tunisian joint stock companies called 'companies for agricultural improvement and development', in which the state directly or indirectly owns a share of the equity (art. 10); or to private individuals. Thus in 1982/83, some 15,000 ha were ceded to Tunisian-Kuwaiti or Tunisian-Saudi private organisations, as well as to Tunisian private entities.

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

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

Finally, in Algeria, public authorities have dissolved the cooperative structures established by the agrarian reform of 1971. The land that had been worked collectively was redistributed to individual farmers, and the service cooperatives which provided the technical assistance and material to certain categories of producers stopped their activities in 1982/83. In particular, the disappearance of the cooperatives' branches handling mechanical implements has resulted in a substantial increase in the rental rate for machinery, affecting the small peasant farmers who can no longer afford the equipment. These measures manifest the state's determination to disengage itself from a category of peasant farmers, because the assistance that it once gave to them, in the form of subsidies and various services has today become too costly.

CLASS RELATIONS AND AGRICULTURAL POLICY

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

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

Countries with large capital surpluses which have made big transfers in favour of agriculture, so as to establish or enlarge their agricultural production structures (Saudi Arabia, Libya and Iraq) should be distinguished from countries with small or medium export revenues, whose agricultural sectors suffered a big retreat in the 1970s. In the case of the latter

(Algeria, Egypt, Tunisia, Syria, Morocco) it is a question of limiting the damage caused on their agriculture by the expansion of the oil economy.

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

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

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

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

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

In Algeria, the difference is bigger. Against a general index of 306.8 in 1983 (1969 = 100), the foodstuffs index rose to 393.2. As can be seen in the table below, the gap is widening after 1980.

Table 8: Algeria, Evolution of Consumer Price Index, 1978-83

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

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

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

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

Improvement in the agricultural terms of exchange does not, in all cases, imply a reversal of financial flows to the benefit of agriculture. Egypt, as opposed to Algeria, is a case where the difference between domestic and international prices is still clearly against local agriculture, notably for basic products such as wheat or cotton, while the increase in the international prices of agricultural machinery is transferred to the farmers in full.

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

The control of prices during the 1960s and the beginning of the 1970s was implemented in a way that damaged growth of agricultural incomes, but did not necessarily favour accumulation in industry, contrary to what has been often suggested. In the Arab countries industry only employs an average of 15 per cent of the active population: 17 per cent in

Algeria and Tunisia, 14 per cent in Morocco and Egypt. In the latter country, industrial activity has been on the decline since 1975; in 1961 it accounted for only 15 per cent of the GDP and 7 per cent of its production was exported as against 9 per cent in 1973.

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

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

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

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

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

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

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

In Egypt, price subsidies fell by almost 300 million US dollars in 1984. In Algeria, two increases of 22 per cent each were introduced in 1985 for cereals, vegetable oils and other basic foodstuffs. Parallel increases took place in Morocco

Tunisia and Jordan. The liberalisation of prices of local products, fruits, vegetables and meats, led to steep increases. The urban middle classes, the working classes, and the agricultural wage earners have been the main victims of the rise in the price of foodstuffs and have had to adjust to a sizeable reduction in their purchasing power. Hardest hit by inflation are the petty civil servants, employees and workers, all especially vulnerable to food price increases.

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

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

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

NOTES

1. 'Producing citrus fruits at great expense for export and importing cereals to cover basic needs is consistent with the requirements of the process of integration of the Moroccan economy into the global market' .See el-Malki, H. (1983) Au delà des chiffres quel développement? Ed. Maghrebines?'.

2. This is a profound transformation of the agricultural strategy envisaged by the Morroccan Plan 1984/85. 'To reduce the negative effects of unfavourable international development, curb the food deficit, restrain the rural exodus, try for a new equilibrium at regional, inter-sectorial and intra-sectorial levels: these are some of the main ideas that arise from developments which the last Five Year Plan 1981-85 has devoted to the agricultural sector' (Habib el-Malki 1983).

3. Egypt receives almost 44 per cent of world 'food aid' supplied by the USA. Wheat in the form of donation has, however, been progressively replaced by credit sales with no special conditions (like the city credit corporation USDA).

4. The second Five Year Plan 1985-89 allocates 30 billion DA just for agricultural investments to which are to be added 40 billion in water investments.

5. In 1985, Saudi Arabia produced 1.7 million tons of wheat for a consumption of about 1 million tons.

6. In Jordan, barely 30 per cent of land receives more than 350 mm of rain annually, and only 600,000 ha between 200 and 350 mm, the rest being unfit for cultivation. In Syria, 65 per cent of the 18.5 ha used by agriculture receives less than 200 mm of rain anually. In Algeria, Tunisia and Morocco from one-third to half of all arable land has less than 400 mm water annually.

7. 'Today's prices and market policy seems to be inadequate, from the point of view of agriculture, which does not make up for ground lost, and from that of the consumer, who pays a higher price. One might think that the support given to products should outweigh the support given farming with prices therefore playing a more determinant role' (Three Year Plan 1978-80).

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

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

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

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Chapter 7

FOREIGN DEBT IN THE ARAB COUNTRIES

Azzam Mahjoub

INTRODUCTION

This chapter discusses the importance of foreign public debt and its different origins for the various Arab countries, leading at the beginning of the 80s to a crisis of variable intensity, depending on the country.

Our starting hypothesis is that the debt crisis of the Arab countries is but one manifestation of continuing structural inbalances (measured in macro-economic terms by the gap between resources and utilisations) that became particularly apparent at the beginning of the 80s and has characterised the recent evolution of the economy. The crisis appears at the time when a peculiar international economic juncture exacerbates the distorsions at hand and accelerates processes under way.

The presence of both common and differentiating factors makes it possible to elaborate a clear basic typology of Arab economies. This typology should enable us to establish at the same time certain common traits as well as singularities of the Arab states, and to understand the nature and degree of political and social readjustment processes are taking place, in which the state is the decisive actor.

First, it is a fact that at the beginning of the 1980s all the Arab countries experienced a clear economic deterioration often directly accompained by explosive social and political instability. The bread riots in Morocco, Egypt, Tunisia and Sudan, renewed military tensions within the Arab region, and financial scandals were irrefutable signs of the exacerbation of a profound malaise. The 1980s marked a turning point in the contemporary economic history of the Arab world.

The social upheaval brought to the fore the fragility of existing political systems and, above all, the widening gaps left over by the economic growth of the 1970s. Feverish growth rates of the 1970s declined and external financial and commercial positions deteriorated during the 1980s.

To varying degrees the Arab economies find themselves increasingly integrated into the international Debt Economy. Certainly, the Arab countries do not constitute the weakest link in the chain; no Arab country unilaterally declared a moratorium, but the Sudan, Morocco and Iraq were obliged to initiate negotiations for debt rescheduling. The situation is rather precarious in Egypt, Tunisia, Syria and Jordan, as well. Current trends could lead to a catastrophe and the danger of a 'Latin-Americanisation' of the debt is imminent if the trend is not subtantially reversed.

It is necessary to note at the outset that the external debt of the Arab countries has grown by more than 10 per cent in 1983 only, to somewhere near 100 billion US dollars, constituting one-eighth of total Third World debt. Between 1974 and 1983, it multiplied twenty times. Clearly the situation is not as catastrophic as in South America, nevertheless all the Arab countries, whether large, medium, or small exporters of oil (or non-exporters, at that) are in one way or another and with varying degrees of intensity, experiencing serious liquidity problems. Austerity, often with explosive social consequences, is the order of the day.

The problem of financial surpluses in the 1970s has turned into an external payments crisis in the 80s. It is only recently that the Arab, and more generally, Third World debt has become a source of concern for the leading centers of international finance. The fact that Algeria, Iraq, Saudi Arabia and Egypt appear on the list of the twenty most indebted countries of the Third World, and the requests for rescheduling made by Sudan, Iraq and Morocco has brought to light the fragility and extreme vulnerability of the external financial positions of the Arab countries and their involvement in the international debt crisis. Arab debt grew by 25 per cent from 1982 to 1984, to the 130 billion dollars estimated by financial observers in the mid 80s.

A TYPOLOGY OF THE ARAB ECONOMIES

As already suggested the foreign payments crisis affects the Arab countries in different and unequal ways, and each country is involved in the Debt Economy to a different degree and in specific ways.

The Arab world is a field of unequal economic forces organised as nation-states, integrated into the world economic system with varying degrees of dependence from the international division of labour, and structured by an intraregional network of interdependence, centred directly or indirectly around the oil surpluses.

The Arab economies as a whole are usually divided into four sub-groups. Though this typology is too simplistic it is nonetheless fairly useful for our analysis.

Group 1 :	Algeria, Iraq
Group 2 :	Saudia Arabia, Libya, United Arab Emirates, Kuwait, Oman, Bahrain, Qatar
Group 3	Egypt, Morocco, Tunisia, Jordan, Syria, Lebanon
Group 4	Sudan, Somalia, Mauritania, Yemen Arab Republic Yemen Democratic Republic, Djibouti

The distribution of population and income clarify the main structural differences between these groups.

Table 1: Distribution of GDP and population and average per capital GDP for groups of Arab countries

Group	Gross Domestic Product			Population	Average per capita GDP (US$)
	1970	1980	1982		
G1	21.6	20.9	16.8	20%	1=$1000
G2	25.5	55.2	56.7	10%	1=$ 4000
G3	43.2	20.2	23.5	51%	1=$ 400
G4	9.7	3.6	2.9	19%	1=$ 300
Total	100	100	100	100	

Source : Arab Monetary Fund, Arab Economic Report, 1982 (in Arabic).

Thus in the early 80s the first group comprised one fifth of the population and one fifth of the GNP; the second group comprised only one tenth of the population for more than half of the GDP; the third group had half of the population, but less than a quarter of GDP; and the fourth had almost a fifth of the population and 3 per cent of GDP.

The most significant changes that took place in the decade 1970-80 were
- The relative stability of G1 is stare of income (with a slight drop since 1980)
- While G2's share of income doubled, G3's was halved.
- G4's share of income decreased to a third.

Thus, the strong and growing polarisation between G2 and G3+G4.
Table 2: Sectorial Distribution of GDP

Group:	All Arab countries		G1		G2		G3		G4	
Year:	1970	80	70	80	70	80	70	80	70	80
Sectors:										
Agriculture	17	7	15	8	3	1	22	15	42	37
Mining	23	23	22	32	59	53	3	16	2	1
Manufacturing	12	9	13	11	5	6	18	16	9	7
Construction	6	10	7	11	6	12	5	6	5	7
Electricity, gas, water	1	1	1	1			2	1	3	2
Transport, telecom.	8	6	7	6	6	5	10	10	8	9
Other services	33	28	34	31	19	23	40	36	31	38
TOTAL	100	100	100	100	100	100	100	100	100	100

Source: Arab Monetary Fund, Arab Economic Report, 1982 (in Arabic)

From the point of view of the sectorial distribution of GDP (table 2) the following is evident:

- The importance acquired by the mining sector, fundamentally in energy. Its contribution has more than doubled, and accounts for two-fifths of GDP.
- The substantial progress recorded in infrastructures, notably in G1 and G2. Manufacturing industries hold their own at around 10 per cent.
- The service sector loses relative weight but remains important.

Mines (thus hydrocarbons) and services account for two-thirds of GDP. As for agriculture, its importance has decreased sharply, pointing to a relative marginalisation. Agriculture received no more than 5 per cent of fixed investment in 1970-80. In fact, the main share of fixed investment went to mining (33.5 per cent) and services (27.6 per cent). Manufacturing industries, construction and transport have egual shares (10 per cent each).

Now, considering the sectorial distribution of GDP by groups of countries, structural differences between G1 and G2, the two groups of oil producing and exporting countries, become obvious. For G2 the mining sector accounts for more than 50 per cent of GDP, agriculture is almost non-existent, the manufacturing industries play a small role. For G1 the mining sector accounts for only two-thirds of GDP, manufacturing industries and agriculture (although in recession) account for one-quarter of the GDP. Though the productive non-mining sector is weak, it is nonetheless 3 times more important in G1 than in G2; however, the service sector is relatively more important in G1.

For G3, which has the largest demographic share (50 per cent), it should be noted that at the end of the decade mining (oil + phosphates), agriculture and manufacturing each generated about one-sixth of the GDP. Services play an important role, 36 per cent.

As for G4, agriculture and the services are predominant, generating two-thirds of the GDP: this is a manifestation of the relative weakness of productive structures in this group.

MACRO-ECONOMIC DISEQUILIBRIA AND DIFFERENTIAL PROCESSES OF FOREIGN INDEBTEDNESS

From the point of view of macro-economic equilibrium (Resources = GDP, utilisations = public and private consumption + gross fixed investment) it is necessary to underline important differences between the 4 groups that explain the processes of indebtedness for G1, G3 and G4. Tables 3 and especially 4 are quite indicative.

With the exception of G2 whose foreign trade balance still are in surplus despite some deterioration at the beginning of the 80s, G2, G3, and G4, with different income utilisation structures, recorded cumulative deficits, requiring foreign funding and originating indebtedness.

For the G1 countries, oil surpluses brought with them developmental (and military) ambitions: hence the very high level of capital accumulation. Over the years they saw a worsening in their trade balances and became dependent on external financial sources.

G3 countries with fewer internal resources and a high consumption/GDP ratio (around 90 per cent) had to systematically turn to foreign financing to sustain fixed capital accumulation (20 per cent of GDP). Here the deficit took on a durable structural form.

G4 countries, with minimal resources and an internal consumption that systematically and sometimes largely outstrips GDP, had a large structural deficit; indebtedness became a vital necessity to ensure economic survival.

Table 3: Resources/Utilisation

		Consumption/ GDP	Gross Fixed Investment/GDP	Trade Balance GDP
Group 1:				
Iraq	71	65.2	15	+19.2
	82	62.7	67.4	-30.1
Algeria	71	73.7	35.6	-9.4
	82	65	40	-4.8
Group 2:				
S. Arabia	71	44.5	11.9	+43
	82	41	33	+25
Bahrein	71	12.5	33	-17.1
	82	50	4.6	+17.7
UAE	71	26.8	32.4	+46
	82	39.8	27	+29.5
Libya	71	48.3	30.7	+33
	82	53.5	18.4	+27.5
Kuwait	71	42.9	18.9	+47.7
	82	62.8	9.3	+15.6
Qatar	71	22.6	21.5	+55
	82	57	12.2	+30
Oman	71	37.9	28.4	+33.6
	82	63	27	+9
Group 3:				
Morocco	71	86.5	15.5	-2.1
	82	90.4	22.8	-13.2
Egypt	71	91.1	13.9	-5
	82	93	20.9	-14
Syria	71	90.1	14.8	-5
	82	97.4	19.7	-17.1
Tunisia	71	82	20	-2
	82	80	30	-10
Lebanon	71	96.2	19.8	-1.6
	82	145.8	---	-4.6
Jordan	71	119.2	18.9	-38
	82	113.6	46.8	-60
Group 4:				
Somalia	71	94.7	12	-5.5
	82	97	20	-16
D Yemen	71	120	18	-38
	82	140	50	-90
A. Yemen	71	107	16.4	-23.7
	82	121	44.6	65.7
Mauritania	71	68	23.7	-2.5
	82	104	37.7	-41.7
Sudan	71	90.2	11.7	-2
	82	95.1	17	-12

Source: Arab Monetary Funds, National Accounts of Arab Countries 1971-1982

Table 4: Resources/Utilisations

In %	G1			G2			G3			G4		
Consumption/GDP	2/3			Between 40 and 60%			90%			100%		
Gross Fixed Invest/GDP	Very high and rapidly growing 40-60%			high and rapidly growing - 30%			moderate growth = 20% except Tunisia (30%)			moderate and variable except Jordan and Yemen (high)		
Trade Balance/GDP	Surplus at beginning of period for Iraq tendency to a growing deficit, stronger for Iraq			Surplus exists on the decrease, strength depends on the country			structural deficit = 1/10 GDP			very large structural deficit, from 40 to 90% of GDP		
Years	75	81	82	75	81	82	75	81	82	75	81	82
X exports/ M imports	101	74	62	295	209	140	69	78	67	46	31	37

In 1960-70 both G1 and G3 countries ran deficits and built up their debt in order to speed up growth, albeit to differing degrees and at different times. They increasingly and systematically resorted to foreign capital.

Foreign financing was an attractive proposition because of the public nature of 'aid', whether bilateral or multilateral, the long-term repayment conditions and their low real interest rates. In 1970, the total debt of the Arab regions ran at about 18.5 per cent of GDP; the ratio of debt service to exports was quite small: around 9.4 per cent. However, fast growth in the G1 countries (fuelled by hydrocarbon production) and medium growth levels in the G3 countries (based on mining - oil, phosphates - and import substitution) failed to solve structural deficiencies and created greater dependence on imports for intermediate and final consumption, thus leading to graning debt.

In the case of G4 countries, as we pointed out, there was no notable growth in the years 1960-70 and foreign indebtedness was a condition of mere economic survival.

ARAB FINANCIAL SURPLUSES, WORLD FINANCE AND THE WORSENING OF THE INDEBTEDNESS

Arab financial surpluses became a feature of world finance and contributed to the privatisation of the international financial and monetary systems, inaugurating the world debt economy. The origins of the Eurodollar market are in US fiscal and monetary policy, but this market offered particularly attractive conditions and absorbed Arab surpluses while financing Arab (as well as non-Arab) deficits.

The starting point is, of course, oil income and the creation of Arab financial surpluses.

Table 5: Current Account Surpluses of the OAPEC Countries (billions of dollars)

1974	1975	1976	1977	1978	1979
39.4	22.1	31.8	27.1	13.2	59.4

Source: A.Martens (1983), L'èconomie des pays arabes, Economica

A break-down of Arab credits shows that three-quarters were invested in developed countries, one fifth in the LDCs and 4 per cent in multilateral financial organisations (World Bank-IMF). Most of these financial surpluses were reinjected, usually in very liquid form, into the international financial system, supporting the Eurocredit market and international private banks. The one fifth going to LCDs, mostly Arab, includes a large part (60-75 per cent) of bilateral or multilateral public development aid.

The considerable increase in oil revenue greatly stimulated demand and especially imports. Some countries (G2) initiated, and other countries (G1 and G3) pursued more intensely processes of deficit growth by opening up more and more to the world market.

For G3 countries such as Egypt, Tunisia and Morocco, processes of deficit growth based on indebtedness took place thanks to greater extroversion and the setting up of suitable institutional rules to attract foreign capital. For Algeria and Iraq military needs and industrial ambitions compelled them to heavily rely on imports.

The other Arab exporting countries with weaker socio-demographic bases very rapidly enlarged their absorption capacity. An extraordinary increase in the demand for goods and services of all kinds (consumer, equipment, services) partially took the place of external financial placements. These countries slowly found themselves consuming excessive quantities of imported goods and products. Their economic bases are disconnected and vulnerable, and they rely exclusively on oil as a resource of external finance. They, too, experienced deficit growth, albeit with latent and deferred indebtdness (4).

As we have already seen, the characteristic common to all the unequal growth processes in G1, G2, and G3 countries is the marginalisation of agriculture and the emergence of an agricultural deficit (5).

For the period 1975-81 the growth rate for agricultural production was 2.6 per cent with the corresponding demand growing at the rate of 5 per cent (the demographic growth rate is 3 per cent). Even if agricultural import quantities (6) decreased, their value at current prices has nevertheless increased tenfold (1.7 billion US dollars - 16.9 billion US dollars). The agricultural deficit moved from less than half a billion dollars to 16.25 billion.

More than three-quarters of imports are manufactured goods and the deficits in this sector have gone from 4.5 to 18.1 billion US dollars. Studies show that, in fact, less than a fifth of total imports are equipment. The Arab world imports almost 100 per cent of its equipment. In 1980 it was seen that less than one-fourth of imports pertained directly to productive consumption (raw materials and industrial equipment). It is important to note, also, that for the G2 and G1 countries the major part of infrastructure work is essentially imported (construction has doubled its share of the GDP).

Finally arms expenditure has a strong impact on the degradation of external commercial and financial positions. Tables 6 and 7 show the arms expenditures for countries such as Kuwait (G2) and Somalia (G4).

Table 6: Military Expenses in Percentage GDP

	1972	77	79	81
Saudi Arabia	18.1	13.5	15	--
Kuwait	2.7	3.4	--	--
Egypt	19.9	32.8	13.1	--
Morocco	2.8	--	5.8	6.4
Syria	10.9	--	14.9	--
Tunisia	1.1	--	1.5	2.7
Somalia	6.2	--	6.8	--

Source: P. Jaber (1982) in Richard (ed.) Poor States in the Middle East, AUP, Cairo; World Bank

Table 7: Military Expenses as Percentage of Total Expenses

Algeria	14.1 % (1981)	12.7 % (1982)
	Defence+interior	
Saudi Arabia	Average 29 % (1981/84)	
Kuwait, Oman	Average 29 % (1969/79)	38 % (1983/84)
Egypt	11.8 % (1979)	19.7 % (82/83)
Morocco	12.3 % (1972)	16.2 % (1981)
Syria	37.2 % (1972)	37.7 % (1981)
Tunisia	4.9 % (1972)	8.3 % (1981)
Somalia	23.3 % (1972)	25 % (1981)

Source: Jaber, P. (1982) in Richard Poor States in the Middle East, American University Press, Cairo.

It should be noted that throughout the 1970s, the total debt of the Arab countries increased tenfold and debt service 14 times. According to the Arab Fund for Economic and Social Development the total debt rose to 69.2 billion US dollars in 1980. The debt/GDP ratio rose substantially from 18.5 per cent to 29.5 per cent with debt servicing rising from 9.4 per cent to 11.9 per cent.

In 1970, four countries accounted for three-quarters of the debt - Egypt, Algeria, Morocco and Tunisia. In 1980, Algeria, Egypt and Morocco constituted 70 per cent of the Arab debt; three countries have seen their situation deteriorate significantly: Sudan, Mauritania and Jordan. Algeria and Egypt are at the top of the indebtedness list: their debt/GDP ratio is over 50 per cent (54.6 per cent for the former and 51.4 per cent for the latter).

The debt service/export ratio is quite high at 27.2 per cent and 21.8 per cent.

Furthermore, according to the statistics of the OECD, in 1970 and in 1980, four Arab countries were among the 20 most indebted countries: Algeria (ranking 5th), Egypt (11th), Saudi Arabia (12th) and Iraq (14th), as shown in Table 8 below.

Table 8: External Debt of Selected Countries (millions of US$)

	1979	1980
5 - Algeria	17	17.3
11 - Egypt	12.2	13.8
12 - Saudi Arabia	2.7	2.9
14 - Iraq	2.3	2.5
TOTAL ARAB COUNTRIES	34.2	36.2
TOTAL OF 20 MOST INDEBTED COUNTRIES	266.2	301.2

Source: OECD

All indications point to a strong trend toward growing debt during the 1970s, the golden period for oil revenues and infitah.

Furthermore it is necessary to point out that the portion of private credit (extended from the financial markets and private international banks) rose significantly from 25.8 per cent on average, during the years 1970-71-72 to 41.2 per cent on average in the years 78-79-80 which, of course, had an effect on debt service.

The amount of interest on debt has increased twenty-five times, going from 119.8 million US dollars to 2874.6 million. Finally, according to World Bank statistics, Arab debt (including funds not yet disbursed) represented in 1970 one-tenth of total Third World debt. During the 70s this portion rose to one-sixth. Among the countries that experienced a deterioration in their situation, particular attention should be paid to Sudan. Its debt has gone up thirteen-fold and the debt/GNP ratio has risen from 14.6 per cent to 44.6 per cent.

The debt service/export ratio rose from 10.1 per cent to 16.8 per cent. In November 1979 the Sudan agreed to a rescheduling of its debt by one-tenth or 475 million US dollars, over a period of 7 to 10 years.
An analysis of external debt identifies two different situations and trends.

On the one hand, there is the case of the G4 countries such as Sudan and Mauritania (and more recently the two Yemens, Somalia and Djibouti), whose resource base is weak and who cannot finance their growth. They are extremely dependent on external assistance and on returns from one or more primary products subject to the whims of the international markets. They have turned to borrowing to be able to import goods needed to meet the basic needs of their population. The amount of their debt is a small portion of total Arab debt and moreover they are strongly dependent on bilateral and multilateral aid and on export credits financed or guaranteed by the public sector.

On the other hand, there is the case of countries in G1 (Algeria and Iraq) and G3 (Egypt, Morocco and Tunisia), whose indebtedness is rooted in the strategy of deficit growth and who experienced some industrial development.

Till the end of the 1970s, the screen of financial surpluses accumulated by the oil exporters hid from view the perverse effects of deficit growth and in any case deferred the crucial deadlines.

At the turn of the decade the awakening was painful. Numerous changes in the global situation particularly affected financial equilibria, leading to the crisis:

- the fall in the price of oil
- the emergence of significant deficits in the oil-exporting Arab countries resulting in reduced growth.
- the implementation of a deflationary monetary and financial policy
  in the USA, restricing and increasing interest rates. The resulting world deflation caused a contraction of international trade and a lowering of Third World exports coupled with a deterioration of the terms of trade.

The shock of the 1980s had serious repercussions on the Arab economies, for which oil revenue is the structural backbone. To be sure, other Third World countries were harder hit and external payment difficulties became macroscopic; requests for rescheduling multiplied; the IMF imposed conditions that often lead to social chaos. What is more, private banks, which had up till then played a major role in Third World debt, shyed away and credit became more difficult to obtain. Many countries found themselves incapable servicing their debt.

Arab total foreign debt reached 100 billion dollars in 1983, an increase of 10% over the year, and 25% between 1982 and 1984.

The case of Iraq stands out with respect to the substantial growth in the volume of debt. Because of the war effort (one billion dollars a month), the situation became particularly critical, requesting negotiations to reschedule the debt. Furthermore, Saudi Arabia and other oil exporters, which till then still enjoyed surpluses, started experiencing deficits and indebtedness; while of little importance, this new experience has nevertheless led to a freeze on numerous projects and to a squeeze of public spending, resulting in reptriation of immigrant workers. The fall in the price of oil has lowered the revenues of these countries by 50 per cent between 1981 and 1983, and they have been forced to turn to the Eurodollar market. The latent and deferred character of indebtedness contributing to growth deficit has become real and immediate.

Countries like Morocco and Sudan, and to a somewhat lesser extent Egypt and Tunisia, have experienced a marked deterioration. It is in these countries that social tensions caused by austerity are the most acute. While Morocco and Sudan have already negotiated a rescheduling of their debt, the situation remains precarious and tense in Tunisia and Egypt.

Countries like Syria and Jordan have experienced the repercussions of the dwindling of financial surpluses. Austerity is the order of the day, but grants which they received from Arab sources have somewhat reduced their financial vulnerability. Deprived countries like Somalia, Mauritania, the Yemens and Djibouti, have a large rate of indebtedness, particularly when taking into consideration their lack of resources. The structure of their debt (public credits, more liberal conditions) is a partial defence against the possibility of a catastrophic involution.

It is not being overly pessimistic to underline the precariousness and fragility of the prevailing Arab financial situation moving into the 1980s. The greater integration in the international economic system of the Arab countries brought their vulnerability. to the surface. To be sure, the Arab external payment crisis is not as severe as in some Latin American countries, yet further complications could cause it to precipitate.

Table 9: Foreign Debt of Arab Countries (billions of dollars)

	1981	1982	1983	1984
Iraq	15	22	30	32
Egypt	13.8	15.5	20	21.1
Algeria	14.4	13.9	15.4	13.2
Morocco	7.8	10.7	13	12.5
Sudan	4.8	7.8	8	8
Tunisia	3.1	4	4.5	4.08
Syria	2.3	2.7	2.8	3.5
Saudi Arabia	2.2	2.1	1.8	
Jordan	1.5	1.7	2.3	
Bahrain	0.42	0.47		0.48
Oman	0.5	0.7		0.97
Lebanon	0.24	0.29		5
Somalia	0.87	1		
Mauritania	0.82	0.94		
North Yemen	1	1.3		
South Yemen	0.64	0.81		1.05
Kuwait		1.3		
Libya		0.8		2.6
Qatar		0.3		

Source: IMF, World Bank

CONCLUSION

In this chapter we attempted to analyse the different processes leading to growing external public debt (and eventually to a series of crises, differentiated and unequal in nature, and implying different modes of economic readjustment). While sticking to the typology that we proposed at the outset, we intend to briefly examine how the specific characteristics of each state and political regime have, to a certain extent, determined the course of the debt process, the crisis, and readjustment possibilities.

For the purpose of simplification we have taken one or two countries per group.

G1 - Algeria
G2 - Saudi Arabia
G3 - Egypt
G4 - Sudan, Mauritania

At the basis of the correlation between the nature of the state and the indebtment process is the acknowledgement that throughtout the Arab world, the state has acquired a central role and primary importance. The state is the backbone of the organisation of society and the economy. The state dominates politics and subordinates economic goals to the predominant concern of enlarging and concentrating power.

The state establishes and reproduces within itself a ruling class which directs the state apparatus and forges alliances with other dominant social forces at a local and international level.

This centrality of the state has come to even greater prominence in these last decades as it enlarged its control of the economy and its reproduction. The substantial growth of oil surpluses has in effect given the state an even more decisive role to play.

Because of its centrality, the state has been at the heart of the debt economy and its crisis, at the heart of perverse deficitary growth and indebtedness.

For the G1 group, Algeria exemplifies a country endowed with a medium sized demographic base and relatively high energy surpluses, which experiences a bureacratic political regime stemming from military origins, a populst ideology, an industrial policy which marginalises the peasantry and embraces the dominant model of technological consumerism. It is from these factor that the debt process takes its structural form. The crisis of the 1980s arises from the failure of the etatiste development model. Economic and social readjustments (balancing the budget, import limitation, economic decentralisation, support of the private sector) are initiated and controlled by an omnipresent state where the army occupies a central position.

In the G2 group, Saudi Arabia is the example of a country with a rather weak demographic base, a significant oil surplus and a political regime which can be described as oligarchic (with tribal and religious support). The ruling class has strong ties to the West, entertains hegemonic ambitions over the region (hence her military effort), and seeks to integrate in the international division of labour by investing in huge export orientated industrial complexes in downstream petroleum. The neopatrimonialist character of the state stemming from the oil rent, has led to the adoption of an ostentatious and imitative consumption model, spread by means of rent distribution.

Here the process of deficit growth and deferred indebtedness is fuelled by an active policy of military expenditure, investment in infrastructure and in export-oriented large-scale industrial development, and by a perverse consumption model deriving from the 'rentier' character of the economy. Debt is at present mostly short-term; the crisis postulates readjustments including redefinition of the model of distribution which is also the essential base of legitimation.

In the G3, group, Egypt is a country with a strong demographic base and modest rent revenue. The political regime is bureaucratic in nature with military origins. The ruling class is formed within the state civilion and military apparatus. An initial phase saw the emergence and development of an étatist industrial project based on a populist ideology, which in practice did not allow for the participation of the popular classes. The pan-nationalist project conceived by Nasser, and its implications in terms of military procurement, combined with modernisation based on imitation of the dominant technologial consumption model, led to deficit growth and indebtedness.

The second phase, infitah, characterised by the importance of rent revenues, further contributed to the import-dependent nature of the economy. The pursuit of military spending, the need to heavily subsidise basic necessities, the upkeep of a plethoric bureaucracy all worked together to make borrowing unavoidable. The crisis questions the ruling class itself, as it is caught between the requirements of the IMF and popular revolts. In this case, the margin for manouver is very narrow and the outlook for readjustment uncertain.

Finally, in the G4 group, Sudan and Mauritania, despite their different demographic make-up, both have the common characteristic of having only very small surpluses. In both cases, the state is characterised by instability (national fragmentation, subnational particularisms). The ruling classes, military-type bureaucracies basing their power on a small surplus which has till now not been channeled into development. One must speak of proto-state with extremely limited legitimacy, where survival depends on external support. Vulnerability is great and readjustments cause social change.

Thus, taking into consideration the class nature of the state, its ideology, its economic policy (or absence thereof), its integration into the international system, the nature and level of surplus on which it is based, we arrive at different conditions determining the process of indebtment and adjustment.

NOTES

1. In 1970, three-quarters of Arab public debt involved one country of the G1 Group - Algeria; and 3 countries in G4-Egypt, Morocco, Tunisia which were the first countries to be affected by the process of deficit growth and indebtedness.

2.	Total Annual budget deficit	Public Debt in billions of $US
1973	14.9	468.4
1974	6.1	485.2
1975	57.2	544.1
1976	73.7	631.9
1977	53.6	749.1
1978	59.2	780.4
1979	40.2	833.8
1980	73.8	914.3
1981	78.9	1003.9
1982	127.9	1147
1983	224.8	1383.8

Source: Economic Report of the President, Washington - 1983

3. It is interesting to note that the US annual budget deficit in 1983 was almost twice that of the total debt of all Arab countries and that the American public debt in 1983 was 1.6 times that of the sum of Third World debt.

4. That is to say, not creating local productive capacities to offset demands sustained by consumption patterns and capital accumulation.

5. Distribution of Imports (all Arab countries)

	1970	1980
Manufacturing products	74.4	78.3
Agro-food products	20.2	15.9
Raw materials	5.4	5.8

Source: Trade Year Book 1970-1980, Yearbook of international trade - statistics 1970-1981

6. Ratio of Imports to Exports X/M (in per cent) (all Arab countries)

	1974-79	1980-82
Cereals	69	50
Meat	93	67
Dairy Products	91	76
Fruit and Vegetables	104	50

Source: United Nations, Trade Yearbook 1970-1980: Yearbook of International Trade Statistics 1970-1981

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Chapter 8

THE RENTIER STATE IN THE ARAB WORLD

Hazem Beblawi

INTRODUCTION

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

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

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

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

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

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

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

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

A RENTIER STATE: ELEMENTS FOR DEFINITION

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

Few characteristics should be kept in mind for a definition of a rentier state in our context.

First, there is no such thing as a pure rentier economy. Each and every economy has some elements of rent. A rentier economy should be defined as one, where rent situations predominate. this, of course, is a matter for judgement.

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

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

A rentier economy is thus an economy where the creation of wealth is centred around a small fraction of the society, the rest of the society is only engaged in the distribution and utilisation of this wealth. The respective roles of the few and the many can hardly be overstated for the concept of a rentier economy. Accordingly, an open economy with high foreign trade is not a rentier state, simply because it relies on the outside world, even if it generates its income from natural endowment (e.g. tourism) in as far as the majority of the society is engaged in the process of wealth generation.

Fourth, a corollary of the role of the few, in a rentier state the government is the principal recipient of the external rent in the economy. This is a fact of paramount importance, cutting across the whole of the social fabric of the economy affecting the role of the state in the society. The role of the government as the principal recipient of the external rent is closely related to the fact that only few control the external rent. In fact, the 'economic power' thus bestowed upon the few would allow them to seize 'political power' as well, or else induce the political elite to take over the external rent from them without major political disruption. A predominantly rentier state will accordingly play a central role in distributing this wealth to the population. This brings us close to a distinction proposed by Giacomo Luciani, that is, between productive and allocative states. (7)

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

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

THE OIL STATES: MULTILAYERS OF RENTIERS

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

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

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

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

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

Of course, governments in the oil states outgrew their role as distributors of favours and benefits and embarked on the modern function of providing public goods and services to their population. Governments are providing their populations with a wide range of genuine public goods and services: defense, national security, education, health, social security, employment, an impressive network of infrastructure, etc. The level and quality of these public goods and services are usually adequate, sometimes excellent. They are also provided free or at very low cost to the beneficiary. However, the original sin remains, sometimes open but mostly latent, thus vitiating the provision of these public goods. It is reported that 'if a prince heads a ministry or some other government department, it is accepted that he is entitled to draw on the budget of that department or take a share of its spending in major projects '(Field 1984: 101-2). To a certain degree, all government contracts are seen as royal favours. Their origin as part of the ruler's benevolence does not fail, thus, to exhibit their peculiarities.

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

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

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

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

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

Land, it was said, has played a major role in the process of trickling down oil money from governments to private individuals. The readiness of governments to purchase land at higher prices sustained ever-growing prices for real estate. A very profitable business was created round land speculation with some very active brokers. Government was always prepared to act as the ultimate buyer.

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

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

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

The government role in the development of this speculative activity can hardly be over-estimated. Not only did governments indirectly help speculations, but in many instances were directly involved in supporting speculative markets. When the Kuwaiti stock market faced its first setback in 1976/77, the Kuwaiti government was prompted to bail it out. Even in 1982, when the Kuwaiti government refused to repeat the role it played in 1976-77, it compensates the so-called small investor - defined as one owed no more than KD 2 million ($ 6.75 million): a no small reward for speculators. In both cases, a number of key members of government and parliament were deeply involved in the stock speculations.

The juxtaposition within Arab oil states of a rentier economy and a productive economy is paralleled by the coexistence of two social communities: nationals and expatriates. Expatriates are called upon to help fill the gap in available manpower in oil states. More often than not, these expatriates assume productive activities to satisfy the growing needs of the society. They earn their living by the work they do. The relationship work-reward is actually maintained in their case. Rent economy, on the other hand, is normally confined to nationals; the privileges it conveys hardly extend to expatriates.

The contrast between the two communities is striking as well as revealing. Nationals live more in a rentier economy and associate to its financial manna all the political rights of citizenship. On the other hand, although earning their living in a more productive manner, the impact of the rentier economy on expatriates is far from negligible, giving rise to serious corruption of the productive system and work ethics. Even if they form the core of the productive manpower, expatriates nevertheless remain alien to the body politic. Though they serve the country, live - and also die - on its soil, they are not part of it. Expatriates are thus part of the labour force but not of the society. The material life of expatriates is usually comfortable and by no means comparable to the living conditions in their homeland. Their emotional life is, nonetheless, unstable, terribly wanting in security and lacking a sense of belonging.

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

THE NON-OIL STATES: SEMI-RENTIERS WITHOUT OIL

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

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

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

Rhetoric aside, inter-Arab aid was related, to some extent, to its effect on the stability and tranquillity of oil rent in oil states. Very often Arab aid to fellow Arab states was used in much the same way as domestic redistribution of oil revenues: to buy allegiance or rather avoid trouble. Pan-Arabism and Arab money were, to a great extent, and in different hands, the stick and the carrot, used to bring about a very subtle equilibrium in sharing oil rent. By conferring and/or withholding super-legitimacy over individual states, the advocates of pan-Arabism used their political clout as a source of financial aid. By distributing and/or promising aid, the carrot in the hands of the oil states helped them buy peace and stability. Arab finance was thus more a counterpart than a complement to pan-Arabism. It is no wonder, then, that Arab financial flow to Arab brothers coincided with the retreat of the pan-Arab system after the 1967 war, which 'marked the Waterloo of pan-Arabism' (Ajami 1978/79). In the wake of the October 1973 war, it was Sadat and Assad - 'revisionists' or 'correctionists' of the pan-Arab doctrine - who obtained Arab finance. With the decline of Egypt's role - in mobilising Arab public opinion, particularly after Camp David, the Baghdad Summit relieved the Arab oil states of their financial commitments to Egypt, shifting them to more assertive Iraq, Syria and the PLO. The subsequent Iraq-Iran war proved to be quite a drain on their treasury. The Baath party, which is in power in both Iraq and Syria, though two competing factions, is notorious for its unscrupulous and ruthless practices vis-à-vis its opponents. Some oil states - Kuwait and UAE for example - had the privilege of actually experiencing firsthand such practices when a number of attacks and/or bombings took place on their territory. They had, of course, the tact and discretion to turn a blind eye to these 'accidents'. But the message is clear.

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

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

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

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

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

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

CONCLUSION: AN OIL ARAB ECONOMY

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

NOTES

1. 'The religious valuation of restless, continuous, systematic work in a worldly calling, as the highest means to asceticism, and at the same time, the surest and most evident proof of rebirth and genuine faith, must have been the most powerful conceivable level for the expansion of that attitude toward life which we have here called the spirit of capitalism'.' Weber, M. (1958) The Protestant Ethic and the Spirit of Capitalism, Charles Scribner's Sons, New York, p. 127

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Chapter 9

THE MACRO BEHAVIOUR OF OIL-RENTIER STATES IN THE ARAB REGION

Mahmoud Abdel-Fadil

BASIC FEATURES CHARACTERISING THE ECONOMIES OF OIL-RENTIER STATES

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

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

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

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

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

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

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

Nonetheless, the important point to be stressed here is that, because of the high import intensity of these construction activities, extensive government expenditure programmes (both current and capital) in oil-rentier states tended to generate negligible inter-sectoral linkages within the domestic economy.

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

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

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

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

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

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

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

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

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

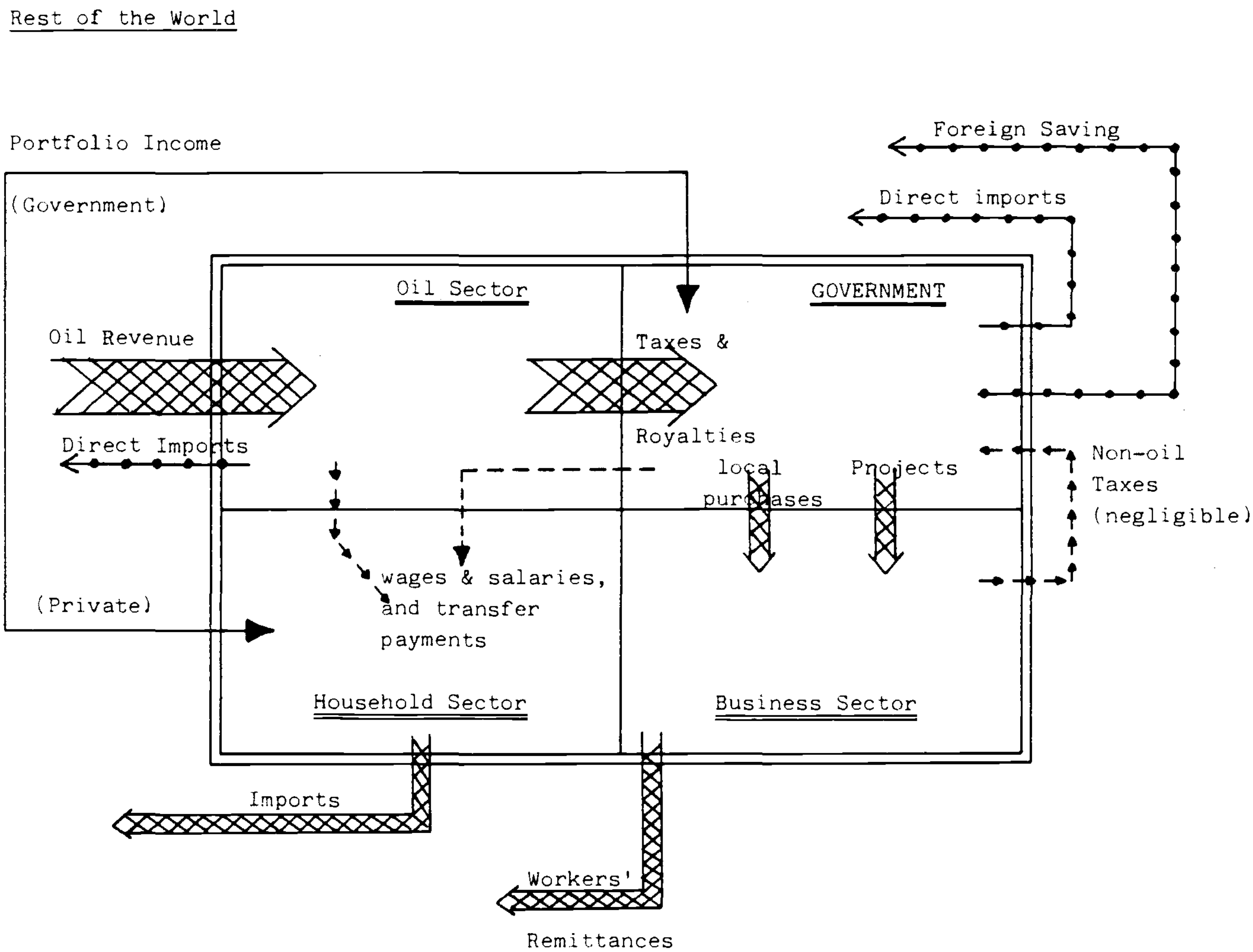
THE MODE OF INTERACTION BETWEEN THE EXTERNAL OIL RENT AND THE INTERNALLY-GENERATED TYPES OF RENT WITHIN THE DOMESTIC ECONOMY

Since oil revenues constitute the primary source of rent in an oil-rentier state, the mechanism of 'internal recycling' of the oil rent within the national economy through the state budget (i.e. programmes of public spending) gives rise to a variety of secondary types of rent. Government expenditures which give rise to these secondary types of rentier income are: (i) project expenditures such as construction; (ii) transfer or welfare payments such as the land purchase programme in Kuwait (see figure 1).

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

As a result, a new pattern of <u>a tripartite alliance between the state, the new business élites</u> (i.e. merchants, contractors and financiers), <u>and circles of international financial capital emerges</u>. Figure 2 depicts the dialectical relationship between these three agents as well as the feedback effects underlying the modus operandi of oil-rentier states in the Arab region.

Figure 1: Flow of Economic Resources in a Rentier State



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

Nonetheless, the degree of dependence on various types of external rentier income: (i) oil rent; (ii) locational rents; (iii) other mineral rents; (iv) workers' remittances; (v) portfolio income; is not usually confined to the recorded volume of various types of external rents and unrequited transfers. For it is well known that all types of external rents and unrequited transfers exercise multiplicative effects upon the recipient economy.

Professor Thomas Stauffer suggested a new kind of multiplier called the 'rentier-income multiplier' to capture the full extent of dynamic dependence of rentier states on external rents and unrequited transfers. The rentier multiplier is similar to the familiar Keynesian multiplier in that it specifies how an initial injection of external rents causes a larger increase in effective demand and thus leads to an increase in national disposable income greater than the initial injection.

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

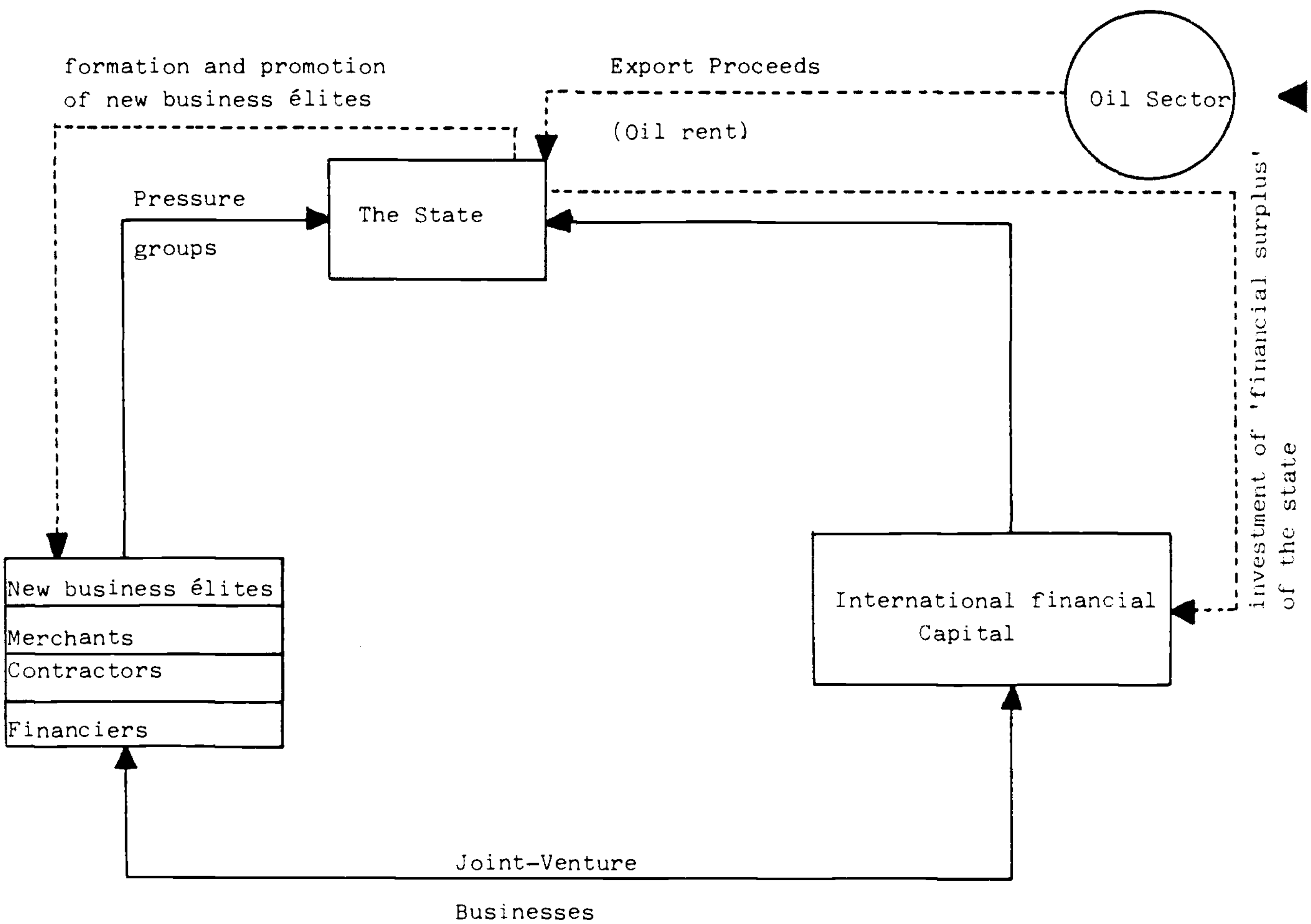
The recipients of these funds - civil servants, local merchants and contractors - spend part of this money on imports, which then leaks out of the national economy, but the rest of the money is respent at home and a second-round effect is generated, and so on.

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

In the case of 'non-oil' semi-rentier states such as Egypt, the Arab Republic of Yemen and Jordan, workers' remittances - the most potent form of rentier income - are usually subject to an important multiplier process.

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

Figure 2. The Dialectical Relationship between the State, New Business Elites and International Capital in an Oil-Rentier State



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

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

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

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

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

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

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

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

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

An attempt will be made here to apply a modified version of the Tableau Economique of F. Quesnay, to serve as a useful tool of static macro-economic analysis. In fact, the French school of the 'Economistes' or 'Physiocrats' of the third quarter of the 18th century, was the first to view the 'feudal mode of production' as the creation of a 'surplus', primarily consumption goods, available for unproductive use to support government activities and the cultural life of feudal seigneurs.

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

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

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

<u>Description of the tableau</u>

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

a) <u>The productive class</u> with which production expenditure is associated. Productive expenditure is employed in the primary sector in order to perpetuate wealth in the form of food, drink and raw materials for manufactured goods.
b) <u>The sterile class</u>, whose sterile expenditure is on manufactured commodities and foreign products.
c) <u>The proprietor class</u>, to which accrues a revenue from the productive class, in return for the rental services provided by that class.

Unlike Quesnay's agrarian economy, the Kuwaiti economy consists of more than three social classes. This is mainly because of the existence of a large non-Kuwaiti labour force.

Instead of a productive class, a proprietor class and a sterile class, we have in our tableau, two major subdivisions consisting of Kuwaitis and non-Kuwaitis.

Non-Kuwaitis are by definition wage earners only, since rent and dividends do no accrue to them because of restrictions on ownership of property and company shares. Non-wage income is restricted mainly to Kuwaiti industrial capitalists, traders and landowners. Civil servants are divided between Kuwaiti and non-Kuwaiti classes at roughly 40 per cent and 60 per cent, respectively (1976 data). There is no Kuwaiti agricultural labour.

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

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

Table 1: SAM 1979 for Kuwait

		1	2	3	4	5	6	7	8
FACTORS	1. Land								
	2. Labour								
	3. Capital								
KUWAITI CLASSES	4. Kuwaiti Landowners	12							
	5. Kuwaiti Traders & Industrial Capitalists			18007		448	276		1
	6. Kuwait Civil sergants								
	7. Kuwaiti Adm. & Tech. Staff								
	8. Kuwaiti Indistrial Labour								
	9. Kuwaiti Other Labour								
NON-KUWAITI CLASSES	10. Non-Kuwaiti Professionals and Adm. & Tech. Staff								
	11. Non-Kuwaiti Agricultural Labour								
	12. Non-Kuwaiti Industrial Labour								
	13. Non-Kuwaiti Other Labour								
	14. Non-Kuwaiti Civil servants								
SECTORS	15. Agriculture								
	16. Industry			354					
	17. Oil				2204				
	18. Construction								
	19. Trade & Finance			483					
	20. Other								
	21. State			532					
	22. Capital a/c								
	23. ROW		147						
	24. GRAND TOTAL	12	147	19376	2204	448	276		19

*Institutions

Sum of Expenditures ** = 70195

** discripancies represent errors and ommissions

9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24
														920	920
															12
	904	6	249	76	4436										24421
												1231			1231
						3	203	253	13	194	129				795
							48								48
								268		7	8				283
						15	952	412	486	2194	1111				5170
						83									83
							1511	161							1672
									998	177	1714				2889
												1162			1162
														36	36
												35	929	272	1590
												15	7458	4781	14458
															483
												2695			2695
								9275			147				9954
												3401			3401
												1646	62		1855
	904	6	249	76	4436	101	1714	10369	1497	1572	3109	10185	8449	6009	70195

Main features revealed by SAM 79 for Kuwait

The Rest of the World Account

1) Investment income from abroad is distributed as follows:

Government	58%
Financial Sector	16%
Other Private	26%

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

2) Workers' remittances (in cash) represented as an expenditure by labour as a factor of production to the rest of the world, are at 147 million K.D. This gives an average propensity to remit of 1.3 per cent out of total non-Kuwaiti wage income (1976) which is extremely low by any standard.

3) Oil export revenue (94 per cent) of total exports accounts for the impressive figure for export proceeds compared to the total import bill.

Kuwaiti Classes Account

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

Distribution of non-wage Kuwaiti income accruing to industrial capitalists and traders was reported to be as follows:

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

* Total may not add up due to rounding.

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

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

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

Non-Kuwaiti Classes Account

Total non-Kuwaiti wage bill is distributed as follows:

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

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

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

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

The State Account

Oil revenue	93.2%
Investment income	5.3
Other	1.5
	100.0%

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

The Capital Account

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

The Tableau Economique for the Yemen Arab Republic, 1973 and 1982

The Yemen Arab Republic (YAR) constitutes a typical example of a semi-rentier state heavily dependent on workers' remittances and aid flows emanating from neighbouring Arab oil-rich states.
Table 2: SAM 1972/73 (millions of YRs)
Table 3: SAM 1981 for Yemen (millions of YRs)

An attempt is made here to construct a Social Accounting Matrix (SAM) for North Yemen for two points in time: the financial year 1972/73 and the calendar year 1981, in order to capture the increasing rentier nature of the Yemeni society (see tables 2 and 3).

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

Table 2: SAM 1972/73 (millions cf YRs)

		1	2	3	4	5	6	7	8	9	10
FACTORS	1. Labour							101.9	4	21.8	57.6
	2. Capital & Land							917.1	12	65.2	68.4
INSTITUTIONS	3. Households	747									
	4. Private business		1592.4				-45.6				
	5. Public business										
	6. Government		9.6	6.8	4.6	31					
ACTIVITIES	7. Agriculture										
	8. Mining										
	9. Manufacturing										
	10. Construction										
	11. Utilities										
	12. Trade & Hotels										
	13. Trasnport										
	14. Real Estate Serv.										
	15. Community Serv.										
	16. Government Serv.										
	17. Prive Serv.										
	18. Financial Inst.										
	19. Imputed Bank charges										
	20. Commodities			2188			317	164	5	129	158
	21. Indirect taxes							7	–	20	–
	22. Capital Account				383.4		-72.4	10	1	11	4
	23. Rest of the world										
	24. TOTAL	747	1602		2613.8		199	1200	22	247	288

11	12	13	14	15	16	17	18	19	20	21	22	23	24
1.5	27.1	15.5	0.9	1.3	250	8	5.6	–				252	747
4.5	347.9	46.5	99.1	17.7	–	–	32.4	-39				30	1602
										147			199
									1200				1200
									22				22
									247				247
									288				288
									14				14
									431				431
									116				116
									111				111
									30				30
									328				328
									9				9
									46				46
									–				–
7	47	40	9	10	76	1	6	39			381	62	3639
–	3	3	1	–	–	–	–	–	113				147
1	6	11	1	1	2	–	2	–				20	381
									684				684
14	431	116	111	30	328	9	46	–	3639	147	381	684	

Table 3: SAM 1981 for Yemen (millions of YR)

		1	2	3	4	5	6	7	8	9	10
FACTORS	1. Labour							427.9	38	274.5	603
	2. Capital & Land							3069.1	112	410.5	410
INSTITUTIONS	3. Households	5294	6961				30.3				
	4. Private business										
	5. Public business										
	6. Government		450	170	165.2	264					
ACTIVITIES	7. Agriculture										
	8. Mining										
	9. Manufacturing										
	10. Construction										
	11. Utilities										
	12. Trade & hotels										
	13. Transport										
	14. Real Estate Serv.										
	15. Community serv.										
	16. Gov. Serv.										
	17. Private Serv.										
	18. Financial Inst.										
	19. Imputed Bank Charges										
	20. Commodities			12942			3043	1040	60	1083	2005
	21. Indirect taxes						252	106		117	24
	22. Capital Account				2323.1		3.9	45	6	52	43
	23. Rest of World										
	24. TOTAL	5294	7411		15864.3		3329	4688	216	1937	3085

11	12	13	14	15	16	17	18	19	20	21	22	23	24
26	231.1	84	5.4	9	1958	24	129					1484	5294
81	1877.9	229	538.6	103			831	705				454	7411
												3579	15864.3
										2280			3329
									4688				
									216				216
									1937				1937
									3085				3085
									227				227
									2434				2434
									699				699
									637				637
									205				205
									3111				3111
									26				26
									1084				1084
116	246	229	70	74	1146	2	86	705			5641	1130	29618
	14	87	18	9			20		1633				2280
4	65	70	5	10	7		18					2989	5641
									9636				9636
227	2434	699	637	205	3111	26	1084		29618	2280	5641	9636	

The semi-rentier nature of the Yemeni economy becomes obvious by 1982, as recorded workers' remittances amounted to 1906 million YRs as compared to 252 million YRS in 1972/73.

The property and entrepreneurial income from the rest of the world as well as other current transfers from the rest of the world (i.e. aid flows and grants), reached about 3.5 billion YRs in 1981 as compared to 50 million YRs only in 1972/73. All in all, current rentier income accruing to the Yemeni economy amounted to around 5 billion YRs in 1981 (or about 40 per cent of the gross domestic income).

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

Table 4: Pattern of Gross Domestic Expenditure in 1973 and 1982 (at current prices) (millions of YRs)

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

The increasing dependence on various types of rentier income in the formation of national disposable income may be deduced from the following table:

Table 5: National Disposable Income (millions of YRs)

	1973 (1)	1982 (2)	Ratio (2/1)
Compensation of employees (domestic)	600	4465	7.4
Compensation of employees from the rest of the world*	252	1609	6.3
Operating surplus (domestic)	1973	7542	3.8
Property and entrepreneurial income from the rest of the world*	75	506	6.7
Indirect taxes	208	2265	10.8
Other current transfers from the rest of the world*	391	4121	10.5
National disposable income	3499	20508	5.8

* Rentier and semi-rentier types of income

The two matrices also reveal the declining importance of the agricultural sector in generating the domestic operating surplus (i.e. economic surplus) as it, in 1981, accounted only for 44 per cent, while that of trade increased its share to 27 per cent. The manufacturing and construction sectors slightly increased their share in total operating surplus to account for 5.9 per cent each. A major development, which took place over the period 1972-81, was the dramatic increase in the role of the fnancial sector. This sector's share in domestic operating surplus (before deducting banking charges), jumped from 2 per cent in 1972/73 to 20 per cent in 1981.

Although national savings increased from YRs 383 million in 1972/73 to YRs 2300 million in 1981 (i.e. a sixfold increase), their capacity to finance investments have greatly declined, and paradoxically enough, dependence on foreign finance grew dramatically. While the deficit on the current account of the balance of payments in 1972/73 amounted only to 20 million YRs, (i.e. 5 per cent of investment expenditure), in 1981 net borrowing covered 53 per cent of the funds required to finance investment. The growing investment/saving gap reflects the fact that most of the increase in income is being absorbed by consumption, which reduces the saving capacity of the economy.

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

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

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

In most oil-rentier states, there seems to be a wide acceptance of the simple value judgement that the preferences of our contemporaries are to be given great weight, and those of unborn generations to be given a negligible weight in the formation of people's attitudes towards intertemporal choices. The presence of a strong pure time preference among members of the powerful business community in oil-rentier states may be conceived of in the following words, put by Sir Roy Harrod:

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

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

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

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

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

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

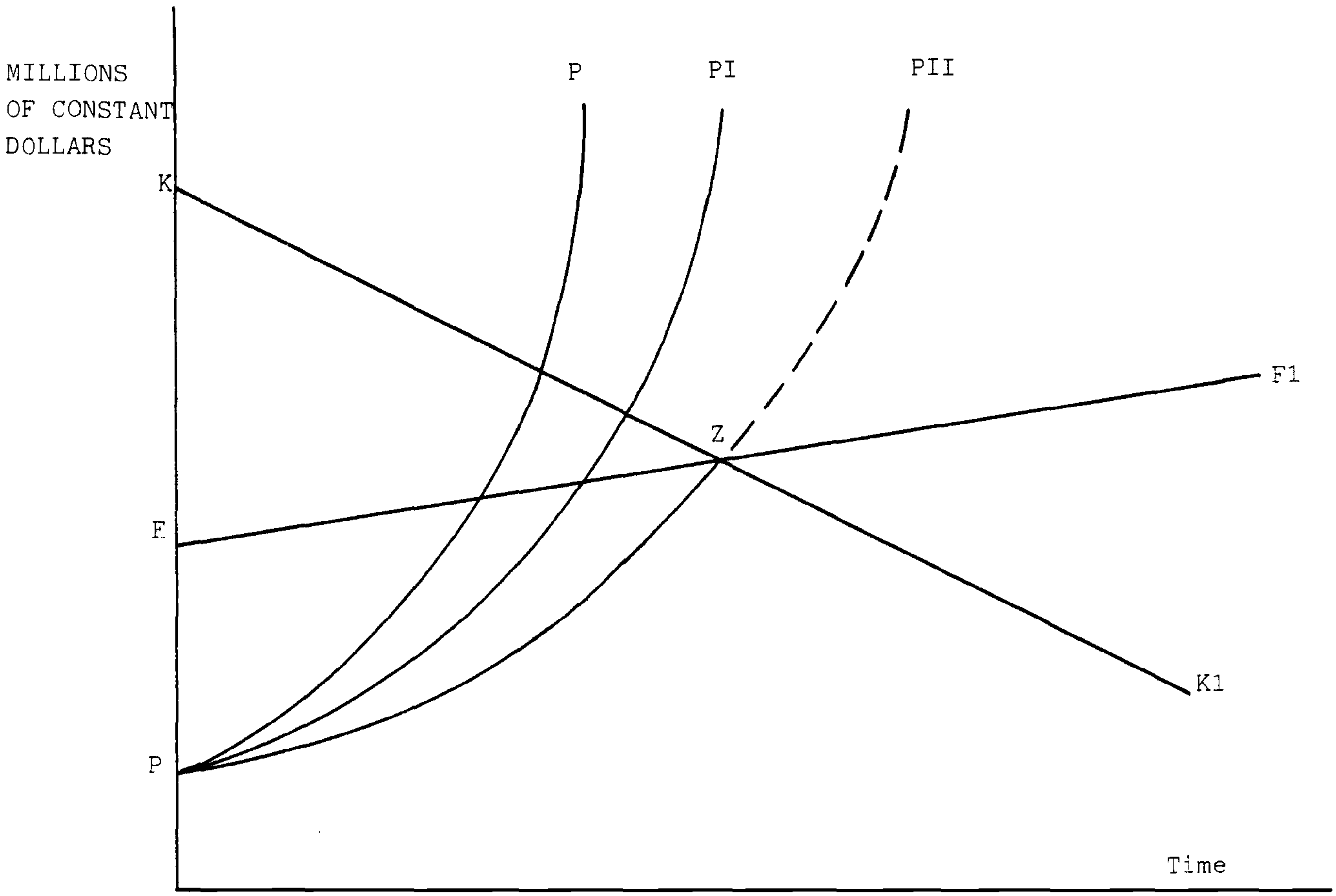
ALTERNATIVE DYNAMIC TRANSITIONAL PATHS OF OIL-RENTIER STATES

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

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

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

Figure 3: The Build-up of Income on Foreign Assets over Time



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

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

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

Moreover, there are many other dynamic factors which need to be taken into account in order to assess the viability and feasibility of the assumed transitional path as depicted in figure 3. A scenario based on a few simplified assumptions was devised by Dr. Hazem el-Beblawi (1978: p. 19), to show that, 'other things being equal', the potential claims of oil-rentier countries on the exports of goods and services of the host industrialised countries (especially U.S.A.) will be unexpectedly high, when they start the annual servicing of financial assets accumulated by the oil-rentier states.

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

Ideally, the national interest would be best served if the oil resources were depleted at a time when the highest possible level of development and diversification of the domestic economy has been attained, a possibility which is highly unlikely under the prevailing set of policies in Arab oil-rentier states.

NOTES

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

2. In the case of Kuwait, this was apparent in the government's land acquisition programme. Purchase of land by the government was considered the simplest and quickest method of distribution of national oil wealth among the Kuwaiti population. Thus, a total of more than KD one billion (equivalent of US $3.4 billion) was disbursed through the land acquisition programme during the years 1952-1975. The government, in fact, distributed by this means about one-quarter of its total oil revenues during the period from 1946 to 1971. The funds allocated to this programme in these years exceeded the country's investments in foreign assets and were almost equivalent to all government development expenditure during the same period. The government was paying for the purchased land sums of money far in excess of what it was worth.

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

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

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