

unsustainable exchange rate pressures and exposing weaknesses in the financial system. Countries can also be subject to contagion effects—the transmission to the domestic economy of shocks occurring elsewhere in the international economy.

There are important lessons to be drawn from other countries' experience with greater integration into the international financial system: there is no room for complacency, even—or perhaps especially—when economic conditions are good. MENA countries will need to manage carefully the risks that accompany the enormous advantages associated with globalization. Diligence in monitoring risks is crucial. In this regard, efforts to increase transparency in financial and government operations and to disseminate to the public timely and comprehensive data on all aspects of the economy will be key to ensuring successful monitoring by both the private and public sectors and to facilitating rapid policy response by the authorities concerned.

Outlined above are the challenges facing those countries that have already progressed down the road of economic reform. For the second group of countries, those that have yet to embark decisively on this journey, the path is even clearer. Determined action is needed in the short term if they are to set a sound foundation for growth and avoid being marginalized in the rapidly globalizing economy. For some countries, the immediate challenge is to reverse unfavorable macroeconomic and debt dynamics. For others, there is a need to tackle longstanding weaknesses in the structural aspects of their economies, starting with the exchange and payments system, the financial sector, and the regulatory structures.¹⁰

While the initial adjustment is likely to be difficult, the payoff will be large in terms of providing for the basic needs of, and ensuring employment opportunities for, the rapidly growing populations in these countries. Indeed, these countries should draw encouragement from the experience of other economies in MENA. The speed with which the latter have benefited from improvements in investor sentiment—domestic, regional, and international—provides an important demonstration effect as to what is both possible and desirable.

V. Conclusion

Recent economic performance for the region as a whole has been favorable, reflecting not only positive developments in certain aspects of the external environment but, more importantly and increasingly, the pursuit of appropriate domestic policies in many countries. As a result, growth has picked up, inflation has moderated further, and the financial balances—domestic and external—have improved.

Of course, performance has varied across countries in the region. Those implementing sustained, far-reaching reforms have generally fared commensurately better. Others, including those facing particularly difficult noneconomic factors, continue to lag with large immediate and medium-term costs for their population.

¹⁰The main areas of reforms are analyzed in IMF (1996).

Looking to the future, countries in the region will not be able to, and should not, rely on a favorable external environment to spur growth and achieve their broader social and economic objectives: oil price developments over the medium term are unlikely to be as favorable as they have been in the past two years; a comprehensive, just, and durable peace settlement remains elusive; and many countries will continue to be adversely affected by the vagaries of weather. On the other hand, there are many aspects of the global environment that offer promise for the region, particularly globalization and its impact on increasing trade opportunities, enhancing capital flows, and accelerating the transfer of technology and managerial knowhow.

It is clear that MENA countries themselves must take the measures necessary to benefit from the possibilities presented by the evolving global economy. Only by intensifying economic stabilization and market opening reforms will they be in a position to reap the potential benefits of globalization. They will also need to keep in mind that the advantages accompanying greater integration in the global economy bring added risks, for example, sudden reversals of capital flows, and certain limitations on various policy instruments. These are risks that are not only worth taking, but can also be minimized through steadfast economic policy management.

For those countries that have successfully established sound macroeconomic fundamentals, the next steps will involve creating an environment that will encourage higher domestic savings, and larger and more productive investment, which in turn will promote sustainable growth over the longer term. For the remaining countries, success in meeting the needs of the population will only be attained if action is taken now to address the financial imbalances and reduce the structural impediments to high and sustained growth.