



COMPOUNDING CRISES

Will **COVID-19** and **Lower Oil Prices**
Lead to a New Development Paradigm
in the Arab Region?

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List of Acronyms

Eora IO	Eora Input-Output
ESCWA	Economic and Social Commission for Western Asia
FCCs	Fragile and crisis countries
GCC	Gulf Cooperation Council
GVC	Global Value Chain
IDPs	Internally displaced persons
ILO	International Labour Organization
IMF	International Monetary Fund
LDCs	Least developed countries
MENA	Middle East and North Africa
MICs	(Non-crisis) Middle-income countries
NOAA	National Oceanic and Atmospheric Administration
OECs	(Non-crisis) Oil-exporting countries
OIMICs	(Non-crisis) Oil-importing middle-income countries
SDGs	Sustainable Development Goals
UNDESA	United Nations Department of Economic and Social Affairs
UNWTO	United Nations World Tourism Organization
WEF	World Economic Forum
WTTC	World Travel and Tourism Council

Country Group Breakdown

Oil-exporting countries (OECs)

Algeria
Bahrain
Kuwait
Saudi Arabia
Oman
Qatar
United Arab Emirates

Oil-importing middle-income countries (OIMICs)

Djibouti
Egypt
Jordan
Morocco
Tunisia

Fragile and crisis countries (FCCs)

Iraq
Lebanon
Libya
State of Palestine
Somalia
Sudan
Syria
Yemen

Foreword

The present report offers a comprehensive overview of the observed and potential impacts of COVID-19 and lower oil prices on sustainable development in the Arab States region. Bringing together qualitative and quantitative analysis on a broad range of sectors, it demonstrates the interconnected scope and scale of the first wave of repercussions on societies across the region. It also proposes frameworks for integrated policy action to mitigate the fallout of the crisis on the most vulnerable while pursuing responses which are inclusive, effective and aimed at leaving no one behind and the achievement of the Sustainable Development Goals (SDGs).

The report makes clear that before the pandemic, the Arab States region was beset by deep development challenges and was not on track to achieve the SDGs by 2030. Now, due to COVID-19, an unprecedented health, economic and social crisis continues to threaten lives and livelihoods, making the achievement of the Goals even more challenging.

What is clear is that more than creating new challenges, the COVID-19 crisis has significantly exposed existing fragilities and exacerbated inequalities at every level. While the crisis has impacted everyone, it has not impacted everyone the same. The most vulnerable are the most affected, including those employed in the informal economy, older people, children and youth, persons with disabilities, marginalized groups, migrants, refugees, and women and girls.

Yet the report also argues that the current pandemic has also moved the frontier of what is possible in the realm of policy. In the face of crisis, countries across the Arab States region have an opportunity to make bold choices to rapidly expand social protection, invest in a green economy, close the digital divide and deliver on gender equality as means to build forward better. In this sense, the crisis offers a once-in-a-lifetime opportunity to transform policies to address long-standing development challenges at a time when it is needed more than ever, with an overarching message emphasizing the need for a renewed social contract between states and populations. Crucially, the impacts of COVID-19 also lay bare the urgent need for peace and for sustained recovery from conflict and crisis.

This report is offered as a reference for policymakers, practitioners and the engaged public seeking to lead or support responses to the current crisis which are informed by data and factual analysis, and have the achievement of the SDGs as the overarching aim. In this sense, the report stands as a

contribution within the context of the UNDP role as technical lead of the United Nations Socio-Economic Response to COVID-19, and is offered as a complement to analytical work by United Nations agencies active across the region, as well as the United Nations Economic and Social Council for Western Asia, and international financial institutions such as the World Bank and the International Monetary Fund.

At the same time, it is a modest report. The crisis is still unfolding around the world and the region, and the extent and nature of its impacts continue to be revealed and unpacked. The fullest impacts of the current crisis will only be known with time.

The stock-taking nature of this report also enables it to serve as an opening reference for a series of focused policy papers the UNDP Regional Bureau for Arab States is to launch in the next future. Within an overall framework of integrated policy responses, these papers will drill down on specific themes and offer evolving policy insights to support the detailed implementation of policies aimed at building forward better and pivoting to a sustainable and inclusive future of development.

Coming at the end of the first year of the Decade of Action for the achievement of the SDGs, and as the world celebrates the 75th anniversary of the founding of the United Nations, this report also echoes the call of the United Nations Secretary-General for renewed ambition, mobilization, leadership and collective action, not just to beat COVID-19 but to recover better, and together.

As the Regional Bureau for Arab States of the UNDP, we are committed to supporting our partners across the region to rise to the challenge and to create more inclusive and equitable societies for everyone.

Sarah Poole

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Executive Summary

The Arab region has been severely affected by a compound crisis triggered by the simultaneous occurrence of COVID-19 and a significant drop in oil prices. As this report is being finalized,¹ the virus is still spreading with increasing speed across the region's largest economies. Initial signs of deceleration, albeit limited, are only found in some of the region's smaller economies that implemented drastic social distancing measures in a timely manner after the pandemic was declared by the World Health Organization (WHO).

Despite many governments' efforts to put in place policies to contain and mitigate the spread of the virus and subsequent economic crises, as well as the many attempts by international organizations, consultancies and think-tanks to assess its socioeconomic impact, that impact is still largely unknown and unmeasurable. This is because of the atypical nature of the shock, its unique interrelations with global and regional economic transmission channels and, above all, the region's underlying social, economic, institutional, and political characteristics and fragilities. Socioeconomic assessments prepared by UNDP's Country Offices together with other UN and development partners indicate that the crisis has affected every aspect of the Arab economies and the lives of people in the region, including entire economic sectors, investment, trade, remittances, labour markets, and health and education systems; the welfare of households, communities and individuals – and in particular women and students; and the many personal dimensions of people's lives.

Moreover, this dual shock presented by the coronavirus and low oil prices has exacerbated the region's existing challenges, such as historically persistent anaemic per-capita growth, high investment volatility, low productivity, fragile political transitions, entrenched economic rentier systems, insufficient opportunities for economic and political participation by women and youth, and

worsening environmental challenges. Indeed, even before the dual shock, structural challenges implied that the region was not on track to achieve the SDGs², which now are going to be further away.

The shock reiterates the fact – as if there was any need – that these challenges have strong regional dimensions and consequently require regional solutions. Thus far, however, the Arab countries have exclusively chosen national policies over regional responses and recovery strategies.

This report aims to provide a clear and comprehensive examination of major, direct and indirect socioeconomic impacts of COVID-19 and lower oil prices in the region at the macro, meso and micro levels, as well as related policy responses. These impacts and responses are consistently analysed across three principal sub-regional groupings comprising countries with broadly similar development challenges in the current crisis: oil-exporting countries (OECs); oil-importing middle-income countries (OIMICs); and fragile and crisis countries (FCCs). As with any such categorization, these groups cannot be considered exhaustive or exempt from overlaps in certain aspects, but are useful in the context of this paper. Special attention is dedicated to conflict-affected countries (Syria, Yemen, Libya, Somalia) and countries undergoing political and economic transitions (Algeria, Iraq, Lebanon, Sudan and Tunisia), where weak health systems and strained institutional capacities often overlap with political fissures in ways that compound underlying socioeconomic fragilities.

Each chapter provides an overview of the challenges and policy responses implemented thus far – which are critical, as they may either improve the situation or make things worse if not properly designed and implemented. The chapters also propose additional policy actions intended to mitigate the impacts of the crisis and support progress towards inclusive and sustainable development in the short and medium terms.

¹ The report has been drafted in summer 2020.

² Arab Development Portal (<https://data.arabdevelopmentportal.com/Sustainable-Development-Goals/>).

01

The pandemic: Challenges in the Arab region

Chapter one reveals how many of the region's healthcare systems were ill-prepared for facing the COVID-19 pandemic, according to a range of commonly used health sector indicators. The chapter demonstrates how socioeconomic challenges risk compounding pre-existing health-related challenges in many countries in the region, creating a vicious circle that over time will be increasingly difficult to disentangle.

02

Macroeconomic aspects

Chapter two illustrates major macroeconomic transmission channels and discusses why a rapid, so-called 'V-shaped' economic recovery in the region is unlikely; rather, the recovery will probably involve a longer period of diminished growth than initially expected by analysts. The pandemic has caused a drop in domestic, regional and global demand; disrupted production, trade and supply chain patterns; and led to a fall in consumer and business confidence, as well as a sudden, parallel tightening of financial conditions. Travel and movement restrictions have severely undermined the region's labour-intensive service sector, resulting in rising unemployment and falling productivity, wages and remittances. Regional financial markets have witnessed increasing asset price volatility, resulting in growing risk aversion among investors. This will likely lead to higher demand for dollar-denominated liquid assets, a significant slowdown of FDI inflows and rising risk premiums in international financial markets. Such tightening financial conditions are likely to result in less favourable refinancing conditions for the region's maturing external sovereign debt over the course of 2020 and beyond. Therefore, government budgets are expected to be affected at least in three ways: i) through a significant increase in public expenditures to deal with the urgency of the crisis and its immediate health and socio-economic effects; ii) by a drop in tax revenue resulting from decreasing economic activity; and iii) by the difficulties governments will face in mobilizing financial resources in international capital markets. While the pandemic's economic impact is expected to be sizeable across the region, it will be felt differently in different countries based on factors including their underlying economic structures, fiscal conditions, and capacity to promptly respond to the crisis.

03

Sector-based transmission channels: Tourism and construction

Chapter three explores two hard-hit economic sectors that are particularly important to the region's economy: tourism and construction. The tourism sector makes up a significant share of Arab countries' overall exports and an important source of foreign currency earnings. The halt in international tourism will increase unemployment mostly among youth – and especially young women – and migrants in many countries. Measures to support the tourism industry and protect its already-vulnerable workforce will prove critical. The construction sector also plays a considerable, albeit variable, role in Arab economies and labour markets. In many countries, the contribution of construction to GDP and employment has expanded as a result of notable flows of oil revenue and remittances, drawn to a sector traditionally considered relatively stable and profitable. Most construction taking place in the region is not energy-efficient and is not conducive to adaptation to climate change. COVID-19 has had a direct impact on the construction sector in Arab countries and the impact will also be considerable on the workforce engaged in construction due to the disproportionately high presence of informal workers and those employed in small- and medium-sized building companies – who risk losing their income in the absence of unemployment benefit schemes or other social protection measures. Some of the stimulus measures put in place might help reduce the negative consequences of the pandemic and the fall in oil prices on this sector, but a more ambitious overhaul of the construction sector in the region might take into consideration additional green measures, which could be included as a requirement for companies seeking access to stimulus measures.

04

Impacts on migrants and remittances

Chapter four assesses one of the critical international transmission channels of the shock – migrants and remittances. With more than 15 percent of the global total in 2019, the Arab States host a sizeable number of migrants, primarily in the countries of the GCC, Jordan and Lebanon. The region hosts irregular and regular migrants, asylum seekers and refugees fleeing conflict and persecution, and people seeking better lives and opportunities. Certain categories of migrants face a host of challenges, including poor labour and living conditions, limited access to clean water and hygienic sanitation, inadequate access to health services, and limited legal protections and access to justice. The dual crises have further exacerbated the vulnerabilities of these migrants

and put them at particular risk. The impact of COVID-19 and the sharp decline in oil prices have led many business enterprises to lay-off migrant workers and cut wages. The crisis is also expected to impact the flow of remittances – a critical source of funds for countries that are among the largest recipients of remittances as a percentage of GDP in the world, as well as a key source of income for millions of households in the region. Current estimates indicate that remittances to the region are projected to fall by about 20 percent in 2020 but in some countries the drop is likely to be higher. Mobility restrictions during lockdowns, as well as high remittance costs, are among the key constraints that impede the flow of remittances and their critical countercyclical role in times of crisis. Some governments in the region have introduced limited measures to address the immediate challenges faced by migrant workers impacted by the dual crises, which mostly relate to residency or visa renewals and testing and treatment for COVID-19. However, greater efforts must be taken by countries to address the severe impacts of these crises on migrants. Among the key immediate priorities for governments in the region should be to ensure gender-sensitive access to healthcare, effective service delivery, adequate work and living conditions, and social protection; and to recognize remittance service providers and their agents as essential, extending fiscal support to remittance service providers accordingly as a means of supporting their continued flow. Looking at migration from a longer term perspective, the outlook is no longer favourable, hence governments should focus on improving the ability of their economies to export goods and services rather than their youth.

05

Impacts on labour markets

Chapter five analyses the potential impact on the labour market, with a particular focus on the informal labour market and vulnerable workers, including refugee and migrant workers who do not have access to social protection measures and are therefore particularly vulnerable in the event of shocks. Given that almost one third of total regional employment comprises work in activities that are at high risk of being hard-hit by the economic disruptions created by COVID-19, the policy response should be tailored to support the most vulnerable sectors in order to achieve an appreciable impact on employment. The policy response must also contend with the challenges emanating from the complex heterogeneity of the labour force of the region – which notably includes sectors that are highly protected at the expense of others. In the medium-term, a coherent menu of public sector, social insurance, social assistance and active labour market reforms is required, with a focus on young people and women.

06

Impacts on MSMEs

Chapter six reviews the preliminary results available from MSME micro surveys conducted in the region. MSMEs, which account for 97 percent of all businesses and represent a major source of new job creation in the region, stand to lose the most from the dual crises. This is in large part a consequence of the lower levels of assets and limited cash reserves they have on hand to cushion against liquidity shortages. In addition, MSMEs and most workers are typically employed in sectors that are particularly exposed to the pandemic's effects, such as tourism, transportation and retail. In those countries for which some evidence of the impact is available, the crisis has resulted in business closures, declines in production, declines in sales, loss of profits, loss of jobs and the emergence of liquidity constraints, with the combined effect of growing threats of enterprise failure. While some enterprises have been able to adapt to the crises and remain operational, for example through intensified use of ICT, not all have been able to do so. The main types of support targeting MSMEs relate to easing liquidity challenges faced by enterprises, allowing for deferrals of tax and fee payments, rolling out employment protection and retention schemes, and lowering (through subsidies) the prices of recurring household fees such as rents or utilities. Disparity in the scope and depth of the response between fragile and crisis countries and others is noticeable, mainly due to the differing fiscal space and institutional capacities of country groups. Moving forward, countries must ensure the continuation of ongoing interventions, with increasing scale and impact. In the medium- to long-term, countries should look at systems or strategies to broaden and ensure the sustainability of their fiscal space, address gaps in the business environment for MSMEs, expand access to social protection for employees of MSMEs, and expand access to digital opportunities to support business continuity. More fundamentally, governments need to reduce the so-called "dualism" in their economies by allowing SMEs to grow – noting that a key characteristic of the private sector in most countries is a huge "missing middle", largely related to the unfair competition that mid-sized firms face from large (and often politically connected, but inefficient) firms and SOEs.

07

Impacts on poverty and food security

Chapter seven uses various assessments, including micro surveys that have been conducted in the region so far, to give an idea of the

welfare impact on households through a poverty and food security lens. While results are preliminary, the impact is clearly sizeable. It is estimated that up to 14.3 million people in the region could fall into poverty in 2020 due to the crisis, if no urgent mitigation measures are taken. This would bring the estimated total number of people living in poverty in the region up to 115 million. There are also serious negative implications of the crisis for multidimensional poverty, because of the impact of the pandemic on access to education and unequal access to technology. The region is especially vulnerable to food insecurity, being the largest per capita importer of grain in the world. During 2020, an additional 1.9 million people are also likely to become undernourished, or food insecure, as a result of the pandemic. The effect is aggravated primarily by weakened purchasing power caused by job losses and increases in food prices, observed particularly in fragile and crisis countries, where about 74 percent of the region's undernourished people live. Countries have implemented extensive policy measures to prevent declines in consumption and prevent people from falling into poverty and food insecurity. These measures include reducing taxes on consumer items, a wide range of social protection measures, income support, market interventions such as price controls, easing of liquidity constraints, enhancing access to credit, trade measures such as import subsidies and export bans, institutional measures, and increased agricultural spending and macroeconomic policy measures. Measures taken so far have certainly prevented even greater increases in poverty and food insecurity, but an extended period of crisis could test the financing capacity of countries to continue implementing such measures. Additional measures may also include addressing economic and social inequalities, enhancing economic diversification initiatives, and ensuring the financial sustainability of existing policy interventions.

08

Gendered impacts and responses

Chapter eight completes the analysis of the potential impact on girls and women provided in the previous thematic chapters and identifies the compounding risks emanating from the COVID-19 crisis and their potential medium-term implications for women and girls. These include increased exposure to risks due to disproportional female representation in the healthcare sector in the region, increased unpaid care work, decreased job opportunities, digital exclusion and school dropout rates, among others. Women are also suffering from the shadow pandemic of domestic violence. So far, governments in the region have not included women in decision making about the policy response nor tailored enough their policy responses to meet the needs of women. The sobering conclusion is that, should the status quo continue, it will be impossible for countries to put themselves on a long-needed gender-inclusive development trajectory.

09

The social protection response

Chapter nine focuses on social protection and, hence, is entirely policy oriented. This is an area where more policy debate and engagement across the region is critical, as social security schemes (e.g. health insurance, pensions, paid leave/sick leave, maternity and unemployment benefits) remain predominantly tied to formal employment. While Arab countries have adopted numerous emergency policy measures to expand social protection coverage, these measures remain temporary, and ad hoc, and in their current format are not sustainable in the long-term. In addition, many important vulnerable groups – such as the elderly, people with disabilities and refugees – remain for the most part excluded by these measures. Sustained investment in social protection will be critical for a sustainable and inclusive recovery and to strengthen the resilience of Arab economies and societies to future shocks.

10

Climate change, sustainable energy and the environment

Chapter ten seeks to put the preceding analyses into a long-term perspective and calls upon policymakers to place the environment and climate action at the centre of recovery efforts. The Arab region is the world's most water scarce and food-import-dependent region and has emerged as a global climate hotspot with temperatures rising faster than the world average. In addition to challenging policymakers to make recovery efforts resilient, the crisis can also serve as an opportunity to rethink the role of the environment and climate action in development policies and paradigms. This chapter reviews three key aspects of this challenge: i) converging risks from climate change, particularly for the poor, and ways climate action can generate co-benefits for community resilience and recovery efforts; ii) implications of the crisis for the region's goal of becoming a sustainable energy economy and ways solar solutions can be harnessed to achieve economic recovery and energy security for poor and other severely affected communities; and iii) risks from a lack of capacities in water, waste and ecosystem management and ways that the more sustainable use of natural assets can reduce future risks and build resilience. The vision of a new balance between people and planet at the heart of the 2030 Agenda and the SDGs seeks to remedy this. The crisis has highlighted the multi-dimensional nature of risks in the region and the need for integrated solutions.

11

A new development paradigm: What would it take to achieve a greener, more inclusive and resilient region?

Finally, chapter eleven puts together all the threads of analysis contained in the previous chapters to delineate a forward-looking agenda. It explores broader, long-term development challenges posed by this dual shock and proposes ambitious policy options and key aspects of a revised underlying development model that could better address future risks and shocks in the region in a more effective, sustainable and equitable manner.

One of the key messages of the report is that the dual shock has laid bare the region's well-known and long-lived fragilities that have resulted in widespread economic informality, a preponderance of micro and small enterprises, inadequate financial markets, widespread youth unemployment, inadequate health systems, low levels of public transparency and accountability, and underarticulated social protection systems, to name just a few.

Another key message of the report is that institutions, economies and societies in the Arab region will need to be increasingly resilient in the face of aggregate risks and unpredictable shocks, even after this twin crisis subsides.

All these structural fragilities, combined with a new matrix of risks and shocks, point to the need for Arab political and economic elites and societies to initiate a candid debate on the kind of state and market that are required in the region to cope with an increasingly complex web of risks and shocks. Ultimately, these will need to be capable of protecting the region's citizens when shocks hit and allow them to actively contribute to their economy and innovate in normal times. This means reconsidering the key shapes and roles of the state and of the market as they have been historically realized. This task is made all the more difficult in a region heavily tilted towards economic rentierism that has been caught unprepared by the crisis. As such, it will struggle to provide enduring solutions in terms of inclusive and green recovery, sustainable development plans that are actually implemented, economic and digital transformations that can benefit everybody, efficient and affordable health and education systems, or the means to keep in check worrying early signals of heightening poverty and inequality.

This will require a new development model, founded on a new social contract, and we hope that this report will serve to initiate the necessary, candid and long-needed debate to launch such a process.