

Characteristics and Prospects of Development of «Shadow Economy» of Arab Countries

The issues of «shadow economy» have always been of significant research interest to economists. Among well-known foreign scientists researching «shadow economy» is Friedrich Schneider. Hernando de Soto worked on the terminology and economic essence of this notion and described in details the causes of the evolvment and development of illegal economy in Peru in his book «The Other Path». Currently, there is no single definition to the notion of «shadow economy», as well as the unified methodological database of its volume calculation, the data given on Arab countries are not homogeneous. The methods used for the volume calculation of «shadow economy» have wide enough variety: from «direct» (research method, method of Tax and Financial Audit), to «indirect» (calculation of the difference between official and actual data on the amount of work force, national expenditures and incomes, MIMIC model, etc.), in the calculations applied in the above methods empirical data are used. Latest data on the calculation of «shadow economy» of some Arab countries given in the studies are dated 2005–2006, so, they do not take into account the events of last 10 years that were occurring in the Middle East.

The structure of «shadow economy» in any country is practically the same, including the corrupt component, tax evasion, illegal migration, smuggling highly illegal narcotics and human trafficking. In fact, the reduction of legal production sector, outflows of cash abroad, including money transfers of individuals, fraudulent transactions, can serve as a catalyst for increase in the volume of « shadow economy».

The Arab spring, the military actions in Libya, Yemen, Syria, Iraq negatively influenced the economy of Arab countries, including the Arab Gulf monarchies. The above events have resulted in the increase in the smuggling of drugs and psychotropic substances and the growing volume of illegal labor migration and slave trade. According to Global Slavery Index «2,54 per cent or approximately three quarters of a million people are slaves in the Middle East and in North Africa». According to some reports, income from slave trade was from \$US34 billion to \$US150 billion. The amount of migration flows has increased due to the Syrian events. According to ILO (International Labor Organization) by the end of 2015 32 million migrants arrived in the Arab Gulf countries, 10 per cent of labor migrants from all over the world are hosted by KSA and the UAE, more than 80 per cent of the population of Qatar and the UAE is labor migrants.

Large volumes of money transfers by migrants, for instance, from such countries as Bahrain, Kuwait, Oman, Qatar, the UAE, KSA amount to \$US100 billion. Concerning corruption in Arab countries it is necessary to mention that the essence of the notion

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«corruption» is not fixed as strictly in Arab countries as in Western ones. Many «additional» payments, for instance, for starting business are practically legal on the territory of some Arab countries¹, besides, investment codes of Arab countries imply control participation of locals in the work of foreign businesses (civil servants or law enforcement officials and security forces officials often serve as co-owners).

The calculation of the volumes of «shadow economy» in Western countries is often produced by some economists on the amounts of tax payments and revenues. The equivalent figure for Arab countries is not main at the fact that many members of the middle class (in Western economic understanding of this term) perform their activities without using CRE, accounting or other monitoring tools with the help of which it is possible to determine business turnover, and tax base and the level of taxation.

To consider the overall economic situation of some Arab countries, below in Table 1 indicators are given.

- CPI – Corruption Perceptions Index (2015) whose calculation is produced by Transparency International. Evaluation criteria: 0 – the highest rate of corruption perception, 100 – the lowest rate of corruption perception;
- Failed States Index (2015) – the composite indicator describing the ability (and disability) of authorities to control the territorial integrity, and demographic, political and economic situation in the country. Evaluation criteria: 10–30 – reliable, 40–60 – stable, 70–90 – warning, 100–120 – alarming.
- CRP – country risk premium – country risk. The risk that investors face in deciding on the investment in sovereign countries. It reflects economic, financial, political and institutional factors and depends on many political events which can cause significant losses in the cost and quality of investments. According to the country risk assessment map PwC (2016), all countries of the Middle East have «very high» rate of country risk, except the Persian Gulf countries, as they have «very low» rate of country risk. Tunisia, Jordan and Morocco also have «high» rate of country risk.

Table 1

Summary on the Countries in the Middle East (Corruption Perceptions Index, Failed States Index, Country Risk, Volume of «Shadow Economy»)

Countries	CPI (100)	Country risk premium	Failed States Index (FSI)	Volume of “Shadow Economy” (per cent) (2007/2015) ²
1	2	3	4	5
Qatar	71	0,77 Per cent	50	18,4/20
UAE	70	0,77 Per cent	50	23,5/20

¹ For instance, additional «tax or payment» paid in a lump sum to an owner of buildings by a tenant in Jordan

² Data for the period of 2011-2015 from unofficial sources. It is necessary to mention that data on some Persian Gulf countries are absent, but it would be useful to assume that they will equal to 20%. Data for 2007 (except Qatar, the UAE, Bahrain, Kuwait, Oman - data for 2005) from the study by Friedrich Schneider. The Shadow Economy and Work in the Shadow: What Do We (Not) Know?. Discussion Paper No. 6423 - IZA DP - March 2012. – Available from: <http://ftp.iza.org/dp6423.pdf>.

Countries	CPI (100)	Country risk premium	Failed States Index (FSI)	Volume of “Shadow Economy” (per cent) (2007/2015) ²
1	2	3	4	5
Jordan	53	6,95 Per cent	80	17,2/44
KSA	52	0,93 Per cent	50	16,8/20
Bahrain	51	3,40 Per cent	50	17,1/20
Kuwait	49	0,77 Per cent	50	17,9/20
Oman	45	1,09 Per cent	50	17,6/20
Tunisia	38	5,56 Per cent	80	35,4/50
Egypt	36	10,05 Per cent	90	33,1/60
Morocco	36	3,86 Per cent	80	33,1/44
Algeria	36	-	80	31,2/60
Lebanon	28	8,50 Per cent	90	32/20–25
Iraq	16	-	110	-/67
Libya	16	-	100	30,9/30–40
Syria	18	-	110	18,5/80
Yemen	18	-	110	26,8/60–80

Prospects of development of «shadow economy» in Arab countries are dependent from the development of the political situation in Syria. The Syrian conflict is geographically local, but economically it is international or global. ISIS operating in the territory of Syria and Iraq (*terrorist organization prohibited in Russian Federation*) is a living example of «shadow economy» which has a negative impact on the activities of countries MENA. Besides ending of the armed conflicts, reduction of illegal human, financial flows, drug trafficking, etc., one of the factors of decreasing of the volume of «shadow economy» is the formation of the middle class in Arab countries (small and medium-sized businesses) which will grow through the action of authorities in financial, tax and social policies. The state must work for people, and not for the enrichment of bureaucracy; according to Sheikh Zayed bin Sultan Al Nahayan: «No governor can be happy when their people are poor and unhappy».

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