Over the last twenty years, there has been a distinct evolution in the thinking on economic reform. Up until twenty years ago, almost all the analysis of development practitioners centered around identifying the common factors of successful economies. The focus was definitely on the “whats” and the “whys” of reform. If you looked at the plenary remarks from an economic conference in almost any country or region of the world, you would have almost certainly seen an outline of specific policy reforms needed to unleash higher growth and improve living standards. Far less attention, however, would have been paid to the “hows” of reform. You might have seen a token sentence on the order of “the task before you is difficult,” but that was about it. It was left up to the developing world to figure out how to implement this complicated system of reforms – reforms which we increasingly realized were interdependent.

Today, we are enormously interested in the “hows” of reform. What makes reform happen? Why does reform take place in some countries but not in others? Why do some reform efforts ratchet up to comprehensive economic
transformations why others fizzle out? What facilitates or hinders the reform process? After years of waxing eloquent on the reform agenda, development practitioners now appreciate the fact that economic reform is difficult and that we need to significantly improve our understanding of what makes initiating and sustaining reform possible.

Within the MENA region, this interest has been no less intense. If you look at the region’s reform effort, I think it’s fair to say that economic reform has been somewhat disappointing. Despite a significant push initiated by MENA economies starting in the 1980s, the region has had difficulty in carrying forward reform.

The World Bank recently released an economic review of the MENA region, the first in an annual series, in which the status of structural reform worldwide was examined along several areas, including trade, business and regulatory reform and governance reform. And the report found that in most areas of reform, MENA economies rank well below other regions of the world. In the area of trade, for example, if you were to take all the countries of the world and rank them based on their simple average tariffs, you would find that MENA economies on average MENA average rank in the 35th percentile worldwide – that is to say, on average about 65% of the world has lower tariffs. In the area of governance reform indicators, the MENA region ranks even lower, averaging in the 30th percentile – again, this means that on average about 70% of the world has “better” governance indicators. There are a few areas where the region has made some strides, but by and large, we are looking at a region that has lagged with reform.

So I welcome this opportunity to look more intensely behind the reform effort, to better understand the region’s reform experience.
In my recent talks about the reform experience in MENA, I have pointed out what I think are the two major factors which have, at least historically, hindered a stronger reform effort.

Oil

The first factor has been oil. Oil has historically allowed MENA governments to delay economic reforms. There is a line of thinking that deep economic reform movements only result from fundamental change, either from leadership change (regime change, or a shift in governing coalition); or from dramatic economic change – in other words economic crisis. In many Latin American countries, for example, economic reforms were undertaken only when the “economic conditions had deteriorated sufficiently so that there emerged a political imperative for better economic performance.”\(^1\) Or, put another way, reform often is only adopted “once the possibilities of throwing money at the problem are foreclosed.”\(^2\) Indeed, the reform movement initiated in the Arab region was a direct consequence of the oil price collapse of the early 1980s.

As we are all aware, oil prices have surged over the last three years, which has allowed the MENA region to realize average annual growth rates of more than 5.7%, the strongest growth in a decade. Among the oil producing economies, economic growth has averaged 6.2%. And equally important, oil prices -- the

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foundation for the growth surge in the region – are expected to remain firm into the medium term.

What impact will oil and higher oil prices have on this region’s reform effort? Since reforms take time to take effect it is not easy to say definitively for the region. But worldwide, when you look at the current oil boom that is occurring, we find there is a considerable difference in the measured reform effort among oil versus non-oil economies worldwide. In the Bank’s regional review, we actually charted the recent structural reform progress worldwide along the areas of trade, business and regulatory reform, and governance reform since 2000, about the time that oil prices began their rise. And when you compare economies which are heavy oil producers\(^3\) with non-oil economies\(^4\), you find that in terms of reform progress, non-oil economies have significantly outpaced oil economies since the beginning of the oil price rise. If you were to rank economies based on their reform effort over the last few years, you would find that heavy oil producers rank in the 29\(^{th}\) percentile in terms of reform of the business and regulatory environment. Non-oil economies rank on average in the 5\(^{4th}\) percentile. Although both groups have maintained similar efforts in terms of reform of public administration, heavy oil producers rank in the 33\(^{rd}\) percentile in terms of improving public sector accountability. Non-oil economies on average rank in the 56\(^{th}\) percentile.

Within the MENA region, the distinction between reform in the oil and non-oil economies is less acute, but overall the reform effort among non-oil producers has outpaced oil-economies since the oil price rise. This has been most visible in

\(^3\) With oil exports accounting for more than 60% of exports
\(^4\) With oil exports accounting for less than 20% of exports
terms of business and regulatory reforms, where progress among oil producers over the last few years have averaged in the 30th percentile, worldwide, relative to progress in the 47th percentile among non-oil economies in the region.

So my point is that we need to consider oil and as one of the issues which we can not leave as a back burner issue. It is deeply important in understanding why reform in this region has been stop and go.

Coalitions

But a second factor behind MENA’s weak reforms has been the lack of coalitions emerging to press the government for deeper reforms and better policy choices.

One of the perhaps encouraging lessons that have emerged from recent research on reform and growth5 has been that countries do not have to simultaneously attack all aspects of the reform process to get the ball rolling, in terms of growth. Relatively minor reforms can have enormous impact on growth. Some might say they function as sparks on growth. But they also function as sparks on the reform effort. And worldwide, the countries which have sustained and mobilized the reform effort have been able to take these few sparks of reform and make them grow into economic transformations.

The question is how? And in my mind, the answer has been coalitions for change. Structural reform depends on both a perceived need for change, and an ability for alliances to develop who can press for those changes. These coalitions

for change can emerge from many different places. The private sector can come together and press for changes to enhance profits. Or they may emerge from labor unions. Or from consumers.

When you look at these traditional advocates for reform, they are not present in MENA. The private sector is greatly underdeveloped. Private sector activity is concentrated in a small number of large firms that have benefited from protective policies, along with a number of micro-enterprises, which account for much of employment but have little access to formal finance, markets, or government support programs. Large scale industries do not press for change because they benefit from the status quo, manipulating government policy for their own gain – the so called “state capture” of government regulation. It ranges from persistent awarding of large public sector contracts to few well-connected groups, to actual change in laws and regulations that lower the costs or increase the profitability of such groups.\footnote{World Bank, 2003b.}

Trade unions, which could also be an effective vehicle for change, are tightly controlled in MENA and without real independence from the political system. As a result, they have not been effective in organizing the labor force to press for reforms.

More generally, the problem of lack of coalitions for change in MENA is not the underdevelopment of the private sector or the lack of independent trade unions. There are innumerable other groups which could press for reforms. But the greater problem, in my mind, is that the governance systems and institutions in the MENA region hinder the ability for most groups to effective unite for change.
In order for groups – be they the private sector, trade unions, civil society, communities, anyone interested and affected by development: in other words, anyone – in order for these groups to effectively unite and lobby for change, they need certain central rights. They need access to information to formulate choices, they need the ability to mobilize, they need the ability to contest policies that are poor.

But these rights are not present in the MENA region. Government information is not accessible by the public. Freedom of the press is carefully monitored and circumscribed in most countries. There are restrictions on civil society. There are restrictions on freedom of association. And the ability to contest government policies is weak.

These fundamental governance weaknesses prevent people from uniting and pressing for change. Before the 1990s, development practitioners firmly believed that governments were the drivers of growth and reform. But the experiences of the 1990s have taught us that growth and reform does not emerge simply from the top down, but as importantly from the bottom up. Coalitions that support change are the tinder in the reform effort – you can light a spark – remove tariffs, reform the budget, change a law -- but unless there is something to fuel that spark, it will go out. And this is what we have seen happen too often in the MENA region.

So I think the major point I would like to make is that addressing the governance weaknesses in MENA is really fundamental to achieving deeper reform. Twenty years ago, we believed if you just limited government discretion, if you tied the hands of governments to implement the “right” policies, the
economy would respond. One of the major lessons we take from the growth experiences of the 1990s is that it is the organization of policy making which matters. The background institutions that support the findings of fact, the coalitions which demand the findings of fact, the ability for groups to evaluate fact and change policy – these are what make policy reforms ignite a growth response.

The fundamental governance challenge is to strengthen the incentives, mechanisms, and capacities for more accountable and inclusive public institutions and to expand allegiance to equality and participation throughout society. Those good governance mechanisms are first steps in improving economic policies that are themselves instruments for improving the climate and incentives for efficient growth. Economic reform cannot proceed without reform of the incentive structure in which reforms are embedded.

Enhancing inclusiveness requires adopting laws and regulations that secure access to widely accepted basic rights and freedoms, including participation and equality before the law. Broader public consultation, greater freedom for the media, fewer restrictions on civil society, more equitable channels of access to social services, and an end to discriminatory laws and regulations are examples of measures that secure inclusion.

Enhancing accountability requires putting in place better systems of transparency and contestability, including greater freedom of information and public disclosure of government operations, wider public debate by an independent media and civil society groups, and regular and competitive elections. It involves strengthening the checks and balances within the government. It involves reforming public administration.
Early in the reform process and beginning in the 1980s, many of MENA countries accepted an instrumental connection between economic and political reform. Governments recognized that they needed to secure popular support for market-oriented economic reforms, and so several countries initiated experiments in political reform, including increased the opportunities for participation by opposition political parties, expanded civil liberties and freedom of the press, and increased participation in the political life by civil-society groups.

But these political openings have largely been reversed, as MENA governments have sought to contain and manage the scope of political change. Constraints on civil society and NGOs, restrictions on the press, and other measures have restricted mobilization and autonomous collective action. As a result, MENA governments have also seriously restricted the range of reforms that could be implemented. Reforms have been limited to those that could be implemented through top-down management, rather than those that would require the compliance and participation of social groups whose well-being might be adversely affected by reforms.

For the region to move forward with economic reforms, and for the region to realize the benefits from reform, the space for greater public participation in reform needs to be opened. Greater voice in development is not only needed to take into account the needs and values of those who have been excluded from the MENA development model. It is equally important to ensure that in the transition to a new development model, the economic outcomes are socially acceptable among those who have benefited from the old development model.
The governance agenda in MENA is large. But without reforming the governance structure – the organization of policy making – the process by which economic reforms can become self-perpetuating cannot occur. The international experience with reform tells us that were reforms were successful, they were seized upon and developed. One reform led to another and to another. One success led to another. Improvement upon improvement upon improvement. This is how economies are transformed.

Thank you.