

## **Arbitration between State and Market; the New Strategies of Development: Case of Tunisia**

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### **Abstract**

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The strategies of development were often built in reference to global optics. However, and since the economy crisis of the 1980s, a revision was introduced on the approach and the dimension of the conceptions of these strategies. Since a few years, the local dimension is set up as a major element guiding the elaboration of such strategies. This paper joins this perspective highlighting the rural governance a major role for the explanation of the development. In this study, the Tunisian reality is taken as support, using the technique of the temporal series.

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**Keywords:** Rural governance, local development, Tunisia.

**ClassificationJEL:** O1, O43, E5.

### **Introduction**

In development strategies based on any State or any market, the structural policies are exclusivist ones. Hence, the arbitration-rebalancing between State and market is needed. In this study, two opposite approaches will be used: the interventionist and the liberal one. This arbitration-rebalancing can take support on local governance. The importance of governance, especially on a local scale, urges to encircle its articulation with the regional development. To put into perspective the scope of this local governance, this paper will seek to illustrate the contribution of rural governance to development by reference to the Tunisian experience. We will highlight the contribution of rural governance in the conduct of regional and human development in Tunisia.

The article is made of three parts. In the first one, the arbitration between the State and the market is reviewed. In the second part, we insist on the importance of the local governance in the explanation of the development. The third part presents the used econometric model and the results analysis.

### **I- State and market: a theoretical review**

The question concerning the respective roles of the State and the market in the process of development is not recent. It dates back to the artworks of F. Quesnay, W. Petty, A. Smith, K. Marx, F. List, etc. From these researches, two main development approaches can be deduced, the liberal strategies of the development based on the free functioning of the market and the centralized voluntarism strategies based on the State planning.

#### **I.1The liberal approach**

The State is considered in the classic view as a disruptive element of the balance. According to this approach, the State has to have a minimal role and is not allowed to intervene in the functioning of the market. The invisible hand is supposed acting to achieve balance. Thus, any State intervention will induce the malfunctioning of the market and hamper its auto-regulator mechanisms.

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Each one is seeking to enrich himself and indirectly this behavior contributes to the achievement of the collective interest and the overall enrichment. Therefore, the State has no role to play in the increase of the wealth; its role is limited to protect the nation, the individuals and the propriety. R. Malthus underlines that the social benefits of the State are harmful because they cannot reduce poverty. In the same lineage, D. Ricardo, through his theory of the comparative advantages demonstrates that countries have an interest in free trade and international specialization.

From the 1980s, further to the debt crisis, the role of the State knew a change. Begin then a wave of criticism of the negative effects of the State intervention. So the rationality of the State and its capacity of management are questioned. This induces the markets liberalization and the public enterprises privatization. But once again, this strategy knew limits concretized by its failure in several countries having adhered; Chile constitutes a striking example. This country practiced an extremely liberal strategy but from the mid-1980s, various imbalances marked the economy. The State was obliged to intervene through various measures taken to develop public structures in order to favor the export, regulate the capital inflows and master the export earnings from copper. Across these actions, the authorities have propelled the complementary relationship between the State and the market.

The neoliberal vision is based on the ideology of any market. The idea of the driving role of the State in the economic growth is exceeded. The State has for mission to assure the internal and external security of the exchanges and to encourage the private initiative. The partisans of this theory believe that the free functioning of the strengths of the market leads necessarily to a greater efficiency and to a better allocation of the rare resources, a greater satisfaction of the customers, a better balance of the terms of exchange and a faster growth. The neoliberals recommend a liberalization of the economy so much on the internal plan, through the privatization and the deregulation, and on the external plan, by a greater openness to the outside. The development results from the free play of the strengths of the market.

According to the liberal optic, the State intervention is a source of crises. Friedrich Hayek considers that the State is responsible of the problem of unemployment. Indeed, State intervention, by fixing salaries and by establishing a minimum wage, leads to the unemployment. Furthermore, the State creates a situation of discrimination by allowing employees to touch an income upper to their productivity.

The solution then lies in the free market and the flexibility of the salaries which allow the full employment because every employee can be assured to be employed according to his capacities and his skills. For Friedman, the intervention of State can generate inflation and raising public deficit. Thus, the functions associated to the State must be limited to the protection and the production of public goods, while respecting individual property rights.

## **1.2 The interventionist approach**

At the opposite of the liberal economists, the interventionists defend the State intervention. They justify this intervention by two main reasons: the market failure to ensure an optimal allocation of resources and the negative effects created by external dependence. They preconize to, ration out the external liberalization, negotiate the insertion in the world market and lead a gradual protectionist policy by setting up a strategy of import substitution. The market is thus criticized for its inability to create industrializing industries. They note that no developing country has happened to develop heavy industries by market strengths, in this approach; industrialization is mainly the result of the effort of the State. Besides, the market cannot insure equality; allow a subsistence income for each individual.

The State intervention was also encouraged by the Marxists and then later by the structuralists who attest that planning can promote economic growth. The market is considered failing in the process of accumulation and still responsible of crises. The structuralists opt for the State intervention in the case of incapacity of the financial resources. State can even block the development of short-term speculative investments, manage external relations and master the rhythms of population demographic growth.

The structuralists advocate a strong presence of the State in the economy. The latter is divided between a developed Center and a Periphery condemned for the underdevelopment. The only solution to go out of the underdevelopment is the impulse of industrialization by public authorities. This industrialization should improve the distribution of income and create the technical progress. The State has to encourage the industrialization and promote its development by the process of planning.

The State is qualified as developer because it takes care of the long-term strategic decisions through the planning or the control to credit access. The State is then invited to develop basic infrastructures, to accelerate the accumulation of the capital by protecting infant industries against the foreign competition, to create sector complementarities between agriculture and industry, to encourage exports, to promote the technology and to encourage private investment. The State is considered, at this level, as a condition of the development by its impulse in the private activity. It has to dedicate resources for the realization of projects identified as priorities.

It is at the beginning of the sixties that the excessive intervention of the State in the substitution process of the imports began to show its signs of slowing in the Latin American countries: lack of internal dynamism in production and technology, sector imbalances, lack of jobs and poverty. The decades 1950-1960 were marked by the nationalization of main services, oil companies and manufacturing industries in many developing economies such as Brazil, Egypt, Algeria, Sri Lanka and Tunisia.

### **1.3 The State teacher**

The new strategies proposed by the World Bank have undermined the extreme conceptions and insisted on the necessity of the conciliation between the public intervention and the market (Reports of the World Bank 1993, 1996, 1997, 1998 and that of the 2001). The rebalancing between the public interventions and the adjustments of the market implies that the State corrects the gaps of the market and establishes number of them through precise rules which insure its viability on financial markets. This idea returns to the neo-institutionalists for whom, the constitutional and legal order shapes the system of incentives thus the type of innovation, the forms of organization and as a consequence the economic dynamics. We say that the State is the teacher of the market. Its task consists of establishing the institutional bases in terms of property, contracts, currency and facilitates the commercial logic for agents.

The question of institutions also occupied O. E. Williamson who proposes the construction of institutions key as the independent Central Bank, a strong budgetary administration, incorruptible judges and still the increase of the educational spending in the primary school and in the secondary. So a growth strategy depends widely on the quality of the institutional architecture.

The construction of a market requires an intervention on behalf of the State for the exact definition of property rights, a unit of account and means of payment, a common evaluation of the quality, conditions that can be satisfied only by the State. Thus, the State must leave involved market mechanisms when they may work but it must act quickly and effectively when they cannot. Always note that the development process takes various forms which vary from a country to another.

Thus, the theory confirms the limits of a system based on either a State or any market. A frugal and modest State would be the best solution in favor of the development. Moreover, in the modern theories the State finds its role. Consequently, exceeding the extremist logic, the contemporary period marks an overtaking of any State and generalization of the planning. It is a temperate balance between public intervention and market. The coordination between the State and the market will be insured by institutions. According to the institutionalists, the State does not only correct market's failures but has to establish number of them by the emission of precise rules which guarantee its viability on the contemporary financial markets. So, the intervention correctly adjusted by the State facilitates the obtaining of a better economic and social balance even. The solution will be then intermediate institutional arrangements between State and market as associations, communities and partnerships that can play an important role in driving growth and improving living standards.

Thus, the best "mix" between State and market requires the development of institutions. This requires a solid state administrative structure which is the striking weakness of developing countries; they suffer from inefficiency of their administrations. Hence, the solution lies in the improvement of the administrative tool of the State, which implies necessary reform of the public sector.

This requires a review of public spending to make them more rational especially in developing countries, where the profitability of these expenses seems quite low. The reform has to touch the privatization of public enterprises. This reform was applied in the 80s in various countries in both developed and developing countries (Argentina, Brazil, Chile, Korea, Ghana, Malaysia, Mexico, Nigeria, Turkey, etc.).

However, the intensification of globalization and the failure of development strategies have conducted to the crisis of governability of the State. The virtues of welfare State are questioned and the governance, especially the local one, became imperative.

## **II- Local governance and local development**

### **II.1 The concept of local governance**

The term governance is deduced from the French language; it dates back to the 13th century and was used as equivalent of government. Its sense evolves and varies according to the institution or the organization. However, the emergence of the concept and its use were amplified during the mid-70s of the twentieth century, it designates a set of prescriptions in administrative and political management. The concept of governance suffers from vagueness and ambiguity that surround its use. Etymologically, this term results from two Greek words; *kybernan* and *kybernetes* which, respectively, mean navigating and piloting. In business, governance involves the use of any mechanism ensuring the management of companies. According to G. Paquet (1999,) the governance explains the action to pilot a system, to coordinate a collective action. The new development theories restored to the governance because of the failure of traditional strategies based, exclusively on State or on market, hence the emergence of the territorial approach to development.

UNDP defines governance as "the exercise of political authority, economic and administrative authority in connection with the affairs of a country at all levels. Governance comprises the mechanisms, processes, relationships and institutions through which, citizens and groups articulate their interests, exercise their rights and their obligations and ensure that they address their disputes."

The territorial or local governance is defined as "a questioning of the traditional functions of the government decision, control or command in favor of a plural and interactive approach of the power where the social interests are associated to the conception of the public action". Thus, good local governance should be based on several pillars, especially the citizens' participation, partnerships between key actors in the local level, the interdisciplinary competence of the local actors, the multiple information sources, the institutions of accountability and the direction priority for the poor. In the optics of international organizations and institutions, such as the UNDP and the World Bank, implement the local governance means the practice of decentralization. The latter involves the transfer of authority and responsibilities in public services since the Central Administration towards the intermediate or local authorities or towards the almost autonomous governmental bodies' and/or towards the private sector.

The decentralization considers that the lower levels of the government mastered better the problems and the priorities at the local level. To be effective, the decentralization must involve local population and organizations. This participation is exercised through the social associations, associations of local artisans, quarter's committees, village committees and representatives of local private companies, voluntary movements of citizens and the delegation of more power decision in favor of local communities.

### **II.2 Rural governance: engine of local development**

Michel Quévité (1986) has examined the institutional frame of the policies of rural development in the developed countries. He insisted on the necessity of institutional supports to establish a kind of "decision grid" between the actors of development, namely local entrepreneurs, financial institutions, research institutions, investors and schools. This requires a decentralized organization of power. In other words, local governments should organize and coordinate communication between these partners. They are then invited to set up public services needed to support local projects, train potential entrepreneurs and organize the local market.

The successes known by the regional institutions in the developed countries is imputed to the areas of staffing skills, decision-making organs and sufficient financial resources to enable them to pursue policies that meet their specific needs. To grasp the rural pact; the main operating procedures of the national politics in rural area, A. Joyal and K. El-Batal (2008) conducted an empirical study. For this, they have used three indicators related to local governance and applied it on a sample of twelve Canadian regional municipalities. They find that regardless of the category of municipality, the rural pact device facilitates the conception of projects within the municipality. Besides, they confirmed that the pact favors the implementation of a mechanism of follow-up of the adopted projects.

Moreover, the authors concluded that the rural governance works better in the municipalities where the overall index of development is higher. In other words, municipalities with a high development index are those where the rural pact device works best. In another study, conducted on a sample of eleven Mediterranean countries (Turkey, Egypt, Morocco, Tunisia, Algeria, Palestine, France, Albania, Portugal, Greece and Spain), O. Bessaoud and S. Druguet have analyzed the role of institutions and organizations in the development of rural areas. They show that withdrawal of the State in these areas, as a corollary of globalization, has produced a proliferation of institutions and rural organizations.

It emerges that the success of the local governance depends on a more detailed knowledge of local and regional tissue. It is necessary to know how to organize the exchanges between the channels, in other words, to direct State interventions to economic activities considered as priorities in the region. This requires skills and sources of funds. Therefore, rural development policies should guide the regional development programs and development approach must be ascending from bottom to top.

### **III- Rural governance and local development in Tunisia**

In this part, we deal with rural governance in Tunisia and its effect on well-being by emphasizing the role of government.

#### **III.1 Presentation of variables and econometric model**

We propose to approximate the development by the Human Development Index (HDI) and we try to explain the evolution of this index by some variables such as, the rate of economic growth (GDPG), added value created in agriculture (VAAG), local governance (GR), the role of the law (RL) and an error term ( $\xi$ ). Our study covers the period 1970-2009. Data are collected from the Ministry of Agriculture and Fisheries and the World Bank statistics for the indicators of governance.

Our equation is written as follows:

$$IDH = c + \alpha GDPG + \beta GR + \delta RL + \phi VAAG + \xi$$

The variable GR or rural governance is a composite variable calculated as a weighted average of the following variables: the number of agricultural associations, the number of cooperatives, the percentage of farmers having areas less than five hectares, the percentage of farmers having areas between five and ten hectares and rural public spend.

### III.2 Method of estimation and interpretations

We first check the variables stationary. The stationary testing showed that they are all non-stationary in level but stationary in first difference.

#### Level stationary Test

| Variables      |     | HDI       | R LOI     | VA AG     | GR        | GDPG      |
|----------------|-----|-----------|-----------|-----------|-----------|-----------|
| ADF statistics |     | -1.284906 | -2.401151 | -1.803045 | 0.498876  | -1.617631 |
| Criticalvalues | 1%  | -3.610453 | -3.670170 | -3.610453 | -3.615588 | -2.627238 |
|                | 5%  | -2.938987 | -2.963972 | -2.938987 | -2.941145 | -1.949856 |
|                | 10% | -2.607932 | -2.621007 | -2.607932 | -2.609066 | -1.611469 |

#### First difference stationary test

| Variables      |     | HDI       | R LOI     | VA AG     | GR        | GDPG      |
|----------------|-----|-----------|-----------|-----------|-----------|-----------|
| ADF statistics |     | -7.670461 | -9.956157 | -7.618226 | -8.525724 | -9.654302 |
| Criticalvalues | 1%  | -3.615588 | -3.615588 | -3.615588 | -3.615588 | -2.628961 |
|                | 5%  | -2.941145 | -2.941145 | -2.941145 | -2.941145 | -1.950117 |
|                | 10% | -2.609066 | -2.609066 | -2.609066 | -2.609066 | -1.611339 |

The co-integration test indicates the existence of a co-integrating relationship.

|       | Statisticaltrack | Criticvalue 5% | Max eigenvalue | Critic value5% |
|-------|------------------|----------------|----------------|----------------|
| R = 0 | 91.37801         | 76.97277       | 45.21006       | 34.80587       |
| R = 1 | 0.437369         | 54.07904       | 21.27987       | 28.58808       |
| R = 2 | 0.312251         | 35.19275       | 13.85029       | 22.29962       |
| R = 3 | 0.193505         | 20.26184       | 7.957144       | 15.89210       |
| R = 4 | 0.079889         | 9.164546       | 3.080653       | 9.164546       |

The results of estimation appear in the table below:

| Variable | Coefficient | T-Statistic |
|----------|-------------|-------------|
| GDPG     | 0.167563    | 5.869       |
| GR       | 0.005515    | 2.451       |
| R LOI    | -1.397013   | 3.133       |
| VAAG     | -0.068062   | 2.770       |
| C        | -0.790081   | 2.494       |

The agricultural added value has a negative coefficient that is due to the low farm income basically created by the work, not by machines, especially with the problem of land fragmentation. In this context, the exploitations having a surface of less than five hectares passed from 40 % to 53 % of the total surface of lands, between 1976 and 2005. A redefining of land policy in the agricultural environment is essential. The government can intervene by an administrative simplification, a reduction of the fiscal penalties or by the establishment of an integrated and code. The poor agricultural income makes that the surplus created does not contribute to the improvement of the educational services or to the health enhancement in the rural environment. In other words, agricultural added value does not manage to improve the indicator of human development.

The rate of income growth is a main component of the indicator of human development which informs about the living conditions. An increase of this rate improves the economy human development. As for the local governance variable, it has a positive impact on human development. A better governance in rural areas improves the income of small farmers and so their living standards.

A study conducted by the World Bank on the agricultural policy in Tunisia, shows that the agricultural cooperatives or the inter-professional groups and, even the Tunisian Union of Agriculture and Fisheries, cannot be considered as representative structures of the farmer's interest. The State may make these groups more effective by a strengthening of their resources and a better redefinition of their modalities of governance, so that the farmers are more involved and really responsible. The State can improve the agricultural sector by funding vulgarization and research which constitute essential services of the government.

Moreover, the vulgarization and the research are not able to respond to the problems faced by farmers. Thus, the State is invited to reform the management of research by, institutionalizing the consultations of farmers and implementing a budgeting by objectives. In this order, a reconfiguration of institutions and processes is necessary so that they meet the expectations and needs of farmers. The problem is that farmers are represented by different groups. Tunisian government must ensure that the dialogue is not monopolized by large farmers to the detriment of small farmers, women and landless.

Since the independence, the importance given to the agriculture hides gaps of the sector in Tunisia. Development projects implemented reflect a top down approach characterized by the virtual absence of people in taking decision and selection of options. The 1970s mark a return of the country towards the liberalism. Rural development has not enjoyed great importance in the adopted development policy. The regional development and the Rural Development programs were the exception of this period. Tunisia knows an unbalance between both rural and urban areas. A simple glance at the distribution of average expenditure per person per year confirms this imbalance.

**The distribution of average expenditure per person per year**

| year/area | 1975 | 1980 | 1985 | 1990 | 1995 | 2000 | 2005 |
|-----------|------|------|------|------|------|------|------|
| Rural     | 106  | 157  | 294  | 460  | 581  | 864  | 1161 |
| Urban     | 192  | 332  | 619  | 890  | 1209 | 1604 | 2171 |
| Total     | 147  | 248  | 471  | 716  | 966  | 1329 | 1820 |

Source: NSI.

It is only during the last decade that the mode of State intervention changes. We then observe a stronger role of the local actors and the representative organs in their territories. So, builds up in each governorate, a regional development council followed by a rural council to achieve the local delegation development council.

The logic of government intervention in Tunisia to develop the rural environment is a descendant approach since the sixties up to the establishment of many local development programs such as, the programs of regional and rural development, the integrated rural development program and the program of elimination of shadow zones (grey areas) especially trough the creation of the national solidarity fund 26-26. However, the success of the programs was limited because strategy practiced by public authorities has neglected the shortcomings of the institutional and political framework.

Local governance is then perceived as a new shape of territorial control capable of encouraging the realization of a participative rural development. But this local governance is not yet defined in Tunisia because of inadequate policy and institutional framework. The imperfection of the institutional framework is attributed to the absence of an effective local participation although recommended by the international organizations (World Bank, UNESCO and UNDP). The participation promotes a decentralization of the power and the definition of choice that meet communities' expectations and aspirations. Economic actors, either owners or farmers, do not enjoy this freedom of participation; the downward strategy exercised by public authorities leaves them only incentives and encouragements given by the State. The rural population is then still unable to represent itself.

Activities' breaks and disappearances of rural communes, cooperatives and community structures show that the State administration continues to prevail by creating a social vacuum. The attempt of the State to fill this void through the creation of local development council in each delegation in order to be responsive to the concerns of the population did not have the expected fruit. This council is not any more the representation of the rural world.

The institutional failure is also explained by another space of legal form materialized by the absence of a legislative framework which regulates the rural planning. Being aware of this space, Tunisian State proceeds by leading a study on the national strategy of rural planning (NSRP).

## **Conclusion**

A review of the past experiences of development shows that we cannot rely either on the market or on the State. The strategies of any State and any market, failed. It is then necessary to set up mechanisms of both correction weaknesses of markets and States regarding human development. The solution lies in the participation of local actors in economic decision-making. Governance of local development is a process that involves a set of institutions and actors who do not belong all to the sphere of the government. Given the scale and complexity of State activities, the process of governance is becoming more and more necessary.

One of the characteristics of the governance of local development is the participation of private and associative sectors by providing services and in making strategic decisions. Local governance assumes that it would be possible to act locally without relying on the authority of the State. The State will not intervene directly but will try to innovate in techniques and tools to help collective actions. The governance of the local development consists in articulating better the institutional variables with the new forms of collective actions by giving a major role to these last ones. In this way, the State needs to apply the decentralization.



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