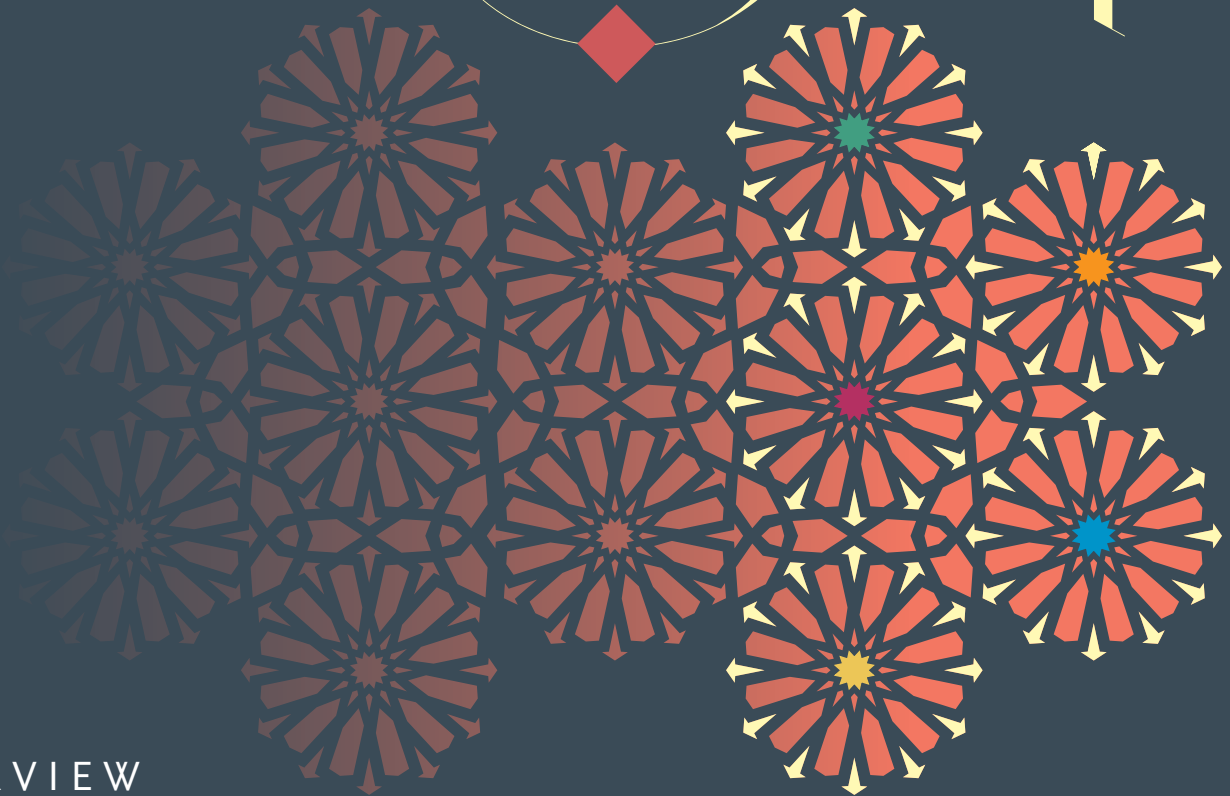


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التقارب



OVERVIEW

CONVERGENCE

Five Critical Steps toward Integrating
Lagging and Leading Areas in the
Middle East and North Africa

Overview

Convergence

*Five Critical Steps toward Integrating
Lagging and Leading Areas in the
Middle East and North Africa*

This booklet contains the overview, as well as a list of contents, from *Convergence: Five Critical Steps toward Integrating Lagging and Leading Areas in the Middle East and North Africa*. Washington, DC: World Bank. doi:10.1596/978-1-4648-1450-1. A PDF of the final book, once published, will be available at <https://openknowledge.worldbank.org/> and <http://documents.worldbank.org/>, and print copies can be ordered at www.amazon.com. Please use the final version of the book for citation, reproduction, and adaptation purposes.

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Memorandum to a Concerned Finance Minister

Subject: Five critical steps toward integrating lagging and leading areas in your country

This memo introduces a report that you may find useful and interesting. Focusing on actions that can put countries in the Middle East and North Africa on a path to territorial convergence, it concludes that governments can take the lead by tackling the economic and institutional causes of spatial exclusion.

Rising spatial disparities are threatening economic growth and social inclusion in your country and across the region. This report shows that opportunities for your citizens are shaped by accidents of where they were born—much more so than in any other part of the world. Decision makers in your country and in other parts of the region have taken steps to respond to the needs of people left behind in your cities and across your regions. Even so, spatial disparities either continue to grow or are closing more slowly than would be expected given the volume of investment you have directed to those locations.

Why is territorial convergence so difficult? First, most lagging areas in your country are limited by an inability to leverage the full returns to their endowments. The business

environment in many cities and towns restricts new firms from entering and growing, and the lack of complementary infrastructure investments hobbles local economies. Second, most residents in your lagging areas are stuck in place, unable to take full advantage of jobs that vibrant urban economies can offer. So, what do your cities need for more vibrancy and private sector jobs? They need larger markets—often beyond national borders—to increase the demand for goods and services, to increase the demand for human capital, and to create fulfilling jobs for young people.

How then, can you start building a *convergence machine* for your lagging areas?

You can reduce territorial disparities more immediately and effectively by taking five steps:

1. **Strengthen coordination and complementarities across sectoral interventions.** Efforts to enhance job prospects in places left behind should operate across and address multiple development axes simultaneously. Development strategies are more likely to succeed if they are multidimensional—including access to energy, transport, land, and markets in the same place, whether sequentially

or concurrently. Because starting anew is extremely difficult, there is little value in single-sector interventions. A good place to start is by anchoring investments around cities, which have many of the missing complements. Complementary reforms that help get the prices right—for energy and for land—can go a long way toward creating the conditions for job creation in lagging areas. The good news is that you don't have to pay more to see better results, because spatial coordination will generate cost savings in the medium to longer term.

2. **Redistribute roles and responsibilities across tiers of government.** Citizens in different parts of the country have varying needs, and local conditions require flexible service delivery models. Devolving responsibilities for local revenue generation and service provision to local governments can make them better equipped and more accountable. Effective decentralization would also empower them to cover the recurring costs of their investments.
3. **Enable greater mobility of your people between lagging and leading areas.** Major gains in living standards can be reaped from greater domestic labor mobility. Research for this report shows that living standards of people moving internally to major cities can increase by 37 percent on average across the Middle East and North Africa region. Women are more likely to move and find jobs in urban areas, but they need support to do so. One of the key constraints to greater mobility is the credentialist education system prevalent across the region. It needs to be more oriented toward marketable skills.
4. **Build dense and connected cities.** Well-functioning cities offer a wide variety of jobs for women and men. Making land markets in cities more efficient is critical for agglomeration and specialization—two dynamics that enhance job creation and economic prosperity. Whether in larger or in smaller (secondary) cities, agglomeration and specialization require the benefits from high economic density,

which concentrates economic activity geographically. For this, the fabric of cities needs to be spatially connected, dense with people, and transit oriented—not sprawling, which perpetuates the dispersion of people and jobs. Planners and regulators can attract firms to invest in cities by reducing frictions such as zoning regulations; impediments to property acquisition and new construction (costs, height limits, density limits); challenges to local business registration and licensing; limits on news and information; and obstacles to developing local business networks.

5. **Enhance market access for lagging areas, nationally and regionally.** Historically, the region's cities were part of economically central global trade networks. Many of these cities persisted into modern times as large, often vastly populated urban areas. Yet with today's thick national borders, their economic reach has been limited. Countries across the region need to enhance links across national borders—reducing tariffs and nontariff barriers (such as logistics and trade facilitation) and easing movements of goods and people. They may also need to enact policies to strengthen domestic markets. Such efforts will expand the size of urban economies, providing much-needed tax resources to redistribute in areas left behind.

The extent and sequence for implementing each transitional step will depend on your assessment of your country's readiness—political, technical, and administrative—to implement these recommendations.

These steps will allow you to promote the building blocks of a convergence machine for spatial inclusion by pursuing economic growth and inclusion rather than spatially targeted mandates. The only spatial requirements are that people across your country have access to high-quality basic services—and that economic development interventions harness the spatial and economic dynamics of agglomeration, migration, and specialization.

All levels of your government have roles: the national, the provincial, and the local. By requiring that all interventions be responsive to the basic needs of all, you can put far more of your nation's forgotten people into jobs than ever before. How? Not by trying solely to bring jobs where people are but by also focusing on where the jobs are most likely to be and enabling people to move there, while

complementing every investment with institutional measures that make the desired jobs more likely to appear.

These steps may appear daunting, even painful. But evidence from two centuries of experience from around the world has shown that the potential gains are worth the pain.

The World Bank Group can help as you decide on a way forward.

About the Authors

Somik V. Lall is the World Bank’s global lead on territorial development solutions, a lead economist for urban development, and the team leader of this report. He is a recognized expert on development policy related to urban and territorial competitiveness, agglomeration and clusters, and infrastructure, with over 20 years’ global experience, most notably in Africa, Asia, and Latin America. He has been a core team member of the *World Development Report 2009: Reshaping Economic Geography* and developed the policy framework for development of lagging areas within countries. He is the lead author of the World Bank’s flagship report on urbanization, *Planning, Connecting & Financing Cities—Now*, as well as the recent *Africa’s Cities: Opening Doors to the World*. Somik heads a World Bank global research program on urbanization and spatial development and previously founded the Urbanization Reviews program. His research and policy advisory interests focus on place-shaping policies around cities, clusters, and corridors and the functioning of factor and product markets, with more than 40 publications featured in peer-reviewed journals including the *Journal of Development Economics* and *Journal of Urban Economics*; edited volumes including the *Handbook of Regional and Urban*

Economics; and working papers. He holds a bachelor’s degree in engineering, a master’s degree in city planning, and a doctorate in economics and public policy.

Ayah Mahgoub, a senior urban development specialist at the World Bank, is the co-team leader of the *Convergence* report. She leads urban and territorial development lending and analytical projects in North Africa and leads the World Bank knowledge groups on competitive cities and results-based financing. Her focus areas currently are urban and territorial development, city competitiveness, intergovernmental fiscal systems, municipal finance, smart cities, and results-based financing. Ayah completed her undergraduate and graduate studies in economics and international development at Harvard University. Before joining the World Bank, she worked for the Center for Global Development, the United States Agency for International Development’s (USAID) Development Innovation Ventures program, the Crown Prince Court of Abu Dhabi, and Phipps Community Development Corporation. She has also worked on urban development in New York City, economic integration of minorities in France, and peace-building initiatives in Sudan.

Abbreviations

AGOA	African Growth and Opportunity Act
CDD	Civil Defense Department
CEPGL	Economic Community of the Great Lakes Countries
COFOG	Classification of Functions of Government
COMESA	Common Market for Eastern and Southern Africa
CPER	State-Region Plan Contract (France)
DAI	Digital Adoption Index
EBA	enterprise bargaining agreement
EPCI	Établissement Public de Coopération Intercommunale
EU	European Union
FDI	foreign direct investment
GAM	Greater Amman Municipality
GCC	Gulf Cooperation Council
GCI	Global Competitiveness Index (WEF)
GDP	gross domestic product
GFS	Government Finance Statistics (IMF)
GHSL	Global Human Settlement Layers (dataset)
GUF	Global Urban Footprint (dataset)
HIP	Hawassa Industrial Park
ICT	information and communication technology
IDA	Industrial Development Authority (Egypt)
IDP	internally displaced person
IMF	International Monetary Fund
ISIL	Islamic State of Iraq and the Levant

LEI	Landscape Expansion Index
LGPA	Local Government Performance Assessment
LGU	local government unit
LPI	Logistics Performance Index (World Bank)
MNAPOV	Middle East and North Africa Poverty database
NASA	National Aeronautics and Space Administration
OECD	Organisation for Economic Co-operation and Development
OSM	OpenStreetMap
PAFTA	Pan-Arab Free Trade Area
PARAS	Project to Restructure Local Government and Services
PIRLS	Progress in International Reading Literacy
PISA	Programme for International Student Assessment
PVH	Phillips-van Heusen
SEDAC	Socioeconomic Data and Applications Center
SEZ	special economic zone
TEN-T	Trans-European Transport Network
TFP	total factor productivity
TIMSS	Trends in International Mathematics and Science Study
TMSA	Tanger-Med Special Agency
TTN	Tunisia TradeNet
TVA	Tennessee Valley Authority
UDLGP	Urban Development and Local Government Program
UN-Habitat	United Nations Human Settlements Programme
VAT	value added tax
WEF	World Economic Forum
WGI	World Governance Indicators
WTO	World Trade Organization
WVS	World Values Survey

Overview

The Middle East and North Africa is suffering from spatially divergent development. The uprisings of the Arab Spring in part reflected grievances of citizens who were (or were perceived to have been) left behind, particularly by accidents of where they were born. Although the trajectory of every nation in the region varies, one stated objective is clear for them all: improve outcomes for people in areas that have been left behind.

Policy makers across the region have long been trying to integrate their people spatially and economically. Wishing to bring communities together and narrow economic gaps, governments have made large capital investments in transport corridors and “new cities.” Wishing to provide jobs in places with little economic activity, governments have designated new industrial zones supported by spatially targeted business incentives and subsidized land and energy.

Yet the results of these place-based initiatives in these countries are mostly disappointing (box O.1). The disparities between capital cities and lagging areas, and between richer and poorer quarters of cities, remain stark. Across much of the region, a fortunate few are connected to opportunity, while many more

people are marginal to the formal economy—or live outside it, seemingly forgotten.

Why do so many place-based interventions fail?

Why have place-based spatial initiatives largely failed in the region’s countries? Why have they not yielded more sustainable jobs and growth? Although the challenges are many and vary across the region, recent work in economic geography shows that most of these place-based policies get one thing wrong: they attempt to treat inequity’s spatial and physical symptoms, not its causes. Thus, to add jobs in a country’s poorer areas, policy makers try to push new production facilities into these areas. And to meet the need for decent homes and amenities in poor urban neighborhoods, funds support mass housing projects. Neither effort has succeeded widely—because the causes of spatial exclusion are not themselves spatial and physical; they are economic and institutional.

First, a *lack of economic density* in rural areas, and even in many smaller municipalities, makes them inherently less competitive than large cities because they are less suitable

BOX 0.1 Place-based policies have not led to spatial convergence

Insufficient attention to the economic causes of spatial exclusion has led governments in the Middle East and North Africa to pursue spatially targeted interventions—yet most countries have little to show for these place-based policies for several reasons:

- *New cities have not yielded the hoped-for returns.* Governments are building new cities as a respite from the chaos of today's large and bustling metropolises—but the main result is that residents are marooned far from jobs. In the Arab Republic of Egypt in 2012, 30 percent of the national built environment budget was allocated to new cities, which host just 2 percent of the nation's people. Today, the people who moved to those new cities must rely on their own cars or fleets of buses to shuttle daily to the older urban centers where they work (especially the Cairo agglomeration) (Sims 2015).
- *New industrial zones and newly designated growth centers lack promise.* Governments have undertaken large-scale investments and offered generous subsidies to create jobs in socially and economically excluded areas. But the proposed new industrial zones and growth centers often lack the agglomeration benefits that larger cities already have. Supplying infrastructure and amenities to

such remote locations can be far more expensive than supplying them in a city (where the cost can be spread across a larger number of customers). And firms that locate far from large urban areas cite constraints in their business environment—the main challenges being political instability, low access to finance, and low access to electricity.

- *New transport corridors have not facilitated regional trade.* Most middle-income Middle East and North Africa countries have invested heavily in national transport infrastructure, yet firms encounter high nonphysical barriers to trade within the region. Outside the Gulf Cooperation Council (GCC),^a the region's countries score poorly on such trade facilitation measures as the quality of customs and logistics procedures. As a result, less than 7 percent of global intraregional merchandise trade occurs within the Middle East and North Africa, compared with 40 percent within East Asia and more than 50 percent within Europe.^b

a. The Gulf Cooperation Council (GCC) includes Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

b. Global intraregional trade data are derived from the World Trade Flows database, Bilateral Data files, of the Center for International Data, University of California, Davis, HYPERLINK https://cid.econ.ucdavis.edu/Html/WTF_bilateral.html.

for large-scale investment. Large urban areas have well-understood advantages in today's global economy. Dense agglomerations favor specialized, scaled-up production for international markets (box O.2). So, an industrial zone set up far from a country's main cities is, most likely, set up to fail.

Second, not only rural but also urban economies in the Middle East and North Africa are constrained by widespread *institutional inefficiencies*. Five main types will be considered here:

- *Barriers to market entry and lopsided business environments, which vary within countries.* Several of the region's countries significantly underperform relative to comparator countries on indexes

of competitiveness, business environment, and governance. Subnationally, firms report in surveys a range of impediments to doing business, and the challenges vary from city to city within countries. One major challenge is the limited coordination of complementary investments and policies needed to make cities and regions attractive for entrepreneurs to establish and grow businesses. Sectorally siloed interventions make cities and regions inadequate homes for businesses that need complementary factors such as good market access, well-serviced land, and a relevant talent pool.

- *Centralized control over local public services.* Outside the capital city in the region's countries, smaller cities and

BOX 0.2 Economic density and agglomeration effects: The urban advantage

For firms participating in today's regional and global value chains, *economic density*—the geographic concentration of economic activity—gives large cities an edge over smaller cities and rural areas. Such density boosts efficiency by making workers and firms more productive. Economic density can make public service provision less costly. And as production becomes more complex and diversified, the physical proximity of firms becomes more critical. Thanks to these agglomeration effects, firms that specialize in producing tradables can operate more efficiently at scale and can thus compete more effectively. (Scale economies and specialization are two key drivers of firm and sectoral productivity. Scale allows a firm to reduce unit costs, increasing productivity. Specialization allows it to narrow its focus to a few products, making the most of its key advantages.)

Source: World Bank 2009.

The higher productivity of efficient urban agglomerations can promote a virtuous circle of economic growth. As a rule, if firms and workers are mobile, both will pursue productive opportunities across space, preferring to settle near existing agglomerations. Large cities become even larger and denser.

Agglomeration effects imply that an efficient economic landscape is not smooth—with equal economic density everywhere—but is instead lumpy, with large cities driving growth. However, *economic distance* (the difficulty of access from lagging to leading areas) may limit economic actors' mobility and location choices by making migration costlier or less beneficial. Friction can also result from less obvious economic factors, such as *divisions*—ethnic, political, religious, or linguistic barriers to interaction.

other localities lack the authority to raise their own revenues and to manage local service provision. These functions can, however, generally be conducted more efficiently by localities—and local government officials can be more easily held accountable.

- *Urban regulatory frictions.* Especially in urban areas, rigid and outdated regulations distort land markets and stymie development. For example, Tunisia prohibits residential buildings higher than three stories, and Jordanian regulations impose a minimum lot size of 100 square meters—restrictions that effectively limit the supply of affordable formal housing. In addition, land transfer fees and building permit fees tend to be high in the region's countries.
- *Credentialist education systems.* In the Middle East and North Africa, education is widely seen as providing a credential—and the credential is valued mainly as a ticket to public sector employment. As a result, even the most educated workers

often lack the tradable skills demanded by the private sector. So, the region's cities are less attractive than they could be to firms and investors, and citizens are constrained in their ability to leverage their skills for employment across places. The emphasis on credentials, rather than on portable skills, also reduces the chances for young women and men to move to cities where they can access better job opportunities.

- *Barriers to the spatial mobility of goods and people.* Input and output flows are impeded within the Middle East and North Africa by barriers, sometimes called “thick borders.” Among the main barriers are limits on news and information and practical constraints on travel and trade (such as visa difficulties, weak infrastructure, and logistical hurdles). Thick borders discourage firms in the region's cities from creating jobs and expanding their economic reach—and also inhibit the growth of smaller specialized cities. In addition, within countries,

migration controls can distort labor markets by reducing mobility from rural to urban areas.

Based on the research for *Convergence*, this overview outlines the roots of spatial institutional inefficiencies across the Middle East and North Africa—within cities, within countries, and across national borders—and it proposes institutional remedies and investment priorities informed by economic geography. The proposed reforms are ambitious. They will require strong leadership from city and national governments. However, getting the region on a path to spatial convergence is worth being ambitious and taking on a challenging agenda.

How can the region's countries approach convergence?

The overview identifies five transitional steps that Middle East and North Africa countries can take starting now, with the urgent aim of getting the region to a path toward convergent development.

Step 1: Enact new, evidence-based criteria to guide future spatial interventions. To move on from decades of failed place-based policy, require that the next generation of spatial interventions ensure efficient access to a large urban market either within the country or across national boundaries. Also focus on identifying major bottlenecks that spatial initiatives could clear—whether in land markets, skill markets, service provision, or trade and labor mobility. And thoroughly consult all stakeholders in an area, including local firms, authorities, and residents as well as potential investors. The key issues here are spatial coordination across complementary sectoral investments and measures to reduce subsidies to large firms that distort the price of labor relative to capital and discourage labor-intensive economic activities.

Step 2: Devolve greater functional authority over local revenue generation and service provision to local governments. To empower lagging areas, make localities more responsible, equipped, and accountable for both

revenue and services. With greater functional authority, they can better tailor their service delivery models to the characteristics of their territories and varied needs of their citizens, including better leveraging digital technologies for service provision. Decentralization of functions and finance is urgent in lagging areas that have been targeted for place-based investments, where local governments need to be empowered to cover the recurring costs of these investments. The speed and design of decentralization may vary based on current and historical institutional architecture, economic geography, and other strategic decisions. But regardless of the specific design choices, decentralization is likely to deliver better results when shifts in functional assignment are accompanied by commensurate shifts in resources and capacity.

Step 3: Step away from credentialist education and toward schooling that cultivates globally tradable skills. Decentralizing school systems could help. But also needed is a shift in public sentiment: citizens who now see the government as chiefly a job creator must come to recognize that marketable skills will attract investment and growth. Such skills will also make workers more mobile between lagging and leading regions, and such mobility is economically productive and desirable.

Step 4: Renew the focus on nurturing urban agglomerations by streamlining land transfer procedures and relaxing zoning regulations in existing cities, lowering the regulatory barriers to their redevelopment. Spatial inclusion is less likely to happen in new cities, since they are often disconnected from contiguous urban fabric. Instead, inclusion follows economic growth, which will most likely occur in existing urban areas. To promote the agglomeration and specialization that drive growth, policies should make cities more economically dense. A first step is to make existing urban land markets more efficient.

Step 5: Expand market access for cities by thinning the “thick borders” that inhibit mobility across the Middle East and North Africa, for both regional trade and migration.

For regional trade, add transit links and other critical infrastructure and reduce nontariff barriers. For migration, streamline customs and reduce internal migration controls. Focus on areas near major cities—but also on any lagging areas that have already been targeted for place-based investment. Expanding cities' access to markets will help to expand the fiscal base that can support greater redistribution to lagging areas.

As Step 1 suggests, policy makers are urged to enhance the design and implementation of place-based policies such that they enable markets to take full advantage of three growth drivers associated with economic geography: agglomeration, migration, and specialization. Rather than solely focusing on attracting capital to places where it is scarce, a refined approach should focus on developing the broader ecosystem that can make places attractive for investment while providing the opportunities for people to seek opportunities *wherever* their talents provide the highest returns.

In the long term, making the most of these growth drivers will require reforming core institutions and, in particular, working toward regional integration in the Middle East and North Africa. But in the short to medium term, the five transitional steps should speed economic growth and thus add to the momentum and demand for further spatial convergence. All levels of government—national, provincial, and local—have roles to play.

Fragmented cities, stuck people, walled-off countries: The symptoms of institutional constraints on growth

Today, Middle East and North Africa countries are not notably benefiting from the three spatial dimensions of market-driven economic growth: agglomeration, migration, and specialization. Instead, their economic development is characterized by three striking symptoms of institutional inefficiency, all of which appear widely (though not universally)

across the Mashreq, the Maghreb, and the Gulf Cooperation Council (GCC) subregions:¹

- *Cities are physically and economically fragmented, precluding the economic benefits of agglomeration.* In the large cities of the Middle East and North Africa, planners and policy makers have tended to start anew rather than work within the existing urban fabric. The resulting new cities and modernist neighborhoods do not support the amount of interaction seen in historic districts or in newer informal settlements. A comparison of 20 neighborhoods across 8 of the region's cities shows that intersection density—a proxy for interaction potential—is almost three times higher in historic city centers and informal neighborhoods than in modernist neighborhoods. Planners who put physical form before economic and social function have thus inhibited agglomeration effects.
- *People are spatially and economically stuck in place, lacking tradable skills and therefore limited in mobility.* Around the world, migration from places not doing well to those doing well has been key for economic integration and the reduction of spatial inequalities. And although disparities between subnational regions in the Middle East and North Africa contribute to a 63 percent larger share of total inequality in consumption than elsewhere (see chapter 2), people are stuck in place. In contrast with other parts of the world where higher education generally increases spatial mobility, earning a university degree in the Middle East and North Africa does not make a person more likely to migrate. One reason is that higher education confers credentials for coveted local public sector jobs, not tradable skills that are in demand by the private sector. Other reasons analyzed in this report include weak private sector dynamism limiting the economic “pull” of cities and frictions in trade and use of land.²

- *Economies are walled off from others, regionally and globally, by many barriers that governments in the Middle East and North Africa have created—or failed to remove.* Compared with Europe or East Asia, few countries in the Middle East and North Africa benefit from growth spillovers from their neighbors. Indeed, most export facilities in the region ship raw materials directly to global markets. The automobile production chains that include Morocco are based in Europe, not in the Middle East and North Africa.

Excess centralization, the nature of place-based investments, and weak institutions have created less competitive economic environments than elsewhere in the world

Why are the Middle East and North Africa's urban areas fragmented, its people still stuck in place, and its economies walled off from each other and from the world? These symptoms have historical roots in a legacy of centralized administration and inattention to lagging areas, first under the Ottomans, then under the Western colonial powers (Brixvi, Lust, and Woolcock 2015; World Bank 2011). Since independence, most of the region's countries have ineffectively sought to address this imbalance with interventionist social contracts that focus on state planning and redistribution over market outcomes. While keeping government central and hierarchical, such social contracts make the state responsible not only for service provision but also for other aspects of welfare—including much employment (Yousef 2004). Yet because natural resource rents and foreign aid have limited the need to collect tax revenues, citizen participation in governance is low across the region (Mills and Alhashemi 2018). In short, institutions remain weak even as the public sector dominates markets.

National governments in the Middle East and North Africa have long used public funds and subsidies to bet heavily on sectors and industrial locations—and these development bets shape markets. More than elsewhere,

governments in the region tend to assume an activist role in shaping markets, whether at the national or the neighborhood scale. The preference for place-based investments inspires various interventions, from industrial location regulations to growth poles and new cities. The bets have high stakes: they consume an outsize share of public expenditures. Yet these countries appear to have worse outcomes than their global peers, with isolated exceptions.

Policies that distort markets, spatially or otherwise, usually fall short of their stated goals. Many place-based interventions fail to achieve even their redistribution objectives—and few are well designed and managed for economic growth. Today, the economic environment across the Middle East and North Africa is less efficient and less competitive than those of comparator countries and benchmark regions. On the World Economic Forum's Global Competitiveness Index, most of the region's countries underperform for their income level (Schwab 2017), as further discussed in chapter 4.³

Most countries in the Middle East and North Africa have national strategies that aim to balance growth spatially, bringing economic activity to lagging areas—but at what cost? Even assuming that a given place-based policy can meet its spatial equity and redistribution goals, do those gains justify the associated compromises in economic efficiency? Such trade-offs presuppose careful calibration. However, in the Middle East and North Africa, the pursuit of spatial equity through central planning has skewed spending toward risky supply-driven interventions that do not yield compensating benefits for growth or inclusion. Celebrated successes—such as Dubai and Tangier—are isolated exceptions that prove the rule: all have inherent geographic advantages, and all receive unusually well-coordinated support.

The weakness of national institutions across the region's countries—combined with the state's activist economic role and compounded by high political risk—is deterring outside investment and thus hobbling economic growth and job growth. On the

World Bank's World Governance Indicators, Middle East and North Africa countries score lower across the board than other middle-income and high-income regions.⁴ Executives in the region perceive corruption and inefficient government interventions as the most significant barriers to doing business there. And in the eyes of the world, despite high financial openness, the Middle East and North Africa is economically a pariah region: its countries receive the lowest inflows globally of foreign direct investment (FDI) relative to gross domestic product (GDP).⁵

Across many of the region's countries, a thriving informal sector attests to the economic potential of the poor. The poor have few roles in the formal economy and no real stake in the formal sector, which is largely overseen by the state. The vast importance of informal employment to the poor points to failed policies and to the urgent necessity of institutional reforms. Without new policies that enable formal markets to function more efficiently, the energies of the poor will not be turned to more economically productive uses, and the Middle East and North Africa will not achieve shared prosperity.⁶

When will the region's countries begin to see faster progress on economic growth and spatial inclusion? Not until governments see and harness the economic potential of all and enable factor markets while expanding them through regional integration. Otherwise, the following will occur:

- As long as the region's cities and city systems remain *fragmented*—with masses of potential workers constrained from accessing opportunities and unable to enter the formal economy—they cannot form the economically dense, efficient agglomerations that equip them to create productive jobs and produce goods and services for regional and global markets.
- As long as the region's education systems keep producing *stuck* people—locally credentialed workers with limited tradable, portable skills—the regional labor force will remain small relative to the

population, predominantly local, and lacking in economic mobility.

- As long as the region's countries are *walled off*—disconnected from their regional neighbors and from the world—their cities cannot fulfill their potential: cities need large markets.

Whereas people throughout the Middle East and North Africa still look to the public sector for social services and for jobs, the region would benefit far more from institutional reforms to integrate markets—creating incentives for private investment, skill acquisition, and urban specialization in tradable goods and services. Short of this set of ideal reforms, the region's economies can realize some benefits by better aligning government interventions with policies for efficiency and competitiveness (see chapter 6). This report presents findings on many specific aspects of the region's economic geography (box O.3). For regional policy makers, the challenge is to confront the picture thus revealed and to give due weight to this evidence in their deliberations.

The moment is critical. Choices today can set the next generation on a course either toward more spatially convergent economic growth—or toward further spatial interventions that, in many cases, are likely to fail.

Fragmented cities

To document the institutional constraints on economic growth and inclusion, this report looks at the Middle East and North Africa across three spatial scales: within cities, within countries, and across national boundaries. Why start with cities? Not just because cities drive economic growth globally but also because the region's urban population share is among the highest in the world (box O.4).

In the Middle East and North Africa's cities, the built-up area is on average quite spatially dispersed—a fact likely to increase future development costs and thus limit productivity and welfare. The cost of this fragmentation is borne by all city residents, but it

is especially costly to low-income households. Take the Abdallah family, forced to move from the home they built in İzbit Khayrallah (a well-located and dynamic informal neighborhood in Cairo's center) to the new

government development Masākin Ūthmān on the outskirts of Cairo (TADAMUN 2015).⁷ The move proved hugely expensive for the Abdallahs. It involved transport costs to access current jobs; service costs for

BOX 0.3 Many signs point to one problem: The Middle East and North Africa's economies are not moving sufficiently

Many recent economic findings, reviewed in this report, raise pointed questions about the Middle East and North Africa's slow economic and job growth—and the relation of these indicators to national policies. For example, why do the region's countries receive the world's lowest net inflows of FDI relative to GDP?^a And why are people with university degrees in the Middle East and North Africa no more likely to be hired away from their places of origin than people with only a primary education?^b

Underlying these and many other symptoms is a basic problem that the region's governments have yet to face: for generations, national institutions and

policies have distorted factor markets. Specifically, *place-based policies* have shaped inefficient land markets and discouraged labor-intensive job creation, while *spatial equity policies* and *a reliance on public jobs* have reinforced a local orientation in the labor market and reduced the regional demand for tradable skills. For the region to achieve faster economic growth—and more convergent growth, with economic mobility and shared prosperity—national governments will need to reduce these distortions.

a. The question of low FDI inflows is examined in chapter 3.

b. For discussion of the returns on education, see chapter 2.

BOX 0.4 Drivers and results of high urbanization in the Middle East and North Africa

Urbanization in the Middle East and North Africa has been rapid, driven by economic development as well as by environmental and political crisis. The region's urban population increased fourfold from 1970 to 2010, and forecasts predict that it will double again between 2015 and 2050 (UN-Habitat 2012). The pace of urbanization partly reflects economic development, geography, and migration to oil-rich countries, especially the GCC countries. But it also reflects drought and conflict: in 2018, the Middle East and North Africa contained an estimated 7.2 million refugees, 10.5 million internally displaced persons, and about 15 million economic migrants.^a

The region's countries nevertheless display varying urbanization shares and urban growth rates resulting from varying confluences of factors. Today's urban population share ranges from

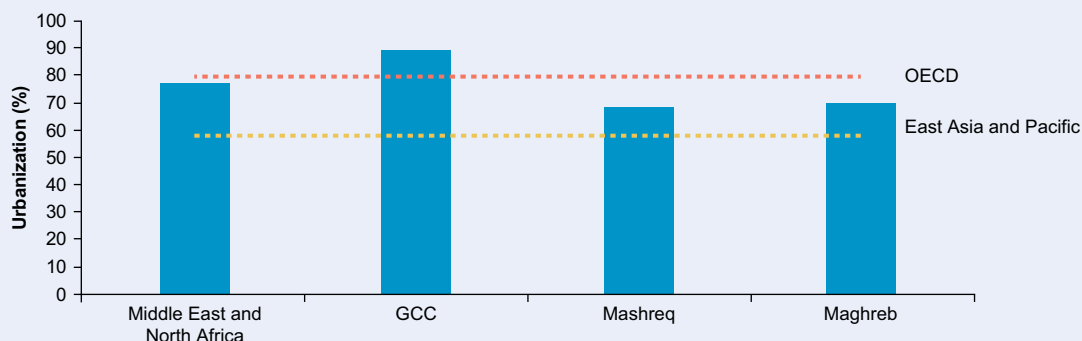
43 percent in Egypt to around 80 percent in the most urbanized countries of the GCC and about 87 percent in Lebanon.^b Among three major Middle East and North Africa subregions—the Mashreq, the Maghreb, and the GCC—the Maghreb now has the lowest national urban growth rates (less than 2 percent a year on average).

The Mashreq is seeing faster urban growth, driven in part by refugees. Economic migration to the cities of the Mashreq and the Maghreb has been chiefly internal and partly climate-driven as migrants are pushed out of rural areas where agriculture is suffering from higher temperatures (UN-Habitat 2012). By contrast, migration to the GCC “city-states” (such as Bahrain, Kuwait, and Qatar) has come mostly from abroad, especially during the oil price boom of 2003–13.

box continues next page

BOX 0.4 Drivers and results of high urbanization in the Middle East and North Africa (continued)

FIGURE BO.4.1 The Middle East and North Africa is a highly urbanized region



Source: World Development Indicators Database 2016.

Note: "Urbanization" is measured as the percentage of total population living in urban areas. The orange dashed line designates the Organisation for Economic Co-operation and Development (OECD) average. The yellow dashed line designates the East Asia and Pacific average. Maghreb refers to Algeria, Libya, Morocco, and Tunisia; Mashreq to the Arab Republic of Egypt, Iraq, Jordan, Lebanon, the Syrian Arab Republic, and West Bank and Gaza; and the Gulf Cooperation Council (GCC) to Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

a. Refugee data from the UN Refugee Agency (UNHCR) 2018 database: <http://reporting.unhcr.org/node/36>.

b. In some countries, the definition of what constitutes "urban" contributes to significant disparities in reporting of urbanization versus agglomeration index levels—the latter being a metric of urbanization that classifies *economic density* using standardized criteria for population density, the population of a "large" urban center, and travel time to that urban center.

amenities that were limited and thus more expensive in the new city; and the cost of losing the family's social network. Significant hardships resulted.

Although cities in the Middle East and North Africa are not equally fragmented (box O.5), many are quite fragmented in population density and the layout of physical structures, especially when controlling for population.⁸

Within a city, spatial dispersion and fragmentation make networked infrastructure and service provision costlier. They also make job matching less efficient and formal housing more difficult to provide. In a highly fragmented city, firms are less likely to quickly find people with the right skills. And low-density neighborhoods may indicate lost opportunities for infill development, contributing to dysfunction in the formal housing market. For example, most Egyptians cannot

afford formal housing, in part because planning and building standards are rigid and outdated. In Cairo, formal housing units are reported to be 20–30 percent vacant—even as 70 percent of the city's population occupies informal housing (World Bank 2012).

The spatial fragmentation of many cities in the Middle East and North Africa reflects both long-term and short-term growth patterns. Thus, Amman's layout has become more linear with the expansion of Zarqa, a nearby industrial town. But low-density informal settlements have also increased spatial fragmentation in Amman as well as in other refugee destinations, such as Baghdad.

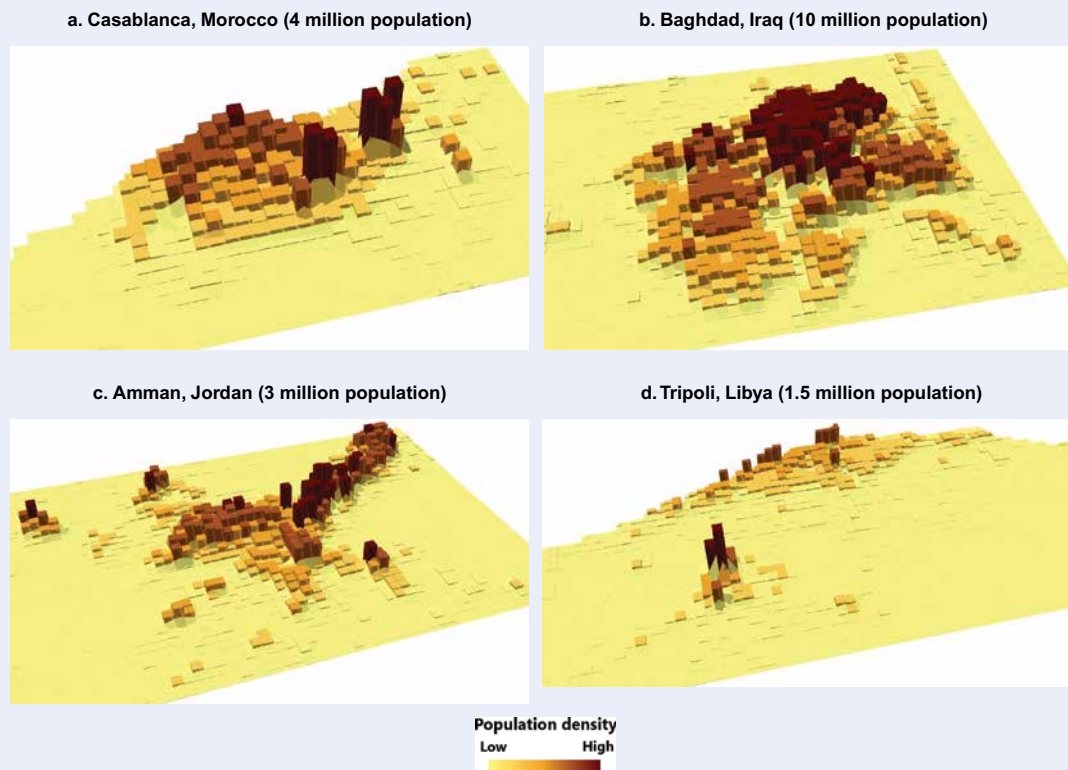
In the long term, modernist urban planning in the Middle East and North Africa has increased spatial dispersion, fragmentation, and infrastructure costs—a pattern that continues today. The low-density urban plans of the modernist era assumed horizontal

BOX 0.5 In the Middle East and North Africa, some cities are more spatially fragmented than others

In the Middle East and North Africa, Casablanca and Baghdad have a fairly high potential for interaction among residents: people are more spatially concentrated than fragmented (figure BO.5.1,

panels a and b). In contrast, Amman and Tripoli have linear layouts and less concentrated populations (figure BO.5.1, panels c and d).

FIGURE BO.5.1 Fragmentation varies significantly across urban areas of several capital cities in the Middle East and North Africa



Source: Developed from LandScan Global 2012 dataset, Oak Ridge National Laboratory, <https://landscan.ornl.gov/>.

Note: Fragmentation is represented by the distribution of population within urban areas. (Each square represents population density per square kilometer.) For a detailed analysis, see chapter 1.

expansion and private car travel. Globally, many cities now reject such plans and promote density through vertical and infill development. Yet most of the region's cities have not adopted policies for density.

In the GCC subregion, city centers are being replaced with business and commercial

districts. And urban expansion in the GCC is nearly as likely to occur through leapfrog development as through infill—while in the Maghreb subregion, infill development is also rare, and extension development is the norm (figure O.1). Leapfrog and extension development both tend to increase a city's

infrastructure costs—leapfrog development more so.

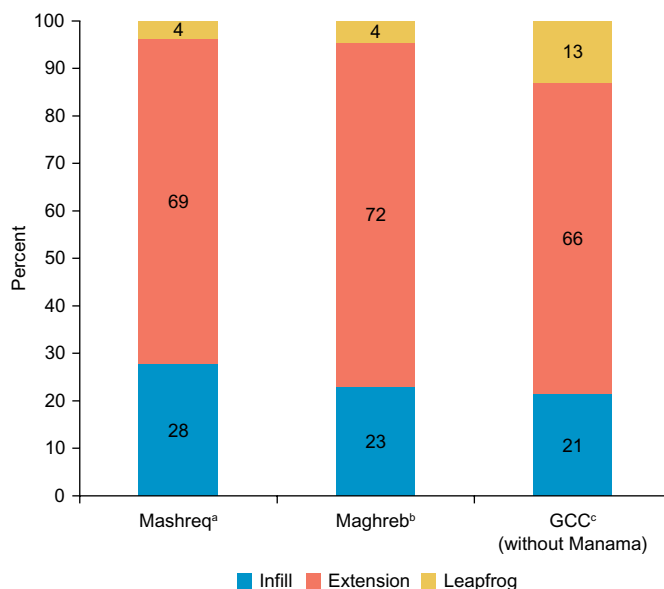
In the short term, the wars and turmoil that have shaken the region since 2010 are transforming many cities, with consequences for their spatial forms and patterns of service delivery. As with past conflicts, such as the Lebanese civil war (box O.6), recent waves of war and unrest have altered urban footprints. Cities in the Mashreq subregion have seen large informal settlements come into being as people flee conflict—in Iraq, Fallujah and Ramadi are two of the country’s fastest-growing urban centers—or as people spill over from refugee camps, such as the 58 established by the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA) for more than 1.5 million such refugees in Jordan, Lebanon, the Syrian Arab Republic, and the West Bank and Gaza (Serageldin, Vigier, and Larsen 2015). In recent years, Jordan’s population growth rate has more than doubled with the refugee influx. Satellite photos show how the city lights of Amman have visibly spread and brightened (see chapter 1, box 1.1).

Across the Middle East and North Africa, informal settlements are spontaneously stitching together the gaps in the urban fabric created by modernist city plans—offering a possible model for formal, planned densification. All but invisible to their governments, the poor build economies of their own. Take the informal areas of Greater Cairo, where about 12 million people lived in 2010: these areas spatially resemble the city’s oldest neighborhoods (photo O.1). Often viewed as relics of medieval squalor, such compact neighborhood structures may in fact represent an approach to reduce future urban spatial fragmentation and limit negative externalities such as air pollution (UN-Habitat 2012).

Stuck people

While fragmented cities limit efficiency and thus reduce workers’ economic prospects, the Middle East and North Africa’s high inequality may also reflect low

FIGURE O.1 Aggregated 1990–2004 urban expansion trends of capital cities in the Mashreq, Maghreb, and GCC subregions show divergent patterns



Sources: Datasets from the European Commission Joint Research Centre’s Global Human Settlement Layers. See Annex 1D for sensitivity analysis.

Note: The analysis uses the Landscape Expansion Index developed by Liu et al. (2010), in which extension and leapfrog expansion increase infrastructure costs, with leapfrog having a higher cost impact.

a. Mashreq comprises the Arab Republic of Egypt, Iraq, Jordan, Lebanon, and the Syrian Arab Republic.

b. Maghreb comprises Algeria, Libya, Morocco, and Tunisia. For Morocco, Casablanca was analyzed instead of the capital city, Rabat.

c. GCC = Gulf Cooperation Council, comprising Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates. Manama, the capital of Bahrain, was excluded because of the bias created by its geographical constraints and resulting in an exceptionally high share of infill urban expansion.

geographic mobility: its people are stuck in place, both spatially and economically. Socioeconomic inequality between areas of most of the region’s countries far exceeds that seen in countries with comparable GDP around the world (figure O.2). This exceptionally high spatial inequality can be related to low spatial mobility. Being located far from a large city also increases business development constraints in the region’s countries (figure O.3).

In most parts of the world, people vote with their feet and move toward opportunity, but this happens less in the Middle East and North Africa (figure O.4).

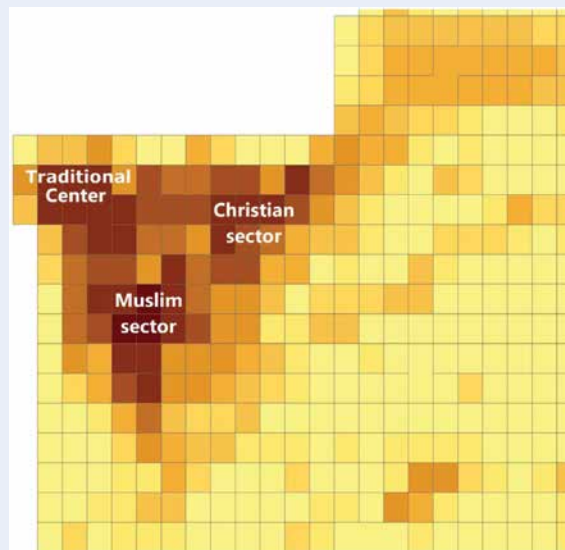
Similarly, around the world, higher education generally increases spatial mobility—but not in the Middle East and North Africa, where earning a university degree

BOX 0.6 Urban fragmentation as a legacy of conflict: Today's polycentric Beirut

In 1975, civil war splintered Beirut into sectarian neighborhoods. The city center, once vibrant, became a no-man's-land. Economic activity relocated to new areas that were defined by firm

owners' religion and ethnicity. The result today is a polycentric city with a Christian sector, a Muslim sector, and the now reoccupied historical center (figure BO.6.1).

FIGURE BO.6.1 After decades of conflict, Beirut became a polycentric city

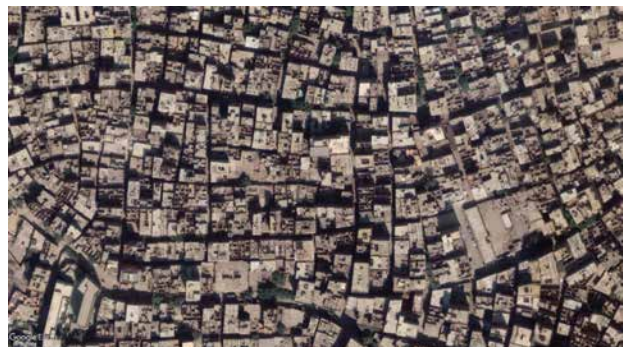


Source: Hanna 2016.
Note: The darker the square, the higher the population density.

PHOTO 0.1 In Greater Cairo, recent informal settlements share a basic spatial structure with medieval neighborhoods

a. Aerial view of Bab el Wazir (established 800 years ago)

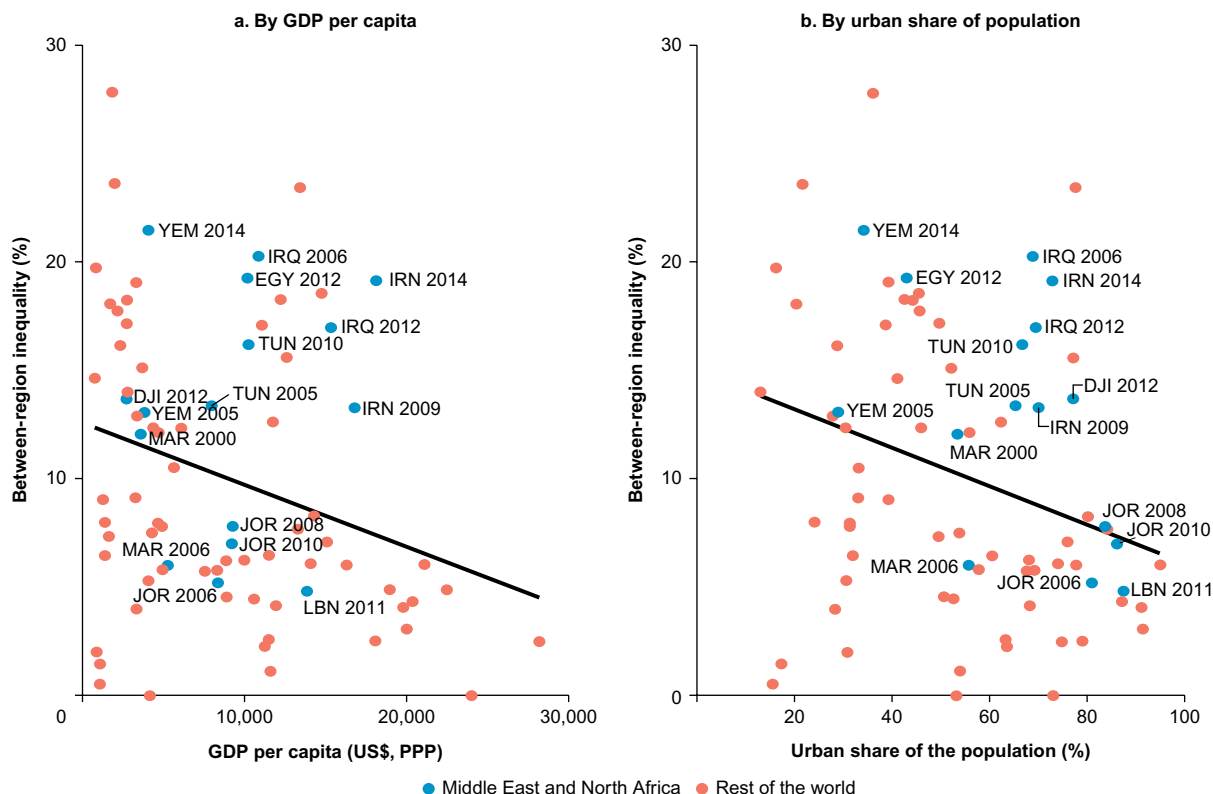
b. Aerial view of Fostat Plateau (established informally in the 1980s)



Sources: UN-Habitat 2012, from Sims 2010; Google Earth satellite images.

FIGURE O.2 Inequality within most Middle East and North Africa countries exceeds that of global peers

Level of inequality in relation to GDP per capita



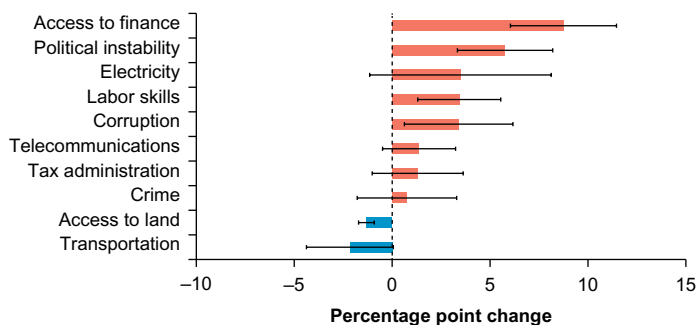
Source: Middle East and North Africa Poverty (MNAPOV) database, Team for Statistical Development, World Bank.
 Note: Each point corresponds to a country's data for a particular year. (Countries represent all income levels. For a list of countries and survey years, see chapter 2, annex 2A.) Inequality between subnational regions was calculated based on a country's first administrative level (for example, governorates, provinces, and so on). PPP = purchasing power parity.

does not make a person more likely to migrate (figure O.5). One explanation is that, in this region, higher education confers credentials for coveted public sector jobs, not the tradable skills in demand by the private sector (box O.7). Notably, women are more likely than men to migrate in Algeria, Egypt, Jordan, Lebanon, Morocco, and Tunisia, which shows that female migrants in those countries are on average more likely to be employed at their destinations (as further discussed in chapter 2).

Across the Middle East and North Africa, rural residents face substantial barriers to migration or have preferences against it—or else they would have migrated already, given the returns to welfare from doing so.

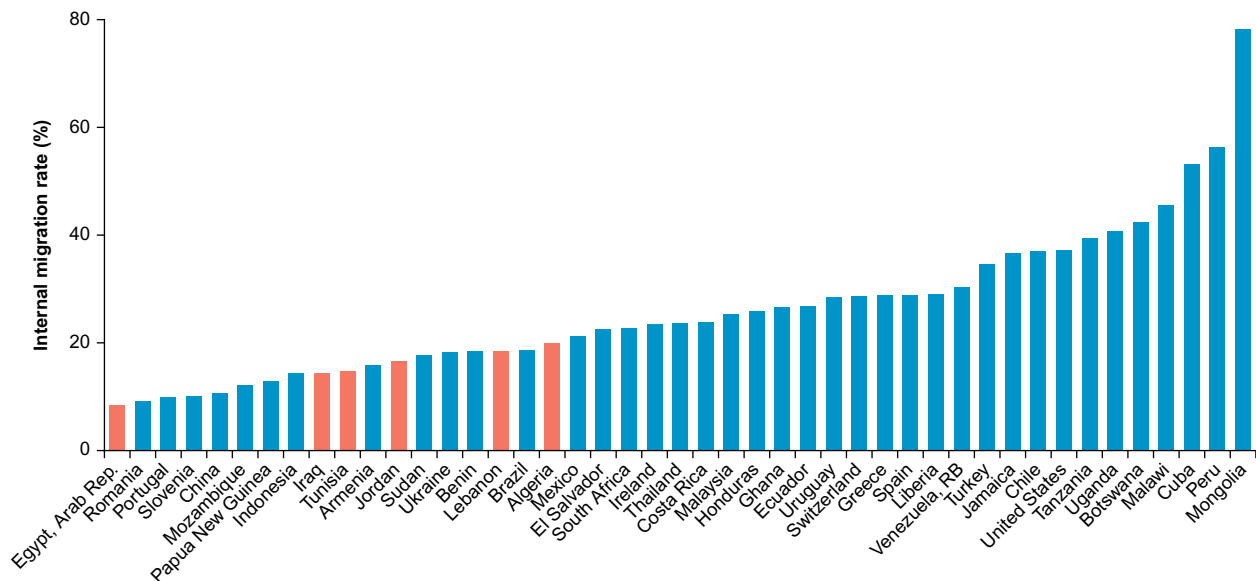
FIGURE O.3 In the Middle East and North Africa, companies located on the periphery face harsher constraints to business development than those in the capital city

Percentage-point change in probability of factor being a major constraint to company on the periphery instead of in the capital



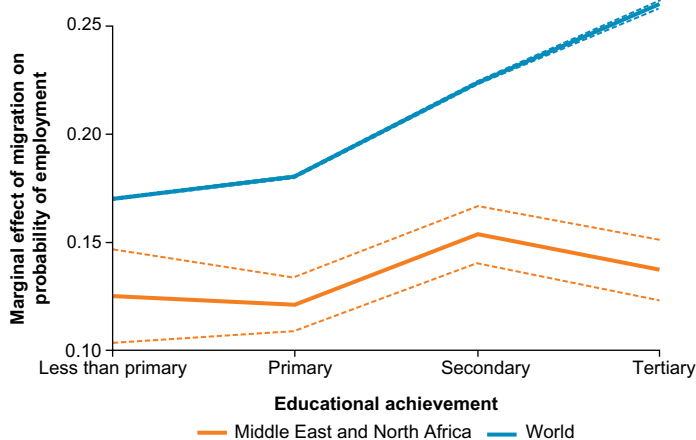
Source: World Bank Enterprise Surveys, 2011–18.
 Note: T-bars indicate 90 percent confidence levels.

FIGURE 0.4 Within-country migration is lower in Middle East and North Africa countries (averaging 14 percent) than in the rest of the world (28 percent)



Sources: Arab Barometer Wave IV (2016–17) data; University of Minnesota’s Integrated Public Use Microdata Series (IPUMS) International database.
 Note: The internal migration rate is the number of lifetime within-country migrants per 100 population. Lifetime migration compares the place of current residence with the place of birth (within the same country). The data are from various years; see chapter 2, annex 2A, table 2A.1. The migration rates in Algeria, the Arab Republic of Egypt, Jordan, Lebanon, Morocco, and Tunisia are computed on the basis of the Arab Barometer Wave IV (2016–17) data; rates for other countries are from latest censuses available on IPUMS in which place of birth was available.

FIGURE 0.5 Globally, the probability of migration tends to rise with education—but not in the Middle East and North Africa



Sources: Arab Barometer Wave IV (2016–17) data; University of Minnesota’s Integrated Public Use Microdata Series (IPUMS) International database.
 Note: Estimations employ a Probit model with controls for gender, age, marital status, employment status, urban or rural residence, education level, and country fixed effects at 90 percent confidence intervals (dashed lines). Migration refers to lifetime internal migration, which compares the place of current residence with the place of birth (within the same country). In this figure, “Middle East and North Africa” comprises Algeria, the Arab Republic of Egypt, Jordan, Lebanon, Morocco, and Tunisia.

An analysis performed for this work of several countries across subregions, using 2006–14 data, shows that living in a metropolitan area brought welfare benefits independent of individual characteristics.⁹ The analysis studies individual characteristics and the returns to these characteristics from living in metropolitan areas of Djibouti (2012), Egypt (2012), the Islamic Republic of Iran (2014), Iraq (2012), Jordan (2010), Morocco (2006), Tunisia (2010), and the Republic of Yemen (2014). The results show that people outside the metropolis were less well-off not simply because of their age, gender, education, marital status, labor force status, water access, electricity access, or possession of a computer. Rather, a substantial part of the welfare gap reflected higher returns to these individual characteristics in metropolitan areas. Similarly, another analysis suggests that across the entire region, if all people were living in capitals—where the returns on their characteristics would be the

BOX 0.7 Low spatial mobility—and high public employment—among university graduates suggest that the Middle East and North Africa’s higher education systems do not impart tradable skills

A university education in Middle East and North Africa countries confers locally valuable credentials—but does it provide marketable skills? Not according to international evidence. Globally, spatial mobility among the educated is a sign of human capital: people with tradable skills are likely to move to places where those skills are in demand (figure BO.7.1). Conversely, the low spatial mobility of the region’s university graduates suggests that their human capital remains low.

This suspicion is strengthened by employment data. In the Middle East and North Africa, a tertiary degree increases the probability of getting a public sector job far more than the probability of working in the private sector (figure BO.7.2). If private sector jobs are lacking for graduates, one reason is that firms require complementarity between human and physical capital investments; they will not invest in a place that lacks a trained, skilled labor force.

FIGURE BO.7.1 Human capital in the form of tradable skills increases spatial mobility

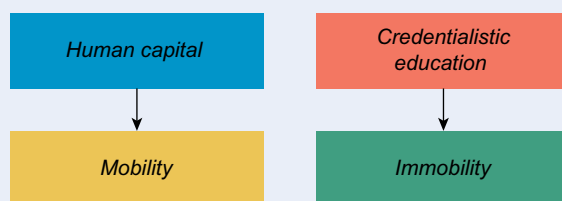
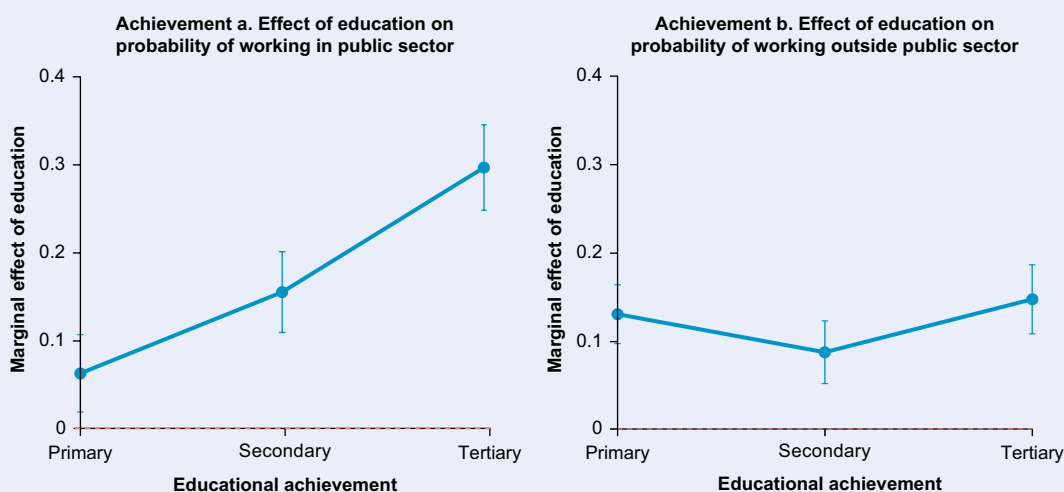


FIGURE BO.7.2 In the Middle East and North Africa, tertiary education diplomas are highly valued in the public sector



Source: Arab Barometer Wave IV 2016–17 data.
 Note: Marginal effects use Probit regressions controlling for urban or rural residence, gender, age, number of children, marital status, and country fixed effects. T-bars indicate 95 percent confidence levels. The regressions were calculated for six countries in the Arab Barometer data: Algeria, the Arab Republic of Egypt, Jordan, Lebanon, Morocco, and Tunisia.

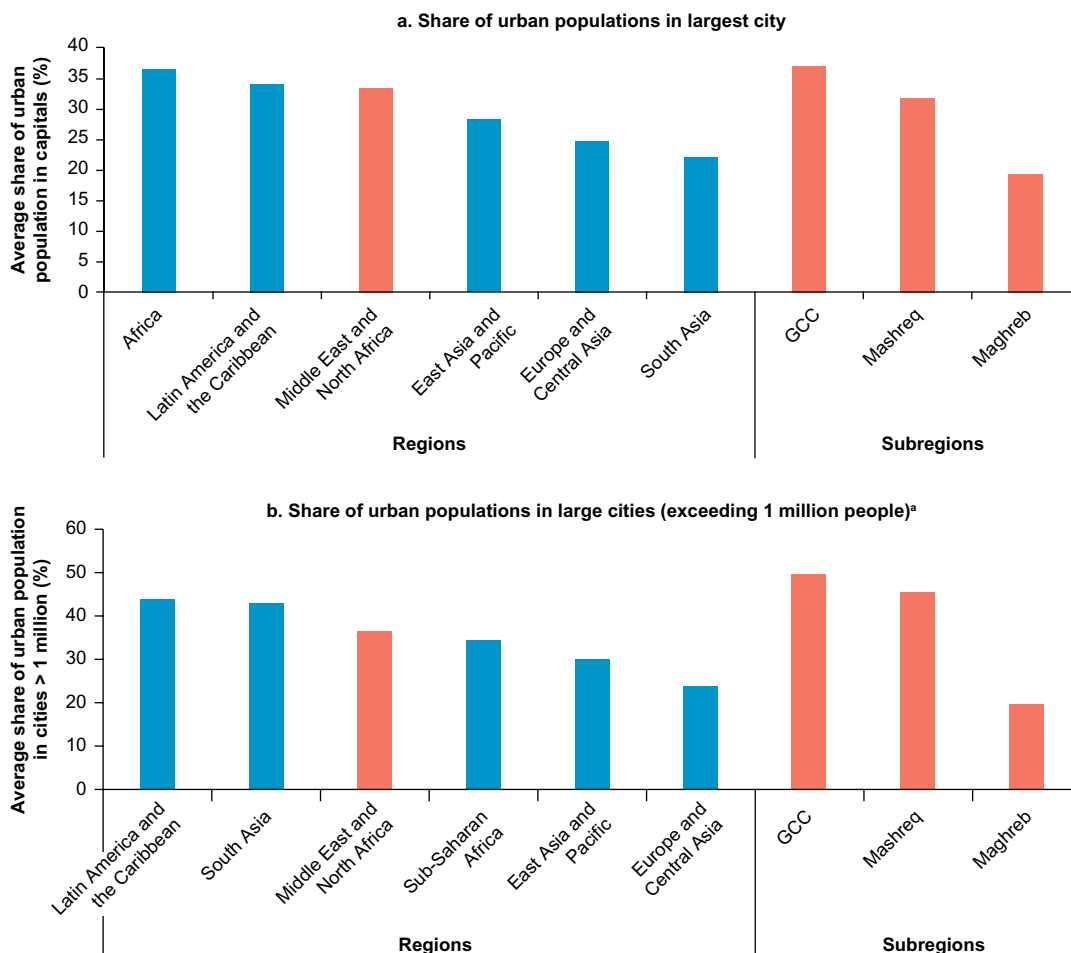
highest—per capita consumption would increase by 37 percent (D'Aoust and Lall, forthcoming).

People in remote areas of Middle East and North Africa countries—especially in the Mashreq and GCC subregions—are stuck partly because their countries lack secondary cities and dynamic private sectors: they live in the long shadow of the capital. Outside the Maghreb subregion, the Middle East and North Africa is dominated by its metropolises. People far from cities lack not only tradable

skills (because of the distorted incentives shaping education systems) but also the nearby markets or infrastructural links to markets that they would need to succeed in business. If not for barriers to migration, many more of these people would have moved to capitals already.

So why do many of the region's countries lack secondary, midsize cities? One reason is another sort of barrier: the “thick borders” that wall off countries, blocking trade and investment.

FIGURE 0.6 Urban populations in the Mashreq and GCC subregions are highly concentrated in the largest city and even more so in large cities (of more than 1 million people)



Sources: 2015 data from United Nations Department of Economic and Social Affairs (UN DESA) World Population Prospects database: <https://population.un.org/wpp/>.
 Note: For subregional figures, the estimates of a few countries were modified, considering the population of the whole agglomerations (which was not always the case in the World Development Indicators dataset). Maghreb refers to Algeria, Libya, Morocco, and Tunisia; Mashreq to the Arab Republic of Egypt, Iraq, Jordan, Lebanon, the Syrian Arab Republic, and West Bank and Gaza; and the Gulf Cooperation Council (GCC) to Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.

a. The country-level figures were computed using either (a) cities of 1 million inhabitants or more, or (b) the share represented by the capital city in countries that had no cities exceeding 1 million inhabitants.

Walled-off countries

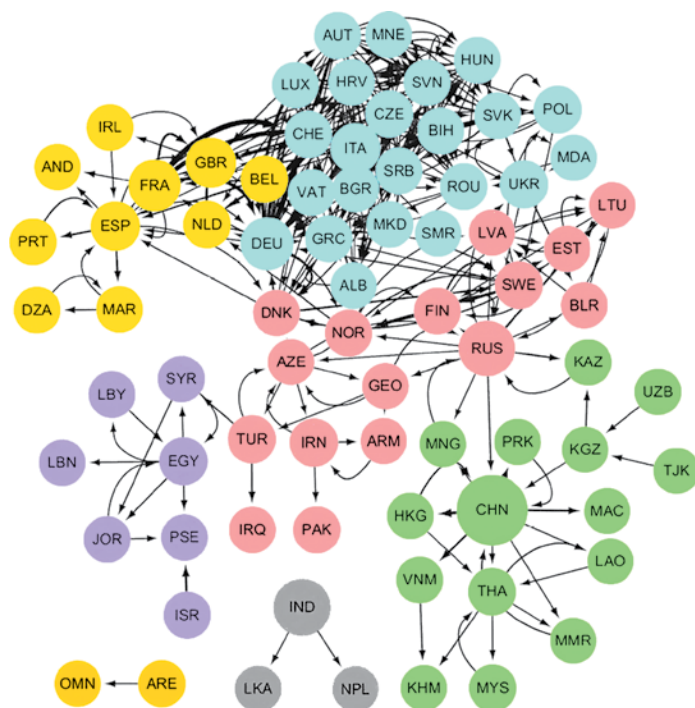
Trade with nearby countries confers economic advantages. But Middle East and North Africa countries are encircled by thick borders that constrain regional trade: onerous customs regimes and visa difficulties, high tariffs and nontariff barriers, regional infrastructure bottlenecks, and customs and logistics inefficiencies. Lacking deep trade agreements, the region's countries are walled off from one another.

Accordingly, firms in these countries trade far less than the region's development levels might imply—and trade among countries within the region is strikingly low. These trade constraints are all the more striking given that the Middle East and North Africa is dominated by its largest cities, which economically should benefit from higher trade volumes. Across the Mashreq and GCC subregions, the share of a country's urban population concentrated in its largest city—termed urban primacy—is among the highest in the world (figure O.6, panel a). And in these subregions, cities of more than 1 million people contain even higher urban population shares (figure O.6, panel b). Yet because the region's large cities lack access to regional or global markets, they fall short of their economic potential.

As a rule, large cities need large markets to be productive and drive economic growth. That is because agglomeration effects presuppose scale. So, the specialized production tasks that make up links in global value chains tend to be concentrated in large urban agglomerations. In the Middle East and North Africa, though, the economic reach of large cities appears to be confined to domestic markets.

Although trade levels averaged across the Middle East and North Africa seem roughly in line with the region's share of global GDP, this statistic is deceptive: the region's trade consists disproportionately of fuel exports. Trade in electricity, by contrast, is less widespread in this region's countries than throughout much of the world (figure O.7).

FIGURE O.7 Few Middle East and North Africa countries trade electricity



Source: Ji et al. 2016, based on the United Nations International Trade Statistics Database (UN Comtrade) electricity trade statistics (<http://comtrade.un.org>).

Note: Figure illustrates the Eurasian electricity trade network in 2010. Arrows indicate an electricity trading relationship between two countries. Full country names correspond to ISO 3 country codes. Colors indicate seven "communities" as defined by Ji et al. (2016): "A community in the electricity trade network consists of a group of nations tightly connected by electricity trade. Changes in one nation have more effects on nations within the same community than on nations outside the community." The Middle East and North Africa countries are spread over four of these communities.

In addition, when firms in the Middle East and North Africa trade across borders, the returns are lower than expected: firm-level data show that the region's exporting firms are no more productive than the firms that do not export. And when its manufacturing firms import critical intermediate inputs, they pay a large and statistically significant productivity premium (Francis and Schweiger 2017). These patterns hint at an economic environment where access is privileged; where firms face barriers to entry, even if their operations may be more efficient; and where countries impose high barriers to buying goods from abroad.

Logistics inefficiencies appear especially challenging—more so, for example, than infrastructure (as discussed further in chapter 6). In 2018, most Middle East and

North Africa countries fell in the middle or lower range of the World Bank's Logistics Performance Index of 160 countries. Among them, three Maghreb states (Tunisia, Morocco, and Algeria) scored between 105 and 117. Exceptions included the GCC countries and Israel, which ranked fairly high across logistics indicators, followed by Egypt and the Islamic Republic of Iran.¹⁰

A country whose major cities are cut off from regional markets loses the opportunity to reap positive spillovers from neighboring countries. Ideally, a favorably endowed and fast-growing country with good policies should add to regional demand for workers,

capital, and knowledge. Nearby countries should accelerate their growth—creating a virtuous cycle of spillovers—and expanding regional markets should enable firms in connected countries to benefit from scale economies.¹¹ Because Middle East and North Africa countries lack deep trade agreements with their neighbors and trade facilitation is limited, the region's large cities are missing out on these spillover benefits (box O.8).

Other regions—notably Europe and East Asia—have made regional trade a key driver of economic growth, while Middle East and North Africa continues to suffer from high restrictions on movements of

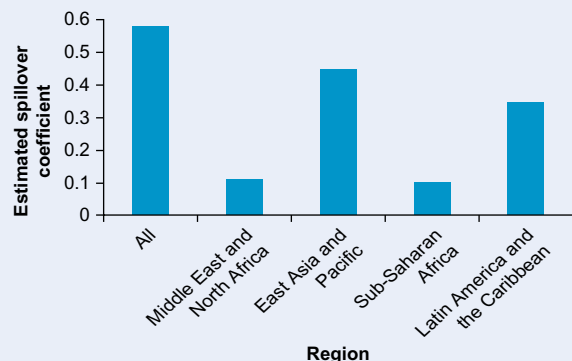
BOX O.8 Large cities in the Middle East and North Africa show few spillover benefits from regional trade

The spatial economic analysis in chapter 3 shows that the positive spillovers to the Middle East and North Africa's large urban areas from regional trade are negligible (figure BO.8.1). In contrast, such spillovers are positive across all countries globally—and strongly positive in East Asia and Pacific countries with regional integration.

Given lower economic spillovers for neighbors in the Middle East and North Africa than elsewhere

in the world, what would happen to economic output in a city from another region with greater spillovers if it were instead in the Middle East and North Africa? A counterfactual for Bangkok is revealing. If Bangkok were in the Middle East and North Africa, its per capita GDP is estimated to drop from approximately US\$12,000 to US\$9,000 (figure BO.8.2).

FIGURE BO.8.1 Spatial economic spillovers to large city economies based on deep trade agreements with neighbors, by region

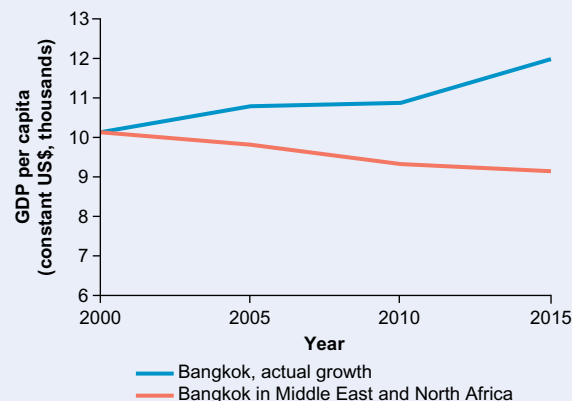


Source: Lebrand 2019.

Note: The dependent variable is city GDP. Figure excludes Europe and Central Asia because the analysis of that region is less relevant to the Middle East and North Africa given the economic differences between the two zones. Also excluded is South Asia because of the small number of observations for the region, rendering the results insignificant.

FIGURE BO.8.2 Bangkok's per capita GDP would have shrunk had it experienced the regional economic spillovers of the Middle East and North Africa

GDP simulation for Bangkok without regional economic spillovers, 2000–15



Source: Lebrand 2019.

goods and people. With increased market access, nonfuel exports could grow. Given the size of many national economies in the region, the regional service trade could be much higher. Countries could buy and sell much more electricity. Unfortunately, conflict and vested interests in many of the region's countries make comprehensive regional integration unlikely in the short term.

Because of thick national borders, Middle East and North Africa cities generally lack access to the large markets they need. To gain such access, the region's countries that border the European Union (EU)—a large world market—can enter its supply chain through trade agreements. So far, Morocco and Tunisia have benefited from this (although trade volumes are still low). The need for such agreements arises from the absence of a large regional anchor economy, as Western Europe was for Eastern Europe after 1990 or as Japan (succeeded later by the Republic of Korea) was for China and other East Asian neighbors. In the long term, regional integration should be a goal of Middle East and North Africa policy makers. Right now, more trade with Europe does not imply less trade within the Middle East and North Africa; the two are complementary.

Place-based and centralized: How national policies and institutions in the Middle East and North Africa perpetuate economic inefficiency and spatial inequity

How does the Middle East and North Africa's fractured economic geography today reflect the impact of state interventions in factor markets, combined with the regional legacies of centralized administration and service provision? How have central governments shaped the region's land, labor, and skill markets economically and spatially at the city, country, and regional levels? What does the persistence of highly centralized government contribute to these spatially and economically distortive dynamics? This section looks at national preferences for place-based investments

and centralized public goods management, assessing their implications for prosperity and welfare.

Place-based interventions in the Middle East and North Africa are distortive while yielding low returns

Public interventions in the economy may be *institution-based*, *people-based*, or *place-based*. Those that are *institution-based* support governance, trade, and functioning markets. Those that are *people-based* support human capital, from health and nutrition to higher education and skill development. In contrast to both these types, *place-based* interventions are often designed to improve development outcomes in particular locations—whether directly through infrastructure investments or indirectly through incentives, subsidies, and regulations.

Place-based interventions, while often well-intentioned to overcome market and coordination failures, typically distort factor markets, limiting economic efficiency by reducing the power of demand to drive specialization and agglomeration. Land markets are hobbled by heavy regulations on land use, which bottle up demand for both residential and industrial structures. Labor markets shrink with disincentives to migrate and to acquire tradable skills: Why specialize and migrate for a relatively high-productivity job in a distant city when you can hope that the state will one day lavish its largesse on your rural province? And private capital follows the lead of policy makers rather than seeking and meeting demand from domestic consumers and international business partners.

In the Middle East and North Africa's cities, many neighborhoods and livelihoods are strongly shaped by place-based policies—and not for the better. Favored policies include heavy zoning and location regulations as well as the construction of modernist neighborhoods and cities from scratch—often deterring formal redevelopment. In response, poor urban residents and migrants develop residential neighborhoods informally. The result is the spatially and socially fragmented city, a

symptom of market and coordination failures (figure O.8).

Within Middle East and North Africa's countries, place-based investments typically loom large in the national budget—not the usual pattern for middle-income countries. The place-based, or spatially targeted, interventions often used in the region include

- Physical infrastructure investments;
- Capital subsidies and other fiscal incentives;
- Subsidies to places such as growth poles and industrial districts;
- Regulation of where industries may locate production; and
- Public sector industrialization, with central planning of investment locations.

Compared with institution-based and people-based policies, these place-based policies consume an outsize share of country investment expenditures in the region (box O.9). When resources flow so freely to place-based interventions, vital investments in institutions and people must be neglected or deferred. In effect, governments place large bets on specific locations and hope for a stroke of luck. Yet place-based interventions have a poor track record in the region's countries (box O.10).

From a regional perspective, place-based investments discourage the formation of

secondary cities that can specialize and trade with neighboring markets—as well as that of efficient agglomerations, which large cities need if they are to serve large international markets. Rather than fostering specialized production centers and economically dense agglomerations to meet market demands, the supply-driven initiatives used by the region's governments to attract private sector investment have done the opposite. Take Tunisia, which used incentives to attract domestic and foreign firms such as Benetton to lagging interior areas: as soon as the incentives expired, many firms closed their operations (World Bank 2018a). Generally, place-based firm location initiatives in the Middle East and North Africa have delivered few jobs, and many apparent success stories have proven elusive.

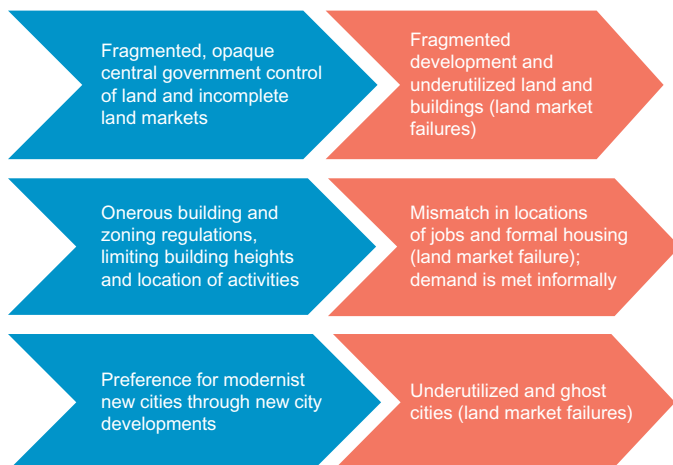
Since the 1950s, as the region's national governments have persisted in shaping markets directly through place-based policies, lagging areas have stubbornly remained behind. Governments initially adopted activist territorial development policies to answer the needs and grievances of neglected areas. Strongly spatial in their focus, such policies had two main aims: to direct compensatory support to the areas left behind and to create new geographic centers for economic activity. But lasting successes—such as Dubai and Tangier (box O.11)—are few and far between.

In cities, within countries, and throughout the region, place-based policies have yielded low economic returns—yet in spite of lessons like Tunisia's, Middle East and North Africa countries continue to rely on such policies. Indeed, several of the region's governments are increasing incentives and transfers for investments in lagging areas, new cities, and industrial development zones without rethinking their approach.

Why bet so much on policies with such unpromising track records? Four reasons stand out:

- *Vested interests.* Despite a spatial intervention's limited returns to the local and national economy, some groups may stand to gain considerably from it.

FIGURE O.8 Place-based interventions distort urban markets—which then fail

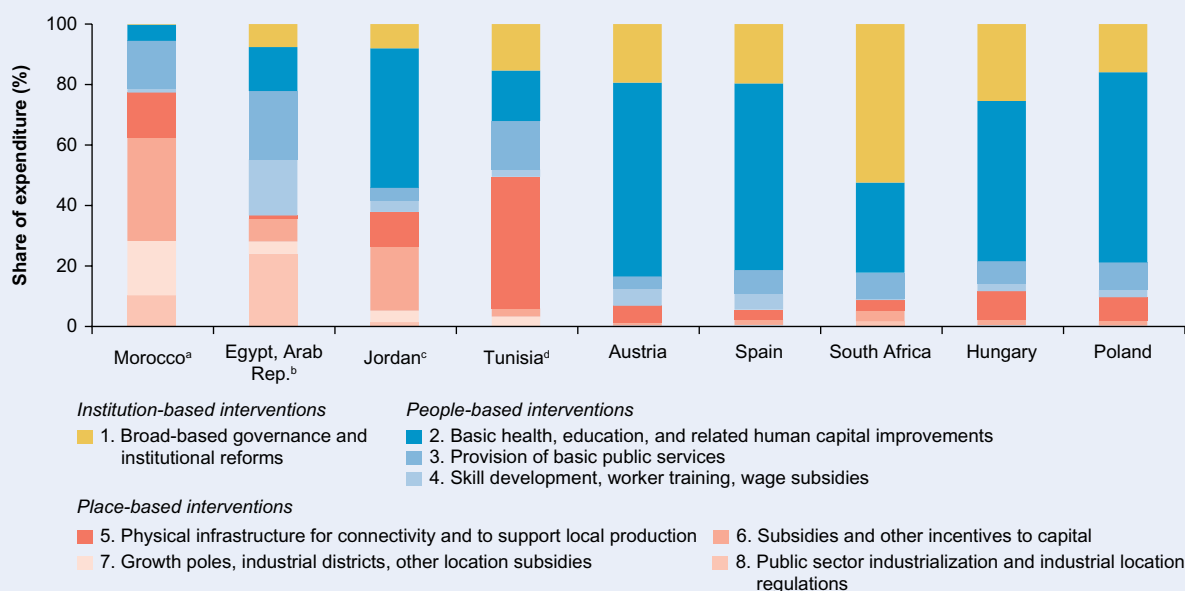


BOX 0.9 Middle East and North Africa countries stand out in directing a large share of investment expenditures toward place-based interventions

Across the Middle East and North Africa, a larger share of public expenditures—including initial investments and recurrent expenditures—are channeled toward place-based interventions than toward institution-based or people-based interventions. In contrast, states outside the Middle East

and North Africa spend less on spatially distortive interventions and more on investments in institutions and people. This pattern is illustrated in analyzing expenditure distributions for one year for several Middle East and North Africa and comparator countries for illustrative purposes.

FIGURE BO.9.1 Government expenditure distribution in selected Middle East and North Africa countries, by spatial category, differs greatly from international comparators



Source: Government Finance Statistics (GFS) database, International Monetary Fund; government data for Middle East and North Africa countries (as described in notes below).

Note: The GFS database does not include data for Middle East and North Africa countries except for partial data for the United Arab Emirates. For Middle East and North Africa countries, report team analysis was based on national data as described in notes a–d:

a. Morocco information came from the 2017 Finance Law, specifically the “General Budget” and the “Public Establishments and Enterprises” segments.

b. Egypt on-budget data came from the Financial Statement 2018–19, and the total expenses of the 48 economic authorities were retrieved from their 2016–17 financial statements from the Ministry of Finance website.

c. Jordan information came from “Capital and Current Expenses (2018),” classified by all line ministries, reported by the General Budget Department of the Ministry of Finance.

d. The Tunisia analysis considers the most recent five-year plan, the Development Plan 2016–20, and in chapter 4, further analysis is provided drawn from the 2017 Finance Law.

- *Path of least resistance.* Investments in vacant land may present policy makers with a course of least resistance, sparking less opposition than reforms affecting developed areas.
- *Lack of credible evidence.* Little concrete information may be readily available on the failures (and the rare successes) of territorial development policies in the Middle East and North Africa.
- *Extrapolating from rare success stories.* Successes such as Dubai and Tangier may inspire hope for replication. Yet the success may not be clearly replicable. Or even more likely, policies may not be carefully designed to account for challenges and complementary factors.

BOX 0.10 Place-based investments amount to risky development bets—and the stakes are high

Most place-based investments in Middle East and North Africa countries have been supply-driven rather than demand-driven. As a result, they have led to inefficiencies. Consider the poor track record of Egypt's 20th-century new cities. In the 23 new cities created from 1979 to 2000, the total population today is less than 800,000—a fraction of the targeted 20 million—and some cities are still unoccupied (Sims 2015). Similarly, Saudi Arabia's established "desert cities" remain unoccupied or house a fraction of their target populations.

Even so, the region's governments keep betting on new cities and vast capital investments. Egypt allocated 30 percent of its 2015–16 national built environment budget to new cities and zones that hosted only 2 percent of the country's population. In contrast, just 29 percent of that budget went toward existing cities and towns hosting 98 percent of the population (Sims 2015). And Saudi Arabia, with its balanced territorial development policy, allocated about 30 percent of its 2017 budget to developing eight planned new cities (see chapter 4, table 4.2).

BOX 0.11 How to make successful spatial bets? Build on natural advantage

Dubai and Tangier stand out as rare successes among the many spatial development bets made by Middle East and North Africa countries. What made these two spatially targeted policies succeed? And what lessons can the region's policy makers take from them to improve their own spatial bets? The answer, broadly, is that both Dubai and Tangier have been blessed with geographic advantages—and their governments introduced institutional reforms, and public investments, that enabled these cities to leverage those advantages.

Dubai benefited from its strategic location at the crossroads between continents. In the early 1900s—even before the 1950s oil discovery in the United Arab Emirates—Dubai was declared a free port, and Dubai Creek served as a trading post for deep-sea merchants. As demand for port services increased, the government of Dubai embarked on an expansion of port facilities that led to the establishment of Port Rashid and later Jebel Ali Port at the end of the 1970s.

In parallel, the government launched Dubai's first free zone at Jebel Ali Port in the early 1980s. The zone was governed by a legal framework that addressed a range of issues raised by investors and allowed local as well as foreign investments to be made in a business environment comparable to any in the world for private sector development. This helped demand for port services to skyrocket at Jebel Ali Port as

well as Port Rashid (jointly managed by Dubai Ports Authority until Port Rashid was closed). Today it is the biggest port between Rotterdam and Singapore and dominates the Arabian Gulf. Based on its success, the government launched many other free zones, each with institutional reforms oriented toward the specific industries Dubai sought to attract to its city.

Likewise, the Moroccan government recognized substantial unrealized potential in Tangier, driven by its strategic geographic location at a historical crossroads of the Middle East, Africa, and Europe. In 2002, the government of Morocco recognized that it could better leverage this locational advantage. It established Tangier-Med Port Authority and invested €1 billion to develop and expand the port and develop the surrounding city and region. The project was developed as part of an integrated framework, supporting the development of four critical sectors:

- Transport infrastructure in roads and rail
- Industrial and logistics free-trade zones
- Training and education of the local workforce
- Collaboration across levels of government agencies and private sector stakeholders to spur international investment.

The Tangier area was also governed by an alternative legal framework that addressed core institutional

BOX 0.11 How to make successful spatial bets? Build on natural advantage *(continued)*

and business environment challenges elsewhere in the country. The development and expansion of the port boosted manufacturing, resulting in 28 percent employment growth over 2002–04 and an annual increase of investment of 13.2 percent (Kulenovic et al. 2015). Improvements in supply chain links, diversification of the local and regional economy, and production increases in manufacturing-intensive sectors such as the automotive industry all benefited from port growth. As a result, the region evolved from being one of Morocco’s most lagging in 2000 to one of the most leading today.

Because the advantages of market access cannot be spread equally across a territory, spatial initiatives must be sensitive to a place’s distinct advantages and potential. Most important is to ask whether a place is suitable to agglomerations. Efficient economies are not evenly distributed in space; rather, they are lumpy, with economic activity clustered in economically dense places—cities, leading areas, and regional economic hubs—and places naturally situated at a crossroads between continents, such as Dubai and Tangier.

Seen in a broader historical perspective, the region’s governments have used place-based policies to offer visible responses to subnational grievances and citizens’ expectation that the state will provide jobs. In a region with some of the world’s worst rates of unemployment and labor force participation, and with episodes of violent conflict and terrorism, governments have identified jobs and stability as central policy goals. Surveys show that citizens across various Middle East and North Africa countries have come to regard the state’s main function as providing jobs—not as providing services and not as providing a voice to citizens (figure O.9).

In practice, public policies that distort factor markets tend to undermine social stability by inhibiting private sector and job development. Policies to shape factor markets are likely to foster a vicious cycle of worse job and inclusion environments. Other distortions are less intentional—reflecting decisions that are centralized, yet uncoordinated, and insufficiently guided by a holistic view of needs across areas. Unless territorial development policy is guided by a strong territorial planning framework (World Bank 2018b), lagging areas are unlikely to get the specific help they need to develop their economies through specialization and agglomeration.

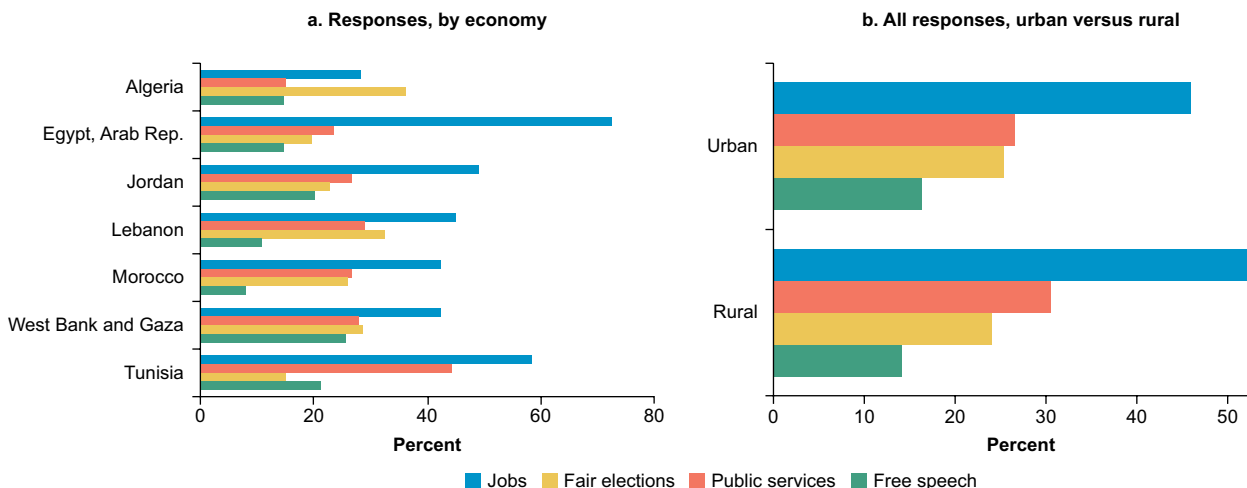
Public investment decisions and service provision in Middle East and North Africa countries are still overly centralized—making spatial convergence through place-based policy even more unlikely

Centralized decision making and budgeting can limit the efficiency of place-based efforts to increase spatial equity. Spatial convergence policies are likely to fail wherever public investment allocation is centralized—especially if budgeting is also opaque, politicized, or unpredictable. In some Middle East and North Africa countries, sectoral and subnational investment expenditures flow to areas with the greatest bargaining power, as in Egypt (World Bank 2012). Thus, grants and transfers are too often directed to leading rather than lagging areas. Even budget allocation formulas risk being biased toward wealthier areas, such as those with natural resources (World Bank 2016).

Centralized service provision, too, can limit spatial convergence—both within cities and within countries. Top-down arrangements typically cause service delivery to be less efficient in places that are less connected to the center, especially poor urban neighborhoods (including informal settlements) or

FIGURE 0.9 Respondents in surveyed Middle East and North Africa economies identified jobs enablement—not public service provision or citizen representation—as the most essential function of a democratic state

Percentage of respondents selecting answers in multiple-choice format



Source: Arab Barometer Wave IV (2016) data.

Note: Percentages add up to more than 100 because they reflect respondents' selection of one statement from each of four sets of answers to the question (Wave IV, no. 515): "If you have to choose only one from each of the four sets of statements that I am going to read, which one would you choose as the most essential characteristics of a democracy?" Categories shown summarize each choice described.

lagging areas of countries. In the Middle East and North Africa, most public services remain overly centralized, including health and education (though the United Arab Emirates is a rare exception in education [World Bank 2018d]).

When different neighborhoods or areas contain citizens with heterogeneous preferences, these differences make centralized administration even more inefficient. Whether within cities or within countries, residents of different areas may differ greatly in their preferences. If so, efficient service delivery will require local involvement, as emphasized in *World Development Report 2004: Making Services Work for Poor People* (World Bank 2003). The same is true for subnational areas.

Further, decentralized service provision can allow for experimentation and for leveraging a variety of service delivery models that allow, through the use of digital technologies and alternative institutional arrangements, more efficient service provision to marginalized populations. For low-density areas, providing mobile services—for example, mobile health units and mobile

schools—can reduce costs and improve access (Boex et al. 2016; Chambers, Wild, and Foresti 2013). For such areas, policy makers need to expand the connectedness of providers and clients: for instance, they could improve accessibility to services through distance learning with radio and cellphones. Other options include having nonstate service providers fill service gaps and training community members to deliver services themselves. For water and electricity provisions, off-grid or off-network solutions, such as local independent water providers or local generators for power provision may be more feasible because of the different levels of scale sensitivity of different types of infrastructure.

Although Middle East and North Africa countries are rightly concerned about spatial disparities in service provision, the prevailing response—territorial development policy directed from the capital—may be perpetuating poor outcomes and distrust of the state. Empirical studies link citizens' trust in government to their perceptions of government performance (Brixi, Lust, and Woolcock 2015).

Recently, countries including Lebanon and Tunisia have embraced initiatives to decentralize local services—a welcome challenge to the Ottoman and colonial legacy of centralized administration. Still, the bulk of service provision in the Middle East and North Africa that could be managed subnationally is not yet decentralized and remains, at best, deconcentrated, with local decisions assigned to remote arms of the central government.

Five transitional steps to reduce institutional inefficiency, speed the Middle East and North Africa's economic development, and enable convergent growth

Can Middle East and North Africa governments steer from today's spatial symptoms and distortions—rooted in institutional inefficiencies—toward a more productive economic landscape, with faster growth and a prospect of spatial convergence? Yes, if policy makers end their overemphasis on traditional place-based development, supply-driven investments, and centralized investment decisions and service provision.

But that is not likely to happen all at once. The following five transitional steps can help policy makers chart a gradual path from territorial development policies that are predominantly place-based and focused on addressing the spatial symptoms of weak economies to ones that address the causes of depressed growth. This would entail a shift away from single-sector, supply-driven, place-based policies to an approach of first mapping a place's inherent economic advantages, then identifying suitable interventions.

Step 1: Adopt new, evidence-based criteria to guide future spatial interventions

Ideally, broad institutional and people-based reforms would make cities more efficient, people more mobile, and countries more connected. But in practice, Middle East

and North Africa governments may remain tied for the short term to spatially targeted initiatives—that is, to place-based policies. To contain the economic damage from these policies, the region's decision makers can, through a new framework, impose criteria on place-based interventions that will make them more efficient (though all are likely to be distortive).

This begins with market size: picking the right policies for each place requires understanding its existing and potential access to markets, which may be domestic or international. Not all places have equal access to domestic markets (including for labor and skills), which are concentrated in economically dense urban agglomerations. And not all places are equally connected to external markets: some have natural advantages such as coasts or borders, while others have better connective infrastructure. Because of varying density and market access, policies that yield high returns in one place may have no impact—or even a harmful impact—in another.

Where place-based policies have already been adopted, this framework would guide decision makers toward supporting it with complements—whether for markets and connectivity or for basic service provision. And those complements should be prioritized based on expressed demand from citizens and firms on what is needed to make those territories effective enabling environments. Yet wherever possible, the approach should also involve transitional steps to reform institutions (such as the other four transitional steps outlined below). And it should focus on enabling agglomeration, migration, and specialization based on a place's natural advantage (as discussed in box O.11). Thus, to enhance market access, locate industrial parks near large cities. Or identify a location's most constrictive trade bottlenecks and then clear them with new connective infrastructure, institutional reforms. Or both.

When considering whether to retain traditional supply-driven, place-based policies or to shift toward this approach, countries

BOX 0.12 Remembering the forgotten: Institution-based policies for the urban poor

The poor of the Middle East and North Africa are, all too often, the region's forgotten people. They lack formal housing and the credentials or connections needed for a formal job. So, they live wherever they must—and work however they can.

The economic dynamism of the poor appears in the informal sector, especially among urban migrants. Their restless economic activity attests to their energy, effort, and ingenuity—but it is not economically efficient. Informal markets are unlikely to generate the specialized scale economies that spur faster, wider growth through trade in goods and services.

To bring poor urban residents and migrants into the formal sector and give them opportunity, countries would first need to reform factor markets. One reason that the region's cities create few opportunities for the poor in the formal sector is that these cities have only weak links to regional and global markets. So, governments should observe informal urban economies for hidden signs of demand and

productive potential within a city's fragmented economic landscape—and should enable formal investment in these hot spots, raising densities and loosening restrictive regulations. Informal settlements point to where labor is in demand and where potential formal sector productivity lies untapped. Policy makers can encourage formal investment in such neighborhoods with institution-based reforms: revising urban plans, relaxing zoning regulations, and allowing higher population densities.

If the urban poor often seem invisible to policy makers, the rural poor are even further from realizing their potential productivity—especially those who live far from cities. In the Mashreq and GCC subregions, the scarcity of secondary cities means that many rural residents cannot access urban markets. More and more of them migrate to the metropolitan capital, not simply because of conflict or climate change but because the investments needed at home are lacking. Once settled in cities, these internal migrants join the informal economy.

should keep one principle firmly in mind: spatial equity arises not from investments in a place but from the economic growth that creates jobs for a country's forgotten people—wherever those jobs may be—paired with policies focused on improving access to basic services for people regardless of their location. Only faster economic growth, with transitional but positive steps toward more efficient institutions, will allow the Middle East and North Africa to harness the economic energies of the poor (box O.12).

Step 2: Devolve greater functional authority and resources for local revenue generation and service provision to local governments

Place-based policies to reduce spatial equity are often undermined by a lack of local authority and resources—whether to

raise revenues, to make investment decisions and allocate expenditures, or to deliver local services. Lagging areas are often the least able to mobilize and manage local revenues, because the central government wields more fiscal control over smaller municipalities than over larger ones. Further, transfers to these localities are often insufficient and lack objective standards, transparency, and predictability. This lack of budget authority, together with the lack of local control over service provision, can undermine the local execution and maintenance of place-based investments—the very investments that are supposed to reduce spatial disparities. In Morocco, for example, a lack of local capacity has caused many municipalities to execute less than 50 percent of their investment plans (World Bank 2018c).

Further, centralized service delivery models make it difficult to offer services tailored

to heterogeneous preferences of citizens through the use of alternative delivery models and digital solutions. The way that functional authority and resources are devolved can and should vary based on economic geography, the current authorizing environment, and the current institutional architecture and historical trajectory. Such reforms, even if gradual and experimental, have proven most likely to succeed when they have ensured that the devolution of functional authority is accompanied by the critical complements of greater resources and capacity support.

Step 3: Step away from credentialist education and toward schooling that cultivates globally tradable skills

Helping stuck people become more spatially and economically mobile could make the region's countries more prosperous—and more stable. Generally, people in underperforming areas around the world migrate to jobs and opportunities. Their choices help to manage excessive population densities in the lagging areas, and it can benefit their relatives in their places of origin.

But in the Middle East and North Africa, fewer people migrate than would be predicted from the welfare gains accruing to migrants. As noted earlier, this immobility results in part from credentialist education that does not impart tradable skills. It also reflects the many frictions that inhibit labor mobility—from land transfer fees to active controls. And it is compounded by strong local identities and identity-related divisions.

Step 4: Renew the focus on nurturing urban agglomerations by streamlining land transfer procedures and relaxing zoning regulations in existing cities, lowering the regulatory barriers to their redevelopment

Making fragmented cities' land markets more efficient will be critical for agglomeration and specialization—two dynamics that amplify factors of production and drive economic growth and jobs. Whether in larger or

in smaller (secondary) cities, agglomeration and specialization require the efficiencies arising from high economic density, or the geographic concentration of economic activity (as discussed earlier in box O.2). Urban economic density and efficiency generally are high if development is spatially compact, dense with people, and transit-oriented—but low if development is sprawling, as with leapfrog development and widely dispersed structures.

One way to make cities more efficient is to reduce local frictions—boosting demand and increasing economic density while also taking care to monitor the externalities (side effects) of economic and population density. Planners and regulators can attract firms to invest in cities by reducing frictions such as

- Impediments to property acquisition and new construction (costs, height limits, and density limits);
- Challenges in local business registration and licensing;
- Limits on news and information; and
- Obstacles to developing local business networks.

All these frictions are pervasive in the Middle East and North Africa and call for policy remedies.

Planners can also address friction affecting households, especially formal housing costs. And they can seek ways to internalize the negative externalities, or social costs, of urban density—for example, by levying congestion charges, repealing fuel subsidies, and improving traffic management.

Efficient city plans must be able to reflect changing demand: if they cannot, frictions, negative externalities, and market failures will result. Governments must, for example, enable zoning and building regulations to evolve with changing social and economic needs. Consider Jordan, where rigid zoning and building regulations impose standards that make housing unaffordable for all but the top 30 percent of the income distribution. More than 70 percent of new housing developed in Jordan is done without a building permit (CAPSUS 2018).

A city's density creates positive externalities in public service delivery, which tends to be more efficient with density—and less so with sprawl. Providing one cubic meter of piped water costs US\$0.70–US\$0.80 in Tunisia's dense urban areas, but it costs US\$2 in sparsely populated areas. Similar differences appear in education and health care costs (World Bank 2014). And in Amman, Jordan, with its rapidly rising population, a World Bank study finds that the cost of new infrastructure through 2030 will depend on whether urban growth is sprawling (low density) or compact (high density). The study concludes that sprawling growth—the pattern of the recent past—will cost 14 times as much as compact growth (World Bank 2018b). Nevertheless, urban plans cannot simply pursue density but must also attend to service quality: where density is too high, service quality can decline (a negative externality from congestion).

Step 5: Expand market access for cities by thinning the “thick borders” that inhibit mobility across the Middle East and North Africa, both for regional trade and for migration

Historically, Middle East and North Africa cities were part of economically central global trade networks. Many of these cities persist in modern times as large, often vastly populated urban areas. Yet with today's thick borders, their economic reach has been limited. Countries across the region today need to enhance links across national borders—reducing tariffs and nontariff barriers, easing movements of goods and people—though at the same time they may also enact policies to strengthen domestic markets.

Expanding the market regionally would help firms in small countries benefit from scale economies in production, including better access to inputs. It is also likely to support secondary cities that can be interlocutors with cross-border economies. Consider what can happen if Jordan and

Egypt start trading more with each other following a decrease in border restrictions. As further discussed in chapter 6, a simulation exercise based on a quantitative economic geography model examined the implications of reducing border crossing times from 50 hours to 20 hours. There are major welfare benefits in South Sinai (Egypt) and around Aqaba (Jordan) from increases in market access. Greater market access can also introduce greater competition by promoting technology upgrading and greater productivity, often facilitated by cross-border investment. And it could trigger the emergence of regional production networks, leading to greater intraindustry trade within the region and allowing growth in one country to spill over to its neighbors.

Increasing the spatial mobility of people makes especially good sense for the Middle East and North Africa, not just because of how migration benefits migrants and their families but also because the alternative—growing productive jobs in lagging areas through place-based policy—is not broadly feasible. Policies to increase both spatial and economic mobility in the region's countries could adopt three central priorities: building skills and human capital, reducing frictions in spatial movement, and finding ways to manage social divisions.

The most urgent priority for making people more mobile is, arguably, to reorient education toward tradable skills (assuming first that health care, water and sanitation, and basic education are present). Next is to reduce the frictions that hinder spatial and economic mobility, including

- Low job market information, with high job search costs;
- High fees for land or property transfers;
- High permit fees for construction;
- Restrictive building regulations; and
- Government controls that limit internal migration.

Finally, social divisions related to identity—in some cases a strong local identity—can

pose the greatest challenge to policy makers. Where intractable social divisions prevent labor mobility, place-based policies could in some cases be justified.

Some may see labor mobility as undesirable, given the challenge the region's cities face in absorbing migrants (including refugees). But leaving people stuck is not a pragmatic alternative. Efforts to induce growth in lagging areas face an even more unyielding challenge: lumpy economic landscapes are persistent. For poverty to be rapidly and sustainably reduced, people must be able to move where the jobs are.

The prospects for regional integration: Distant yet vital to the Middle East and North Africa

This overview has recommended five transitional steps toward more efficient spatial investments and initiatives to promote faster growth and eventual spatial convergence. In the longer term, the Middle East and North Africa should envision regional integration that will break down walls between countries; connect firms to larger markets; and foster ever-larger scale and agglomeration economies that are specialized for tradable goods and services. All of the region's countries would gain from such integration—just as some are already gaining from trade agreements with large markets elsewhere.

Although the prospects for the Middle East and North Africa's regional integration may seem remote today, the subject bears discussing because of the high stakes of regional trade. Cooperation among the region's countries today is strikingly weak, but not for any known structural reason. A more apparent cause lies in political tensions and violent conflict. The upshot of today's scant cooperation is clear: the Middle East and North Africa's economies produce less than they could by trading more—and more freely—with each other.

Closer regional integration has been a long-stated objective of the region's countries, and there have been a number of initiatives.

But the economic impacts of those efforts have been minor, especially when compared with those in other world regions. Apart from natural resource exports, trade and integration with the rest of the world have also remained below potential, with such notable exceptions as Morocco's automobile sector.

Regional integration and global trade are complementary, so both should be pursued. Both expand product markets: regional integration also increases supply capacity in large part by enlarging input (factor) markets, and global integration facilitates investment and access to technology and know-how. Deeper trade agreements that the EU is negotiating with Morocco and Tunisia could perhaps become templates for similar cooperation between neighbors.

Ultimately, effective steps to closer regional integration will always require giving up some sovereignty to regional institutions that set and enforce certain rules. So far, governments of the Middle East and North Africa have not been willing to transfer regulatory powers to regional institutions that would govern intraregional trade. But steps can be taken today that do not require giving up sovereignty or giving it up only in limited areas. Such steps would help to build the trust and experience to promote more comprehensive integration later. Initial examples involving different types of policy instruments could initially involve just two or a few neighboring countries, as follows:

- Tariffs have mostly been removed within the Pan-Arab Free Trade Area, but trade costs remain relatively high because of nontariff measures and transport prices. Information about nontariff measures is scarce, but they mostly represent red tape and cause major complaints. They contribute to the Middle East and North Africa's low scores on logistics performance. Transport prices would fall if more competition were allowed in logistics and restrictions to operations in neighboring countries were reduced.

- Institutions could be established in limited areas where contributions and benefits can be more clearly defined and a transfer of some sovereignty is therefore more acceptable. For example, regional electricity pools, a regional transport authority, or, where willingness of countries is greater, even a competition authority or dispute settlement mechanism would be possible.
- Cross-border integration of physical infrastructure is generally quite acceptable, but there is often little coordination in upgrading transport links on different sides of a border. A clear, long-term vision for regional transport integration could guide future investments including, in the longer term, reestablishing or newly constructing rail links in the region and consolidating port operations where several smaller ports currently operate.

Although prospects for formal integration may remain uncertain, spatially sensitive physical infrastructure investments that connect neighbors can create conditions for later growth to spread. Again, places with access to large markets—whether in existing urban agglomerations or potentially through regional and global trade—are the most favorable to scale economies and specialization.

Regional integration for the Middle East and North Africa can be broadly envisioned as a six-point plan.

- *Make the business climate more favorable and state functions more efficient.* Institution-based reforms to speed government processes—and to make doing business easier across the region—would be a prerequisite for integration.
- *Reduce tariffs and nontariff barriers.* Tariff reductions would be accompanied by the removal of inefficient subsidies (such as energy subsidies) with care to address regressive impacts of removal.
- *Liberalize the logistics sector.* Private sector logistics firms would replace today's inefficient state monopolies. Morocco offers a model with its logistics zones, elimination of regulatory barriers, and introduction of new customs regimes suitable for logistics activities (Rouis and Tabor 2013).
- *Reform customs regimes.* Customs procedures would be streamlined and customs regulations harmonized across borders with private sector participation (as in logistics), and border control information would be shared internationally.
- *Fill infrastructure gaps.* Connective infrastructure—perhaps on the emerging model of a development corridor anchored by transport links (roads, rail, and ports)—would involve not just paving roads and laying rail but also ensuring an environment that benefits the wider economy, with incentives for development.
- *Ensure compensation for relative losers.* Gains from integration should more than suffice to compensate those who may end up worse off as a result of trade.

Notes

1. The Maghreb subregion includes Algeria, Libya, Morocco, and Tunisia. The Mashreq subregion includes Egypt, Iraq, Jordan, Lebanon, the Syrian Arab Republic, and West Bank and Gaza.
2. These and other reasons are being further analyzed in forthcoming World Bank Middle East and North Africa reports.
3. The GCC countries are no exception: most score below their income peers.
4. Data from the World Governance Indicators Database, <https://info.worldbank.org/governance/wgi/>.
5. Data from the World Development Indicators Database: <https://databank.worldbank.org/source/world-development-indicators>.
6. Even middle-income citizens in Middle East and North Africa countries participate extensively in the informal economy. Their resources, too, could be used more productively if factor markets in the formal sector were more efficient.
7. Actual names of the interviewees in the TADAMUN (2015) report, “The Hidden Cost of Displacement,” have been withheld.

8. The potential-of-interaction method (De la Roca and Puga 2017) measures the average number of people within a given distance from any spot in the city. To capture the practical likelihood of interpersonal interaction, one can control for city population, and one can also control for GDP—an inverse proxy for the cost burden of commuting. Controlling for both, cities in the Mashreq and GCC subregions have some of the world’s highest potentials for interaction, making the average across all Middle East and North Africa cities still quite high. But controlling for population alone (that is, disregarding the commuting advantage conferred by higher GDP), the average city in the region appears more fragmented.
9. The welfare aggregate (in most countries comprising total food and nonfood expenditures) was temporally and spatially deflated to account for price differences over time and between areas.
10. See the World Bank Logistics Performance Index (LPI) 2018: <https://lpi.worldbank.org/>.
11. Close proximity remains advantageous in buyer-supplier networks despite the rapid decline in global transport costs.

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Policy makers across the Middle East and North Africa have for many years articulated plans to integrate their people spatially and economically. Wishing to bring communities together and narrow economic gaps, governments have made large capital investments in transport corridors and “new cities.” Hoping to provide jobs in places with little economic activity, governments have designated new industrial zones supported by spatially targeted business incentives.

Yet the results of these place-based initiatives in the region have largely underdelivered in terms of yielding more sustainable jobs and growth. Spatial inequality contributes to a 63 percent larger share of inequality in this region than in any other region. Sharp disparities remain between capital cities and lagging areas, as well as between richer and poorer sections within cities. Across much of the region, a fortunate few are connected to opportunities, while many more people are marginal to the formal economy—or live outside of it.

Convergence: Five Critical Steps toward Integrating Lagging and Leading Areas in the Middle East and North Africa considers the numerous and varied challenges. It explains that many of these place-based policies are ineffective because they treat the spatial and physical symptoms of inequity rather than its root causes, which are economic and institutional.

Convergence presents the five roots of spatial inequity in institutional inefficiencies across the Middle East and North Africa—urban regulatory frictions, credentialist education systems, centralized control over local public services, barriers to the spatial mobility of goods and people, and barriers to market entry and lopsided business environments—within cities, within countries, and across national borders. It proposes five transitional steps to enable convergence informed by economic geography:

- Strengthen coordination and complementarities across initiatives.
- Redistribute roles and responsibilities across tiers of government.
- Enable mobility of people between lagging and leading areas.
- Build dense and connected cities.
- Enhance market access nationally and regionally.