World Development Vol. 66, pp. 532–556, 2015
0305-750X/© 2014 Elsevier Ltd. All rights reserved.
www.elsevier.com/locate/worlddev
http://dx.doi.org/10.1016/j.worlddev.2014.09.011

Economic Inequality in the Arab Region

NADIA BELHAJ HASSINE*
World Bank, Washington, USA

Summary. — The paper assesses the levels and determinants of economic inequality in 12 Arab countries using harmonized household survey micro-data. It focuses on the sources of rural–urban, as well as metropolitan–nonmetropolitan, inequalities.
The analysis finds moderate inequality levels, with Gini coefficient for the distribution of per capita total expenditures ranging between 30.7 in Libya and 45 in Mauritania. Differences in households' endowments such as demographic composition, human capital, and community characteristics appear as the main sources of the urban–rural welfare gap. Inequality between metropolitan and non-metropolitan regions is resulting mainly from differences in returns to human capital.

Key words — inequality, unconditional quantile regression decomposition, Arab countries

1. INTRODUCTION

Deteriorating standards of living, high and rising unemployment, and growing perceptions of exclusion were among the many reasons that prompted the Arab streets to rise in early 2011 and demand, inter alia, a new model of economic, political, and social participation and development.

Following their independence, most Arab countries adopted a state-led economic development model characterized by heavy reliance on state planning and public sector investment. Initially, and until the late 1980s, investments in infrastructure and public education, government employment, land reforms, and redistribution of assets have led to remarkable improvements in human development indicators and a moderate incidence of poverty and income inequality (Page, 2007; World Bank, 1995).

However, and beginning in mid-1990s, as basic education and land ownership began to lose their importance in determining economic status, and as the public sector became bloated, these gains started to unravel ushering in different forms of rising inequality (Bibi & Nabli, 2009). Indeed, disparities among socioeconomic groups and along urban–rural and regional lines have widened. Other forms of inequality such as inequality of opportunity in economic and non-economic dimensions have emerged also as serious concerns in the region (Assaad, Kraft, Belhaj Hassine, & Salehi-Isfahani, 2012; Belhaj Hassine, 2011).

The social and political unrest sweeping the Arab world has led to a further deterioration in the economic and social situation and fueled perceptions of declining welfare of average citizens and rising inequality (AfDB, 2012). Understanding the factors that are driving economic inequality in the Arab countries is a critical issue, not just for equity and economic inclusion reasons, but also for political reasons. Even though the roots of the popular discontent go further than the economic factors and inequality, they are inextricably entwined and further exacerbate the tensions (Nel, 2008).

This paper aims to contribute to this understanding by examining the extent and evolution of economic inequality and exploring the critical factors underlying distributional patterns in 12 Arab countries.

Inequality is no longer considered as an ineluctable precondition for growth, but rather as an obstacle to both economic growth and its poverty-reducing potential (Bourguignon, 2003; Ravallion, 1997, 2001). Despite the underlying complexity of the relationship between inequality and growth and the existence of some inconclusive evidence on the sign and direction of this relationship, empirical research generally confirms that inequality tends to undermine economic growth and poverty alleviation efforts in developing and poor countries (Barro, 2000; Chambers & Krause, 2010; Kanbur, 2013). The welfare costs of inequality are likely to be even higher in relation to inter-group inequalities which lead to inter-generational transmissions of inequities and self-perpetuation of poverty, stocking social tensions and conflicts (Kabeer, 2010; Stewart & Langer, 2007).

Regional inequalities and rural–urban divide, in particular, may exacerbate the social and economic instability that pervade the Arab world, and could undermine popular support for transition reforms. Lagging regions might perceive inequality as the unfair consequence of biased regional development strategies and structural adjustment policies, and could resist further reforms toward market-oriented and private sector-led economies, obstructing the process of economic development.

Analysis of the extent of economic inequality and the determinants of regional disparities is of high importance for informing policy discussions as the countries are preparing their shift away from a state-led economic system. This is particularly salient in light of the dearth of studies on inequality in the Arab region.

Lack of accessible household surveys and problems in the quality and comparability of data have hitherto prevented empirical analysis of economic inequality in the region. Cross-country studies and analysis of trends in inequality within countries are further hampered by difficulties related to the choice of the welfare indicator to be used for the measurement of inequality. Using welfare measures based on consumption expenditures is not enough to ensure comparability, as differences in the comprehensiveness of the consumption

* The author thanks Arun Agrawal and two anonymous referees for insightful and helpful comments and suggestions. The assistance of Christian Wissa forhousehold surveysharmonization and helpful discussions with Raed Safadi are also acknowledged. Final revision accepted: September 21, 2014.

bundle may be misleadingly attributed to differences in the distribution of welfare.

This paper attempts to address these issues and fill some of the knowledge gaps by examining the levels and determinants of inequality in the distribution of household consumption expenditures. It draws on harmonized micro-data from twenty eight household surveys for 12 Arab countries and combines a descriptive analysis of inequality with an empirical investigation of the sources of within-country regional disparities. The first examines the levels and recent trends in inequality using comparable welfare measures and explores how alternative definitions of consumption expenditures affect the extent of inequality. It also examines the structure of inequality as it relates to the nature of the households within these countries.

The second uses the Recentered Influence Function (RIF) regression approach proposed by Firpo, Fortin, Lemieux (2009) to examine the sources of urban–rural, and metropolitan–nonmetropolitan, inequalities. More specifically, it explores how the differences in the distributions of household characteristics and in the returns to these characteristics contribute to inequality across locations. This could shed some light on the role of development policies and structural reforms in shaping the patterns of regional inequality within Arab countries.

To the best of our knowledge, this is the first paper that provides detailed analysis of economic inequality in a large panel of Arab countries, including within-countries analysis of regional inequalities, and doing so on the basis of harmonized household survey micro-data.

Our analysis reveals moderate levels of inequality in consumption expenditures with Gini coefficients varying from a low of 32 and less in Egypt and Libya to a high of 40 and over in Mauritania, Tunisia, and Yemen. These findings are consistent with earlier studies which show a moderate incidence of inequality in the region (Adams & Page, 2003; Deininger & Squire, 1996). Inequality appears to have persisted in most countries and increased in Mauritania, Syria, and Yemen by the mid of the last decade. Analysis of the structure of inequality indicates that the family type, the geographical location of the household, and, to a lesser extent, the level of education of the head are the most important determinants of overall economic inequality.

The differences in living standards between urban and rural areas appear to be mainly driven by the better endowment of urban households of marketable characteristics compared to their rural counterparts. On the other hand, the difference in many countries between metropolitan and non-metropolitan distributions appears to be the result of higher returns to household attributes in metropolitan regions.

These results suggest an urban and metropolitan bias in many Arab government development policies which led to growing welfare inequalities along rural–urban and regional lines. Furthermore, the lack of employment opportunities and agglomeration economies in non-metropolitan areas may have led to lower returns to human capital investments than in metropolitan areas.

Promoting more market-oriented policies and private sector development to enhance job creation and reinvigorate the national economies may benefit Arab citizens differentially according to their human capital endowments, and could translate into larger regional differences in returns, and higher inequality. The liberalization policies implemented in the context of the structural adjustment programs pursued by many countries during the 1980s and 1990s do not appear to have facilitated resource flows and equalization of returns across regions. Further reforms may aggravate inequality if the obstacles to balanced regional development are not well identified and addressed. In these challenging times, the Arab countries have a unique opportunity to embark on a comprehensive strategy of economic restructuring and to undertake reforms premised on broader inclusion and more equitable development.

The rest of the paper is organized as follows: Section 2 briefly discusses Arab countries' development experience and compares the region with international evidence on growth, employment, poverty, and inequality. Section 3 provides an overview of the literature focusing on the main findings of the recent research and the specific studies on inequality in the Arab region. Section 4 presents the data and reports the inequality and static inequality decomposition results. Section 5 analyzes the sources of urban–rural and interregional inequality. Section 6 concludes.

2. A BRIEF OVERVIEW OF THE DEVELOPMENT INDICATORS IN THE ARAB REGION

Poverty and inequality levels in the Arab countries began to improve in a dramatic way, albeit from low levels, following these countries' independence in the 1950s, and this trend continued unabated until the mid-1990s (AfDB, 2012). By the end of the 1990s and onward, and despite a deceleration in the rate of improvement in inequality and poverty, their levels compared favorably with all other developing regions, save in the case of Europe and Central Asia (Table 1). [1] This achievement took place despite the fact that growth in the Arab region lagged behind that in all the other developing countries' regions over the past two decades. This was also the case at the country level, except in the case of Yemen. As is evident from the data reported in Table 1, economic growth in Egypt, Tunisia, and Jordan was higher than the region's average level and was accompanied with a decrease in poverty and inequality; however, these are the very economies that have been suffering from the highest youth unemployment rates in the developing world.

Studies show that the success of these countries in achieving low poverty and broadly equitable growth owes a great deal to the post-independence development model that was adopted across the Arab region. This model included heavy reliance on state planning, import substitution policies, nationalization of private and foreign assets, and a social contract where the state provided education, housing, health care, and food subsidies. Rising oil prices, intra-regional flows of capital and labor, and workers' remittances fueled these expenditures (Adams & Page, 2003; Bibi & Nabli, 2009). Thus, for many years the region's economies were sustained by high dependency upon economic rents which contributed to introducing inefficiency and distortions throughout the economy, undermining productivity and sustainable growth.

Declining oil prices since the mid-1980s and until the early 2000s exacted a heavy toll on social expenditures, with commensurate deterioration on both the poverty and inequality fronts. Despite the recovery in oil prices during the early 2000s and the accompanying pick-up in economic growth in most of the countries in the region, the state-led economic model began to feel the burden of its weight: a bloated public sector with declining real wages and productivity combined with obstacles to migration that reduced employment opportunities for the rapidly expanding labor force.

The progressive liberalization and privatization reforms adopted by many countries in the late 1980s as part of the