

THE ARAB WORLD AT A CROSSROADS: FACING THE ECONOMIC AND SOCIAL CHALLENGES

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Abstract. The popular uprisings that shake the stability in the Arab World represent a turning point in the history of this region. The events which have happened in the latest months highlight the serious difficulties and uncertainties surrounding the transition process in Arab countries. The demands being made in countries across the region transcend purely political matters and attain economic and social issues. The purpose of this paper is to capture the transformations which have taken place in the Arab World – and, accordingly, the main economic and social effects and to identify possible solutions to the contradictions generated by the complex process of transition in these countries.

Keywords: Arab World/ Arab countries, transition, social environment, globalization, demography.

Jel classification: F50, J11, J20, O53, R11

1. Introduction

The popular uprisings in the Arab World which flowered at the beginning of 2011 represent a peak in people dissatisfaction, with its roots in development failures. The uprisings seem to constitute a structural break with decades of authoritarian rule, mediocre economic growth, chronic unemployment and weak institutions. The challenges facing the Arab countries at their current juncture lie at the crossroads of governance and development.

The economic performance of the Arab countries has been middling over the past half century; while the region has suffered no major crisis, it now faces a major challenge, namely the *demographic transition* (the labour force is increasing rapidly because of the change in the age structure of the population). This is a major challenge for all Arab countries, despite the differences among their economies.

Besides the internal demographic, social and economic pressures, the region faces an external challenge as well: the global economic environment in which the Arab states have to operate. The process of globalization is restricted by the region's reputation as a risky business environment, but the current social transformations may lead to better future prospects.

The purpose of this paper is to highlight the peculiarities of Arab economies, to review the main economic and social challenges and to identify possible solutions to the contradictions generated by the complex process of transition in these countries. The proposed research topic is based on

the analysis and critical evaluation of available literature (literature review). Being a descriptive study above all, this paper will focus on using the conceptual framework which aims at making connections between all aspects of the research.

2. Identifying the constraints

The Arab World is not really one place, a monolithic structure, so change will have many faces. According to Wright (2008) the region today is arguably more stereotyped than any other part of the world. But the peoples, histories, political systems and economies are considerably different. Therefore, the patterns and demographics of the protests varied widely across countries like Tunisia, Egypt or Libya. Although "they shared a common call for personal dignity and responsive government, the revolutions across these three countries reflected divergent economic grievances and social dynamics - legacies of their diverse encounters with modern Europe and decades under unique regimes" (Anderson 2011).

Economically, the region includes the world's richest nations, like "glamorous" Qatar, which had the world's highest growth rate in 2010 and a GDP per capita of \$76,168 (ILO 2011). On the other extreme is Yemen, where the capita income is a mere \$1,282 (Table 1).

The economic development of the Arab countries during the last fifty years, since they gained their independence, has been middling. It has been worse than East Asia and about the same as Latin

America and South Asia: in a nutshell, not the worst, not the best, falling behind the West (Noland, Pack 2007).

Table 1. Economic context 2010 (Source: Authors' selection based on ILO Department of Statistics, Statistical Update on Arab States and Territories and North African Countries, 2011)

Country	GDP per capita (US\$)	GDP growth (%)
Egypt	2.789	5.1
Sudan	1.705	5.1
Algeria	4.435	3.3
Iraq	2.564	0.8
Morocco	3.249	3.2
Saudi Arabia	16.996	3.7
Yemen	1.282	8.0
Syria	2.877	3.2
Tunisia	4.200	3.7
Libya	11.314	4.2
Jordan	4.500	3.1
U.A.Emirates	59.717	3.2
Lebanon	10.044	7.5
Kuwait	36.412	2.0
Oman	18.657	4.2
Qatar	76.168	16.3
Bahrain	20.475	4.1

Making comparisons is a dangerous task and a subject of controversy mainly because it has been seen as an attempt to denigrate Islam (Owen 2002). On the other hand, Kuran Timur (2007) has provided a powerful argument for comparative economics: looking at the problems of one region without comparison limits vision and understanding.

Global democratization accelerated in these parts of the world (East Asia and Latin America) during the 1980s and 1990s. The conventional explanation regarding the development of East Asia refers to free market policies, high levels of public investment, agricultural productivity improvements, and technical progress due to investment in education. Latin America witnessed numerous military *juntas* fall to political change (Sorenson 2011), although the development efforts led to monetary expansion, inflation and foreign debt.

Regarding the Arab World, one of the most important themes in its economic history has been the role of the state (Rivlin 2009) and this role has been considered to be negative in many respects. The Arab Human Development Report (2002) highlighted the relationship between Arab political systems and economic performance. Decades of political stagnation and uncertainty about the future of many of the region's political regimes have also impeded successful globalization and sound economic growth. These regimes, the most power-

ful forces acting against change in this part of the world are, according to Ayubi's terminology (2008), fierce but weak. They feel that major economic reforms might threaten their power – it is known that, in general, economic reforms cannot be separated from political reforms (one exception is China) and this is the reason why they invested huge amount of money in modern technology in order to make their control bodies (army, secret police - the "Muckhabarat") more effective.

Another peculiarity of the Arab World is represented by Islam, as there has been much debate about the role of religion in the economic development of the region. Islam "inspires fear and fascination in the Western imagination" (Lapidus 1996) and it has become increasingly influential in social, political and economical life, even an important point of reference in debates about how the Arab World should be governed. Some political organizations stated that "Islam is the solution", attracting thus new adherents, including women, young people, especially well-educated persons (Tessler 2002).

The concept of "Islamic economics" became prominent during the decolonization process in Muslim countries after World War II (Sramek 2009) and it was considered to be a political tool to re-create Islamic authority over economy. The prohibition of usury ("riba") - commonly believed to be equivalent to the charging of interest - is the central principle of Islamic economics. In his empirical study, Sramek explained that Islamic banking, based on prohibition of interest and profit and loss sharing (PLS paradigm), underperformed and became inefficient compared to Western banking systems.

On the other hand, many authors argued that Islam was not the cause of economic stagnation in the Arab World. Noland (2005) made an econometric study and concluded that the influence of religion on economic growth was not significant: "Islam does not appear to be a drag on growth". Platteau (2008) stated that not religion was the problem, but the use of it and Kuran (2005) explained that change was refrained by conservative views put forward in the name of Islam (Rivlin 2009). It is possible that the Islamic religious tradition or other cultural or historical experiences could have indirectly affected economic performance in the region.

3. Demography and economics: addressing the challenge

The Arab World is endowed with 58 % of the world's proven oil reserves (including Iran) as presented in Figure 1 and 22 % of proven gas re-

serves. The Arab World as a group remains the world's larger producer of crude oil (accounting for 30 % of global exports). Over the medium term, most of the increase in the global production of crude oil is expected to come from the region, mainly from Saudi Arabia and Iraq (Institute of International Finance 2011).

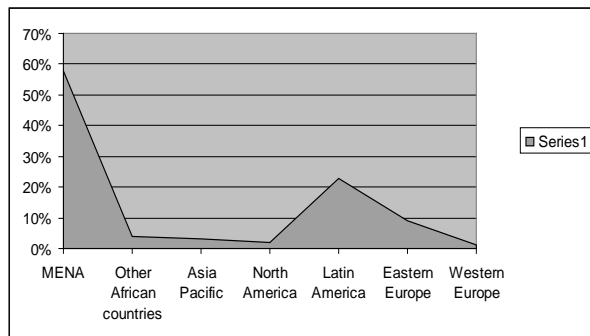


Fig.1. World proven crude oil reserves by region, 2010 (Source: Authors' selection based on Arab Competitiveness Report 2011 statistical data); MENA = Middle East and North Africa

But not all Arab countries are endowed with such great natural resources (oil, gas) and therefore they are oil importers (Siria, Lebanon, Egypt, Morocco, Tunisia). Because of the recent uprisings in these countries the situation will become even worse; in particular, tourism, foreign direct investment and local private investment will be hard-hit. Two-thirds of Arabs do not live in major oil-producing countries, and they are confronting with the most revocative situations: job creation, technological gap surmounting, demographic transition with its implications and poverty alleviation.

The central economic challenge confronting the Arab World and a key issue over the next decade is to provide employment for its rapidly growing labour force. The number of young people entering the labour markets in these countries has been rising rapidly because of the large increases in population in the 1980s and 1990s. This situation will continue for the next two decades, adding another difficulty to the problems young people are already facing in finding employment that meets their expectations.

Throughout the region, labour force is growing about 4 % annually (Noland, Pack 2008) posing a significant challenge for job creation. Demographic growths, insofar as it is the main cause of increase in the labour force, represent also a supply factor. And the labour market's role is to balance the supply of labour with demand; if this cannot be efficiently managed and there is an excess of supply, unemployment occurs. Sources of demand for labour depend on the structure and growth of the economy. According to Rivlin

(2009), the main reason for low employment rate in Arab countries has been the unstable or low economic growth rate, due to the fact that the region has missed out the process of industrialization. And this happened because of government policies, the weakness of the private sector and weak linkages to the outside world (Arab governments hesitated to grasp the opportunities offered by globalization).

Although economic growth has enhanced since 2002 (IIF 2011), the longer term growth record has been weak. Between 1980 and 2010, annual real per capita GDP growth was less than 1 %, well below the average per capita annual growth in South and East Asia. Private investment averages recorded less than 15 % of GDP in the region, compared to more than 20 % in the other mentioned regions. Another area of significant unrealized potential is technological readiness, which remains relatively low in much of the Arab World (Arab World Competitiveness Report 2011/2012). The government's dominant role in economy has tended to undermine productive private sectors activities. Rationalizing the role of government and improving institutional quality could put Arab economies on a higher growth.

3.1. Demographic transition and the pressure on labour market

Internal pressure across the region resides mainly from demographic patterns. Mortality rates have fallen, life expectancy is rising, and fertility rates have begun to decline. According to Noland and Pack (2007), between 1980 and 2000, life expectancy in the region increased by more than eight years, infant mortality was cut in half and fertility rates fell dramatically (by more than two births per woman). This change in the age structure of the population is called *demographic transition*.

Eltigani (2005) argues that the changes in the level and pattern of fertility are mostly determined by changes in marriage patterns (it is increasingly delayed), and the economic hardship experienced by many Arab countries was another contributing factor to fertility transition. The restructuring of the economies of Arab countries determined increased reliance on taxation, rationalization of jobs in the public sector, elimination of subsidies on essential consumer goods, and the introduction of fees for goods and services. All these changes affected the marriage patterns and induced a decline in marital fertility. An earlier, but also interesting point of view (Rashad 2000) suggests that Arab culture can be held responsible for resistance to change, thus the decline in fertility being delayed. For some countries and for more fortunate people,

the decline was driven by higher aspirations and wider opportunities; for others and for the less fortunate, worsening economic conditions were the cornerstone for this phenomenon.

In his study on fertility transition Eltigani also found that there is no important connection between the increasingly share of education among women in Arab countries and the process of demographic transition. The labour force participation rate of women in Arab countries is the lowest in the world (ILO 2011) and the role of female in reducing fertility rates depends on increases in women's formal work. Taking into consideration the major problem confronting these economies - the imperative to create jobs for the large cohort of young people reaching working age - it is unlikely that the economies of Arab countries will absorb substantially more women in the labour force.

The demographic transition started earlier in North Africa than in the Middle East (Rivlin 2009). Many Arab countries, especially Saudi Arabia and Siria encouraged population growth between the 1970s and 1980s and the consequences are now obvious. Syria, for example increased its population with more than 2.5 million inhabitants in one decade (between 1970-1980). Sudan and Yemen registered a worrisome demographic growth, as they are among the poorest countries in the region. The Gulf States population increased also with the large number of workers, mainly from other Arab countries, but also from outside the region.

The demographic transition (with low fertility rates which resulted in a change in the age structure and growth in working-age population) implies a significant challenge for the unprecedented growth of young people entering the labour market. A World Bank study from 2007 estimates that the region needs 80 million jobs between 2000 and 2020 to absorb new entrants to the labour force (AHDR 2010). Youth aged 15-24 represent 30 % of the region's working-age population and roughly 25 % are unemployed, compared to 14 % the international share.

The Arab World has one of the most problematic labour markets. It has the fastest labor-force growth rate, the lowest female labour-force participation and the highest rate of youth unemployment in the world. According to AHDR (2010) the highest labour participating rates are in labour importing resource countries (the rich ones). In these countries male participation is three times higher than the female rates (Figure 2). In poor countries female rate is around 50 % of the male rate. Roughly 40 % of women work in agriculture (ILO 2009). For women, their labour-force participation rate was and remains the lowest in the world:

about 25 % in 1995 and about 29 % in 2005 (Rivlin 2009). At present, average women participation rate is 31.5 % (ILO 2011).

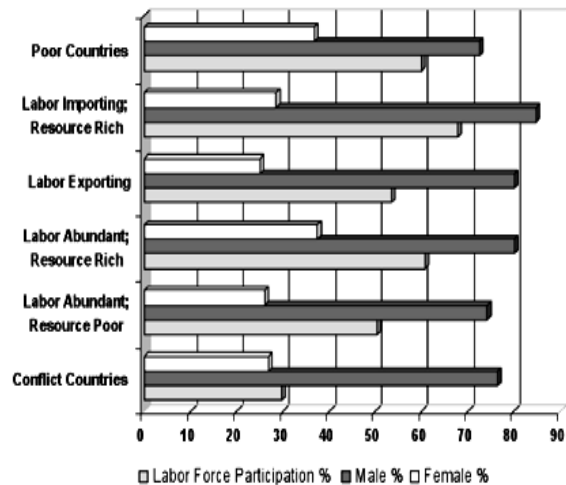


Fig.2. Labour force participation rates by major country groups (Source: AHDR 2010, Employment patterns)

In Arab countries much of the official job growth data is accounted in public sector, agriculture (where productivity is declining) and the liberal classification of informal home work and cottage-industry activity as employment (Noland 2008). According to the ILO experts (2011), the labour market problems in the region are very similar, although the countries differ in many respects. Large regional imbalances exist between labor supply and demand within each country. In addition, there is a serious mismatch between the specialization of young university graduates on the one hand and the skills needed by labor markets on the other. The educational attainment level of the labor force continues to grow. This is largely due to the arrival of first-time entrants with higher levels of education. Finally, there is a serious information deficit that limits awareness of emerging job opportunities. In short, the region faces a demographic imperative to create jobs.

3.2. Unemployment

Unemployment has been considered a major problem in Arab (particularly non-oil producing) countries. According to International Labour Organization (2011), the region has today the highest rate of unemployment in the world, 10.3 % compared to 6.2 % on average globally.

In Arab countries unemployment particularly affect youth. As Table 2 demonstrates, youth register higher rates compared to overall unemployment (the only exception is Syria). The Arab World youth unemployment is more than double the overall rate of unemployment, which is one of the highest globally. An extremely high youth

(aged 15-24) unemployment rate of 23.4 % in 2010 (ILO 2011) is most worrying. The ILO experts also argued that “even if young people have jobs, working conditions are often very poor: low wages, little social protection, lack of secure contracts and career prospects and weak or lacking trade unions to give them a voice”.

Table 2. Youth vs. overall unemployment rates 2010 (Source: Authors' selection based on AHDR 2010, Unemployment characteristics and impediments to job creation)

Country	Youth(15-24) unemployment	Overall unemployment
Egypt	25.8%	8%
Sudan	41.2%	21%
Algeria	45.6%	10%
Iraq	45.3%	30%
Morocco	15.7%	10%
Saudi Arabia	25.9%	5%
Syria	19.8%	21%
Tunisia	26.5%	14%
Libya	27.3%	7%
Jordan	38.9%	11%
U.A.Emirates	6.3%	2%
Lebanon	21.3%	12%
Kuwait	23.3%	3%
Oman	19.6%	7%
Qatar	17.0%	1%
Bahrain	20.7%	5%

An econometric study from 2008 (Moosa) explains in a novel manner that unemployment in Arab countries is not cyclical, but rather structural and it results from changes in economy that are not related to changes in education. He also admits that labour markets in this region are very rigid and dominated by the governments, as the main source of demand for labour. The structure of the economies also may determine unemployment, if the dominant sector (which propels overall economic growth) is not labour-intensive. For example, the oil sector, which accounts for much of the growth in oil-producing countries, is very capital-intensive and generates relatively few jobs. Creating good jobs for young people in the Middle East is a longstanding challenge, but one that is now attracting more attention in the aftermath of the Arab Spring.

In Arab World unemployment mainly affects youth, but also women and individuals with higher educational attainment. The main factors affecting employment are related to cultural norms (AHDR 2010). The report also shows that women receive less schooling than men and earn less than men in the private sector. According to World Bank (AHDR 2010), women unemployment increases with their level of education.

Unemployment is particularly acute among young educated. This phenomenon has been

documented: the ratio of secondary and tertiary graduated in total unemployed is over 51 % in Tunisia, 44 % in Morocco and 34 % in Algeria (Jelili 2010). These figures represent a source of concern not only for economic reasons, but also because of their socio-political effects especially in autocratic regimes. Indeed, experiencing unemployment at lower ages could constitute not only an obstacle to young people's productive potentials and future employment opportunities, but can also lead to marginalization, exclusion, frustration, low self-esteem, as Jelili concluded. In all cases, the skills gap between current level of education and business needs implies greater involvement of the private sector in contributing to skills development.

To sum up, unemployment represents the greatest challenge of many Arab governments and a key issue for the future development of the region. Reforms are imperative to pave the way to more private sector activity and competitiveness that will lead to gainful and sustainable employment not only for the present but also for the future generations.

4. Globalization: opportunities and challenges

The forces of globalization have been powerful during the last two decades, but for some reasons Arab countries have not participated in the process of globalization to the extent found in other regions of the world (Sakmar 2008).

The subject of globalization in Arab countries is complicated, as it has many dimensions. One may explain the limited globalization of Arab economies invoking deeper problems within these societies, reflecting suspicions about the benefits of international economic integration. Other may argue that the absence of greater integration resides from the intention of avoiding the cultural impact on globalization. On the whole, perception on globalization is based on preconceived ideas that regard globalization as a new ploy for domination by the West. Globalization, despite its numerous advantages, poses substantial threats. It means “opening most domestic markets to foreign competition that is usually better equipped in skills, capital, and marketing power than local producers” (Henry, Springborg 2010).

In their study from 2007, Noland and Pack tackled in a comprehensive manner the subject of globalization in Arab countries. According to them, these countries register “low scores on some indicators related to cross-border economic integration and transfer, dissemination and application of technological knowledge and innovation.” Even if many of these countries are attractive from a geographic and historic point of view (the Pyra-

mids in Egypt or the old city of Damascus which seems to be “stuck in time”), the Arab countries as a group have kept weak linkages to the outside world, “whether measured in terms of merchandise trade, import of capital goods (which embodies technological advances from abroad), cross-border investment, integration into transborder supply networks, technology licensing and internationally recognized intellectual achievements”. But, the countries benefiting the most from their vast natural resources and rising energy prices are Gulf countries which have used the resulting revenues for improvements in their competitiveness.

Statistics show that foreign investment in the region has increased, but is still concentrated in resource rich countries and is expected to decrease in countries suffering political instability (Arab World Competitiveness Report 2011/2012). According to the report, two-thirds of the total US \$64,5 billion of foreign direct investment (FDI) in 2010 went to resource-rich, labour-importing countries, with Saudi Arabia alone accounting 44% of FDI in the region. The relative isolation from international technology inflows inhibited the ability of firms, most locally owned (e.g. Algeria, Egypt or Morocco) to penetrate international markets in new product areas, despite membership in World Trade Organization or other preferential agreements.

Openness to foreign trade is one of the keys to rapid economic growth. All Arab countries, but especially those with smaller economies and energy poor, can benefit from trade gains and cross-border flows of technologies, ideas and management practices. By opening up opportunities for trade, in aggregate, business opportunities are enhanced and consumer welfare rises. Future economic growth in these countries will depend on their capacity and ability to create and sell products and services abroad.

5. The Arab countries – a challenging transition

The Arab region is experiencing a crucial moment in its modern history. Millions of individuals (men, women, even children) across the region “have issued a resounding call for change” (UNDP 2011) and the only certainty about the political and social tsunami is that nothing will be as it was before 2011. The roots of the revolts are a combination of socio-economic, demographic and political factors; poverty, unemployment and social inequality determined an unprecedented number of young people to risk everything for the chance of a better life.

After decades of authoritarian rule in-creasingly self-confident people decided that change is imminent. The upheavals across the region brought

into scene a new force that had previously been suppressed, marginalized or ignored: the people. And “contrary to the expectations of many observers, it was not the religious groups which took to the streets. A broad coalition from different parts of society challenged the prevailing political systems and socio-economic orders” (Bertelsmann Stiftung 2011). But transition requires patience, as it is a complex process which implies structural transformations; and establishing a new political or social order is not an easy task. Moreover, deep problems as huge unemployment among youth, lack of sustainable development and education deficits cannot disappear as the result of political change.

Some researchers (Ayubi 2008) argue that the premises for democratic transformation are not available in most Arab countries because these are not advanced capitalist societies and state in these societies is “fierce rather than strong” mainly because it is “structurally and ideologically weak”. Arab countries, explains the same author “are among the most dependent and vulnerable countries in the world, and this may explain at least partly why democracy has not been a prominent objective among the middle classes”.

Transition to democracy is hampered by the lack of social and governmental cohesion. Transition toward democracy needs strong civil societies. Bertelsmann Stiftung Report (2011) argues that when coping with globalization and modernization “societies must be willing to adapt in order to seize opportunities and deal with risk”. This is the reason why “agents of change” in Arab countries such as entrepreneurs, civil society, political, religious and other social groups should be encouraged to develop new ideas and to contribute to the complex process of transition in these countries.

It is tempting to consider the Arab revolts as a single movement, but the young protesters are confronting different opponents and they are fighting within different contexts. While Egypt and Tunisia must find alternatives to build political institutions – political parties, constitutions, electoral systems, Libya will need to put up a civil society and to “construct a coherent national identity” (Anderson 2011). The list of major national actors in the Arab convulsions is completed by Syria and Yemen. The civil war and extreme repression in Syria and anarchy in Yemen do not foster the creative discourse of which modern societies are made. A greater cohesion, a renewed emphasis on economic policies and an enhanced effort to help build civil societies and democratic institutions are the decisive ingredients of a response to the Arab Spring.

6. Conclusions

The historic winds of change are sweeping over the Arab region. Arab countries are under multiple changes. It is imperative to rapidly generate employment in order to absorb the new labour force entrants. Besides the internal demographic pressure, the region faces another challenge – the successful globalization of China and India; therefore the external competitive pressures are increasing. In order to accomplish their main economic and social challenges, Arab economies have to move forward on comprehensive structural reforms that will improve the competitiveness of their economies, improve public sector governance and increase the role of private sector. Structural reforms are imperative in order to address the need for higher growth and job creation.

Openness to foreign trade is one of the keys to rapid economic growth. Future economic growth in these countries will depend on their capacity and ability to create and sell products and services abroad. The governments should also focus on creating a legal and institutional environment for strengthening the investment climate, making more room for private investment in services and network industries, improving access to finance and fostering regional and global integration in order to reap the benefits of globalization. These strategies should be not only comprehensive, but also adapted to the particular circumstances, needs and potential of each country.

Despite the considerable differences among Arab economies, the common denominator across the region is the imperative to deliver sustainable employment. The lack of capital is a barrier to job creation and to ensure sustainable employment. Attracting Foreign Direct Investments (FDI) could be a solution. But this strategy is determined by a political and social stability and a predictable legal framework. This stability is also dependent on the level of poverty. Arab Countries are facing now one of the highest levels of social inequality in their history. As long as the governments of these countries will not provide a reliable plan in order to reduce poverty, social inequities and the privileges of a minority, welfare in the region is unlikely to occur.

Another challenge is to modernize the educational system. The Arab countries have a crucial asset which is wasted: the human capacity. These countries have a large population, but most of them, unfortunately, have a high illiteracy which eradicates the capacity of human resources to boost the modernization. Instead of contributing to the creation of welfare, people in the Arab World are a burden for the budget. Through a more inte-

grative educational system, through policies that address to a larger inclusion of children in schools people can be transformed into the most valuable resource of the region.

Globalization is a fact of the present, and Arab states must face up to this reality and prepare their youth to become active participants at the global level. As argued before, this requires upgraded education systems, knowledge about the rest of the world, and involvement in whatever issues or problems it faces.

The recent popular uprisings demanding more social equity and stronger economic development led to significant turbulence in the region and to unprecedented and unexpected political change. Although these events have contributed to uncertainty in the short term, they present great promise for the future development on the long run. Despite these huge challenges, the Arab Spring offers unprecedented opportunities for positive and sustainable changes. For the transition to succeed, the Arab economies will have to generate economic growth of unprecedented dimensions in the upcoming period.

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