MIDDLE EAST AND NORTH AFRICA
GOVERNANCE NEWS & NOTES

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A NOTE FROM THE PUBLISHER

The noted Prussian military strategist Carl von Clausewitz once famously quipped, "everything in war is very simple, but the simplest thing is often difficult." The same could certainly be said about institutional economics and the quest to understand the relationship between ideas such as good governance and the rule of law with economic growth and development. This issue of *Governance News & Notes* reflects upon this difficult and complicated issue. The question is analytically interesting and remains far from being resolved, although a great deal of progress has been made in recent years.

We are fortunate in being able to feature the reflections of one of our own on this issue, Mustapha Nabli. In the following interview, he brings to bear his decades of experience as an academic, senior government official and international civil servant on the question of good governance for development in the MENA region. Mr. Nabli joined the World Bank in 1997 after a long and distinguished career in Tunisia, where he served as Minister of Economic Development and Minister of Planning and Regional Development, Chairman of the Tunis Stock Exchange, and a professor of economics at the *Faculté de Droit et des Sciences Politiques et Economiques de Tunis*.

This edition of *Governance News & Notes* is also marked by a transition. After serving for nearly a decade, Mustapha Nabli recently left his post as Chief Economist and Director of the Bank's Middle East and North Africa Social and Economic Division (MNSED) for a new role as Senior Advisor in the Bank's Development Economics Vice Presidency. This new position will allow him more latitude to probe these issues carefully, and he recently oversaw the conduct of a major conference on the empirics of governance at Bank Headquarters in Washington. The position of Director MNSED has been filled by Ritva Reinikka, whose background and interests are discussed in greater detail below. Ms. Reinikka comes to the region having made major intellectual and practical contributions to the quest for improved front-line service delivery in developing countries.

While scholars work hard to advance our knowledge and understanding of the empirical and analytic linkages between governance and development, many others—including a variety of bilateral and multilateral donors and development institutions—are grappling with these issues on a daily basis. UNDP and OECD have recently launched a major initiative, *Good Governance for Development in the Arab Countries (GfD) Initiative*, predicated upon the assumption that improvements in MENA institutions will have an important impact upon the region's overall development trajectory. In this edition, Wassim Harb and Arkan El Seblani of UNDP's Program on Governance in the Arab Region (POGAR) discuss this important cross-country effort.

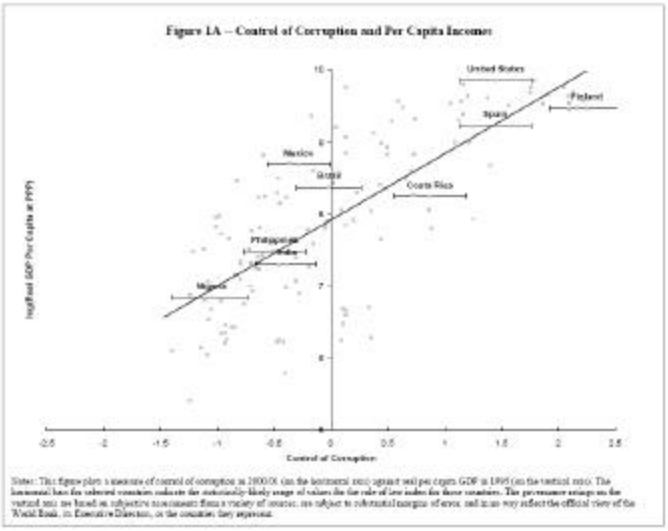
ON GOVERNANCE AND GROWTH

BY ROBERT P. BESCHEL

In his Nobel Prize lecture in 1993, Douglass North put the case for governance and growth succinctly when he stated, "institutions form the incentive structure of a society and the political and economic institutions, in consequence, are the underlying determinant of economic performance." Subsequently, a host of econometric analyses have backed up what for many is intuitively obvious—there is a close correlation between levels of economic wealth and development and the quality of public institutions, with the latter measured along numerous dimensions. The attached graphs, cited from Daniel Kaufmann and Art Kraay's path breaking work on this topic, neatly illustrate this point.

But as any first year graduate student would affirm, correlation does not prove causality. It could very well be that improvements in governance improve the quality of service delivery and create a regulatory environment where private sector growth can flourish, thereby raising GDP. Or it could be that, as countries grow richer, they are able to devote more resources to strengthening public institutions, so the quality of their governance improves. It could be that both the wealth of nations and the quality of their institutions are influenced by other dynamics, such as the emergence of a middle class that demands better services, so that they rise together in a fashion that appears to be related but in fact is not. Or finally, it could be that, as countries grow richer, perceptions of the quality of governance may improve even if the reality does not.

The effort to unbundle and better understand these relationships has been hampered by a number of challenges. Scholars such as Melissa Thomas and Thomas Carothers have noted conceptual and definitional problems in developing testable hypotheses and constructing valid indicators. Many indices purporting to measure topics such as the "rule of law" are composites that are weighted in ways that are occasionally arbitrary, which may in turn cast doubt upon what the indicator itself is measuring. Almost always, these efforts are divorced from a broader and more comprehensive theoretical framework. (Kaufmann and others would reply that the lack of an overarching, unified theory has not prevented work from moving forward in a wide variety of disciplines, from physics to economics.)

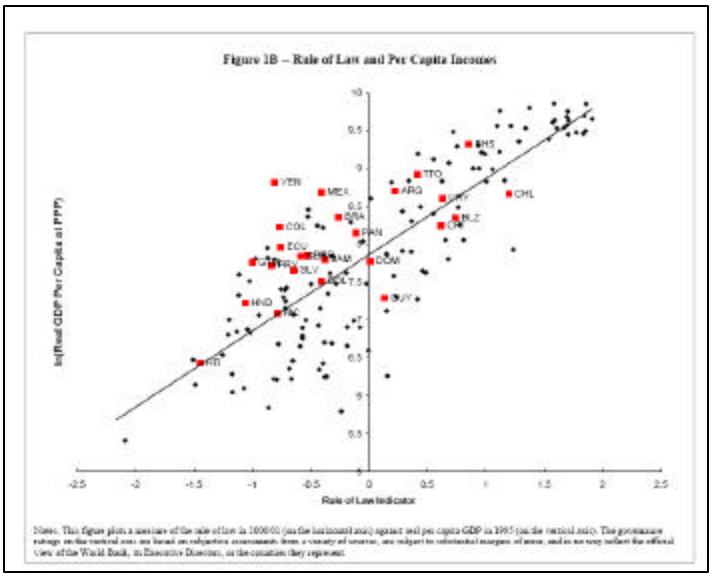


We simply do not know what elements of more narrow concepts such as "rule of law" are most important, let alone the broader notions of governance. Does rule of law apply to the basic legal system itself or its supporting regulations, the functioning of the police and judiciary, access to justice, the speed or predictability of judicial decision-making, the ability to ultimately enforce contracts, the availability of

alternative means for dispute resolution, etc.? How important are each of these component factors, and how do they interact in creating an effective legal system? Furthermore, there is often a gap between the existence of formal institutions, which can be quite sensible and appropriately designed on paper, and how these institutions actually function in practice. Measuring such gaps can be a difficult and occasionally contentious exercise.

Others have criticized the methodologies behind efforts to measure the quality of governance and link it to economic growth. A major OECD study by Christiane Arndt and Charles Oman noted a number of methodological challenges, including the likelihood of correlation between different data sources from which composite indicators are constructed; the lack of comparability over time (contrary to popular perceptions, indices such as Transparency International's *Corruption Perceptions Index* are created separately each year, so country movement up and down the index is analytically meaningless); and potential problems with sample bias.

Yet in spite of these difficulties, over the past two decades a growing army of economists, econometricians and political scientists have devoted vast energy and intellectual effort towards improving our understanding of the link between governance and development. A great deal of interesting and innovative research is moving forward. As a recent article in *The Economist* notes, "there have been huge improvements in monitoring and measuring the rule of law, even though people cannot agree exactly what it is." Historical studies have demonstrated that institutional factors can play a major role in shaping the ability of poorer states to catch up with more advanced ones. Econometric studies have demonstrated that there is a strong and positive linkage between foreign direct investment and confirmation that the rule of law; control of corruption; regulatory quality; government effectiveness and political stability are positively correlated with foreign direct investment, which is in turn correlated with increased GDP growth. Other studies have focused on the domestic distributional impacts of corruption, noting that it increases income inequality and poverty through lower economic growth, biased tax systems favoring the rich and well-connected; poor targeting of social programs; lower social spending; unequal access to education; and a higher risk in investment decisions of the poor.



Beyond the realm of scholarly debate there lies a world of perceptions—which at times can be even more real in its impact than the empirical phenomena upon which it is grounded. There is an analogy with the Nielsen Ratings, which are used in the United States and many other countries to measure audience size and composition for television rankings. The task of measuring audience size is a notoriously tricky business, and for a number of years it was known that Nielsen methodologies may suffer some bias and inaccuracy. (In fact, in June 2006 the company announced sweeping plans to correct some of the more obvious discrepancies.) Yet for decades, the Nielsen Ratings have been

accepted by the relevant stakeholders as the currency through which major programming decisions were made and hundreds of millions of advertising dollars were allocated.

In a similar fashion, thousands of decisions are being made daily by a wide variety of actors on the basis of their views regarding the quality of a given nation's governing institutions and their likely contribution to prosperity and economic growth. Foreign and domestic investors decide how and where millions of dollars will be committed. Ratings agencies make judgments about sovereign risk, financial sustainability and ability to repay debt that influence the cost at which governments can borrow. A number of donors are increasingly factoring in governance considerations into decisions about aid allocation. Citizens themselves are often acutely interested in how their countries fare on various indices of good governance. In a variety of MENA countries, the perception of clean and effective governance—whether grounded in robust empirical data or not—is increasingly having an impact upon the composition of cabinets and the ability of governments to rule effectively.

As of this point, enough evidence exists that countries would ignore the linkage between well performing public sector institutions and economic growth at their peril. The aerodynamic principles underlying insect flight may be difficult to model, but few would dispute that bees or butterflies can fly. In a similar fashion, the nuances of "good governance" may be difficult to fully weigh and measure, and it may be years before its component parts and their impact upon economic growth are fully parsed and understood. But the high correlation between economic wealth and the quality of institutions is well-established. The hypotheses linking institutions and growth are plausible even though they may not be validated conclusively. A rapidly growing body of evidence is fleshing out the linkages between various sub-components of "good governance" and factors that are known to produce favorable development outcomes. While not established beyond a reasonable doubt, the burden of proof is increasingly falling upon those who would argue that there is no meaningful causal relationship between the two.

MUSTAPHA K. NABLI INTERVIEW

BY RAMI G. KHOURI

Governance and Economic Growth: Lessons Learned, Tasks Ahead

WASHINGTON, D.C. – In recent years, economists, political scientists and development specialists have identified a clear relationship between good governance and equitable, sustainable economic growth. Yet, these same analysts have not identified the precise nature or sequence of governance reforms needed to promote good outcomes and successful development in the Middle East and North Africa (MENA) region.

This is the conclusion after several decades of work in this field of Dr. Mustapha K. Nabli, the Chief Economist and Director of the Social and Economic Development Group of the World Bank's MENA division, who has been a pioneer in the analysis of linkages between institutions, governance and economic growth. He is now shifting to a new position in the Bank's Chief Economist office.

Looking back at advances in this field, he said in an interview at the World Bank in late February that, "We have come to understand that governance institutions are really critical for growth, development, sustainability, efficiency and equity. The problem is that we do not all

agree on what we mean by governance, exactly, what needs to be changed, and how we do that."

Economists have learned that growth and development issues in MENA countries are influenced by pure economic factors, along with phenomena that are not strictly economic. "We started thinking about this and soon saw that the root cause of lack of progress on all these dimensions was the governance dimension, which also applies in many other areas like private investment, banking reform, quality of education, health, water sector management, and others."

Mustapha K. Nabli

- Currently Senior Advisor to the World Bank Chief Economist
- Chief Economist for the World Bank's MENA Region and Director of Middle East North Africa Economic and Social and Economic Development Unit from 1999 to 2008
- Minister of Economic Development and Minister of Planning and Regional Development in Tunisia from 1990 to 1995
- Chairman of the Tunis Stock Exchange from 1988 to 1990
- Professor of Economics, *Faculté de Droit et des Sciences Politiques et Economiques de Tunis* and visiting professor at various universities in Canada, USA, Belgium and France prior to 1988
- Ph.D. and a Masters degree in Economics from the University of California at Los Angeles

He singled out the "checks and balances dimension" as the single most critical element in good governance, rather than a single branch of government such as the judiciary, civil service, or legislature.

"Our research and experience suggest that the single most important aspect of good governance is whether or not you have a system of checks and balances that allows society as a whole – the government, judiciary, NGOs, the private sector, the media – to give feedback and interact in a way that moves forward and corrects mistakes and weakness," he said. "The most critical governance issue is transparency and checks and balances that cut across all sectors."

Dr. Nabli expects the World Bank to continue its emphasis on promoting good governance as a good foundation for long-term, equitable economic growth, even anticipating some scaling-up of the bank's focus on fighting corruption and enhancing good governance practices in the years ahead.

However, he acknowledges that much work still needs to be done on identifying the most effective means for external parties to influence and promote domestic good governance. The World Bank has learned from its own experience and defined mandate that it can only work by bringing information and experience to the attention of governments that wish to improve their governance practices and achieve sustainable economic growth.

"We cannot tell governments what to do or issue instructions. Typically, we identify an issue, do some analytical work to understand what is happening, bring in international expertise, and start a dialogue with the authorities. Then it starts moving and we can assist, if the government is convinced to move towards reform," he explained.

Is good governance the same thing as democracy?

"I would distinguish between them," Nabli said. "You can theoretically imagine a system where the accountability mechanisms and transparency are strong, without having a democratic or

electoral system. Some countries experience strong economic growth without democratic institutions. That doesn't mean they have good governance; it means they have good outcomes."

There is a growing body of analytic work that demonstrates countries that do well on governance indicators also tend to have high levels of per capita GDP. However, the linkages and causal relationships are less well understood. Growth and successful development outcomes can result from many things other than governance, such as a rich natural resource base. Growth and employment expansion cannot automatically be equated with good governance, he warns.

"For a period, a country can have high growth in the context of not-so-good governance, and can even become rich. In some resource-rich countries higher income and bad governance go together. We have to be careful with the causality. It goes from good governance to better outcomes, but better outcomes don't necessarily mean you have good governance. That debate is still on-going."

How to measure and define the outcomes of good governance is another area where much work remains to be done.

"We focus on economic growth and its impact," he explains, "but we go beyond that to address equity issues. In the MENA region, this means creating the good quality jobs that are needed, along with quality education and health services. Public services delivery is an important part of the growth and equity goal."

So what should a country focus on if it aspires to sustained, equitable economic growth?

"My own view is that democratic institutions are more likely to lead to better governance, but not necessarily so. Democratic institutions can also produce bad governance. That's why the focus has to be on good institutions, defined by accountability, transparency, and checks and balances. That's what good governance is all about," he concludes.

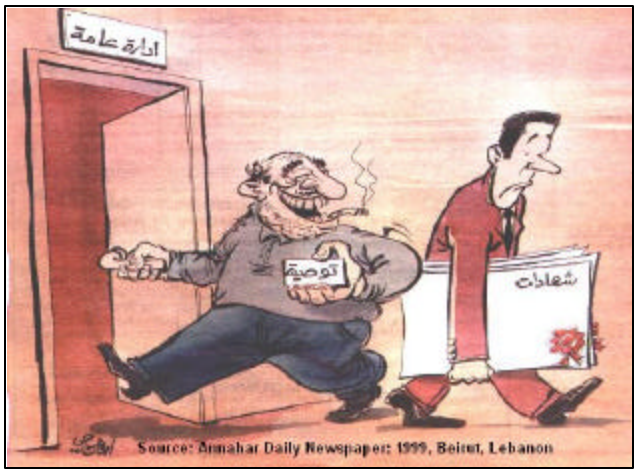
Now that he is shifting his professional focus from the MENA region to the world beyond, how does he compare the MENA countries' performance globally?

"Broadly speaking, in terms of promoting checks and balances in governance, the MENA region has not experienced much progress. Governance reforms have essentially focused on public administration and technical aspects of the judiciary, customs, the budget, civil service, and other such areas. These are very partial attempts at governance reform. A few countries have achieved good economic advances, but it's hard to say if this is due to any of the governance reforms. As a region, MENA still lags behind the rest of the world, and we do not really know why. Perhaps we need more time for significant progress to happen."

RITVA REINIKKA: NEW DIRECTOR IN THE WORLD BANK'S MENA REGION

RITVA REINIKKA has recently been appointed director of the Social and Economic Development Group, which is responsible for the Bank's work on economics, trade and competitiveness, governance and public sector management, poverty, gender, finance and private sector development. She joins the MENA Vice Presidency from the Bank's Africa region, where she was previously Country Director for Botswana, Madagascar, Mauritius, Lesotho, Namibia, South Africa and Swaziland.

Ms. Reinikka's career combines extensive practical experience with a strong research orientation and long-standing commitment to improving the quality of governance and public administration. Before working in South Africa, she was a research manager in the Development Research Group and co-director of the *2004 World Development Report*, "Making Services Work for Poor People." This path breaking study focused on the political, institutional and managerial challenges that can often interfere with efforts to provide public services such as health, education and water to the most disadvantaged groups of society. "I've always been interested in how the man on the street experiences governance," she noted in a recent interview.



"Within MENA, it is very important that the Bank leverage our limited resources and assist our clients in making the greatest impact possible. The Bank has historically been active on a host of important issues involving public sector reform, such as public financial management and civil service reform. While it is important to continue work on these systemic issues, it is also essential to ensure that changes in central institutions and practices are ultimately linked with improvements in front-line service delivery." Towards this end, she envisions spending considerable time and effort in helping clients throughout the MENA region carefully benchmark the quality of their service delivery through new micro-level evidence and careful impact evaluation. "My personal experience," she notes, "backed up by a growing body of research, indicates that services can improve markedly when you combine transparency with accurate measures of government performance. Most of my career in the Bank I have worked on topics related to governance—especially on information, participation and client power—and I am very much hoping to contribute to these agendas in MENA too."

"Another passion of mine is impact evaluation. With limited resources and nearly unlimited needs, impact evaluations should be an integral part of policy and public spending decisions. We need to know what works, what doesn't, and why. I intend to work with my team and our counterparts to put together a multi-sectoral impact evaluation program. This should serve the MENA region particularly well."

One of the most formative experiences in her career came in the mid-1990s, when she began looking into problems with the flow of funds for education in Uganda. A survey revealed that during 1991-95 on average only 13 percent of grants made it to the schools. The disbursements were rarely audited or monitored, and most schools and parents had little or no information about their entitlements to the grants. Most of the funds were used for purposes unrelated to education (to fund the local political and bureaucratic machinery) or for private gain, as indicated by numerous newspaper articles about indictments of district education officers after the survey findings went public.

As evidence of the degree of leakage became public knowledge in Uganda, the central government enacted a number of changes. It began publishing the monthly transfers of public funds to the districts in newspapers,

broadcasting information on the transfers on radio, and requiring primary schools to post information on inflows of funds. The objective of this "information campaign" was to promote transparency and increase public sector accountability by giving citizens access to information needed to understand and examine the workings of the capitation grant program for primary schools. An assessment of these reforms shows that the flow of funds improved dramatically, from 13 percent on average reaching schools in 1991-95 to around 80 percent in 2001. The World Bank and others have subsequently replicated this public expenditure tracking survey (PETS) methodology in over forty other countries.

A Finnish national, Ms. Reinikka joined the Bank in 1993 as a country economist in the Eastern Africa Department. Her research and professional interests include public expenditure, service delivery, and macroeconomic and trade policy. She has published widely on development in peer reviewed journals as well as through policy-oriented outlets. Prior to joining the Bank, Ms. Reinikka was a researcher at the Centre for the Study of African Economies in the University of Oxford and the Helsinki School of Economics. She also held operational positions at UNICEF and with the Ministry of Foreign Affairs in Finland. She holds a Ph.D. in Economics from the Oxford University.

THE GOVERNANCE FOR DEVELOPMENT INITIATIVE: *Achievements and Future Directions*

BY WASSIM HARB AND ARKAN EL SEBLANI

The drive towards reform in the MENA region continues to gather momentum despite increasing security threats and political and economic instability. Indeed, good governance has moved from being a proscribed topic to one of the most debated topics, not only at the level of government, but also at the level of society at large.

The changing dynamics of reform are mostly attributed to internal and external pressures that have been exerted on MENA governments in order to acknowledge the need for reform as a pivotal issue for development. Consequently, the region witnessed a surge of initiatives that have, slowly fostered a shift from the question of "whether reforms are needed or not" to the question of "how to design and implement needed reforms."

The *Good Governance for Development in the Arab Countries (GfD) Initiative*, which is jointly supported by UNDP and the OECD, is one of the leading initiatives in this regard. Launched by Prime Ministers and Ministers from eighteen Arab countries in 2005, the GfD, today, has become the main regional forum for results-oriented policy dialogue on governance reform priorities in the region. It has also become a cornerstone for sustainable partnerships between MENA and OECD countries.

In terms of achievements, the GfD has succeeded in building an extensive network of committed policy makers from 18 Arab countries and most OECD countries. Through this mechanism, MENA policy makers identified governance challenges and have been engaged in a wide array of regional activities since 2005. Ten MENA countries have successfully established national coordination teams, composed of key policy makers, to design and implement ensuing governance reforms. These countries include Bahrain, Egypt, Jordan, Lebanon, Morocco, Oman, Syria, Tunisia, the UAE and Yemen.

Four regional pilot projects have been developed, endorsed and are going to be implemented in the next three years, including a major project on supporting the implementation of the UN Convention against Corruption (UNCAC). In parallel, seven MENA countries have developed, endorsed and began implementing their own country action plans, which are based on a series of stocktaking activities and the ongoing regional policy dialogue and capacity building.

The GfD has also supported peer advice and cooperation at the national level including peer-learning exchange on multilingual law drafting to improve regulatory quality, among other things. Finally, the GfD has supported the setting up of regional networks and centers to build capacity and advance common priorities for MENA countries. These regional institutions include, but will not be limited to, a regional tax and financial management center in Egypt; a regional center for public policy evaluation in Morocco; a regional center for legislative and regulatory quality in Tunisia and a regional network on UNCAC implementation that is expected to bring together most of the MENA countries.

In terms of future directions, the GfD will continue for another three years through its programs of work for 2008-2010, which tackle two institutional spheres, the public sector and the judicial system while integrating civil society participation, gender and environment as cross-cutting issues. It will seek to (a) deepen policy dialogue and capacity building at the regional level; (b) foster peer advice and partnerships for reform at the national level; (c) monitor and measure reform progress; and (d) anchor the initiative in a regional framework of institutions for reform.

These directions, which have been adopted by MENA countries at a recent Ministerial meeting held in Cairo (Egypt) provide signals that the GfD has the potential to build effective partnerships at the national, regional and international levels that will be necessary to foster yet another strategic step forward, without which it may argued that governance reform will remain lacking, i.e. benchmarking reform in the MENA region.

The UNDP and OECD are working closely with the World Bank on many of these initiatives, and Bank staff have participated actively in GfD workshops and conferences. Plans are underway to expand collaboration along several dimensions, particularly those involving the conduct of comparative analytic work and outreach and dissemination.

UPCOMING EVENTS AND ACTIVITIES

- **June 24-28, 2008:** ***Global Governance for Sustainable Development: The Need for Policy Coherence and New Partnerships: 12th EADI General Conference.*** Geneva, Switzerland. Hosted by the Graduate Institute of International and Development Studies. gc2008@eadi.org and www.eadi.org

- **June 30, 2008**: ***Roundtable Event on Associations' Governance in Lebanon.*** Beirut, Lebanon. Organized By the Lebanese Transparency Association (LTA) in Cooperation with the Lebanese Corporate Governance Task Force (LCGTF), and the Center for International Private Enterprise (CIPE). ckhalil@transparency-lebanon.org; and www.transparency-lebanon.org

- **June 30-July 3, 2008:** ***Training of Trainers on Corporate Governance.*** Tunis, Tunisia. CIPE and L'Institut Arabe des Chefs d' Entreprises (IACE). mkortbawi@cipe.org and www.cipe.org

- **July 4, 2008:** ***Steering Group Meeting at Technical Level of the GfD in Arab Countries Initiative.*** Cairo, Egypt. Organized with UNDP POGAR, under the chairmanship of H. E. Dr. Ahmed Darwish, Minister of State for Administrative Development, Egypt and Chair of the Steering Group. info@pogar.org and www.undp-pogar.org

- **July 7-8, 2008***: Workshop on improving Parliamentary oversight on revenues.* Beirut, Lebanon. Organized by the Arab Region Parliamentarians against Corruption (ARPAC) in cooperation with Revenue Watch Institute (RWI). hmansour@arpacnetwork.org; and www.arpacnetwork.org

- **July 30-31, 2008:** ***Regional Conference on "Anti-corruption bodies and related institutional reforms under the UNCAC", launching the Arab Network on Supporting UNCAC Implementation in Arab Countries.*** Amman, Jordan. Organized by UNDP in partnership with Jordan's Anti Corruption Commission, United Nations Office for Drugs and Crimes (UNODC), Organization for Economic Cooperation Development (OECD). info@pogar.org and www.undp-pogar.org

NOTEWORTHY LINKS

World Bank MENA Governance Website

http://www.worldbank.org/mena-governance

World Bank General Governance Website: *http://www.worldbank.org/governance*

MENA-OECD Initiative on Governance and Investment for Development: *www.oecd.org/mena*

Governance and Social Development Research Centre: *www.gsdrc.org*

The Arab Center for Rule of Law and Integrity: *www.arabruleoflaw.org*

The Arab Administrative Development Organization (ARADO): *www.arado.org*

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Ms. Alexandra Sperling
Economic and Social Development Unit
Middle East & North Africa Vice Presidency
The World Bank
1818 H. Street N.W.
Washington, D.C. 20433
+1 (202) 473-7079
+1 (202) 477-0432 (fax)
asperling@worldbank.org

FOR FURTHER READING

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