

THE LIBYAN ECONOMY : A DESCRIPTIVE ANALYSIS

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Introduction

At the time of national independence, Libyan development prospects appeared to be extremely unpromising. Principally an agricultural economy, cultivation was basically confined to a narrow coastal belt constituting less than three percent of the country's total land area. Primitive techniques and a hostile environment combined to keep agricultural productivity at a low level. Nor did the possibilities of developing other forms of viable economic activity appear encouraging. Libya seemed marked for a destiny of continued dependence upon foreign aid.

Today, however, Libya is a vital, growing economy. Some six years after its initial entry into the petroleum export market in late 1961, Libya now occupies a position of international importance as one of the world's major oil producing nations. Stimulated by the rapid pace of oil development, gross domestic product has risen from a 1958 level of about £L 52 million to over £L 408 million in 1965¹. Continued economic expansion is confidently expected. In the indicated context of dynamic change, this paper presents a descriptive analysis of some of the more salient characteristics of the Libyan economy.

The Dual Economy.

In common with all the developing nations, Libya possesses what could be called a dual economy. A modern market economy has been superimposed upon a traditional subsistence economy. The former has

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1. Kingdom of Libya, Ministry of Economy and Trade, Census and Statistical Department, *Statistical Abstract, 1965* (Tripoli : Census and Statistical Department, 1966), p. 232.

its distinctive characteristics and differs in important respects from, say, the British economy or the modern sector of the Indian economy. However, in its essential operational features, the modern Libyan economy is similar to all market economies and is amenable to the usual tools of analysis.

On the other hand, the traditional economy presents the theorist with possibly insurmountable analytical difficulties. Of particular significance, the traditional sector, although considered as a distinct entity when contrasting it with the modern economy, is actually composed of many non-related parts, e.g., it is doubtful if the level of economic activity in Ghat has any measurable influence upon activity in Kufra.

The multi-component traditional economy is largely based upon subsistence agriculture. Occupational specialization, where it exists, follows conventional lines and is focused on serving the needs of the local community. Organized markets provide an outlet for surplus agricultural output and supplementary goods and services. The geographic and economic scope of the various non-integrated markets is, however, narrowly limited. The specialization that gives necessary rise to economic dependency is only marginally in evidence and the local community, in a basic sense, is self-sufficient.

The isolation of the traditional Libyan community is accentuated by geographical factors. However, this economic insularity is not essentially a geographic phenomenon. In many respects the isolation of the Indian village is equally real although not based upon considerations of physical proximity. Self-sufficiency and specialization are antithetical. The self-sufficient community is necessarily isolated and it is only through the rise of specialization that the need for establishing outside trade relations becomes manifest.

Analytically, the self-sufficiency of the traditional Libyan community constitutes a denial of the existence of economic interdependencies, i.e., integrated markets for the exchange of commodities do not exist. In this context, it would be futile and inappropriate to formulate an

explanatory model that, by its essential nature, implies interdependencies. It may well be impossible to incorporate the traditional economy into an analytical behavioral model, and the conspicuous failure of economic analysis to cope with the problems besetting the developing nations might be explained by this analytical problem. It is perhaps noteworthy that the more successful analyses of development have been broadly sociological in approach.

The Oil Economy.

The most obvious characteristic of the Libyan economy is its rich oil base. About 50 per cent of gross domestic product (or about 70 per cent of gross national product) originates in the petroleum sector. Oil accounts for over 99 per cent of Libya's export revenue and about 75 per cent of gross private capital formation can be assigned to the petroleum sector. Government revenues are principally based upon oil royalty and tax payments. In addition, most of the gains registered in other industrial sectors can be indirectly traced to the stimulus of Libya's rising prominence in the international petroleum market.

Despite its critical importance, the oil prosperity is, in many ways, deceptive. Oil was discovered and developed by foreign interests largely employing imported capital and technical skills. The product flow, crude oil, has been entirely to foreign markets. Although employing some ten thousand Libyans, the oil industry's principal direct contribution to the economy, it can be argued, has simply consisted of providing the government with considerable amounts of once scarce foreign exchange.

Government oil revenues have replaced foreign financial assistance. And, as with foreign financial aid, oil revenues do not directly increase the productive capacity of the economy. The foreign exchange that is earned does, however, allow for increased imports and does give the government a greater relative command over goods and services. Appropriately directed, the increased financial resources do offer possibilities for expanding domestic production. At the same time, the potential dangers of inflation become more real.

The Absorptive Capacity of Capital and the Entrepreneurial Tradition.

Some of the earlier treatments of economic development emphasized capital scarcity as the underlying factor leading to the observed wide disparities in the wealth of nations. It is more fashionable today to view the developing economy in terms of its ability to absorb capital, i.e., in terms of the available investment opportunities that yield a sufficient return to attract capital. In this context, the dichotomy between the traditional and modern economies is of critical importance. As would be expected, capital is scarce and its absorptive capacity is low in the traditional sectors of the economy. The lack of an effectively integrated market mechanism, i.e., the absence of economic interdependencies, can be said to imply this conclusion.

Focusing attention on the modern sector, the opportunities for profitable investment have been reasonably ample. However, aside from oil, the modern Libyan economy is more or less limited to four industrial sectors, viz., construction, transportation, trade, and services. Within these sectors, relatively large amounts of domestic capital have been forthcoming. The capital needs of the oil sector, on the other hand, have been primarily satisfied from foreign sources.

The shortcoming of the Libyan economy, albeit understandable, has been the inability to widen the modern sector. As presently constituted, the modern economy has been largely limited to those activities which are directly or indirectly related to oil or the government demands arising from oil receipts. Thus, for example, in 1964 over 75 per cent of the reported value of construction arose in the government and oil sectors.² Based on less reliable statistics, it would appear that at least that percentage of transportation services can also be attributed to oil sector demands.

2. Kingdom of Libya, Ministry of Economy and Trade, Census and Statistical Department, **Report of the Industrial Census, 1964** (Tripoli : Census and Statistical Department, 1965), p. 24.

The fact that not more of the economy has been absorbed into the modern sector can only partially be attributed to a lack of investment opportunities. Of perhaps equal importance is what might be termed the absence of an entrepreneurial tradition. Obviously this is a qualitative attribute not amenable to precise measurement. But it is interesting to note that in large measure the modern economy consists of traditional activities that have expanded in response to the strong stimulus of oil induced demands. That is, expansion has been most evident in those areas which did not require breaking the "crust of tradition". For example, there has been a boom in residential construction without any appreciable change in traditional building methods. On the other hand, despite its attractive profit potential, government efforts to interest private capital in the establishment of cement manufacture, a nontraditional economic pursuit, were completely unsuccessful.

The absence of an entrepreneurial tradition has been a major factor in retarding the development of a broader based modern economy. Unfortunately, the required entrepreneurial talents and imagination are only slowly acquired. Gradually, however, with a widening of educational opportunities, such a tradition can be expected to develop.

The Supply of Labor, Import Dependency, and Inflation.

The aspirations of most developing economies have been constrained by the limited availability of foreign exchange. The spectacular growth of oil exports over the past five years has virtually eliminated any foreign exchange problems for Libya. Given this position of strength and the coincident limited production capacity of the domestic economy, Libya has increasingly relied upon imported commodities. As oil exports and government revenues continue to expand, import dependency can be expected to increase.

Within this context, it is important to distinguish between those goods and services that can be effectively provided only by the domestic economy and those commodities for which practically unlimited importation is possible. Most services and construction, for example, can only

be provided by the local economy. In contrast, there are some commodities that need not make any demand upon domestic resources. For example, most food and clothing needs can be fully satisfied by imports. In a loose sense, the distinction might be drawn between those commodities that can or cannot be transported across national frontiers.

This dual classification of goods can only be maintained if it is assumed that labor cannot freely cross international boundaries. Otherwise, it is conceivable that even such characteristically domestic services as those provided by the barber can be imported. The assumption that the importation of labor is restricted is not logically necessary. However, from the practical view-point, and particularly given the political considerations involved, it is reasonable to assume that Libya is not in a position to draw heavily upon pools of surplus foreign labor. Thus, the distinctions made in the preceding paragraph are meaningful.

Although not in a unique position, Libya is somewhat unusual among developing nations in that there is a general shortage of labor. Shortages are not only acute in skilled labor categories (this is commonly the case in most developing economies), but extend critically to unskilled labor as well. The labor supply problem, basically attributable to low population, is further complicated by the local tradition that makes difficult the absorption of potential female workers into the labor force.

Government oil revenues continue to expand and pressure to use these financial resources to further development is understandably great. The resultant increases in demand, however, can only partially be absorbed through import channels. Some of the increased demand can only be satisfied by the domestic economy. Rising demands have indeed stimulated output and the expansion of productive capacities; however, acute labor shortages seriously limit the possibilities for further expansion. Given the Government emphasis on providing basic infra-structural needs and the ambitious, currently proposed housing program, the situation has become particularly critical in the construction sector. Hampered by the scarcity of labor, construction costs have reportedly risen by over 100 percent in the past twelve months.

Although prices in Libya are generally high, inflationary pressures have been only selectively experienced. In large measure, this "selectivity" has followed the broad distinction previously drawn between domestic and imported goods. Commodities that can be effectively provided only by the domestic economy have risen, often substantially, in price. Residential rents and construction costs in general have been particularly susceptible to inflationary pressures. On the other hand, prices on imported goods have remained relatively stable. However, under the impact of rising import volume, port handling capacities are being rapidly reached. If the situation is not rectified by immediate action, inflationary pressures will also be felt in the imported goods area.

In the Libyan context, the government development program is especially vulnerable to inflation. As prices rise, increasingly larger expenditures are required to achieve the goals of a non-expanded program (or, put differently, the initially allocated expenditures will only achieve a program of reduced scope). Under more usual circumstances the inflationary induced rise in government expenditures will be wholly or partially offset by a rise in government revenues. That is, the same basic factors that lead to increased prices of expenditure items should cause revenue items to similarly increase. In a closed economy, rising prices will merely lead to a redistribution of income, which need not adversely affect the government development program. But, no compensatory balancing of expenditures and receipts can be expected in Libya. Government revenues are primarily derived from oil tax and royalty payments which are based on prices obtaining in the international market. These prices will not, of course, be influenced by local inflationary pressures. Thus, inflation will only affect the expenditure side of the government budget. The implications of this observation for a government sponsored development program are obvious.