Reducing State Socialism in the Middle East

Although precise measures of government ownership across the Middle East and North Africa (MENA) are hard to come by, the governments of Algeria, Egypt, Libya, Syria, and Yemen all operate sizeable segments of their economies—in some cases accounting for more than two-thirds of the GDP. International experience suggests that private ownership tends to outperform public ownership. Yet, as Cato policy analyst Dalibor Rohac writes in **"The Dead Hand of Socialism: State Ownership in the Arab World"** (Policy Analysis no. 753), "MENA countries have made only modest progress toward reducing the share of government ownership." Rohac argues that these countries need to sustain their transitions toward more representative political systems and inclusive economic institutions. "In order to address this problem, privatization has to cease being a dirty word," he writes. Three main lessons emerge from the experience of countries that have done this. First, "transparent privatization, using open and competitive bidding, produces significantly better results than privatization by insiders, without public scrutiny." Second, private ownership and governance of the financial sector is crucial to the success of restructuring. Third, privatization needs to be a part of a broader reform package that would liberalize MENA economies. "If governments in the region are serious about creating mass prosperity, reducing the role of public ownership should be one of their priorities," Rohac concludes.

RISK MODELING RISKS

The U.S. financial system faces a major, yet underappreciated threat from the Federal Reserve's risk modeling agenda—the "Fed stress tests." The purpose of these models is to determine banks' regulatory capital requirements in order to make the financial system safe. But as Kevin Dowd, a professor of finance and economics at Durham University, argues in **"Math Gone Mad: Regulatory Risk Modeling by the Federal Reserve"** (Policy Analysis no. 754), they instead create the potential for a new systemic financial crisis. Risk models, Dowd writes, are subject to a number of major weaknesses. They are usually based on poor assumptions and inadequate data, are vulnerable to gaming, and often blind to major risks. They have difficulty handling market instability and tend to generate risk forecasts that fall as true risks build up. "Most of all, they are based on the naïve belief that

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markets are mathematizable," he adds. The solution to these problems is legislation to prohibit risk modeling by financial regulators and establish a simple, conservative capital standard for banks based on reliable capital ratios instead of unreliable models.

A FALSE SENSE OF INSECURITY

Terrorism is a hazard to human life, and it should be dealt with in a manner similar to that applied to other hazards. Although allowing emotion to overwhelm sensible analysis is both understandable and common, it is inappropriate for officials charged with keeping the public safe. "To do so is irresponsible, and it costs lives," argues John Mueller, senior fellow at the Cato Institute, and Mark G. Stewart, professor at the University of Newcastle, in **"Responsible Counterterrorism Policy"** (Policy Analysis no. 755). Risk analysis is an aid to responsible decisionmaking that has been developed, codified, and applied over the past few decades. The authors deal with four issues central to that approach and apply them to the hazard presented by terrorism: the cost per saved life, acceptable risk, cost-benefit analysis, and risk communication. They find that, at present, decisionmakers appear to be overly fearful about negative reactions to any relaxations of security measures that fail to be cost-effective. "If other uses of the funds available would more effectively save lives, a government obliged to allocate money in a manner that best benefits public safety must explain why spending billions of dollars on security measures with very little proven benefit is something other than a reckless waste of resources," they conclude.

HIDDEN COSTS OF EX-IM

Proponents of reauthorizing the Export-Import Bank claim that by increasing exports and jobs, it benefits the U.S. economy. But as Daniel J. Ikenson, director of the Cato Institute's Herbert A. Stiefel Center for Trade Policy Studies, writes in **"The Export-Import Bank and Its Victims: Which Industries and States Bear the Brunt?"** (Policy Analysis no. 756), the benefits are exaggerated and the costs totally ignored. The Bank's skeptics speak of the opportunity costs that arise when government attempts to allocate resources

according to nonmarket criteria. They also note that subsidies provided for the benefit of one exporter put competing firms at an artificial disadvantage. In addition to these opportunity and intra-industry costs, there is a third set of significant costs that are too often forgotten. This analysis estimates the downstream costs of Ex-Im subsidies that are inflicted on manufacturing firms in every industry across every U.S. state. Ikenson finds that these policies reward some companies in the short run, but penalize many others in the process. "These kinds of data are often obscured or ignored, but they are essential to any informed judgments about the propriety and efficacy of the Export-Import Bank," he concludes.

OPEN AIR

The European Union (EU) and the United States began negotiations for a Transatlantic Trade and Investment Partnership (TTIP) in 2013, with the primary goals of reducing impediments to cross-border trade and investment and achieving greater economic integration between the two economic areas. Curiously, there has been a near absence of discussion in the TTIP negotiations of freeing trade and investment in commercial airline services. In **"Opening the Skies: Put Free Trade in Airline Services on the Transatlantic Trade Agenda"** (Policy Analysis no. 757), Kenneth Button, a professor at George Mason University and a world-renowned expert on transportation policy, notes that air passenger and cargo industries' supply chains are rife with restrictions. "Given the economies of scale and the scope for specialization that increase by enlarging markets, airline services liberalization would markedly increase the gains from an agreement," he writes. This paper argues that the objections to liberalization lack genuine merit and describes some of the benefits that have emerged as aviation markets have been freed up over the last 35 years. It offers insights into how U.S. airline passengers and transportation-consuming businesses would benefit from opening the domestic air market to competition from foreign carriers. Finally, it urges the U.S. and EU governments to put free trade in commercial air services on the TTIP negotiating agenda.

THE PUBLIC ON FEDERALISM

For much of its history, the United States had a notably decentralized government structure. Since the 1930s, the national government has undertaken new efforts to regulate the economy and society and to redistribute resources. Those new efforts have implied a greater centralization of authority in Washington. In the past the public often supported such centralization. But, as John Samples, vice president and publisher of the Cato Institute, and Emily Ekins, polling director at Reason Foundation, find in **"Public Attitudes toward Federalism: The Public's Preference for Renewed Federalism"** (Policy Analysis no. 759), public opinion about federalism has changed. "Voters are more supportive of decentralized policymaking on many issues where they previously supported a stronger national role," they write. This shift indicates profound distrust in the capacity of the federal government to act on behalf of the public good. On some issues, like national defense, much of the public continues to support national primacy. Such issues are often assigned to Washington by the Constitution. In contrast, much polling finds that many citizens believe state and local governments are likely to perform better than Washington. "Americans support a more decentralized federalism than in the past both on particular issues and as a general matter of institutional confidence," Samples and Ekins conclude. ■