SOLiD

SOUTH MED SOCIAL DIALOGUE

Fiscal Policy, Price Levels, and Wages in Selected Arab Countries

(Morocco, Tunisia, Jordan, Algeria, Lebanon, & Palestine)

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CONTENTS

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EXECUTIVE SUMMARY

This report aims to infer government interventions that contribute to overcoming chronic and more recent challenges and crises. It focuses on financial policies and actions adopted by some Arab countries (especially Morocco, Tunisia, Jordan, Algeria, Lebanon, and Palestine) to drive the financial policy toward achieving the state's economic goals and sustainable development. This report's significance stems from its focus on issues that concern Arab citizens and directly impact their daily lives. Such matters require that countries work to reform and develop their financial policies, using various tools that help achieve economic growth and paying attention to all segments of society, especially the poor and marginalized groups. Finally, this report utilizes a descriptive, analytical, and deductive approach, reviewing and comparing relevant data and analysis from the selected countries.

The Report's main Conclusions are the Following:

1- There are many commonalities in fiscal policy in the six countries covered in the report, with their focus on stimulating economic growth and improving the standard of living. However, the countries differ in their methods of fiscal policy implementation. For example, some countries impose income and sales taxes to finance public spending. In contrast, others rely on external borrowing (such as Tunisia).

2- These countries face common challenges, such as increasing public debt, inflation, and rising energy and food prices. Some countries face unique challenges, such as outbreaks of epidemics and internal conflicts.

3- The six countries are similar in the composition of their public revenues. They often rely on several revenue generation sources. However, taxes remain the primary source of generating public revenues in these countries. Tax revenues constitute a significant portion of public revenues and grants in all six countries. They exceed two-thirds of revenues in five countries (Morocco, Tunisia, Lebanon, Jordan, and Palestine) while constituting about 40% in Algeria.

In 2021, non-tax revenues comprised about 11.7% of the total revenues for the selected Arab countries combined. However, their composition varies by country and highly depends on their particular economy and vital sectors.

4- Some countries receive international aid from donor countries and international organizations. This aid is an essential source of public revenues and financing vital projects in some countries. However, this aid has been decreasing (as a percentage of public revenues) year after year; it decreased from about 17% in 2017 to about 7% in 2021. In Jordan, it decreased slightly from about 8% in 2017 to 7.6% in 2021.

5- Current spending makes up most of the public expenditures of the Arab countries combined. Between 2017 and 2021, it increased from 80.3% to 86.1%, while capital spending decreased during the same period from 19.7% in 2017 to 13.9% in 2021. The high rate of current expenditures indicates the weakness of fiscal policy and its low economic impact.

6- Between 2017 and 2021, the six countries suffered from a budget deficit. However, its value and share of GDP varied. In 2021, the highest deficit was recorded in Lebanon, reaching 18.4%, followed by 12.4% in Algeria, then 7.5% in Tunisia. The other three countries (Jordan, Palestine, and Morocco) were close, with a share between 5.2 and 5.5%.

7- The total public debt increased in the six countries. The most significant increase was in Lebanon, which faces a stifling economic crisis and a sharp deterioration in the value of the currency and the standard of living. Public debt exceeded the GDP in Jordan, Tunisia, and Lebanon. It comprised about 90% of the GDP in Morocco, about 57% in Algeria, and about a fifth of the GDP in Palestine.

8- Inflation increased globally, including in Arab countries, for various reasons, including oil price fluctuations, climate change, and geopolitical factors such as the Ukrainian-Russian crisis. Arab countries were significantly impacted, especially regarding food security and tourism, especially in Tunisia and Morocco. The Covid-19 crisis had a significant impact on supply chains and transportation. The recovery from the pandemic also led to higher inflation rates due to increasing consumer demand. The matter has also become more complicated in Arab countries concerning food security, fiscal space, and the local currency exchange rate.

9- Wages in Arab countries did not react to the significant rise in inflation; they "crawl" as inflation rates "run." In the past few months, demonstrations denouncing high prices were on the rise in many Arab and non-Arab countries, in which protesters demanded the improvement of wages, which had stagnated for years amid a significant increase in the cost of living, especially the rise in the price of basic materials. In 2022, wages in Arab countries witnessed a slight increase of 1.2%, compared to 0.5% in 2021 and 0.8% in 2020. In Morocco, wages decreased by 2.6% in 2020, while they increased slightly in Jordan by 0.1% in 2020.

The Main Reform Proposals are as Follows:

Fiscal Policy: The target countries must start improving tax justice. This process requires changing the budget style from budgeting items to budgeting programs and performance; applying strict rules to combat all forms of corruption and tax evasion in tax departments; placing more emphasis on collecting direct tax revenues (income and wealth) instead of indirect taxes (consumption taxes); redesigning tax incentives to target not only significant investments, but also small and medium-sized companies, which represent more than 95% of businesses in these countries; reconsidering the current tax base to include non-traditional and unproductive activities such as real estate deals and speculation in financial markets; expanding the circle of community participation, and prioritizing dialogue and discussion with social groups affected by the tax law.

Limited Fiancial Resources: The efficiency of public spending must be improved, which requires restructuring government spending by reallocating more resources to public investments, reconsidering the share of wages in total spending (which is very high), and increasing financial resources allocated to social security and service programs that benefit the poor, reducing or rationalizing government spending on weapons and security, and directing any financial surpluses to social services and economic empowerment.

The permanent deficit and continuing high public debt could be avoided by focusing on providing non-traditional financial tools to finance the development process, programs, and projects, automatically reducing countries' need to borrow from within or abroad. This group includes several innovative financing tools that are not sufficiently implemented in the Arab countries, mainly in terms of converting debt into an ownership instrument in what is known as debt-to-equity swaps, securitization, Islamic bonds (sukuk), activating partnerships between the private and public sectors, and diaspora bonds.

Prices and Inflation: Monetary policy effectiveness to combat inflation cannot coexist with high public debt. Governments must work on activating monetary policies to avoid the spiral of rising prices and rising wages. Banks must increase communication with all sectors to establish more flexible economic expectations and improve understanding of monetary policy tools.

Wages and the Labor Market: Salaries and wages can be improved by improving the business environment and increasing productivity, companies' commitment to governance principles, strengthening the role of labor organizations and providing them support and encouragement from governments and civil society, setting a minimum wage, improving the social welfare structure, applying fair taxes that protect the poor and middle classes and reduce social inequality, focusing on employing youth and providing them with job opportunities, and promoting social dialogue and consultation with labor organizations, workers, employers, and civil society.

1. INTRODUCTION

In the past three years, the world has witnessed severe developments and shocks that have contributed to structural changes in the economies of many countries worldwide. The first shock was the repercussions of COVID-19 in various economic, social, and even political aspects. No sooner had the world recovered from the consequences of the pandemic than Russian military operations began in Ukraine. This time, the effects impacted the economic sectors, financial markets, and various vulnerable and marginalized social groups. The main impact of the war was the wild rise in prices of essential commodities (food and energy), the significant effect on the flow of goods, and the decline in international trade.

The combined repercussions of the pandemic and war led to profound economic and social crises in various countries. They included the major shortage in energy and food supplies, the significant and successive rise in prices, the exit of many small and medium enterprises from the market, and millions of people losing their jobs. Successive price increases were not accompanied by increased wages, which caused a gap between wages and prices.

Therefore, **price** levels must be looked at continuously and carefully, and economic, monetary, and financial policies must be developed to achieve economic sustainability, sustainable growth, and future prosperity for all[1]. On the other hand, **wages** are one of the most critical economic issues facing different societies worldwide. They play a significant role in determining the standard of living for workers and directly affect the economy in general. The numbers indicate a considerable variation in wage levels between countries and within each country, reflecting differences in economic growth, human development, and local conditions[2].

To better control price levels, many countries rely on monetary and fiscal policies to control supply and demand for products and services and reduce inflation rates. These policies include reducing interest rates on loans and deposits, regulating government spending and investments, stimulating economic productivity and innovation, encouraging foreign direct investment, and improving the investment climate. The effectiveness of these policies varies between countries and depends on local and global conditions and economic challenges.[3]

These gaps demanded vital interventions from governments and decision-makers. The interventions mainly included increasing public spending, especially for affected and marginalized groups. The intensity, tools, and effectiveness of interventions varied between countries, depending on their capabilities and orientations. Interventions in developed countries were a significant factor in reducing the repercussions of successive crises. It was mainly limited to increasing support for affected groups (expansionary financial policy) and using contractionary monetary policy to reduce inflation. Such interventions seem logical in developed economies capable of dealing with crises using traditional tools. However, even in developed countries where the applied procedures and measures did not convince social actors and forces, they could express their opinions and exert significant pressure on governments to improve the conditions for negotiation. This ability is one of the most prominent advantages of societies in these countries.

On the other hand, there have been attempts and measures to mitigate the severity of crises and their repercussions in developing countries and weak economies. However, the main factors determining the form, unity, and effectiveness of these measures remain the economy's weakness, the chronic structural imbalances in its productive sectors, and its reflection on the lack of financial resources available to finance spending and interventions. They are accompanied by weak community participation and marginalization of the role of civil society in formulating public policies.

Fiscal policy is one of the most essential tools for achieving economic stability and development in countries[4]. It includes many tools that directly affect the economy, such as determining the level of taxes and government spending and setting interest rates, which control economic activity to direct it in a particular direction[5]. Through these tools, fiscal policy is crucial in reducing economic deterioration, inflation, and unemployment, providing job opportunities, and encouraging investment. Furthermore, fiscal policy is an essential tool for improving wealth distribution in societies, as it uses taxes and government spending to achieve social balance and reduce the gap between the rich and the poor. It is a means to achieve financial stability and economic growth and enhance competitiveness. Fiscal policy depends on managing financial resources and directing them toward specific economic and social priorities[6].

The importance of fiscal policy is increasing in developing countries as they suffer from significant challenges to economic growth, sustainable development, providing job opportunities, and improving living standards. Developing countries face immense challenges in implementing successful financial policies due to the lack of experience and efficiency in financial management and the weak economic and financial infrastructure. Therefore, developing countries must adopt appropriate financial policies, provide the necessary support and training for financial departments, and develop the economic and financial infrastructure. Fiscal policy in developing countries also requires greater attention to the international financing dossier and its related aspects. Foreign aid, financial aid, and global financing are provided to enhance fiscal policy as an essential component of budget financing and financial policies in developing countries.

In conclusion, wage levels are vital issues in economic and social dialogue. They require greater attention, focus, and joint action to achieve appropriate wage levels, improve working conditions, and achieve sustainable economic and social development[7]. Countries use their available economic tools to address imbalances and gaps resulting from shocks. Fiscal policy is the most prominent of these tools. Judging the efficiency of the measures taken depends on the incubating environment and the results achieved.

The SOLID project sought to create a suitable environment for achieving national economic agreements and promoting social dialogue in the countries on the southern shore of the Mediterranean. At the time, the project sought to provide employers, workers, and civil society organizations (CSOs) in the targeted countries with the necessary expertise and to enhance the capacity for dialogue (social and community) of the different target groups. As the SOLID project entered its second phase with the addition of three countries (Algeria, Lebanon, and Palestine), the project participants renewed the necessity of strengthening the capabilities of activities and organizations participating in social dialogue, adapting the dialogue charter to national contexts, and developing action plans for each targeted country.

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[5] International Monetary Fund. (2020). Fiscal policy for the COVID-19 era. Retrieved from https://www.imf.org/en/Publications/fiscal-monitor/issues/30/09/2020/october-2020-fiscal-monitor.
[6] World Bank. (2018). Fiscal policy for growth and development. Retrieved from https://openknowledge.worldbank.org/handle/29687/10986.
[7] International Labor Organization. (2020). Future of work. https://www.ilo.org/global/topics/future-of-work/lang--en/index.htm

This report was developed in the context of the project's General Secretariat's directives to explore the risks and crises that threaten the economies of the countries participating in the project. It diagnoses the reality and capabilities of countries to intervene and develop necessary policies to deal with the repercussions of the crisis, focusing on community dialogue and expanding participation in identifying risks and prioritizing treatments.

1.1 Report Goals

This report aims to infer government interventions that contribute to overcoming chronic and more recent challenges and crises. It focuses on financial policies and actions adopted by some Arab countries (especially Morocco, Tunisia, Jordan, Algeria, Lebanon, and Palestine) to drive the financial policy toward achieving the state's economic goals and sustainable development. This report attempted to answer the following questions:

1- What are the most prominent features of fiscal policy in the countries mentioned in the report? What are the commonalities between them?

2- To what extent does fiscal policy contribute to achieving economic growth and take into account social aspects?

3- What programs do these countries adopt to support goods?

4- What is the wage structure in these countries?

5- What are the most prominent reforms proposed to activate financial policy in these countries?

1.2 The Report's Relevance and Motivations

This report's significance stems from its focus on issues that concern Arab citizens and directly impact their daily lives. Such matters require that countries work to reform and develop their financial policies, using various tools that help achieve economic growth and paying attention to all segments of society, especially the poor and marginalized groups. Finally, this report utilizes a descriptive, analytical, and deductive approach, reviewing and comparing relevant data and analysis from the selected countries. The report's added significance is in exposing societal dialogue as a major requirement for development and addressing crises through formulating and implementing public policies, serving social stability and sustainable development.

1.3 Report Methodology

This report utilizes a descriptive, analytical, and deductive approach by reviewing and comparing relevant data and analysis from the selected countries.

2. Diagnosis and Analysis of Public Financial Policy in the Past Five Years

2.1 Overview

In general, fiscal policies in the six countries covered in the report have much in common in their focus on stimulating economic growth and improving the standard of living. These countries use multiple tools to achieve these goals, such as public spending on infrastructure and public services, stimulating private investment, improving the business climate, and enhancing competitiveness.

However, the countries differ in their methods of implementing fiscal policies. For example, some countries impose income and sales taxes to finance public spending, while others rely on external borrowing. Moreover, tax rates vary widely between these countries. For example, Tunisia and Lebanon impose high taxes on personal income, while lower taxes apply in Jordan and Palestine. Taxes on consumption, such as value-added tax (VAT) or sales tax, are the most common in these countries. Some countries use strict monetary policies to reduce inflation, while others follow more lenient ones. However, all these countries strive to improve their economies, achieve sustainable development, and provide job opportunities for their citizens. Their achievement requires cooperation and coordination between these countries and working to find standard solutions to the economic and financial challenges they face. It also requires implementing wise and effective financial policies to improve their economic and financial situation and achieve economic stability that benefits society as a whole.

These countries also face common challenges, such as increasing public debt, inflation, and rising prices of energy and food commodities. Some countries face unique challenges, such as outbreaks of epidemics and internal conflicts.

2.2 Size and Structure of Public Revenues and Their Development Trends

The six countries are similar in the composition of their public revenues, often relying on several sources to generate income, mainly:[8]

Taxes: Taxes are the primary source of public revenue in these countries. Tax revenue exceeds three-quarters of public revenue in 4 countries: Palestine, Morocco, Algeria, and Lebanon. It reaches 65% in Tunisia, where about 15% of revenues come from incidental revenues and special funds, and about 53% in Jordan, where other revenues constitute about 33% (including property income, sales of goods and services, and various other types). Tax rates vary between these countries, but value-added tax (VAT) is the most common. Some countries also impose taxes on personal and corporate income, inheritance and gifts, and public spending. There is a fundamental problem with relying on indirect taxes (blind taxes), as they are imposed on the final consumer. Thus, the tax burden falls on consumers (citizens), regardless of their social and economic circumstances, which means that tax evaders are the ultimate beneficiaries.[9]

Customs and Fees: These countries rely on import and export customs and service fees to generate public revenues, constituting about 7% of the revenues in Palestine, Tunisia, Algeria, and Morocco. The rate decreases in Lebanon to 5% and 3.4%. The prices of these customs and fees vary between these countries. They are greatly affected by international trade agreements and global economic conditions.

International Aid: Some countries receive international aid from donor countries and international organizations, which are essential sources for generating public revenues and financing vital projects in some countries. However, international aid has decreased (as a percentage of public revenues) year after year. In Palestine, it dropped from about 17% in 2017 to about 7% in 2021, and in Jordan, it decreased slightly from about 8% in 2017 to about 7.6% in 2021.

Oil and Gas Sector: It is one of the most important sources of public revenue in countries like Algeria and Morocco. These countries depend on oil and gas exports to generate public revenues and finance their economic activities.

Tourism Sector: Tourism is another essential source of public revenue, especially in Tunisia, Lebanon, Jordan, and Palestine. These countries have many famous and diverse tourist sites that attract visitors from all over the world and contribute significantly to improving the local economy and increasing public revenues.

Industrial Sector: The industrial sector contributes significantly to public revenues in some countries like Morocco, Tunisia, and Lebanon. It includes textile industries, food industries, chemicals, electronics, machinery, metallurgy, and petrochemicals.

There are various sources for generating public revenues in these countries. However, they vary between the countries and depend on factors such as the national economy, economic policy, and international and regional circumstances. In recent decades, some Arab countries, such as Lebanon, have been exposed to economic and financial crises due to internal and external challenges affecting their ability to generate public revenues and finance their vital activities. Public revenue generation and strengthening of the local economy could be enhanced by implementing comprehensive economic, financial, and political reforms to improve the business environment, encourage investment, and improve economic performance. These reforms include liberalizing the economy, promoting free trade, improving infrastructure, developing the private sector, improving financial institutions, enhancing governance, combating corruption, and advancing the legislative and administrative process.

On the other hand, public revenues witnessed continuous growth in Tunisia, Morocco, and Algeria, compared to their fluctuation in Palestine, Lebanon, and Jordan, countries impacted by the surrounding circumstances and political developments.

Financial data in these countries indicates that taxes are the primary source of public revenues. Thus, these countries need to improve the tax system and diversify the sources of public revenues to achieve economic growth and improve the general living conditions of the population. This analysis also shows the commonalities between these countries regarding the composition of public revenues and the challenges they face in improving the tax system and diversifying revenue sources.

1.2.2 Tax Revenues

Table 1 shows the tax revenues in the six countries under study. It indicates that:

- Tax revenues constitute the most considerable portion of public revenues and grants in all six countries. They exceed two-thirds of revenues in five countries (Morocco, Tunisia, Lebanon, Jordan, and Palestine) and reach 40% in Algeria. The high share of these taxes from revenues and GDP violates the basis of tax adequacy, as the tax burden is less than the potential tax capacity of these countries' economies.[10]

- There was a noticeable increase in the value of tax revenues in 2021 compared to 2020 in five countries: Morocco, Tunisia, Algeria, Jordan, and Palestine. The highest percentage of increase was in Palestine, 26.6%, because of the improved tax collection following the start of economic recovery in 2021, compared to the slow growth witnessed in 2020 due to the COVID-19 pandemic. Lebanon was the only country where tax revenues decreased by -0.4%, although its share of the GDP had doubled. In 2021, Lebanon witnessed many challenges that seriously impacted government revenue collections. They included tax evasion and a continued decline in economic activity by about 11% in 2021 compared to a drop of about 21.4 percent in 2020.

- Furthermore, the deterioration of the exchange rate of the Lebanese pound against the US dollar led to higher inflation rates. In Morocco, the percentage of tax revenue from the GDP increased considerably, jumping from 2.1% [in 2020] to 18.9% [in 2021]. The rise was due to the increase in tax revenue collection by 8.8% between the two years mentioned above, as tax revenue represents 87.6% of total government revenue.

- The percentage of tax revenues from the total public revenues and grants of the six Arab countries combined increased and reached about %37[11].

- The large amount of tax revenue raises an essential question about the services these countries provide to citizens, who are the primary sources of revenue. The composition of tax revenues in the six countries varies from one country to another, as shown in **Table 2**. These revenues depend on the nature of economic activities and tax systems, which vary between these countries. This difference is also evident compared to the components of tax revenues in the Arab countries combined. While 37.1% are imposed on goods and services, 21.2% are customs duties on foreign trade, 18.5% are taxes on income and profits, and 23.2% are other taxes and fees.

Table 1: Tax revenues in Morocco, Tunisia, Algeria, Lebanon, Jordan, and Palestine (2021-2020)

COUNTRY	2020	2021	PERCENTAGE	SHARE OF TOTAL PUBLIC REVENUES AND GRANTS		SHARE OF THE GDP	
				2020	2021	2020	2021
Jordan	6,994	7,756	10.9	70.6	67.5	16.0	17.1
Tunisia	9,657	11,045	14.4	89,0	89,5	22,7	23,5
Algeria	17,077	19,422	13.7	39.1	41.4	11.8	12.3
Palestine	3,137	3,973	26.6	79.7	87.3	20.2	22.0
Lebanon	6,948	6,918	-0.4	68.3	75.0	28.2	47.7
Morocco	23,088	25,120	8.8	88.6	87.6	2.1	18.9

Source: Arab Monetary Fund (2022), Joint Arab Economic Report 2022, Abu Dhabi, UAE

Table 2: Percentage distribution of tax revenues in Morocco, Tunisia, Algeria, Lebanon, Jordan, and Palestine in 2021

MILLIONS OF USD

COUNTRY	INCOME & PROFITS	GOODS & SERVICES	CUSTOMES ON EXTERNAL TRADE	OTHER TAXES	TAX REVENUES
Jordan	22.8	70.1	5.9	1.2	7,756
Tunisia	30.9	42.3	8.4	18.4	11,045
Algeria	41.3	38.6	---	20.1	19,422
Palestine	5.6	16.0	72.5	5.9	3,973
Lebanon	35.6	39.0	3.3	22.0	6,918
Morocco	41.3	51.3	7.1	0.3	25,120

Source: Arab Monetary Fund (2022), Joint Arab Economic Report 2022, Abu Dhabi, UAE

[8] World Bank (2021). "Middle East & North Africa Economic Update: Building Bridges. https://www.worldbank.org/en/region/mena/publication/mena-economic-monitor-october-2021-building-bridges.
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2.2.2 Non-Tax Revenues and International Aid

In 2021, non-tax revenues comprised around 11.7% [of total revenues] for the Arab countries combined[12]. The composition of non-tax revenues in the six countries under consideration varies from one country to another. It is also highly dependent on each country's economy and vital sectors. For example, Morocco depends primarily on the agricultural, tourism, industrial, and mining industries and financial services. Insurance and communications constitute a large part of non-tax revenues. Furthermore, the Tunisian economy depends heavily on industries such as textiles, clothing, medicines, cars and electronics, and tourism. Transport and international trade also form a significant part of non-tax revenues.

On the other hand, the oil and gas sector, agriculture and manufacturing industries, and banking, insurance, and communications services make up a large portion of non-tax revenues in Algeria. Moreover, Jordan's economy relies on tourism and services, agriculture, manufacturing and mining industries, and financial and communications services. Lebanon's economy is based on financial services, trade, tourism, manufacturing industries, agriculture, and fishing, which comprise a large portion of non-tax revenues. Finally, Palestine's economy focuses on services, trade, manufacturing industries, agriculture, fishing, and mining. The tourism sector also plays a vital role in non-tax revenues. It should be noted that this composition may change with time, the development of these countries' economies, and global political, social, and economic conditions.

2.3 Volume and Structure of Public Expenditures and their Future Trends

Current spending constitutes most of the public expenditures of the Arab countries combined. It increased from 80.3% in 2017 to 86.1% in 2021. On the other hand, capital spending decreased during the same period from 19.7% in 2017 to 13.9% in 2021[13].

Public spending makes up around 31.5% of the GDP of the six Arab countries combined. However, the rates of public spending vary. It is close to the combined percentage in Jordan, Tunisia, and Palestine. It decreases slightly in Morocco, at 27.8%. However, it increases significantly in Algeria to around 42%. In Lebanon, in particular, it takes up the largest share in the Arab countries, reaching 82%.

There is also a significant disparity in the distribution of public spending in the six countries under consideration. As shown in **Table 3**, current expenditure on Lebanon and Palestine constitutes about 97%. In Jordan, it is about 90%, and in Tunisia, it is about 82%. Morocco's current spending is about three-quarters of public expenditures; in Tunisia, it is around two-thirds.

The high percentage of current spending points to the weakness of fiscal policies and their low economic impact, as increasing capital spending helps develop performance and boost economic growth. Therefore, some Arab countries have tried to apply several financial policies and measures to strengthen their financial situation. Jordan adopted policies to rationalize public spending by controlling fuel, electricity, water, and travel expenses, stopping the purchase of cars and furniture, and transferring the budgets of 29 independent government units and bodies from the Government Unit Budgets Law to the General Budget Law to control and rationalize expenses and enhance internal transparency. Specific procedures and mechanisms were adopted to reduce water sector losses. In Morocco, the regulatory law for the Public Finance Law was issued in 2015 to reform the balance sheet, implement the medium-term budget framework (three years) for government budget estimates, and rationalize spending on water, electricity, communications, transportation, and internal and external travel and enhance the efficiency of public investments.

Table 3: Percentage of current and capital expenditures in Morocco, Tunisia, Algeria, Lebanon, Jordan, and Palestine 2021-2020

MILLIONS OF USD

COUNTRY	PUBLIC EXPENDITURES		CURRENT EXPENDITURES				CAPITAL EXPENDITURES			
	2020	2021	2020		2021		2020		2021	
			VALUE	%	VALUE	%	VALUE	%	VALUE	%
Jordan	12,984	13,921	11,831	91.1	12,397	89.1	1,153	8.9	1,523	10.9
Tunisia	14,543	15,857	11,925	82.0	12,844	81.0	2,618	18.0	3,013	19.0
Algeria	62,563	66,585	40,666	65.0	42,000	63.1	21,897	35.0	24,585	36.9
Palestine	4,977	5,490	4,809	96.6	5,249	95.6	169	3.4	241	4.4
Lebanon	12,886	11,892	12,499	97.0	11,654	98.0	387	3.0	238	2.0
Morocco	35,218	36,911	26,520	75.3	29,040	78.7	8,698	24.7	7,872	21.3

Source: Arab Monetary Fund (2022), Joint Arab Economic Report 2022, Abu Dhabi, UAE

2.4 Size and Development of the Public Budget Deficit

Table 4 shows how the six countries suffered from a budget deficit between 2017 and 2021. However, there was a discrepancy in the deficit's value and its share of the GDP. In 2021, the most significant deficit percentage was in Lebanon, reaching 18.4%, followed by Algeria, 12.4%, then Tunisia, 7.5%. The remaining three countries (Jordan, Palestine, and Morocco) were close, recording 5.5-5.2%.

These Arab countries finance their deficit by borrowing from internal and external sources through short- and long-term financing instruments (bonds, treasury bills, Islamic bonds), loans, and advances. Each country balances its economic and financial policy priorities and available financing opportunities to achieve the required balance between the various sources of financing the budget deficit.

For example, in 2021, Jordan issued debt bonds and treasury bills totaling 6.6 billion Jordanian dinars. In Palestine, external grants and internal borrowing from banks are relied on. In Tunisia, total financing reached approximately 21.1 billion Tunisian dinars in 2021 (borrowing from abroad approximately 12.2 billion Tunisian dinars and from within approximately 8.1 billion Tunisian dinars).

Table (4) The value of the deficit (surplus) in the public budget in Morocco, Tunisia, Algeria, Lebanon, Jordan, and Palestine 2021-2017

MILLIONS OF USD

	2017		2018		2019		2020		2021	
COUNTRY	VALUE	% OF GDP	VALUE	% OF GDP	VALUE	% OF GDP	VALUE	% OF GDP	VALUE	% OF GDP
Jordan	-1,083	-2.6	-1,026	-2.4	-1,493	-3.4	-3,078	-7.0	-2,438	-5.4
Tunisia	-2,286	-5.4	-1,694	-4.0	-1,163	-2.8	-3,695	-8.7	-3,510	-7.5
Algeria	-9,330	-5.6	-10,884	-6.2	-8,248	-4.8	-18,858	-13.0	-19,704	-12.4
Palestine	319	2.0	172	1.1	87	0.5	-1,040	-6.7	-940	-5.2
Lebanon	-3,301	-6.2	-6,246	-11.4	-5,836	-11.0	-2,709	-11.0	-2,671	-18.4
Morocco	-4391	-4.0	-4,818	-4.1	-4,567	-3.9	-9,161	-7.6	-8,242	-5.5

Source: Arab Monetary Fund (2022), Joint Arab Economic Report 2022, Abu Dhabi, UAE

2.5 Size and Distribution of Public Debt

In recent years, radical transformations have occurred in the indebtedness of Arab countries due to their exposure to successive crises and their impact on public budgets. It began with the global financial crisis in 2008 and went through instances of instability in several countries in 2011. Furthermore, the significant decline in oil prices since 2014 led to the shrinking of the fiscal space available to the economies of oil-producing Arab countries. A decrease in tourism revenues and remittances from workers abroad to non-oil countries was also witnessed. Then, COVID-19 arrived and placed additional pressures on their budgets without exception due to the financial policies they adopted to limit the pandemic's impact. At the same time, public revenues declined due to the slowdown in growth and the decline in global demand. The rate of this debt has increased in Arab countries, including GCC countries, which are historically known as financial surplus countries. Available data varies on the size of the debt owed by Arab countries. There are estimates that it was about $1.54 trillion in 2020[14].Some reports estimated it at about $766.7 billion by the end of 2021 (about 41% being external debt)[15].

Total public debt increased in all six Arab countries. Lebanon ranked at the forefront as it faced a stifling economic crisis and a sharp deterioration in the value of the currency and the standard of living. One of the best indicators of public debt is its percentage of the GDP. However, as shown in **Table 5**, public debt exceeded the GDP value in Jordan, Tunisia, and Lebanon. It reached around 90% in Morocco, 57% in Algeria, and about one-fifth of the GDP in Palestine. Another indicator related to public debt is the burden of external debt servicing on the budget, which amounted to about $3.2 billion in Jordan and Morocco, $3.8 billion in Tunisia, $4.3 billion in Lebanon, and $261 million in Algeria.

Table (5): Public debt in Morocco, Tunisia, Algeria, Lebanon, Jordan, and Palestine in the years 2021-2020

MILLIONS OF USD

COUNTRY	INTERNAL PUBLIC DEBT		EXTERNAL PUBLIC DEBT		TOTAL PUBLIC DEBT		TOTAL PUBLIC DEBT TO GDP	
	2020	2021	2020	2021	2020	2021	2020	2021
Jordan	18,006	19,474	19,317	21,030	37,323	40,405	107.5	104.2
Tunisia	9,091	14,631	40,425	39,761	49,516	54,392	116.4	115.9
Algeria			3,466	3,800			2.4	2.4
Palestine	2,528	2,201	1,320	1,320	3,848	3,702	22	18.4
Lebanon	59,563	61,609	33,399	38,103	92,962	99,712	376.7	687.2
Morocco	66,646	75,824	39,599	42,117	106,245	117,941	92.7	88.9

Source: Arab Monetary Fund (2022), Joint Arab Economic Report 2022, Abu Dhabi, UAE

[12] Arab Monetary Fund, 2022, op. Cit.
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3. GOODS AND SERVICES PRICE LEVELS

Inflation rose in most countries, including Arab ones. The rise was brought about by several reasons, including oil price fluctuations, climate change, and geopolitical factors such as the Ukrainian-Russian crisis. It had a significant impact on the Arab countries, especially regarding food security, and hit the tourism sector, especially in Tunisia and Morocco. The COVID-19 crisis was detrimental to supply chains and restricted the freedom of transportation. The recovery from the pandemic led to higher inflation rates due to increasing consumer demand. The matter has also become more complicated in Arab countries as a result of the deficit in food security, fiscal space, and the local currency exchange rate[16].

The Arab Monetary Fund expects that 2023 will witness an increase in the inflation rate in the Arab countries as a group due to inflationary pressures resulting from global economic developments, especially energy prices (oil and gas). Other factors include pressures on local currency exchange rates in some Arab countries and other inflationary factors that differ from one Arab country to another, such as unfavorable internal conditions. After excluding the Arab countries that face pressures on the local currency exchange rates, inflation projections for Arab countries are entirely consistent with global inflation expectations. Signs of controlling the inflationary wave are expected to appear in 2023, as inflation in the Arab region is expected to reach a rate of 4.1. percent in 2023 and 3.8 percent in 2024[17].

The six countries under consideration witnessed a significant rise in food inflation rates. The most prominent increase occurred in Lebanon, reaching 441% at the end of 2021 declining to 142.9% in 2022. The country is going through an unprecedented financial crisis due to an unsustainable accumulation of debt, heavy dependence on imports (about 60%), the rapid depletion of its foreign currency reserves, and failure to pay off its sovereign debts. It also broke the thirty-year peg of its currency to the US dollar at 1507.5, leading to a significant decline in the exchange rate. On the other hand, inflation reached 11.9% in Algeria at the end of 2021 and rose to 13.3% at the end of 2022. It was 1.6% in Palestine at the end of 2021 and reached 6.9% at the end of 2022. In Tunisia, it doubled from 7.7% in 2021 to 15% in 2022. In Morocco, it rose from 4.6% to 15%. At the end of 2021, it reached 2.7% in Jordan, decreasing to 0.6% at the end of 2022. Food inflation is the biggest problem, especially in middle-income countries. Food constitutes about 60% of the consumption basket, summed up by the saying: *"We sleep hungry because of high prices."*

3.1 Consumer Goods Subsidies

The forms of government subsidies differ according to the economic conditions in each country: subsidizing food supplies, petroleum products, electricity, medicines, subsidizing water, reducing public transportation prices, providing soft loans, supporting some economic activities, such as industrial zones and farmers; tax subsidies by reducing tax obligations; cash subsidies to producers or consumers; or supporting producers through the government purchasing goods and services from their producers at high prices. MENA countries are considered to be the most subsidized globally, especially with regard to energy subsidies, which reached about 8.5% of the GDP in 2011. Subsidies witnessed a noticeable increase in Arab countries over the past decade due to the rise in the prices of many goods and services, especially imports, leading to a rise in government support and the number of goods and services it includes. More recently, however, this support decreased. Government cash subsidies in the budget, which provide food and supplies, electricity, petroleum products, housing programs, and allocations to government institutions, witnessed a significant decline between 2013 and 2016.[18]

Available data from Morocco, Jordan, and Lebanon indicate a decrease in the proportion of government cash subsidies out of total public expenditures for these countries combined, from 8.5% in 2013 to 4.6% in 2016. This drop is due to the reduction of government subsidies for imported oil products and electricity services and the slight decline in the volume of cash support for food supplies under the reform policies pursued by many of these countries. Some countries reduced their subsidies for some products. Other countries stopped the subsidies altogether. Subsidies on commodities vary from one country to another. For example, Jordan subsidizes wheat and its derivatives, rice, sugar, infant formula, and edible oil. Lebanon subsidizes housing, education, and health. Still, it does not support transportation, while in Palestine, the government provides no subsidies for social services except transportation. In practice, subsidies are often ineffective, failing to benefit the intended target group, and expensive. That is, they have adverse effects on well-being and social justice. The costs of social subsidies usually exceed the explicit or apparent cost in the public financial budget. Subsidies often lead to the overproduction of subsidized goods. Several studies have concluded that subsidy reform in the MENA region could significantly increase well-being, especially for low-income families.[19]

In 2019, the total expenditure on subsidies (cash and in-kind income support, pension systems, support for food, fuel, and electricity producers, and other spending on social protection and assistance to farmers) amounted to 5.4% of GDP. By 2022, the impact of the Russian-Ukrainian war on food and energy prices will increase subsidy bills in import-dependent countries trying to maintain existing subsidy schemes. Income support and assistance to families and children constituted 2.4% of the GDP in 2019. Retirement pension systems, especially social insurance expenditures for formal sector employees, comprised 1.8% of the GDP but amounted to more than 4% in Jordan.[20]

4. WAGE STRUCTURE IN THE LABOR MARKET

Wages in Arab countries did not react to the significant rise in inflation; they "crawl" as inflation rates "run." In the past few months, demonstrations denouncing high prices were on the rise in many Arab and non-Arab countries, in which protesters demanded the improvement of wages, which had stagnated for years amid a significant increase in the cost of living, especially the rise in the cost of basic materials. In 2022, wages in Arab countries witnessed a slight increase of 1.2%, compared to 0.5% in 2021 and 0.8% in 2020. In Morocco, wages decreased by 2.6% in 2020, while they increased slightly in Jordan by 0.1% in 2020.

The monthly wage rates show a discrepancy between the six countries. They are $837 in Lebanon, $778 in Palestine, about $600 in Jordan, $385 in Morocco, $277 in Tunisia, and about $250 in Algeria.[21] The wage structure varies based on several factors, such as the economic, service, and industrial sectors, the size of the economy, the average per capita income, and the practical laws in force in each country. Wages in Jordan, Lebanon, and Palestine are much higher than those in Morocco, Tunisia, and Algeria. Wages in Jordan, Lebanon, and Palestine are also characterized by their noticeable increase in the private sector. The services sector has the highest wage rates, followed by industry and commerce. On the other hand, wages are lower in Morocco, Tunisia, and Algeria, where the lowest rates are in the agricultural and industrial sectors.

Like other countries, the prevailing economic and social conditions in the Arab region are affected by international changes. The data indicate that inflation is the main characteristic in the countries concerned. It seems clear that wage levels in Arab countries do not correspond to extensive and continuous price increases. A gap was created between wages and prices, accompanied by a significant decline in purchasing power and levels of well-being. Government interventions were needed to address crises through various economic policies, including fiscal policy. However, the structural and chronic imbalances in the field of public finance in Arab countries have posed a severe challenge to decision-makers in using fiscal policy. Tax systems are neither efficient nor fair. They lead to high levels of tax evasion and a significant waste of financial resources. Governments' opportunities to finance their public spending are declining. As a result, high levels of fiscal deficits accumulate. Thus, financing (internal or external) becomes required to cover the deficit. The continuation of this vicious circle of action and reaction (cause and effect) contributes to thwarting ongoing attempts at advancement and development. Therefore, it is necessary to formulate a practical and effective way out of this closed circle.

5. EVALUATION OF PREVIOUS INTERVENTIONS

Various countries worldwide, including the Arab countries targeted in the report, attempted to deal with the economic crises that their societies experienced. Naturally, government interventions contributed to reducing the impact of crises and their repercussions, but to a varying extent. The remainder of this report attempts to survey the primary government interventions and efforts in confronting the economic and social consequences and gaps.

Between 2017 and 2021, interventions generally entailed providing financial and economic support to citizens, companies, and various economic sectors, including government loans, tax exemptions, cash aid, and support for health sectors. Interventions varied according to each country's circumstances and challenges.

In **Morocco**, an ambitious plan was launched to support the Moroccan economy and society worth 120 billion dirhams,[22] exempting small and medium enterprises from taxes for three months, increasing financial grants for needy families and those affected by the pandemic, supporting the health sector and providing the necessary protective equipment for health workers, and financing training and qualification programs for youth to increase employment opportunities and economic growth.[23]

Tunisia launched the Covid-19 Fund to provide financial support and relief to families impacted by the pandemic, provide tax exemptions and deferrals to affected individuals and companies, increase government spending on the health sector to provide the necessary protective equipment and deliver healthcare for those infected with Covid-19, and launch a program to provide job opportunities for youth and women affected by the pandemic.[24]

Jordan launched an economic stimulus plan worth 1.3 billion dinars to support sectors affected by the pandemic. The plan includes increasing government spending on the health sector and providing the necessary protective equipment for health workers, exempting small and medium enterprises from taxes for six months, and financing programs to train and qualify youth and increase job opportunities.[25]

Algeria launched a plan worth 1,000 billion dinars to support the economy and mitigate the economic impact of the pandemic. This plan includes exempting small and medium enterprises from taxes for three months, financing programs to support companies and encourage investments, increasing government spending on the health sector to provide the necessary protective equipment and medicines, and implementing structural reforms to improve economic performance.[26]

In Lebanon, financial support was provided for deprived families and those affected by the pandemic. Small and medium enterprises were exempted from taxes for three months. Food and basic medical materials were secured for those infected with Covid-19. Other measures included supporting companies and institutions affected by the pandemic and improving structural reforms to increase productivity and improve the investment climate.[27]

In Palestine, financial and food support was provided to families affected by the pandemic. Measures included increasing government spending on the health sector to provide the necessary protective equipment and medicines, supporting companies and institutions affected by the pandemic, securing job opportunities for young people, improving economic reforms, and implementing incentive policies to support productivity and economic growth.[28]

The results of the financial interventions governments took to confront the COVID-19 epidemic and fight inflation varied according to each country's economic, political, and social conditions. Government financial interventions may help mitigate the economic and social impacts of the pandemic and inflation. In some cases, effective government interventions contributed to improving the economic and social situation. In other cases, these interventions may have been insufficient to address the economic and social challenges of the pandemic and inflation. It is crucial to evaluate the long-term results of fiscal interventions to determine whether these measures have helped address these countries' economic and social challenges and infer whether additional measures are needed to support the economy and promote growth.

It is worth noting that some of these countries, as explained throughout the article, say that financial policies and tools suffer from a structural defect in the composition of revenues and expenditures. They already suffered from economic and financial problems before the COVID-19 epidemic, making it challenging to provide the financial interventions needed to confront the pandemic and fight inflation. Some countries also rely heavily on oil and gas exports, which means that fluctuations in oil prices may affect their economic and financial situation.

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6. MAIN CONCLUSION

1- Fiscal policies in the six countries covered in the report have much in common, focusing on stimulating economic growth and improving the standard of living. However, countries differ in their methods of implementing fiscal policies. For example, some countries impose income and sales taxes to finance public spending. In contrast, others rely on external borrowing (such as Tunisia).

2- These countries face common challenges, such as increasing public debt, inflation, and rising energy and food prices. Some countries face unique challenges, such as outbreaks of epidemics and internal conflicts.

3- Taxes are the primary source of generating public revenues in these countries. However, there is a fundamental problem with relying on indirect taxes (blind taxes), as they are imposed on the final consumers without considering their social and economic circumstances, which means that tax evaders are the ultimate beneficiaries.

4- Some countries receive international aid from donor countries and international organizations, essential for generating public revenues and financing vital projects. However, these funds have been decreasing year after year, which exacerbates the deficit in these countries.

5- Current spending comprises most of the public expenditures of the Arab countries combined. The high current spending rate indicates fiscal policy's weakness and low economic impact.

6- Between 2017 and 2021, the six countries suffered from budget deficits. To finance the deficits, they resorted to borrowing from internal and external sources, leading to the exacerbation of the total public debt in all of them. Servicing external debt increased the burden on the general budget and exposed it to financial risks.

7- The six countries witnessed a significant increase in the rate of food inflation. The most prominent example is Lebanon. This increase causes the biggest problem for these countries, as food constitutes about 60% of the consumption basket.

8- Wages in Arab countries did not react to the significant rise in inflation, leading to the spread of demonstrations denouncing the high prices, in which the protesters demanded improved wages in light of their low or stagnation for years in exchange for the significant rise in the costs of living, especially the rise in the prices of basic materials.

7. SUGGESTIONS FOR REFORMS

7.1 Fiscal Policy

- **It is essential to start improving the level of tax justice in the target countries, and this requires:**

◆ Changing the budget style from item budgeting to program and performance budgeting and integrating gender issues by adopting economic and social policies that respond to the different or differentiated needs of males and females.

◆ Implementing strict rules to combat all forms of corruption and tax evasion in tax departments.

◆ Placing greater emphasis on collecting direct tax revenues (income and wealth) rather than indirect taxes (consumption taxes).

◆ Redesigning tax incentives to target significant investments small and medium-sized companies, representing more than 95% of businesses in these countries.

◆ Reconsidering the current tax base to include non-traditional activities and non-productive, non-value-added activities that generate significant and quick profits, such as real estate deals and financial market speculations.

◆ Expanding the circle of community participation and prioritizing dialogue and discussion with social groups affected by the tax law.

- **In light of limited financial resources, the efficiency of public spending must be improved as follows:**

◆ Restructure government spending by reallocating more resources to public investments because of their positive long-term economic results and sustainable development.

◆ Reconsider the share of wages from the total spending (which is very high) by auditing this bill to exclude the payment of wages to fictitious employees, and this is called "refining the salary bill."

◆ Increase financial resources allocated to social security and service programs that benefit the poor. It is also necessary to create, design, and finance programs to generate job opportunities for youth and women and restructure support for essential goods and services to target the poor more than the rich.

◆ Government spending on weapons and security should be reduced or rationalized, and any financial surpluses should be directed to social services and economic empowerment.

- **To overcome the permanent deficit and the continuing high public debt, focus should be placed on providing non-traditional financial tools to finance the development process, its programs, and projects, which will automatically reduce the need to resort to borrowing internally or externally. This group includes several innovative financing tools that are not sufficiently implemented in Arab countries, the most important of which are:**

◆ Converting debt into an ownership instrument in what is known as debt-to-equity swaps.

◆ Securitization, which in turn represents a new financial instrument that relies on collecting a group of homogeneous debts secured as assets, placing them as a single consolidated debt, and then offering it to the public through a specialized credit institution for subscription in the form of securities.

◆ Islamic bonds (Sukuk) are based on converting a group of illiquid income-generating assets into tradable instruments secured by these assets and then selling them in the financial markets, taking into account trading controls.

◆ Activating the practice of partnership between the private and public sectors in various forms according to the nature of the development projects that the state wishes to finance (energy, roads, communications, transportation, ports, etc.).

◆ Diaspora Bonds: Expatriates are an essential source of financing for many Arab countries, and immigrant bonds can represent an effective tool in mobilizing a portion of these remittances. They are treated like long-term securities and are redeemed only upon maturity.

7.2 Prices and Inflation

1- The effectiveness of monetary policy in fighting inflation cannot coexist with high public debt. Every increase in the interest rate tightens the noose on public finances, putting the state budget under pressure from the growing public debt service, which increases the drivers of unsustainability.

2- Governments should work to activate monetary policy to move away from the cycle of rising prices and rising wages through a participatory approach with all social frameworks. High inflation increases the risk of its transmission to other sectors, generating more sustainable inflation. Wage levels must be determined in consultation and coordination with social frameworks so that the continuous rise in prices does not lead to demands for a parallel increase in wages.

3- Banks should work to increase communication with all sectors to establish more flexible economic expectations and a better understanding of monetary policy tools.

7.3 Wages and the Job Market

1- Improve salaries and wages by improving the business environment and increasing productivity, especially by developing infrastructure, enhancing technology and education, and developing the private sector.

2- Companies must commit to governance principles, which include transparency, accountability, auditing, and close monitoring of government budgets.
3- Strengthen the role of labor organizations, providing them with support and encouragement from governments and civil society.

4- Determine the minimum wage to improve the financial situation of workers in the private and public sectors. These wages should reflect the cost of living and inflation.

5- Improve the social welfare structure, including health care, education, housing, social protection, and providing appropriate job opportunities.

6- Apply fair taxes that protect the poor and middle classes and reduce social inequality.

7- Focus on employing young people and providing them with job opportunities, as they constitute a large percentage of employment in Arab countries. This can be achieved by supporting entrepreneurship, improving the business environment, and providing job opportunities in promising sectors.

8- Promote social dialogue and consultation with labor organizations, workers, employers, and civil society to help find comprehensive and effective solutions to improve wages, salaries, and social justice.

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