By building up the private sector and free market economies, the European Bank for Reconstruction and Development will help to foster democracy in the Arab Spring countries.

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In his second article, Thomas Mirow, President of the European Bank for Reconstruction and Development (EBRD) argues that one of the most pressing economic problems in the Arab Spring countries is the lack of an independent and competitive private sector. With cautious privatization and the building up of the free market economy, the EBRD hopes to foster democracy by building up the number of people who feel they have an important stake in their country's future.

The most pressing economic problem for many of the Arab Spring countries and the region is that it has been unable to develop a private sector that is independent, competitive and integrated with global markets. In Egypt, Tunisia, Morocco and Jordan the European Bank for Reconstruction and Development will be focusing on supporting the private sector. In fact, the countries of the region have relatively few private companies, under a third of the number per person in our existing Eastern European countries of operations. The state is the dominating force in the economy.

We will be working hard to remedy that, just as we have done in the former communist world. Strikingly, companies in the southern and eastern Mediterranean are often not part of global supply chains. There is also much less intra-regional trade than there should be. In fact, inter Arab trade, is virtually at the same level as fifty years ago, in terms of the overall percentage of exports. There are too many non-tariff barriers, as well as too much regulation and poor infrastructure. According to some recent studies, it costs companies an average of 95 man days a year just to deal with trade bureaucracies. It is more time consuming and more expensive to move goods between two ports in the region than it is to transfer them to Europe or the United States.

In trying to shift the balance away from often state domination of economies, we will be bringing important lessons from our existing countries of operations. After the collapse of communism, there was a rush to privatise state owned companies, with often mixed results. Privatisation was meant to symbolize change – the shift away from central planning to capitalism. However, we now know that efficient privatisation is better than speedy privatisation. There is evidence that speed risks bringing incorrect implementation, inadequate supporting institutions and the danger that the process is hijacked by anti-reformers primarily seeking to consolidate their own position. Insider-dominated privatisation can produce oligarchs that are not concerned with moving towards competitive, free markets. So, when we look at privatisations in the emerging Arab democracies, we will be cautious. We are convinced that private enterprises, on the whole, perform better than state-run firms. This can only happen, though, against a backdrop of well regulated, efficiently supervised markets. That is part of our approach, ensuring that we have the policy dialogue with governments to bring this about.

All these challenges are not new to us. Just as we have done in Eastern Europe, we will be engaging in that policy dialogue with governments in Egypt, Tunisia, Jordan and Morocco. We work very hard to modernise the business environment. There is no point in us trying to build up small and medium sized enterprises if they are cut down by over regulation and outdated rules. Apparently, the average Middle Eastern firm is ten years older than in eastern Europe because the barriers to new entrants are so high. Contributing to the dismantling of that disincentive is part of our role.

Again, though, we should accept that the task of making a case for capitalism, for the private sector, has rarely been harder. Over two decades ago, when the Berlin Wall fell, the majority of the newly freed peoples embraced the idea of capitalism. They knew that their old system had failed, communism had not proved superior. The countries of Western Europe felt confident about extolling the capitalist cause as the best way to run an economy, it had delivered growth. Now, of course, that self-confidence is damaged by the crisis of the past four years, the questioning of whether the capitalist model needs to change.

Whatever adjustments are needed, and some clearly are, it does remain the best model, and that belief in the private sector is something that we will stress in our work in our new countries. In nations like Tunisia and Egypt, the private sector, at least its upper segment, is questioned not because there is an alternative such as communism, but because it has become tainted by cronyism. When these countries did try to shift more emphasis from the state to the private sector, it was often well connected insiders who benefitted and became wealthy. The EBRD's efforts will be towards ensuring a much broader private sector and one which underpins the capitalist model.

Our philosophy, as an institution, is simple. By concentrating on building up the private sector and free market economies, we also build up the number of people who feel they have an important stake in their country's future. It is an indirect way of fostering democracy. Eventually, those individuals are so numerous that they want more of a say in the democratic process. They believe that their interests and improved financial circumstances are best served by democracy. This can take years and it is that which we are hoping to promote in the emerging Arab democracies.

So, one year on from the Arab Spring should we feel optimistic about democracy gaining ground in the region? It is a mixed picture. Tunisia began the season of dramatic change and it continues to develop promisingly. It is turning in to a genuinely pluralistic, multi-party system, capped by last winter's successful election. The biggest of the revolutionaries, Egypt, is harder to decipher. It still has to be seen whether the military will step back from both overt and covert control. A Presidential election is due to take place at the end of May and that should give us more insight in to the overall direction of travel.

Then, there are the two monarchies, Jordan and Morocco, which are following an evolutionary rather than a revolutionary model. Power is being handed down from the top. All of those countries understand that there is much at stake, as to try to rein in change is to provoke the wrath of citizens and unrest. That pressure, alone, should make us hopeful that governments or kings will carry on pursuing this new path.

So, our tale of two revolutions – some two decades apart – is a story about both similarities and differences. In both these historic events, there is a need for change and dangers if it is not delivered. In the early 1990s, in Eastern Europe, some countries flirted with the idea of a return to communism as people became disillusioned, including in Russia. There is a worry, too, that in Egypt, Tunisia, Morocco and Jordan, disillusion will lead to extremism and instability. These are concerns, and the burden on us and the rest of the international community is huge. Just as we did two decades ago, we need to convince people that for all the short and medium term pain, the long term gain is worth it.

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This article is based on a talk that Thomas Mirowgave at the LSE's Capstone Showcase ,"Where next for the Arab Spring? Learning from EBRD engagement in Eastern Europe" on 15 March. *Listen to the podcast.*

Note: This article gives the views of the author, and not the position of EUROPP – European Politics and Policy, nor of the London School of Economics.

About the author

Thomas Mirow – *President of the European Bank for Reconstruction and Development*
Thomas Mirow is the fifth president of the European Bank for Reconstruction and Development (EBRD). Mr Mirow has worked as the Assistant and then as Chef de cabinet to former German Chancellor Willy Brandt, then Chairman of Germany's Social Democratic party, and served as Director of the Press Office of the city-state of Hamburg, Mr Mirow held several senior positions within the Hamburg administration between 1991 and 2001, including state minister for economics. He also held several senior management and advisory positions in the private sector. More recently, Mr Mirow was Director General for Economic Policy in the Federal Chancellery in 2005 and appointed State Secretary at the Federal Finance Ministry in November 2005.

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