

**Arab Economic Integration:
An Awakening to Remove Barriers to Prosperity**

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Former Minister of Economy and Trade and Minister of Industry and former First Vice Governor of the BDL. I would like to thank the participants in the AMF-IMF High Level Seminar and the discussant of the paper, Dr. Ali Sadek, for their comments, Dr. Ali Bolbol of the AMF who kindly provided hard to find data and statistics.

The analysis, views and opinions expressed are those of the author and should not be interpreted or construed to represent any official policies or views.

Abstract

External challenges frequently offer an impetus for internal unification. The Arab countries, faced with the challenges emerging post September 11, the war in Afghanistan and Iraq and the declared war on terrorism, should grasp the strategic opportunities to create a turning point in the history of the region.

This paper calls for an Arab awakening, a strategic renaissance, to be embodied in a strategy of regional economic integration. The business sector has already taken up the challenge, with the region witnessing an increase in intra-regional tourism, capital and direct investment flows. While the corporate sector and the new generation of entrepreneurs aspire to enjoy the benefits of regional economic integration, it faces barriers.

The paper reviews the empirical evidence and analysis relating to trade, investment, and labour and capital market integration. The Arab countries are less integrated than countries with a similar level of development and per capita income. Major impediments to integration and prosperity include economic policy and administrative obstacles that impede trade liberalization and economic integration and lead to relatively high costs of doing business. The institutional legacies of colonialism leading to weak regional integration institutions, poor regional infrastructure leading to high logistics costs and the “curse of natural resources” are important structural factors retarding integration.

The paper concludes with a number of policy recommendations. (1) Renegotiation of the GAFTA to establish an Arab Regional Integration Agreement (ARIA) with a wider scope, encompassing trade in services consistent with GATS, liberalization of capital flows and investment, freedom of labour movement and freedom of establishment. (2) Finance investment in trans-national, regional infrastructure projects to help regional integration with private sector participation, leading to a pan-Arab integrated network of transport, communications, energy, telecommunications and a broadband backbone to provide the “infostructure” for an entry of Arab economies and societies into the digital age. (3) Assist and finance economic and social policies supporting the convergence of incomes in the Arab region. (4) Prioritize the development of the capital markets and set the basis for their integration and integrate the payment systems in the Arab countries to create an ‘Arab Target’ system, establishing the infrastructure for an Arab exchange rate system. (5) Establish a set of institutions to enable and support economic integration and the creation of a regional integration and development financing facility. (6) The set up of a strategy for economic policy reform and public and corporate good governance.

Implementation of a comprehensive, regional policy reform package would enable the emergence of the region’s home-grown common “voice”.

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Introduction

1. The September 11, 2001 terrorist attacks, followed by the war on Afghanistan and the continuing war on Iraq and their aftermath pose a challenge to the Arab countries. The declared ‘war on terror’ has led to discrimination against the Arab and Islamic countries with greater impediments and barriers to business and to the flow of capital, labour and people. The challenges and discrimination provide, however, a historical opportunity for Arab Economic Integration. External challenges are frequently an opportunity for internal unification. The Iraq-Iran war encouraged the GCC to take the initial steps towards unification. Post-colonial confrontations in the 1950s and early 1960s led to aborted unification attempts between Egypt and a number of Arab countries. Indeed, the establishment of the League of Arab States in 1945 was also an attempt to develop a common “voice” for the Arab world, with plans for an Arab Common Market. More recently, the emergence of large trading blocs and regional trade and integration agreements encouraged the Arab countries to move towards a Greater Arab Free Trade Area. However, while promising, none of these initiatives has resulted in greater integration.

This paper calls for an Arab Awakening, a strategic renaissance, to be embodied in a strategy of economic integration. We should not miss this strategic opportunity to create a turning-point in the history of the region. A silver lining has emerged in the post-September 11 world: an impetus towards increased regional business, investment and tourism. Our business sector has seen the opportunity and taken up the challenge: intra-regional tourism flows have been rising, as have intra-regional capital flows and direct investment. Higher energy prices have generated large trade balance, capital account and fiscal surpluses, with increased liquidity leading to a boom in real estate and the region’s stock markets. The private sectors, businesses, enterprises, civil society, have the incentive to seek the benefits of integration arising from the expansion of markets. A new generation of entrepreneurs seeks to expand outside their small, national markets. On the other hand, protected sectors, in particular the

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State Owned Enterprises (SOEs), are the main lobbyists against trade liberalization and integration.

2. Successful regional integration requires a number of building blocks. First, Governments should seize the opportunity to provide the enabling framework for the private sector to act as a major unifying force and integration promoter. This requires a vision and an Arab Economic Integration Treaty. Second, integration requires investment in physical infrastructure to break down physical barriers, reduce transport and communication costs, and the costs of logistics. Third, the Arab countries must move beyond the superficial integration represented by free trade in goods (represented by the Greater Arab Free Trade Area), toward 'deep integration' and the harmonization of institutions, laws and regulations to facilitate comprehensive economic integration. Given the small economic size of the majority of the Arab countries, differences in legislation, legal systems, regulations, norms and standards, lead to high costs of transactions, reducing intra-regional trade, capital flows and labour movements. Four, successful regional economic integration requires the creation of compensation mechanisms to overcome resistance to opening-up and economic integration. The Arab countries will need to provide institutional financing for regional investment and development, along with the creation of social cohesion and structural funds as mechanisms during the transition period. Five, the process of Arab Economic Integration (AEI) should be a public-private partnership program designed so as to achieve consensus. The private sector must be kept informed of the process for efficiency in effecting the transition. Opening-up and economic integration will necessitate substantial investments to undertake structural change and transition towards market economies. Providing full information to the private sector on strategy and policies will reduce the costs of adjustment during transition and beyond.

Concepts of Economic Integration

3. Traditionally, economists thought of economic integration as being openness in trade in goods. Two countries (or more) were considered highly integrated if a substantial amount of their trade was bilateral (multilateral), with each other. With increased globalisation during the 1980s and 1990s, the concept of economic integration has evolved to encompass trade in services, labour and capital mobility, as well as financial market integration. More recently, with the increased importance of regional integration agreements and the resurgence of interest in the role of economic institutions and New Institutional Economics¹, economic integration refers not only to

¹ Largely inspired by the seminal work of Ronald Coase, the 'New Institutional Economics', incorporates a theory of institutions into economics." It builds on, modifies, and extends neoclassical theory. It retains and builds on the fundamental assumption of scarcity and hence competition - the basis of the choice theoretic approach that underlies microeconomics. It has developed as a movement within the social sciences, especially economics and political science that unites theoretical and empirical research examining the role of institutions in furthering or preventing economic growth. It includes work in transaction costs, political

reducing barriers among countries to transactions and to the movements of goods, capital, and labour, but also to the harmonization of laws and regulations, and the adoption of common norms and standards in organizing economic activities.

Economists distinguish between: (a) Shallow integration between economies resulting from the reduction or elimination of tariffs, quotas, and other barriers to trade in goods at the border, such as trade-limiting customs procedures; and (b) Deep integration, where economic integration goes well beyond removal of formal barriers to trade and includes various ways of reducing the international burden of differing national regulations, such as the acceptance by one country of another country's certification that a satisfactory level has been met for ability, performance, health, sanitary and phytosanitary, and safety standards. Deep integration therefore requires the changing of government regulations and practices, as a result of bilateral and international agreements, to make those of different countries the same or more compatible.

We can divide cross-border transactions into 4 main groups:

- The exchange of goods and services across national boundaries through *international trade*;
- Factor market integration: labour and the establishment and operation of a business in one country that is substantially controlled by residents of another, through *foreign direct investment*;
- The purchase and sale of financial assets either through portfolio investment or lending and borrowing, which can be referred to as *banking and capital markets integration*;
- The offer of labour services in one country by residents of another through *labour migration*.

In particular, the General Agreement on Trade in Services (GATS) identifies four modes of supply: cross-border supply (mode 1), consumption abroad (mode 2), commercial presence (mode 3), and the presence of natural persons (mode 4).

Thus, the GATS extends traditional trade law to include both foreign direct investment (mode 3) and movements of labour (mode 4)

The Arab countries could be said to be perfectly economically integrated when their residents face no official obstacles to negotiating and executing economic and financial transactions anywhere and with anyone within the integrated area, and, face the same transactions costs independently of where they reside. It is clear, that this is not the case. There are official or policy-based barriers to international integration including tariffs, quotas and non-tariff barriers impeding international trade; official controls on current payments and on international capital movements, laws and regulations limiting or constraining the freedom of establishment of firms, or labour and immigration laws that prevent workers from freely offering their labour services in the Arab countries.

In addition, there are policy-based ‘behind-the-border’ barriers deriving from differences in national regulatory systems, licensing of businesses and service providers or government procurement practices that discriminate against foreign suppliers. Other obstacles to integration can have private origins arising, for example, from the collusive behaviour between domestic firms to prevent entry by foreign firms and leading to the formation of lobbies against liberalization and/or deregulation and the protection of vested interests.²

Finally there are also barriers to integration that derive from logistics costs, from transportation and communications costs, or as a result of information asymmetries that give domestic firms superior knowledge of local business conditions.

Economic Integration: Some guidelines from theory

4. Jacob Viner’s path-breaking work on customs union and related forms of trade integration identified two sets of forces resulting from increased integration: trade creation and trade diversion. Trade creation occurs because consumers and producers have access to wider markets and a larger variety (and/or better quality) of products produced according to the comparative advantage of each country (countries) and benefiting, *ceteris paribus*, from lower production costs (and/or higher quality goods). These are the gains from trade. Trade diversion occurs however, if as a result of customs union or trade integration, imports are diverted from lower cost producers from the rest of the world toward the higher cost products and services of the partner country (or countries). The countries –viewed jointly- lose if the costs resulting from trade diversion outweigh the benefits from trade creation. The argument can be further refined to include the quality of goods. The argument of the gains from trade applies if *all* trade barriers were removed. However, the gains may not apply if partial or discriminatory reductions in trade barriers are effected.

Viner’s model and the subsequent literature adopted a static view of the pros and cons of economic integration. The more recent literature has examined dynamic aspects of Regional Economic Integration (REI), blending in new trade theoretical aspects, including the potential benefits from economies of scale and scope, as well as dealing with imperfect competition³. REI and cooperation can be a tool for overcoming disadvantages of the small size of the economies making up a Regional Integration Agreement (RIA). With a larger market size, firms can invest and benefit from economies of scale leading to lower costs and allowing increased product diversification and better product quality. Further, the removal of trade barriers generates more competition and breaks down monopolies or quasi-monopolistic industrial organization structures.

² See the interesting paper by T.G. Srinivasan on “Globalization in MENA – A Long Term Perspective, presented at The Fourth Mediterranean Development Forum, Amman, Jordan, 2002.

³ See the survey of the literature in Baldwin and Venables, (1995).

REI may also be the means to overcome the disadvantages of smallness and border effects by pooling, integrating and networking infrastructure. In particular, RIAs can be creators of *regional public goods* that improve trade related logistics, lowering the cost and distance of trade in goods and services as well as the overall costs of doing business.

Evidence on the Non- Integration of the Arab countries

5. The evidence on the lack of regional economic integration of the Arab countries is extensive and well documented.

The main ‘stylized facts’ are as follows:

- The Arab countries did not participate in the recent globalization wave of the 1980s and 1990s and are weakly internationally integrated. The AT Kearney Globalization Index ranks 62 countries worldwide according to four measures of international integration (not necessarily independent): Economic Integration (trade, portfolio, FDI and investment income), Political Engagement, Personal Contacts and Technology. The Globalization Index is important since it goes beyond the traditional (economic) measures of integration to others, including technology that may affect long term productivity growth. The ‘digital divide’ of the Arab countries will- unless remedied and convergence achieved- affect medium and long term growth and development prospects. *Table 1*, reveals that the countries of the region rank poorly on the Globalization Index. Out of the countries of the region for which data is available and reported (Tunisia, KSA, Morocco, Egypt and Iran), the highest ranked is Tunisia (35 out of 62 countries), the others are among the least ‘globalized’, with Iran at the bottom of the international scale. Note as well that the traditional measure of trade openness is not indicative of globalization in other domains.

Table 1: A.T. Kearney Index

2004 Ranking	Country	Change from 2003	Economic	Personal	Technological	Political
1	Ireland	0	1	2	14	11
2	Singapore	2	2	3	10	40
3	Switzerland	-1	9	1	7	33
4	Netherlands	1	3	11	8	14
5	Finland	5	7	15	4	12
35	Tunisia	4	25	31	46	42
41	Saudi Arabia	0	49	24	43	59
47	Morocco	-18	54	30	54	55
60	Egypt	-12	58	47	53	49
62	Iran	0	59	62	48	61

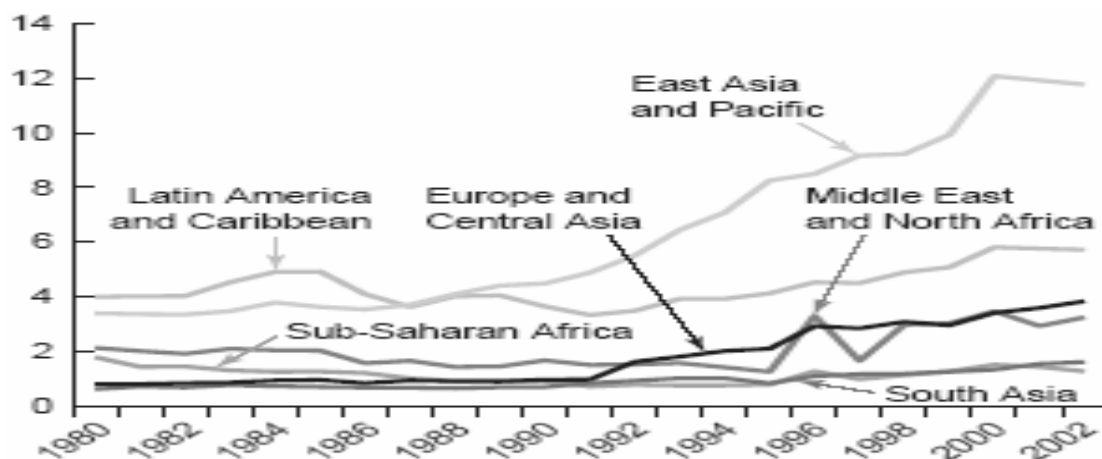
Source: AT Kearney http://www.atkearney.com/shared_res/pdf/2004G-index.pdf

Table 2: Evolution of GDP Per region

Country/Region ⁴	GDP % of the World GDP				Annual GDP growth rate % of the World GDP		
	1962	1980	1990	2000	1962-1979	1980-1989	1990-2000
Americas	42.89	35.01	0.00	35.52	4.27	2.78	3.24
Asia	19.28	24.56	28.58	29.76	6.88	4.75	3.10
Sub-Saharan Africa	1.37	1.23	1.11	1.04	4.82	2.14	2.05
MENA	1.16	2.08	1.84	1.94	8.90	1.95	3.20

Source: Carrere and Schiff, (2003)

- The foreign trade of the Arab countries remain limited at 2.7% of world trade (Figure: 1), similar to their share in world income (Table: 2). Indeed, the trade performance of the Arab countries is comparable to the sad performance of the African sub-continent. Total non-energy exports stood at 80 billion in 2003, about the size of Finland's exports⁵, which has a population of 6million as compared to some 310 million in the Arab world. Apart from the energy exports of the oil producing countries which reflects the volatility of oil prices, the growth of imports and of exports has been sluggish in the Arab countries, consistent with their low overall economic growth rates.

Figure 1: Regional exports as percentage share of world exports (oil excluded)

Source: Global Economic Prospects, 2005

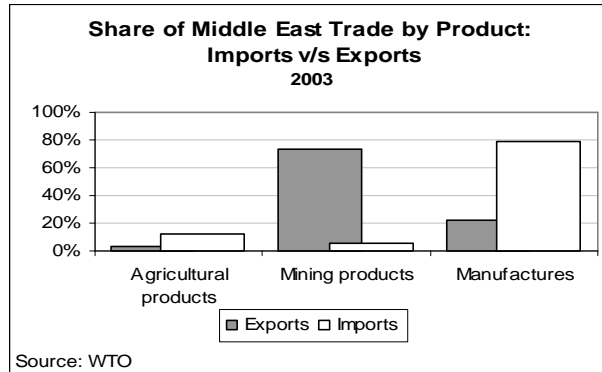
- Despite some policy efforts at production and export diversification (figure 2), the product base and range remains limited. Hence, there is a high degree of concentration in exports (73% are energy/mining) and imports (79% are manufactures). Further, the exports are natural resource intensive, with low value-

⁴ See Annex table 7, for further breakdown of GDP evolution per region

⁵ See Annex for a comparison of the economy indicators of Finland, Spain, MENA and the World.

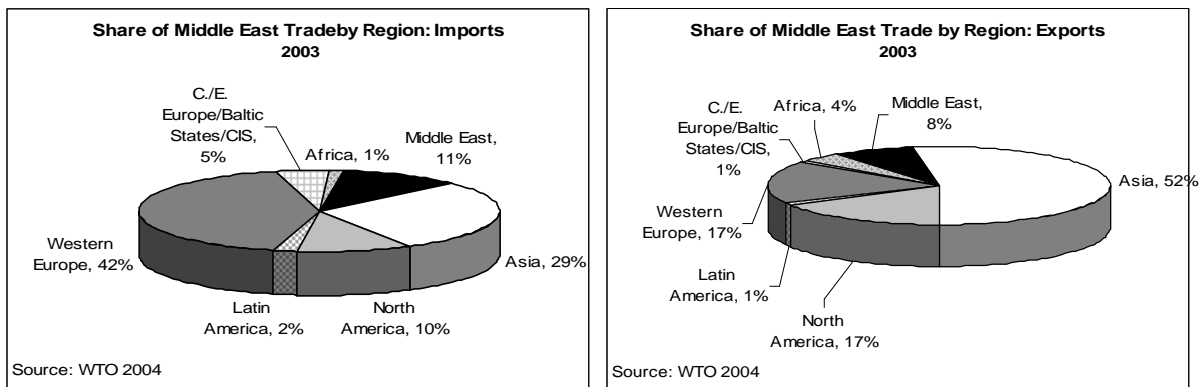
added. The related feature is that there is a near absence of trade in intermediate products, reflecting limited international supply-chain integration.

Figure 2: Share of Middle East Trade by Product



- More critical for the future is that the Arab countries have not developed services exports, the fastest growing component of world trade, and potentially the most promising, given their young and growing populations.
- There is also a mismatch in the direction of trade, with Asia representing more than 52% of exports, while Europe is the source of about 50% of the imports of the Middle East. (Figure 3). Given that the majority of the Arab countries peg their currencies to the US \$, they are vulnerable to substantial real effective exchange rate movements and/or terms of trade shocks⁶.

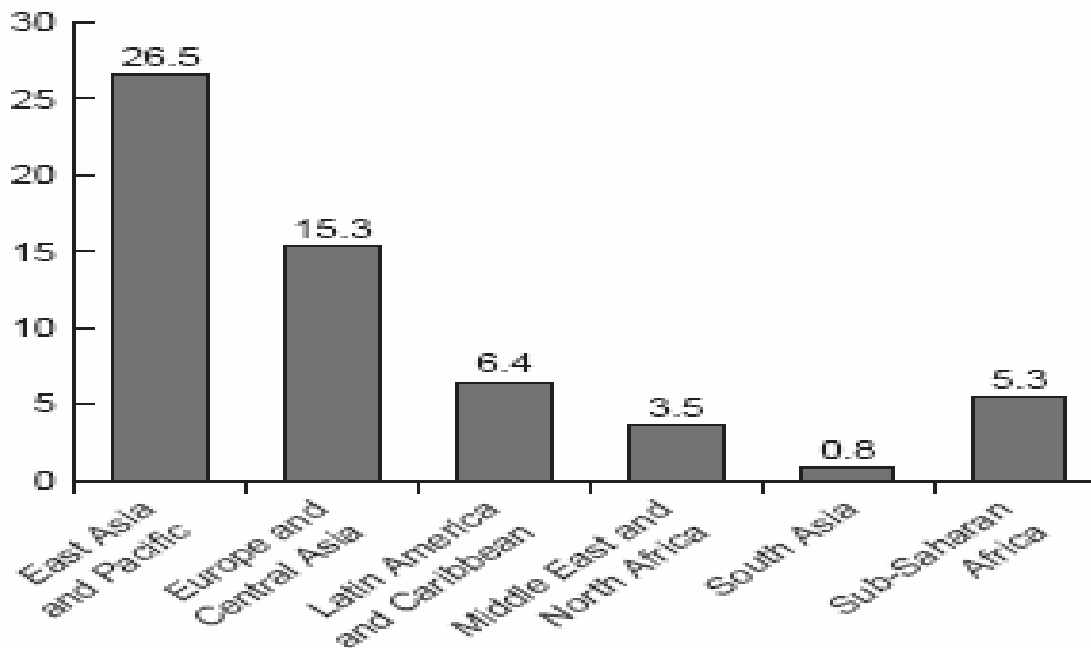
Figure 3: Share of Middle East Trade by Region



⁶ Saidi, N. (2003) notes that based on the methodology in Alesina, Barro and Tenreyro (2003) for a country that would seek to adopt a foreign currency, which includes three important criteria for judging the benefits of an exchange rate anchor: (i) the expansion of international trade that could result from a currency area; (ii) the effect on the degree of co-movement of prices and output; and (iii) the reduction of inflation resulting from linking to a low-inflation anchor currency. The empirical results suggest that for the Arab countries an optimal anchor policy would call for linking to the Euro and not the US\$, given the importance of trade and output linkages.

- Given the lack of international trade integration, the limited extent of intra-Arab trade is not surprising. Intra-regional trade represents about 3.5% of GDP. (figure 4) On average, intra-Arab trade represents some 11% of the region's imports and some 8% of their exports. Two other characteristics are noteworthy. One, most intra-Arab trade is within sub-regions. Some 75% of GCC trade with the Arab countries is with GCC countries. Similarly, the trade of the North Africa Arab countries is mainly with themselves, as is the case for the Levant countries.⁷ The pattern of intra-Arab trade is similar to their non-Arab trade, with energy exports representing over 60% of exports. Product complementarity, as measured by the 'complementarity index' of Havrylyshyn⁸, is largely similar to that of other regional groupings. Three, there is wide variation in the extent of intra-Arab trade across the Arab countries, with countries pursuing liberal trade regime policies having a higher fraction of intra-Arab trade.

Figure 4: Intra Regional Trade as a share of GDP (Percent), 2002



Source: Global Economic Prospects, 2005

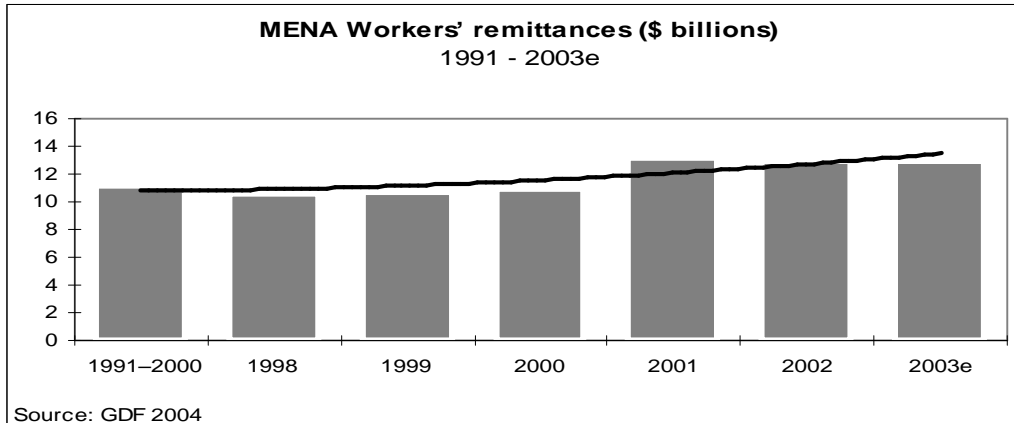
- Labour movements and the accompanying flow of remittances appear to be the exception to the lack of regional integration. (Figure 5). The intra-Arab labour flows are from the resource poor but labour rich countries (Lebanon, Egypt, Jordan) to the resource-rich but labour poor countries. However, Arab labour is facing increased competition from lower wage labour from the Asian countries resulting in a reduced

⁴ Al-Atrash, Hassan M. and Yousef, Tarik, Intra-Arab Trade - Is It Too Little?, IMF, Working Paper, 2000.

⁸ Havrylyshyn, O. and Al-Atrash, H. Opening Up and Geographic Diversification of Trade in Transition Economies, IMF Working Paper, 1998.

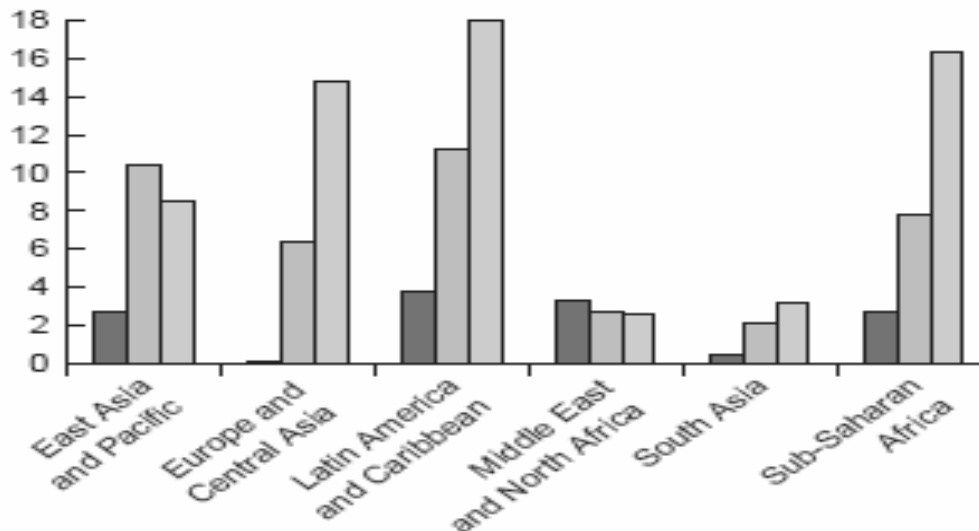
flow of labour from the labour exporting Arab countries and providing a possible reversal of the wage and income convergence process.

Figure 5: MENA Workers' Remittances



- The same observations underlying (a), apply ‘a *fortiori*’ to economic integration with the Arab countries, whether the indicator is trade in goods, services, financial assets, FDI and to a lesser extent labour. The accompanying charts show that the MENA region has not been able to attract FDI or other forms of capital flows. Out of FDI flows to the developing countries of US\$135 billion, total FDI flows to the MENA region did not exceed US\$2 billion in 2003, which is less than Finland at US\$2.9 billion! Indeed FDI represented about 2% of investment in the region. The accompanying table shows summary indicators and contrasts two economies, Finland and Spain with the Arab countries, illustrating the effects of different growth patterns and the impact of alternative trade and financial policy regimes.

Figure 6: Share of region’s net FDI inflows in the region’s total investment (percent) for 1980-89, 1990-1999 and 2000-2002



Source: Global Economic Prospects, 2005

6. To summarize: the Arab countries are not well integrated⁹ on an international basis or on a regional basis. The lack of regional integration is a reflection of the lack of globalization, although some evidence suggests that there is under-trading at the regional level, as compared to some benchmarks, such as a gravity model¹⁰. Across a broad variety of indicators, trade in goods and services, capital flows and to a lesser extent labour flows, the Arab countries are relatively less integrated than countries with a similar level of development and per capita income.

Table 3: Regional versus International Trade Integration

	Total Arab External Trade of World Trade			Total Intra-Arab Trade of Total External Trade		
	2000	2001	2002	1999	2000	2001
ALGERIA	1.57%	1.61%	1.59%	1.87%	2.00%	2.17%
BAHRAIN	0.57%	0.60%	0.61%	6.08%	5.94%	6.02%
EGYPT	1.44%	0.86%	1.26%	5.95%	6.58%	5.62%
JORDAN	0.30%	0.37%	0.39%	5.53%	5.58%	7.21%
KUWAIT	1.34%	1.22%	1.19%	5.77%	6.03%	5.65%
LEBANON	0.35%	0.37%	0.35%	3.47%	3.69%	3.66%
LIBYA	0.86%	0.79%	0.75%	3.56%	3.45%	3.15%
MAURITANIA	0.06%	0.06%	0.07%	0.13%	0.12%	0.20%
MOROCCO	1.05%	0.92%	1.06%	3.40%	3.23%	5.29%
OMAN	0.80%	0.82%	0.74%	10.79%	10.76%	9.99%
QATAR	0.76%	0.86%	0.79%	3.06%	4.29%	4.04%
SAUDI ARABIA	5.41%	5.70%	5.66%	29.47%	27.08%	25.76%
SOMALIA	0.02%	0.02%	0.02%	0.55%	0.36%	0.36%
SUDAN	0.16%	0.19%	0.20%	1.75%	1.54%	1.66%
SYRIA	0.52%	0.61%	0.63%	4.25%	3.98%	4.12%
TUNISIA	0.75%	0.83%	0.80%	3.84%	3.87%	3.88%
UAE	4.14%	4.25%	4.28%	20.85%	22.50%	21.47%
YEMEN	0.33%	0.34%	0.36%	3.59%	3.51%	3.56%

Barriers to Integration and Prosperity: Colonialism, Geography and Logistics

7. Why are the Arab economies not more integrated? The evidence on economic growth and its determinants and on the external trade of the Arab countries suggests that growth under-performance and limited globalization result from a similar set of factors. One, there is a legacy of protectionist trade policy regimes that favoured inward-oriented policies during the 1960s and through the 1970s and early 1980s. Tariffs and non-tariff barriers have remained high –apart from the liberal outward oriented trade policy regimes

⁹ See Annex table 8, to learn about Arab's World Share of World's Total.

¹⁰ The 2002 World Economic Outlook provides a summary of the evidence and reports on research.

See <http://www.imf.org/external/pubs/ft/weo/2002/02/pdf/chapter3.pdf>

of the GCC countries- despite the initiation of trade liberalization policies during the past decade. This is evidenced, at the institutional level, by the relative delay in entry into the GATT/WTO whose members accounted for more than 96% of world imports in 2003. Out of the 22 members of the Arab League, only 10 are members of the WTO, while four others are observers. Two, political and/or security factors affected both the pattern of trade and the extent of intra-regional trade as a result of sanctions or trade embargos, in both North Africa as well as in the Middle East and the Levant. Three, the combination of protectionist trade policies and similar factor endowments generated similar production structures, resulting in a lack of product diversification, or product complementarity.

Box 1: MENA WTO Members and Accession Date

Members and WTO Accession Date			
Bahrain	1 Jan 1995	Tunisia	29 Mar 1995
Kuwait	1 Jan 1995	Qatar	13 Jan 1996
Malta	1 Jan 1995	United Arab Emirates	10 Apr 1996
Morocco	1 Jan 1995	Jordan	11 Apr 2000
Egypt	30 Jun 1995	Oman	9 Nov 2000
Observer Governments			
Algeria	3 Jun 1987	Yemen	14 Apr 2000
Saudi Arabia	13 Jun 1993	Libya	10 Jun 2004
Lebanese Republic	30 Jan 1999	Iraq	-

Source: Trade Profile, WTO

Hence, there appears to be limited basis for trade based on comparative advantage resulting from differences in factor endowments (Heckscher-Ohlin-Samuelson) across the Arab countries and differences in relative factor intensities industries leading to differences in relative production and cost structures. Similarly, the wide variation in per capita income between the countries of the region could have resulted in product differentiation. However, specialization and trade in product quality was constrained by the limited size of the markets. Four, the relatively small size of the economies prevented product diversification by limiting economies of scale and of scope. Five, and more fundamental, are the relatively high costs of doing business and the high trade logistics costs in the countries of the region leading to high transactions costs and limiting the extent of trade and negatively affecting competitiveness, though there are large cross-country differences in the cost of doing business¹¹, with the GCC countries having lower costs. However, the high costs of doing business results in high transactions costs and is accompanied by inadequate, inefficient infrastructure and related services, leading to high

¹¹ See the Annex Table 5 on the cost of doing business in the Arab countries

logistics costs. These are part of the ‘deep determinants’ of growth and trade under-performance.

8. **Colonialism.** A contributory factor to the lack of economic development has been limited institutional development and evolution since the colonial period. Our public administrations and government structures are mostly inherited from the Ottoman Empire and that of the colonial powers. Colonial legacies in the form of legal origins of laws and institutions have mattered. The fact that a majority of the countries of the MENA region are under the French Napoleonic Code tradition is likely a contributory factor to the lack of legal and constitutional evolution, particularly in economic and financial legislation, preventing an adaptation to a changing and more open world. Colonialism has been a negative and persisting factor in economic integration. (a) Through the design and shape of emerging nation-states and its impact on economic geography. The colonial powers imposed borders that led to the emergence of small sized entities with small markets, primarily linked and economically integrated with the former colonial power. In particular, trade and trade patterns remain strongly imprinted and distorted by colonial ties, not least because the colonial regimes imposed non-tariff barriers in the form of the technical barriers and product specifications of the colonial power. An example is the use of the metric system for weights and measures in the former French colonies as compared to the non-metric British standard in former British colonies. (b) Through the effect on trade credit: the emerging banking systems of the Arab countries were either dominated by banks from the colonial or mandatory power that were given privileged access or by tying domestic banks to correspondents in the colonial power creating a financial hub-spoke effect favouring trade credit for transactions with the former colonial power.

The ‘Curse’ of Natural Resources¹²

9. Salai-i-Martin and Subramanian (2003) develop systematic evidence that an abundance of natural resources and rents damage the quality of institutions and governance. The natural resource rich countries of the Arab countries –as in other regions- became reliant on their natural resource wealth and have avoided undertaking fiscal reform and diversifying tax revenues and align the pricing of public utilities (transport, communications, water, electricity and other public services) in line with costs, relying instead on revenues from the exploitation of natural resources. The availability of low extraction cost oil and gas led to a high degree of specialisation and prevented economic diversification, resulting in economies with a high degree of concentration in the structure of production and exports and vulnerable to the risks of energy price volatility. (figures 7 and 8). The obverse is that those Gulf countries or entities with low or declining natural resource endowments –Dubai, Bahrain and Yemen- are the leaders in evolving new economic strategies based on economic diversification into services and other non-oil sectors. (figure 9).

¹² The recent study by Martin and Subramanian, discusses the negative impact of the presence of natural resources on economic performance and more generally on governance.

Figure 7: Fuels Imports from the Middle East

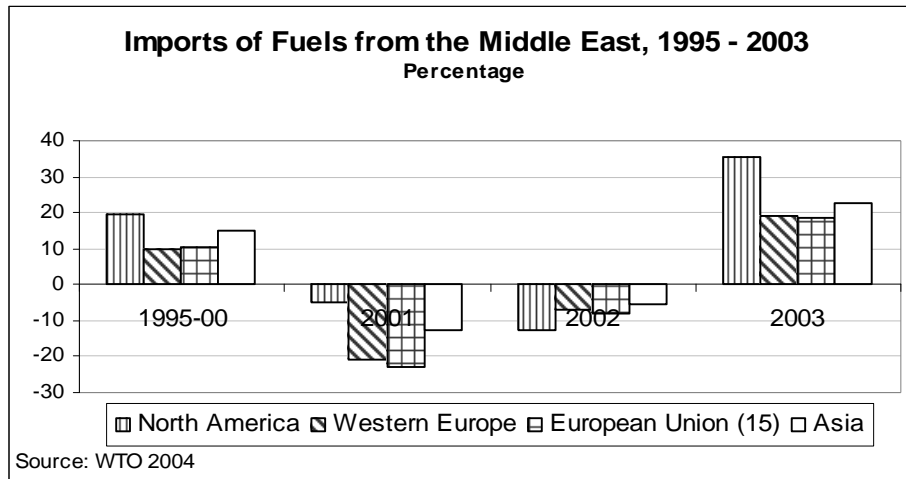


Figure 8: Energy Export Prices

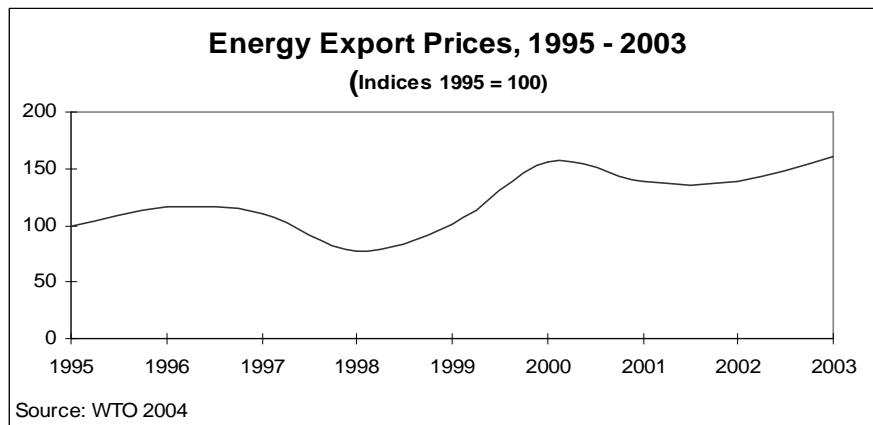
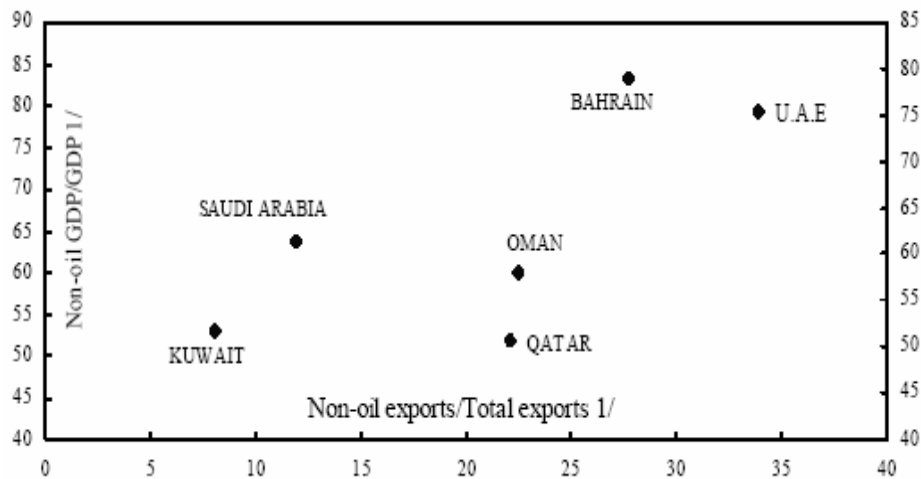


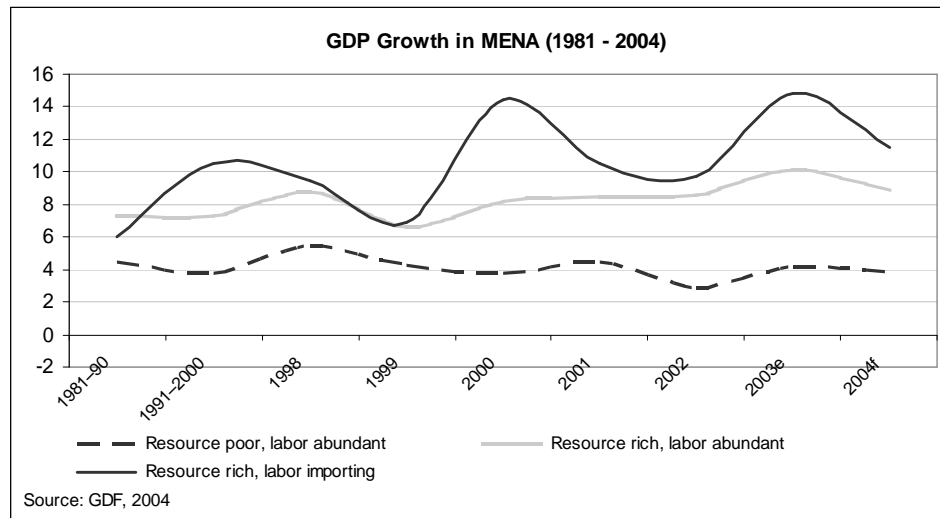
Figure 9: Diversification and Composition of GDP, 1995 - 2003



Source: IMF (2003)

In turn, the relatively liberal labour migration policies of the resource-rich but labour poor GCC acted as a pressure valve for the labour abundant countries, such as Egypt or Lebanon. As a result, the labour exporting countries became reliant on remittance income and transfers, and were able to avoid undertaking necessary reforms when faced with changing economic circumstances requiring change in economic strategies and policies. Moving forward will require establishing new fiscal and tax administrations, the introduction of a system of direct and indirect taxation and reform of the pricing of public utilities and services to provide an alternative to oil revenues. Public sector reform, tax and fiscal reform will have to be priorities on the agenda of economic integration. (figure 10).

Figure 10: Comparative GDP Growth



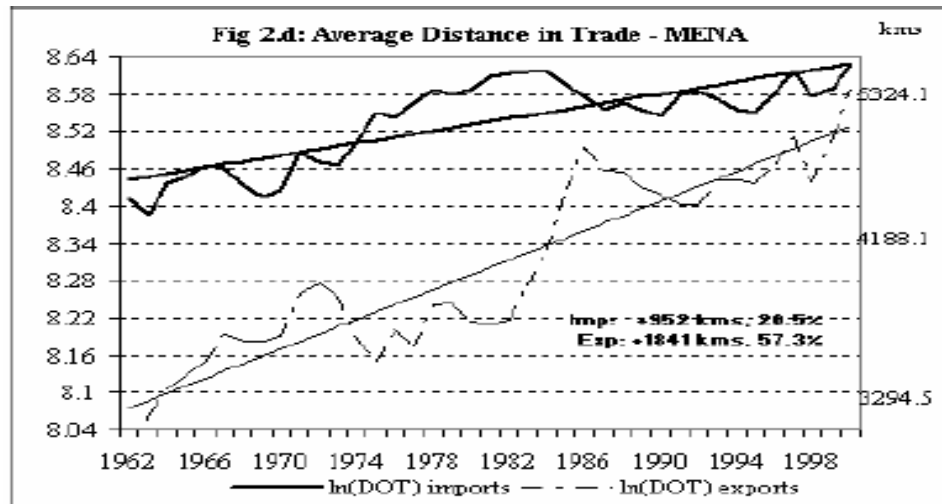
Size and Geography

- Small-sized countries and markets result in a lack of diversification of available goods and services, due to the limited diversification of natural endowments and factors of production. As reviewed above, all the indicators of international integration show the Arab countries as lagging in international integration, but also in regional integration. This is contrary to the prediction that the smaller the size of countries and economies, the more likely they are to be open and integrated to obtain access to goods and services unavailable given domestic factor endowments. The reason lies in protectionist policies. High tariff barriers in the non-oil producers and the pursuit of non-market economic development strategies stressing 'self-sufficiency' and import-substitution, but without the adoption or transfer of knowledge, technology and ideas resulting in limited or no innovation through learning-by-doing, has implied the use of old technologies and limited

resulting in low growth of total factor productivity. The GCC countries, though small, have pursued liberal policies, with low external tariff barriers, and are more open and trade-oriented, though with limited domestic production, resulting in non-diversified, non-integrated economies.

The sub-discipline of economic geography has been undergoing a revival in the past decade. In particular, economists are highlighting the role of geography in affecting economic activity, notably as a factor systematically affecting growth performance and trade. Sachs (2003) and Gallup and Sachs (2003) provide empirical evidence on the impact of geography on transport costs and on the public health environment. In turn, the public health environment affects the accumulation and quality of human capital, mortality, mother and family health, fertility and hence economic growth. Thus, proximity to the tropics is a retarding factor in economic growth due to its negative effect on health and human capital accumulation. Similarly, J. Diamond (1999) shows how accidents of geography have had long-lasting effects on technical development and diffusion. Thomas Sowell (1998) in a series of books shows the impact of conquests and migrations on the spread of technology and cultures, but also shows the importance of geography and location in preventing the spread of know-how, innovation and technology.

Figure 11: Average Distance in Trade - MENA



Geography, in the form of distance of trade (DOT) to market, that is, measures of the proximity to the centre of world economic activity in North America and Western Europe, is empirically, an important factor in international competitiveness. An important recent paper by C. Carrere and M. Schiff¹³ provides evidence on the evolution of the

¹³ Carrere and Schiff find that “that the DOT falls over time for the average country in the world, and that the number of countries with declining DOT is close to double those with increasing DOT. In other words, distance has become increasingly important over time for a majority of countries.” And that: “One of the conclusions is that the evolution of the DOT is unrelated to that of the overall level of trade costs but

DOT in 1962-2000 for different countries, regions and the world as a whole. They compute the distance of exports, imports and total trade for 150 countries and 39 years (1962-2000), from the COMTRADE bilateral (non-fuel) trade data. The average DOT (ADOT) varies substantially across regions, with a world average of 4,850 kms. When ranked by continent/region, the ADOT is smallest for the EU-15 (2,800 kms), larger for the MENA16 (4,590 kms); the Americas are more than double the EU-15 ADOT (6,160 kms), followed by Sub-Saharan Africa or SSA (7,790 kms), Asia (8,085 kms), and South America (8,180 kms). Carrere and Schiff show that despite improvements in technology leading to lower transport costs, the MENA region 'distance of trade' index has increased over the past decades, (by +57% for exports and +21% for imports), contrary to the experience of most countries and regions. This is confirmatory evidence that logistics and regulatory structures have been a continuing drag on economic growth and productivity, resulting in inability to enter international markets. (figure 11).

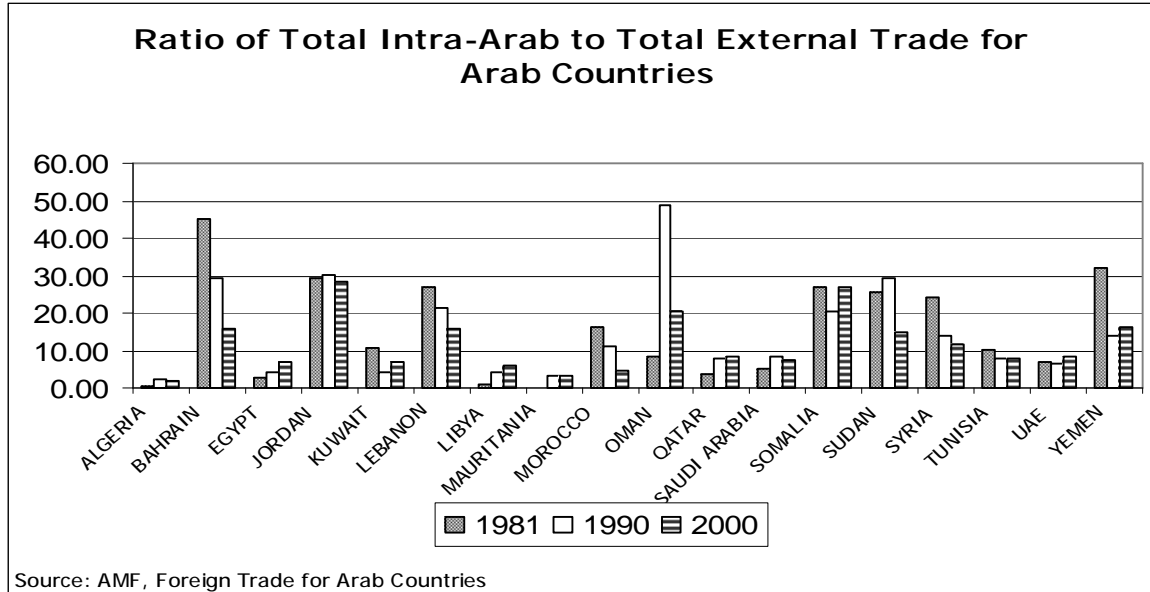
Arab Economic Integration and Lessons from the EU Experience

What forces drive economic integration? Can the Arab countries emulate the example of Europe and other country groups that have successfully integrated through Regional Integration Agreements? The contributors to Hoekman and Messerlin (2003) argue that the initial, pre-integration- conditions of the European countries are different from those in the Arab countries, even if the motivation is similar: a desire for political unity and integration. In particular, there were key institutional features that helped drive integration: (a) Strong political backing that enabled and supported a central executive body to manage and drive the process. (b) Financial and other mechanisms for redistribution, devised to sustain integration and cooperation. These 'enabling factors' may not be strong in the Arab countries. However, other factors favouring integration are present: a common language and ethno-linguistic traditions, culture, history and geographical proximity. The Arab countries share a number of characteristics that favour their economic integration and expansion of trade and direct investment, as well as capital flows. Geography, short distances between main urban centres and long common borders suggest that transport and transactions costs should be low, favouring, according

depends on the relative evolution of its components. For instance, the DOT falls over time as long as dwell costs fall proportionately more or rise proportionately less than distance costs, irrespective of the direction of change of transport costs as a whole. The paper also examines the impact on the DOT of changes in production costs, customs costs, domestic transport costs, of air relative to land and ocean transport costs, of competition, exchange rate policy, regional integration, uneven growth, counter-season trade, and of just-in-time inventory management. We show that changes in production costs, domestic transport costs, customs costs and specific tariffs have a similar effect on the DOT as changes in dwell costs. One of the more surprising findings is that, despite the negative impact of regional integration on the DOT over time, the share of countries with a positive trend in the DOT is larger for countries that are members of trade blocs than for countries that are not. “

to the gravity model¹⁴ of international trade, a large volume of trade between the Arab countries.

Figure 12: Intra-Arab Trade



In addition a common language greatly reduces the transaction costs associated with gathering information, making contacts and conducting negotiations. A recent study Shang-jin Wei¹⁵ finds that sharing a common language is a highly significant determinant of trade - countries with this tie typically have a volume of trade 80% higher than otherwise. It is the institutional features and governance of the process that need to be addressed.

- Two other structural elements are problematic for the integration process. One, the consequences of nationalistic regimes that pursued nationalization policies and state expansion through extensive ownership of the means of production through State Owned Enterprises (SOEs). These led to non-market economic development strategies based on socialist models and on import-substitution policies, characterized by large, protected and stultified SOE industrial and service sectors incapable of innovation and of facing international competition. The result has been low real economic growth and low total factor productivity growth¹⁶. The other element, noted above, is the ‘Arab-Dutch-disease’, or the curse of abundant natural resources, which established an equilibrium between the resource-rich but labour-poor countries, interacting with labour-rich but

¹⁴ Gravity models posit that bilateral trade flows are inversely related to distance (which increases transport and transactions costs): $T_{ij} = AY_iY_j/D_{ij}$, where T_{ij} is exports from country i to country j , Y_i, Y_j are their national incomes, D_{ij} is the distance between them, and A is a constant. Other constants as exponents and other variables are often included

¹⁵ Wei, Shang-jin. (1996). “Intra-National Versus International Trade: How Stubborn Are Nations in Global Integration?” NBER, Working Paper No. 5531.

¹⁶ See the discussion in D. Rodrik (2004).

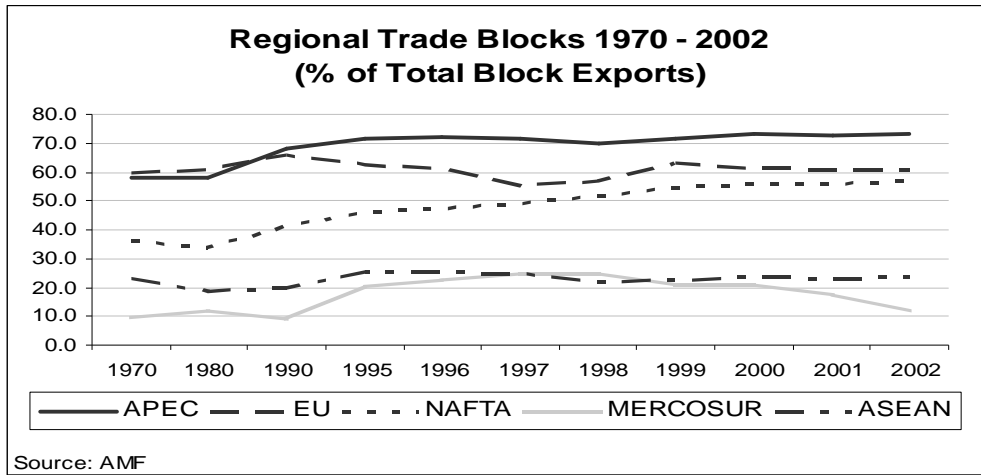
resource poor countries. This equilibrium is now threatened by the availability of competing labour from the Asian countries and can no longer serve as a paradigm for the future.

12. How will the process of change and reform be managed? It is clear that Arab Economic Integration cannot succeed absent the creation of enabling institutions. The success of the EU in economic integration owes much to the role played by Legislative (the European Parliament), Judicial (Court of Justice and Court of First Instance), Executive (Commission and Council) and Economic institutions (the EIB European System of Central banks and then the ECB). This required devolution of power from sovereign states and governments, which was achieved through consensus on a vision of a common Europe with an integrated market and institutions. The EU adopted a series of agreements that supported the economic integration institutions. The Arab countries have to face the issue of the loss of sovereign decision-making and independent government policy. Economic integration will be a matter of political will and of the willingness to make and implement compensatory mechanisms.
13. Currently, the Arab world lacks the integrating institutions. The implementation of an Arab Regional Integration Agreement (ARIA) and other agreements such as the EuroMed Association Agreements (AA) will require deep political reforms of existing institutions, such as the Arab League and the creation of new institutions that will drive the REI process. The Arab League has not been able and was not enabled to play a regional integration role. To take an example, to-date, the Arab League Economic Commission has not been able to agree common rules of origin to regulate trade between the Arab partners despite years of, so far, sterile negotiations. By contrast, the Arab countries that have signed Association Agreements with the EU¹⁷, (Tunisia, Morocco, Egypt, Jordan, Syria and Lebanon) have agreed rules of origin relating to their bilateral trade with the EU. This creates an incongruous situation whereby similar goods from the EU or Arab countries face different conditions for entry to a common economic area! A recent proposal for reform of the Arab League and its related institutions has been tabled but was shelved for lack of consensus. Similarly, regional economic institutions such as the Arab Monetary Fund have not evolved into economic integration institutions.
14. An agenda of economic reform and regional economic integration requires strong **political leadership**. Regional integration allows –by lowering intra-member political and other tensions- to lower defence expenditures. This can free up substantial resources that can be used to foster and support regional economic integration whether through investing in regional infrastructure, the creation of structural adjustment funds or ‘cohesion’ funds or to fund institutions for economic integration. Historically, the EU benefited from the Franco-German partnership as the major driver of European economic integration. Who will be the Arab champion or champions? Leadership criteria include regional economic size, trade and economic linkages. The country or countries likely to lead are those with the largest expected gain from regional economic integration. Based

¹⁷ see Annex Table 4, for a review of Trade and Services Agreements, Preferential Agreements and Others

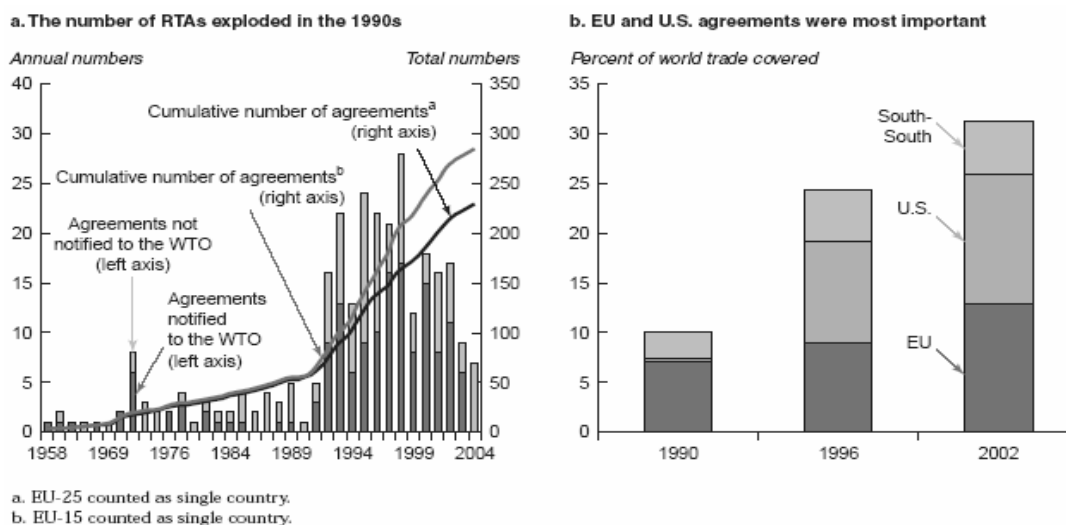
on these criteria, it is the GCC that should take the leadership in driving the process of AEI. The GCC given their resources and their ongoing drive towards local integration are best able to play the role of ‘integrators’.

Figure 13: Regional Trade Blocks of Total Block Exports (Percent)



Regional Integration Agreements (RIAs)

15. By May 2004, some 208 RIAs (free trade areas, customs unions including those which are asymmetrical in nature) had been notified to the GATT/WTO of which 178 had been established since 1990. Indeed, the rate of formation of RIAs has accelerated with the establishment of the WTO. More than 1/3 of world trade is now conducted within RIAs, but with a great deal of variance across RIAs. Some 60% of EU trade is now intra-EU, whereas only 10% of WAEMU takes place within. This is similar to the fraction of intra-Arab trade. The RIAs cover a number of dimensions including trade in goods and services, factor market integration, monetary and payment systems, institutions, laws, and in some cases, political systems.

Figure 14: Regionalism Spread

Source: Global Economic Prospects, 2005

There has also been a surge in the number of Free Trade Agreements (FTA)s during the 1990s. (Figure 14). Most FTAs are North-North or South-South. Few are North-South. Though these have been increasing, primarily as a result of the EU's policy towards the Mediterranean which has resulted in FTAs with the 12 Med partner countries, as well as the FTAs the US has signed with a number of countries in the area: Jordan, Israel and Morocco and more recently with Bahrain.¹⁸

Issues raised by RIAs.

16. The formation of RIAs goes against the MFN principle incorporated in the GATT/WTO that trade policy be non-discriminatory. RIAs are allowed under Article XXIV of GATT, on condition that they cover "substantially all the trade".¹⁹ As *table 4* shows, note that the average frequency of MENA country participation in RTAs is similar to the world average (5 per country) and that nearly all participate in an RTA (20 countries out of 21).

¹⁸ Apart from NAFTA, the US has also signed FTAs with Chile, Singapore,

¹⁹ The relevant part of article XXIV reads as follows: "(a) A customs union shall be understood to mean the substitution of a single customs territory for two or more customs territories, so that (i) duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories, and, (ii) subject to the provisions of paragraph 9, substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union;..."

Table 4: MENA Participation in RTAs

	East Asia and Pacific	Europe and Central Asia	Latin America and the Caribbean	Middle East and North Africa	South Asia	Sub- saharan Africa	North	Total
Number of countries	32	36	39	21	8	48	25	209
North-South bilateral								
Countries belonging to at least one RTA	4	12	6	10	0	2	10	44
Average number of RTAs per country	2	1	2	1		1	4	2
Maxim number of RTAs per country	4	4	4	3	0	1	24	24
All others								
Countries belonging to at least one RTA	24	22	33	20	8	47	10	164
Average number of RTAs per country	2	6	8	5	4	4	8	5
Maxim number of RTAs per country	3	12	17	12	9	9	15	17
Total								
Countries belonging to at least one RTA	26	26	35	20	8	48	11	174
Average number of RTAs per country	2	6	8	5	4	4	11	5
Maxim number of RTAs per country	7	12	19	13	9	9	29	29

Source: Published WTO data, World Bank staff.

Note: Bilateral agreements are defined as an RTA with two members. North is OECD 24 plus Lichtenstein, and South is all other countries

It is not clear yet whether the RIAs will be a force for a more or less liberal external trade policy. (Table 5). In particular, the presence of an increasing number of RIAs may act to retard progress on the multilateral system and in advancing the Doha agenda. Countries are choosing to form RIA clubs with their most important partners, with dominant countries or with blocs such as the US or the EU. This raises the issue of the fiscal consequences of such RIAs. The fiscal dimensions of RIAs are important for countries in which trade taxes generate a significant share of government revenue. For the Arab countries, reliance on trade taxes remains substantial, particularly for the Mashrek countries and to a lesser extent the Maghreb countries. Further, in case of RIAs with dominant countries or blocs, the blocs are seeking to extract additional preferences in the framework of the RIAs or introducing non-trade related provisions into the agreements, including political (human rights), environmental, investment, labour and other provisions, which detract from the fundamental trade related issues.

Table 5: Intra Regional Trade in Selected Trade Blocs

Intraregional Trade in Selected Trade Blocs, 2001. (Billions of US dollars)		
	Intraregional trade value	Intraregional trade as share of total trade (%)
ASEAM	166.1	22
EU	2650	59
GAFTA	30.54	7.5
NAFTA	622	19

Source: ESCWA, based on Canadian Department of Foreign Affairs and International Trade, "NAFTA at eight: a foundation for growth". IMF, Direction of Trade Statistics Quarterly, June 2002.

Evidence on the Impact of AEI

17. Two types of evidence have been adduced relating to the impact of AEI, namely, econometric studies and the simulations of computable general equilibrium (CGE) models. Recently, Konan (2002) and the IMF (2003) have undertaken CGE simulations calibrated for the Arab countries of shallow (trade in goods) and deep (goods and services) forms of integration. It is clearly more difficult to model or simulate ‘deeper integration’ including the harmonization of laws and institutions and their effects on ‘Coasian’ transactions costs.

The results of these exercises are:

- Comprehensive service sector integration would generate greater gains than those attained through trade and tariff liberalization. For the cases of Tunisia and Egypt, the magnitude of the gains is a multiple from what would be generated from shallow integration.
- In the case of Yemen (which is not a member of the GCC) and the GCC, the gains from integration, “output could grow by up to 14 percent in Yemen and by 7 percent in the GCC countries over the long run”.²⁰

Can the results from these simulations be a guide for policy makers and reliable for simulating the effects of alternative trade policy reform proposals? The CGE simulations are attractive in that they are based on microeconomic foundations, are helpful in identifying the role of transactions costs and impose consistency of economic and financial interrelations. However, the models have to be “calibrated” to be used for the Arab countries. A number of problems arise in this context. One, we lack reliable statistics and econometric estimates for the main macroeconomic aggregates, let alone the microeconomic evidence at the firm and household level for the majority of the Arab countries, that are necessary for well designed calibrations. This makes ‘calibration’ closer to an art than an informed exercise. How useful are CGE models based on data and estimates for developed countries for the Arab countries dominated by SMEs? Two, the CGE models may not adequately model agents’ expectations and their role in economic behaviour. Like their econometric counterparts, they are prone to the Lucas economic policy critique. Agents and economies will take into account policy changes and reforms: the announcement of trade regime or other economic policy changes will affect agents’ expectations and lead to changes in behaviour that are not captured by the current generation of CGE models. Three, the CGE models used for the Arab countries do not capture the role of money and finance and the payment system in the economy. Four, more important is the silence of CGE models concerning the institutional structure of the economy. Does it make a difference to the simulations what laws and regulations, what economic institutions underlie the economy in Tunisia, Egypt and the GCC countries and the differences between them? Finally, the nature of REI agreements is that they are comprehensive and involve changes in economic structure that affect the dynamics of the economy.

I make these comments not to critique CGE or econometric models, but rather to point out the difficulty of estimating the impact of RIAs and to advocate building statistical

²⁰ See IMF

capacity in the Arab countries to provide information and data allowing better assessment of the impact of changes in trade regimes. It is one thing to estimate the effects of a change in a tariff on domestic consumption, production and imports; it is quite another to simulate the effects on the economy of structural and institutional changes brought about through ‘deep integration’ and joining or forming an RIA.

That said, the evidence from the process of European economic integration suggests that economic integration, the creation of markets that lower transactions costs and break down ‘barriers to prosperity’ generates medium and long term benefits. As a betting man, I would venture that the estimates and simulations underestimate rather than overestimate the benefits from economic integration of the Arab countries, on condition that the process of AEI is accompanied by structural and economic policy reforms.

REI, Fiscal Reform and Harmonization

18. Apart from the oil producing countries of the GCC, trade taxes contribute an important fraction of government revenue for the countries of the region. Implementing an ARIA will imply a loss of tariff revenues which will have to be compensated through the introduction of alternative broad-based taxes such as VAT or general sales taxes and other fiscal measures, such as removing the subsidies to and reforming the pricing of providing public services and amenities in many of the oil-producing countries.

Regional Integration and FDI

19. The region is suffering from low external investment rates, low FDI. It is clear –as noted above- that micro-economic aspects play a leading role. The WB report on the cost of doing business shows that the countries of the region impose large costs on establishing and conducting business. The process of Regional Integration (RI) is likely to lead to an increase in intra-regional FDI (from the members of the RI group of countries) and from outside the region. A recent study²¹ has examined the impact of regional integration on FDI flows, comparing different types of integration: North-South (US-Mexico), South-South (MERCOSUR) and North-North (Canada –NAFTA). Importantly, responses to integration depend on the environmental changes brought about by the regional integration and locational advantages brought about the REI. The most positive impact of FDI occurs when REI is accompanied by or coincided with domestic liberalization and macroeconomic stabilization in the member countries. However, while plausible, this raises the issue of causality and identification: is it possible to identify the independent effects of REI on investment flows as compared to liberalization and reform?

²¹ See the by M. Bloomstrom and A. Kokko, Regional Integration and FDI, NBER 6019, April 1997.

Integrated Infrastructure is the Basis for Economic Integration

20. The success of modern economies and societies owes much to the overcoming of physical obstacles to communication and access to markets and trade. As a major component of the REI, the Arab countries should invest to link and integrate the physical networks that underlie and facilitate trade, the mobility of factors of production, capital flows and direct investment. These include: air, rail and road transportation, energy, oil and gas pipelines, and modern ICT networks.

The economic integration of the Arab countries should be based on an integrated infrastructure and networks. The Arab countries have underdeveloped transport (air, road and rail), energy (oil, gas, and electricity), water, and information and communications networks. Even in the relatively well-endowed countries of the GCC, the existing infrastructure has aged –embodying technologies of the 1970s and 1980s- and needs replacement, development and modernization. In the non-oil countries and non-GCC oil producers, existing infrastructure is inadequate to serve the needs of modern economies and societies and fast-growing populations and labour forces. More generally, the infrastructure is, typically, managed by State Owned Enterprises (SOEs), resulting in high cost, inefficient enterprises unable to provide the private sector and the general public with adequate services. The region lacks the infrastructure, its interconnectedness, its quality and density. The result is a high cost of infrastructure services and logistics leading to high production costs of goods and services and to a low quality of final services to consumers, whether households or businesses. In turn, small markets protected by import-substitution policies and the absence of a performing, high density and quality infrastructure has reduced the extent of diversification of economic activity in the Arab countries, and prevented the development of trade in intermediate and processed goods. An important consequence is that the structure of production and trade in the Arab countries remains highly concentrated in labour-intensive and high resource content, low value-added products, with limited vertical specialization.

The infrastructure gap extends, particularly, to cross-border infrastructure. Poor quality logistics negatively affects trade in goods and services, tourism and the movement of people and has resulted in a growing ‘digital divide’ with the developed countries. The other characteristic is that the existing communications and transport infrastructure is largely designed for extra-regional, North-South, contact and inter-action with former colonial or mandatory powers. The result is poor intra-regional infrastructural services and communications. It is easier and most frequently cheaper to contact the West from any capital in the region than to establish communication within the region!

Table 6: Logistics Costs for MENA Exporting Firms

Logistics Costs for MENA Exporting Firms (US\$)							
	Yemen			Egypt		Jordan	
	Tuna	Coffee	Banana	Garments	Potatoes	Garments	Okra
Non-Transport Logistics Costs							
Ordering and other adm. cost	25	25	25	60	60	90	40
Load/unload	462	526	159	560	14,000	2,200	110
Capital carrying cost in transit	21	1,830	3	996	591	2,000	1.35
Capital carrying cost in storage	10	4,238	2	670	295		0.25
storage cost	370	1,800	40	475	800	240	25
shelf-loss in Transit/Storage	4,800		520	90	3,750	50	100
Filing loss and damage claims	25	25					
Safety Stock/Stock-Out Cost				30			
Emergency shipment cost	2,772						
Subtotal	8,459	8,444	749	2,881	19,496	4,580	268
Transport charges							
Truck	1,167	950	590	400	19,200	4,400	210
Airfreight	12,348			7,000		19,000	1,925
Ship		1,700		3,800	8,400	9,200	
Subtotal	13,515	2,650	590	11,200	27,600	32,600	2,135
Logistics Costs as % Landed Price	54.9	7.2	23.0	15.4	26.0	6.7	48.0

Trade competitiveness is strongly affected by the cost of logistics. The intra-regional and international trade of the Arab countries is impeded by inefficient trade logistics; bureaucratic procedures, time consuming transit procedures, bribery, corruption and customs clearance all lead to high logistics costs which substantially reduce the volume and value of trade. A recent study on trade logistics in the MENA countries²² finds that logistics costs can vary from 7% to some 55% of the landed price of exported goods depending on the per unit value of the goods! (Table 6). For the Arab countries with low value-added or low value per unit exports high logistics costs the costs of trade logistics are more important than other barriers to export. It is not surprising that our export performance is lacklustre!

Similarly, a recent study shows that there is strong positive relation between the share of total exports that is driven by vertical specialization and the quality of infrastructure. Trade in intermediate goods depends on the availability of infrastructure services and efficient trade logistics. In particular, vertical specialization is sensitive to trade barriers and infrastructure quality and the cost of infrastructural services.²³

The bottom line is that poor quality and costly infrastructure services and other barriers have prevented regional integration and economic integration with the rest of the world.

²² "Global links to regional networks: trade logistics in MENA countries", by Julia Devlin and Peter Yee, Paper Presented at the Fourth Annual Mediterranean Development Forum Held in Amman, October 6-9, 2002

²³ See H.K. Nordas, "Vertical specialization and the quality of infrastructure", WTO, Staff Working Paper ERSD, December, 2003.

We are not benefiting from geography and proximity of the major markets of the EU and the rapidly growing Asian markets. What should be done?

Removing the Barriers to Prosperity

Regional Infrastructure Investment for Regional Trade and Growth

Figure 15: East Mediterranean Gas Rink



21. Regional Infrastructure Investment for Regional Trade and Growth to remedy the high logistics costs the Arab countries should invest massively in infrastructure and networks and integrate them with their main trade partners' (the EU and Asia) infrastructure and networks. Such investments, which will break down barriers and reduce logistics costs, are likely to create large benefits from economies of scale and generate high returns to investment. Three major infrastructure networks should be envisaged: (a) Energy: electricity, oil and gas; (b) an Integrated Information and Communications (ICT) Arab network; and (c) an Integrated Payments Network to facilitate and support trade and growth. I comment briefly on each.

The Trans-Euro-Mediterranean Networks (TEN)

22. The **Trans-Euro-Mediterranean Networks (TEN)**, to ensure gas and electricity interconnections South-South and South-North in the region have been identified as a clear priority and should be extended to the Arab countries of the Gulf.

The Euro-Mediterranean Energy Forum program

23. The Euro-Mediterranean Energy Forum program and action plan should be accelerated and extended to the Gulf to:

- Create the **Mediterranean Electricity Ring** which will link the countries of the Euro-Med process. The electricity ring should be further integrated to link with the countries of the Gulf.
- A **EuroMed oil and gas link** should be a priority, with oil and gas pipelines linking the EU with oil and gas producing countries of North Africa, Egypt and the Gulf. At the moment planned pipelines by-pass the Mashrek countries to pass through Turkey. (Figure 15).
- Create a **EuroMed integrated road and rail network** to be linked to the integrated transport network, developed for the Mashrek, Integrated Transport System in the Arab Mashrek (ITSAM)²⁴. The importance of the railroads is that they would link the Arab Mashrek countries with Europe and with the Arab countries of the Gulf, reducing transport costs and enhancing the overall integration of the region, allowing the efficient transport of goods and people throughout the area. Two strategic transport projects should be given priority on both the bilateral and regional level: road and rail transport. Briefly these include:
 - The “**International Roads in the Arab Mashrek**” which has been long delayed.
 - The rail network should be re-developed with two projects: the ‘**Berlin to Baghdad**’ railway would link the heart of Europe to the centre of the Arab world, passing through Eastern and Central Europe and through Turkey and the Arab Mahsreq.
 - The “**Hejaz**’ railway, took 8 years to build with about 7000 soldiers at a cost of about US\$16 million in 1908. With new superior technologies it would cost about US\$300 million today and deliver fast, reliable transport services. It would link Turkey to the Arab Mahsreq and the GCC.
- **Integrated ICT Infrastructure.** The Arab countries have to bridge the digital divide. In particular, they need to undertake substantial investments in the ICT infrastructure of their economies and societies. Investment in telecommunications and in broadband technologies will be critical in the economic integration of the Arab countries. This calls for integrated high speed broadband technologies networks to be established. This would enable the region to harness the powers of

²⁴ See “The Role of the ESCWA in Promoting Trade and Transport Facilitation in the ESCWA Region”, by Nabil Safwat, 2002.

modern ICT for economic and social development, for e-Services, e-Government, and e-Society.

- **Payment System Integration.** Economic integration in the Arab countries requires the support of a modern, efficient payments infrastructure that will underlies trade, investment and economic links. The successful introduction of a common currency for the GCC currencies will imply a reduction in transactions costs, both within the GCC and cross-border. The monetary authorities and finance ministries should work at the set-up of an **Arab-Payments System**, which would unify the payments systems of the Arab countries, and integrate them into the EuroSystem. In particular, I would advocate the extension of the EU TARGET system, to create an **Arab-TARGET** system. This would form the basis of a new payment system, allowing and facilitating the use and adoption of the Euro. In turn, an integrated payment system would facilitate monetary integration through the set-up of an Arab exchange rate system. The planned adoption of a common currency by the GCC countries could provide the currency and exchange rate anchor of an Arab exchange rate system linked to a currency basket of international currencies.

24. The envisaged infrastructure program, likely to extend over a generation, would develop and strengthen the links of the Arab countries, lead to a strong expansion of trade and private sector investment, raise economic growth in the region, create jobs and raise labour and total productivity growth. Regional infrastructure investment should be considered a **Regional Public Good** and a policy priority, undertaken through a revival of the privatization and private sector participation programmes initiated in the 1990s and through public-private partnerships.

Financing mechanisms for Economic Integration and the Creation of a Regional Investment and Development Bank

Role of the Banking and Financial Sector in Economic Integration

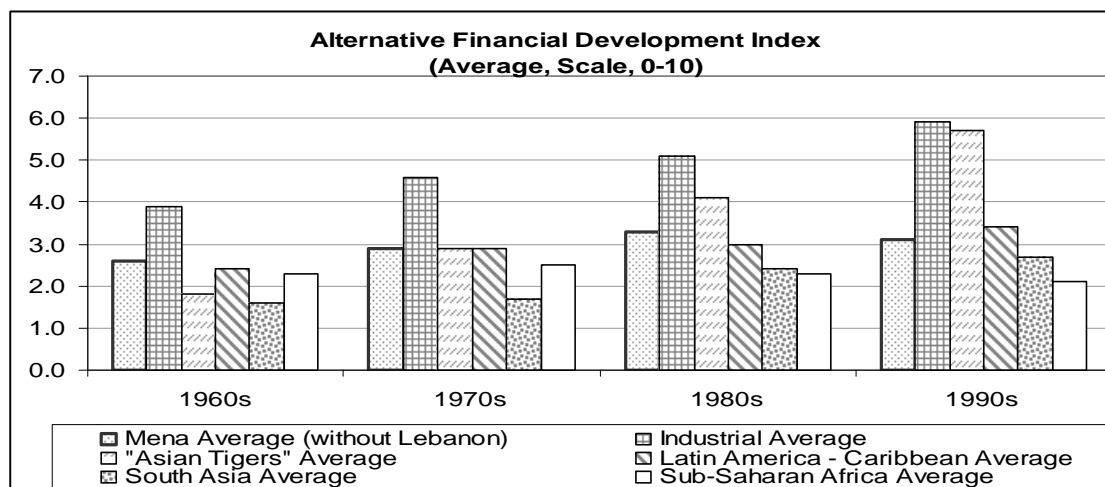
25. The banking and financial sector should spearhead the process of regional economic integration of the Arab world. Indeed, it is in the interests of the sector to have access to a unified market and its benefits, including economies of scale and scope, risk diversification, deployment of modern ICT technologies applied to banking, and an integrated payment system. In turn, this would allow the banking and financial sector to finance the process of economic integration, by participating in the finance of regional infrastructure projects. In addition, the creation of a single banking market would lead to a channelling of funds from the liquidity-rich, capital exporting, natural resource rich countries, to high return investment and lending in the capital importing countries of the Arab world. Similarly, the development of the Arab countries' capital

markets and their integration would allow the financing of economic development and transition towards market-based economies.

26. The creation of an integrated Arab economic zone cannot be successful without a supporting financial mechanism, including grants and financial transfers. Increased integration should be supported by the set-up of economic integration institutions. Specifically, adjustment to trade liberalization, structural reform and transition to a market economy –including a reduced role of the State and increased private sector participation- in the Arab countries, the requirements of financing large scale infrastructure projects to support the regional integration of the Arab countries, call for the set-up of a **Regional Investment and Development Bank**. Note that the Regional Investment and Development Bank could emerge from a restructuring of existing institutions and funds, without the need to create a new institution and its related costs. What is important is the mission, objectives and programme. The Regional Bank would provide special priority to the development of private-sector economic activity and to projects contributing to the creation of a favourable climate for private investment. The EU’s successful regional integration and the central lesson from the EIB’s experience confirm the importance of a dynamic public bank to support integration and convergence processes²⁵. The Regional Bank would work with the Arab Monetary Fund and the various Arab Funds and other international financial organizations to provide financing for regional infrastructure projects. Infrastructure and *info*-structure are major factors in fostering physical and communication links, reducing transactions costs, lowering transport and communication costs, foster intra-Arab trade and investment, bringing the region into the digital age, and generating economic growth.

²⁵ See the working paper by S. Griffith- Jones, A. Steinherr and A.T. Fuzzo de Lima, “The European Investment Bank: A useful inspiration for emerging countries?” presented at the Seminar on Regional Financial Arrangements, UN, July 2004

Figure 16: Alternative Financial Development Index



Source: "Financial Sector Development in the Middle East and North Africa", Creane, S., Authors' calculations.

27. The rationale for a Regional Investment and Development Bank is a reflection of the limited financial sector development in the region. Financial markets are pre-emerging, incomplete and segmented. (Figure 16). In particular, most of the countries do not have developed government debt markets, except for short-term Treasury bills. The consequence is that governments cannot rely on domestic debt markets in order to finance long-gestation or infrastructure projects. They have to rely on financial reserves, short-term bank finance or turn to the international capital markets. Similarly, the near-absence of modern financial technologies and in particular of securitisation tools and technology limits the possibility of financing infrastructure and development projects. In turn, basic physical infrastructure networks –roads, transport, energy, water, communications and telecommunications- are inadequately developed leading to high information and logistics costs, segmented goods, services and labour markets both within countries and –*a fortiori*- between the Arab countries.

Arab Economic Integration: the Framework for Reform and Governance

28. The empirical evidence reviewed above shows that the Arab country economies are not internationally integrated. The various indicators of trade in goods, services, labour and capital flows, the indicators of capital markets integration, all suggest that the Arab economies did not benefit from the wave of globalisation that dominated the world economy in the 1990s. The Arab economies are also not regionally integrated. Indeed, the degree of regional integration is less than the extra-regional integration. Existing trade liberalization agreements are inadequate to foster integration. GAFTA, even when implemented, is unlikely to lead to a large increase in income or a

sustained increase in economic growth. GAFTA is limited to free trade in goods and much remains to be done to remove non-tariff barriers to trade and ‘beyond the border’ barriers, arising from different product technical specifications, government procurement practices and the like. The GAFTA should be re-negotiated to include free trade in services consistent with the GATS. Theory and empirical simulations suggest that the benefits from liberalizing trade in services are likely to be a multiple of the benefits from free trade in goods.²⁶

29. Policy reforms leading to the liberalizing of trade, capital movements and labour flows are important if not critical in order to benefit from AEI and to raise economic growth on a sustainable basis in the Arab countries. In particular, reform, de-regulation and liberalization of services improve the overall efficiency of the economy, in both the traded and non-traded goods sector, reduce barriers to growth, and lower the cost of doing business. There are also production efficiency gains because in many cases services are an intermediate good, a factor of production for final goods and services. Services liberalization can lead to higher total factor productivity growth as well as increasing labour and capital productivity growth. A case in point is financial services. The Arab countries have not developed their financial sectors and capital markets commensurately with their economic growth and development. Indeed, the lack of financial development and in some cases financial repression, have been a retarding factor in total factor productivity growth and economic growth.

Trade Policy and Regional Integration: Changing the Development Paradigm

30. The individual Arab countries are faced with a number of policy options relating to their trade policy and economic agendas. Clearly, each sovereign country can proceed, in pursuing a trade liberalization policy. Many of the countries have pursued a policy path of bilateral FTAs with the EU (all the Arab Mediterranean countries with the exception of Libya), other Arab countries, or the US (Bahrain, Jordan and Morocco). Others have pursued multilateral policies through entry into the WTO or regional trade integration through the Agadir agreement²⁷ and the GAFTA. The absence of a comprehensive trade strategy results in a ‘spaghetti bowl’ of cross-cutting agreements which complicate customs procedures and impede trade and investment. From this perspective, moving to a regional integration agreement, within a strategy of multilateral liberalization is preferable. Moving towards regional economic integration will require a change in the development paradigm that has guided economic policy for the past several decades and led to a ‘governance gap’. Policies based on import-substitution, protection of domestic production, nationalization and a preponderant role of the State, have not delivered sustained

²⁶ See the studies included in Galal and Hoekman (2003) and Konan (2002).

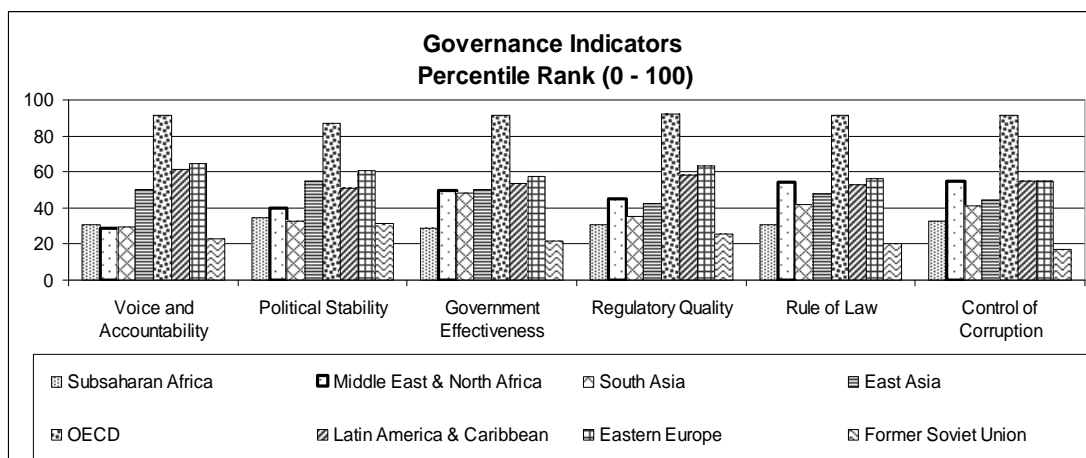
²⁷ This creates a FTA between Egypt, Tunisia, Jordan, Morocco and Algeria.

growth and prosperity. The initial high growth rates of the 1960s and 1970s resulted from high population growth rates, high investment rates and catch-up effects related to initially low levels of per capita incomes. For the Arab countries to achieve the dynamic benefits of economic integration, including a sustained increase in growth and total factor productivity, requires “deep integration”: institutional convergence through the adoption of common codes and standards and the harmonization of laws and regulations, the establishment of common rules of the game for economic activity and property rights. The focus of policy should be to create a framework for the private sector to play the dominant role.

Corporate Governance, Investment and Competition policy

31. **Corporate Governance, Investment and Competition policy** should be at the forefront of the concerns of MENA policy-makers seeking to obtain the benefits of increased private sector participation and investment, whether domestic or FDI. In particular, both theory and empirical evidence suggest that attracting FDI and encouraging domestic investment is predicated on an effective implementation of the principles of good corporate governance²⁸, and the implementation of a framework of competition. Good corporate governance and an effective competition policy will be a main factor influencing investment and, in particular, foreign direct investment in the region.

Figure 17: Governance Indicators



Source: D. Kaufmann, A. Kraay, M. Mastruzzi, 2003: Governance Indicators for 1996-2002

²⁸ See the discussion and references in Saidi, N. (2004), “Transparency and Disclosure: CG for the MENA countries”. Beirut, Lebanon, http://www.gcgf.org/Events_Roundtables_Fora/MENA_Forum/TransparencyandDisclosure_CGMENA.pdf, which discusses the role and applicability of the OECD CG framework and the state of good CG in the MENA area.

In moving towards REI, the Arab countries will have to bridge the existing ‘corporate governance’ gap and develop competition policy. The framework for private sector participation should include well-designed privatization strategies including implementing laws and the creation of regulatory bodies. However, this should not imply a simplistic approach to ‘privatization’ or ‘private sector participation’ in infrastructure. All too often –as was frequently the case in the 1990s- privatization or the devolution of State Owned Assets has been undertaken within a protectionist regime and in the absence of a well-designed regulatory framework. Indeed, in many cases, private monopolies have been turned into private monopolies in the hands of insiders. As a result, privatization and related economic reforms did not lead to the expected improvements in efficiency and to a private sector resumption of economic growth. To be successful, privatisation should be accompanied by a strategy for implementing good corporate governance principles and the implementation of anti-trust or competition policy. Given the small size of the Arab economies, it will be important to ensure that privatisation does not transform public monopolies into private monopolies. In this context, moving towards regional economic integration will lead to more ‘contestable markets’ and increase the forces of competition. A case in point is the networking of national electric power grids allowing users to benefit from cross-border competition and achieve economies of scale. Deeper integration with an ARIA is also likely to reduce the risk of investment in the Arab region and its instability. A recent paper²⁹ finds that the MENA countries have higher investment risk than other developing countries and that the greater instability of investment risk is an additional deterrent to investment. This is confirmatory evidence that security, political and economic risk and its volatility are an important factor negatively affecting capital flows to the region, and in particular FDI.

32. Regional Integration Agreements (RIAs) are more likely to be stepping stones on the road to multilateral opening-up and liberalization, rather than being a block. The political argument is clear: coalitions are more likely to emerge in favour of regional trading blocks than in favour of immediate multilateral liberalization.³⁰ The argument is that global free trade, which is best or is a Pareto-dominant strategy, may not be politically initially feasible. RIAs can be stepping-stones towards multilateral liberalization. It will also be important to make sure they are not stumbling blocs; that countries do not find themselves in a sub-optimal equilibrium situation that will block further liberalization. Further, membership of an efficiently organized RIA can be a ‘policy commitment mechanism’. RIA membership would strengthen the credibility of policymakers as it implies, among other, an investment in time-consistent policies. An ARIA would also allow the Arab countries to go beyond the trade policy tariff and equivalent reduction and binding commitments resulting from GATT/WTO membership, to policy commitment in other areas, including services, investment, labour, the environment and other areas. More generally, an ARIA would allow cooperation and commitment with respect to regional public goods.

²⁹ See K. K. Chan and E. Gemayel, “Risk, Instability and the Pattern of Foreign Direct Investment in the Middle East and North Africa Region” by (*IMF Working Paper* WP/04/139, August 2004).

³⁰ See the analysis in Wei and Frenkel, 1996.

33. For the Arab countries and RIA should be viewed as complementary to and not a substitute for multi-lateral opening-up, via entry into the WTO. Economic integration agreements are comprehensive agreements that imply trade liberalization through the removal of tariff and NTBs, agreement on Technical barriers to trade, TBTs, but also ‘deep integration’ agreements on investment, agriculture, services, rights of establishment and related areas.
34. Adjustment and Transition. The Arab countries need to consider –as did the European countries- a comprehensive package of policy measures to accompany and support a RIA, an Arab Regional Integration Agreement (ARIA). These measures are important to deal with the trade creation and trade diversion effects, the dynamic effects of implementation –in particular those related to FDI and capital flows- fiscal impacts, and the development of economic integration institutions.

Final Remarks

35. The Arab countries should consider an ARIA as part of an overall ‘awakening’ and development strategy to deal with the challenges facing them. In particular, it is important to make a clear commitment to reduce the income gap between the Arab countries by pursuing policies that are consistent with the cross-country convergence of income.
36. To move ahead, the Arab countries need to design a comprehensive regional policy reform package, including:
- a. Renegotiation of the GAFTA to establish an Arab Regional Integration Agreement (ARIA) with a wider scope, encompassing trade in services consistent with GATS, liberalization of capital flows and investment, freedom of labour movement and freedom of establishment. To initiate the process, the Arab countries could sign a framework Association Agreement, at least as comprehensive in terms of content, scope and preferences as those negotiated within the bilateral EuroMed AA, which would set the basis for ‘deep integration’ based on a harmonization of laws and regulations, including a series of ‘mutual recognition agreements’ (MRAs), with a focus on trade facilitation and the removal of barriers to capital and labour flows.
 - b. Finance investment to help integration. Specifically, the Arab countries need to invest in trans-national, regional infrastructure projects. Specifically, the Arab countries should undertake massive investments in infrastructure with private sector participation, leading to a pan-Arab integrated network of transport, communications, energy, telecommunications and a broadband backbone to provide the “infostructure” for an entry of Arab economies and societies into the digital age. A Trans-Arab Network should be integrated in two strategic

directions. One direction is towards the EU and the Trans European network. Two, towards Asia to provide China, ASEAN and Japan with access to the region's energy supplies.

- c. Assist and finance economic and social policies supporting the convergence of incomes. Increased openness of the Arab countries and integration will require adjustment and are likely to lead to an initial greater divergence of income levels between the partners, given that the poorer countries in the Arab world are also the less-open countries requiring more extensive policy reforms.³¹
- d. Prioritize the development of the capital markets and set the basis for their integration and integrate the payment systems in the Arab countries to create an 'Arab Target' system, establishing the infrastructure for an Arab exchange rate system.
- e. Establish a set of institutions to enable and support economic integration. In particular, it is critical that ARIA be supported by a financial mechanism to include the establishment of a Regional Investment and Development Bank, and consider developing Structural Adjustment Funds.
- f. Assist in the financing of the Arab's entry into the digital age and becoming knowledge-based economies. In particular, the digital gap between the Arab world and the industrialized economies is wide and despite recent progress, may be growing.

37. The next 50 years will, for the Arab countries and their economic and financial integration, hopefully, be unlike the past 50 years. A confluence of factors may induce an Arab awakening. External threats and discrimination may be an active force working towards market creation and economic integration.

There are two roads ahead. One road is one where the Arab countries, neglecting regional integration, continue with unstructured trade policies, without the benefit of the negotiating power of a trading bloc, resulting in limited gains from trade creation and losing from trade diversion, notably in relation to the rapidly growing Asian economies and China in particular.

The other road is one of REI based on 'deep integration'. The Arab countries should sign a unified set of Association Agreements among each other, with a minimum scope and content as those signed with the EU. Such an inter-Arab AA covering economic, diplomatic, social, cultural, environmental and political relations could subsume the large number of existing bilateral and regional agreements. The resulting breakdown of barriers to trade, investment and the movement of people would gradually lead to an Arab awakening and create a market with over three hundred

³¹ There are lessons to be learnt from the EU's financing mechanisms. These included Structural Funds (1958), the EIB (1958), the European Regional Development Funds (1975), the Cohesion Funds (1993) to assist the new members, the European Investment Fund (1994), and the EBRD to assist in the transition of Eastern and Central Europe towards a market based economic system.

million consumers and producers, and allow producers and consumers the benefits of economies of scale and scope. This Arab awakening through REI will lead to a resurgence of economic growth and employment, to an improvement in socio-economic conditions and reduction of poverty, allowing the Arab countries to meet the MDGs.

An Arab awakening is a new 'Welt Anschauung', a vision developed of a region that is 'deeply' economically integrated with the rest of the world, with the EU and Asia, potentially forming the largest market zone of the world. It is a zone where barriers to prosperity and riches, physical and virtual, will have been eliminated. Where our children can interact, trade, invest, and work, without barriers. The vision is realistic and within our grasp. The resources, technology, knowledge are at our disposal.

We need the leadership, the institutions and efficient mechanisms to carry out the vision. It requires courage, determination and long-term commitment. Our children and future generations will not forgive us if we do not steer in that direction. We owe it to them to try. It is time to act. We must take our future in our hands; we must build it and own it. It is strategically irresponsible and unacceptable that our children's future be forged by initiatives from outside the region and through violence and conflict and force of arms.

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<http://www.e-lebanon.com>

<http://www.europa.eu.int>

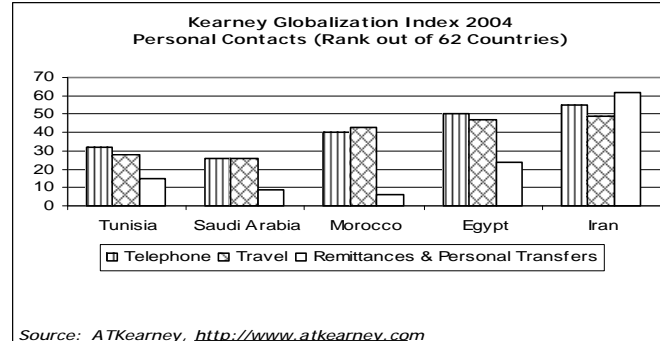
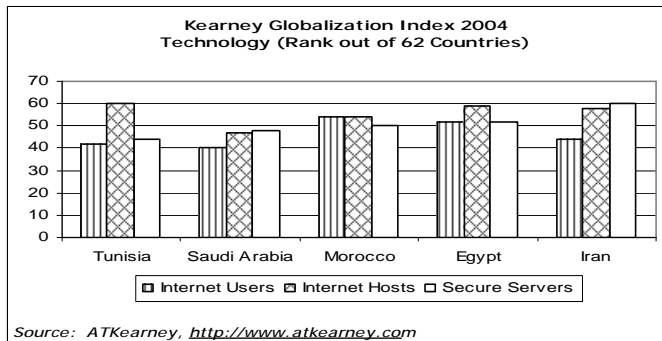
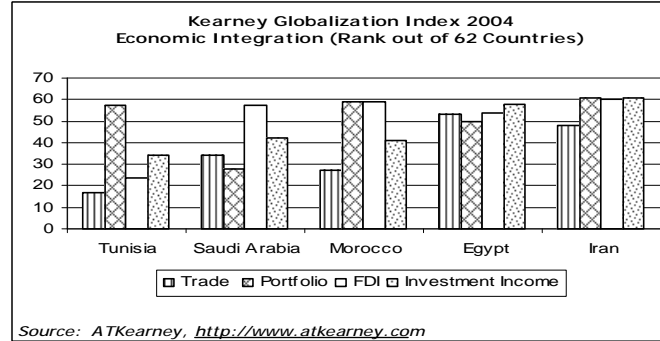
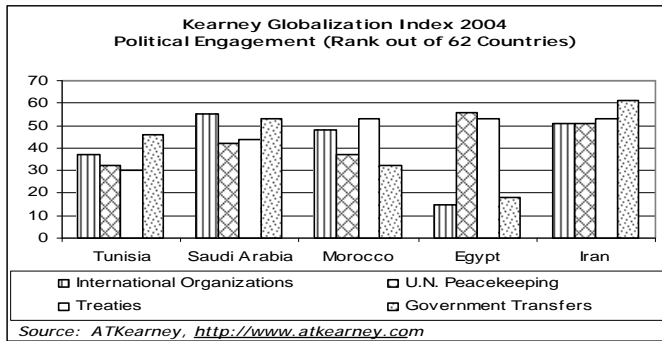
<http://www.imf.org>

<http://www.unctad.org>

<http://www.worldbank.org>

Annex

Annex, Figure 1: A.T. Kearney Globalization Index 2004.



Annex, Table 1: MENA, Spain, Finland and World Comparative Table

	Spain	Finland	MENA	World
People				
Population, total	41.1 million	5.2 million	311.6 million	6.3 billion
Population growth (annual %)	0.4	0.2	1.9	1.2
Economy				
GNI, Atlas method (current US\$)	698.2 billion	140.8 billion	689.4 billion ¹	34.5 trillion
GNI per capita, Atlas method (current US\$)	16,990	27,020	2250 ¹	5,500
GDP (current \$)	836.1 billion	161.5 billion	677.0 billion ¹	36.4 trillion
GDP growth (annual %)	2.4	1.9	3.1 ¹	2.6
Value added in agriculture (% of GDP)	3.4 ¹	3.4 ¹	10.8 ¹	4 ²
Value added in industry (% of GDP)	30.1 ¹	32.6 ¹	41.3 ¹	29.6 ²
Value added in services (% of GDP)	66.5 ¹	64 ¹	47.9 ¹	66.4 ²
Exports of goods and services (% of GDP)	28.5 ¹	38.1 ¹	34.2 ¹	23.8 ¹
Imports of goods and services (% of GDP)	30 ¹	30.2 ¹	28.7 ¹	23.2 ¹
Gross capital formation (% of GDP)	26 ¹	19.6 ¹	23 ¹	20 ¹
Technology and infrastructure				
Fixed lines and mobile telephones (per 1,000 people)	1330.4 ¹	1390.9 ¹	180.2 ¹	363.8 ¹
Personal computers (per 1,000 people)	196 ¹	441.7 ¹	38.2 ¹	100.8 ¹
Internet users	6.4 million ¹	2.7 million ¹	9.7 million ¹	622.6 million ¹
Paved roads (% of total)	99 ²	64.5 ²	63.8 ²	45.1 ²
Aircraft departures	500.0 K ¹	108.5 K ¹	428.6 K ¹	20.5 K ¹
Trade and finance				
Trade in goods as a share of GDP (%)	41.9 ¹	59.6 ²	50.5 ¹	40.3 ¹
Trade in goods as a share of goods GDP (%)	117.3 ¹	141 ¹	90.9 ¹	107.3 ²
High-technology exports (% of manufactured exports)	6.9 ¹	24.2 ¹	2 ¹	21.4 ¹
Foreign direct investment, net inflows in reporting country (current US\$)	25.5 billion	2.9 billion	1.8 billion	630.8 billion ¹
Aid per capita (current US\$)	21.3 ¹	11.3 ¹

Source: World Development Indicators database, August 2004

¹ Year 2002 Figures, ² Year 1999 Figures

Annex, Table 2: Arab Countries Intra-regional Imports and Exports

Exports by: 1/					
	Arab Countries	Maghreb Countries	GCC Countries	Selected Mashreq Countries	Other Countries
(Intra-regional exports, in billions of U.S. Dollars)					
Export to:					
Arab Countries, of which:	12.0	1.6	7.5	2.6	0.3
Maghreb	2.0	1.0	0.6	0.4	0.0
GCC	6.8	0.1	5.3	1.2	0.2
Selected Mashreq	2.6	0.5	1.2	1.0	0.0
Other	0.6	0.0	0.4	0.0	0.1
(Intra-regional exports, as percent of exports to world)					
Arab Countries, of which:	8.2	4.9	7.7	22.7	12.5
Maghreb	1.4	3.1	0.6	3.3	0.0
GCC	4.6	0.4	5.5	10.2	7.5
Selected Mashreq	1.8	1.4	1.2	8.6	0.1
Other	0.4	0.0	0.4	0.6	4.9
(Intra-regional exports, as percent of exports to Arab countries)					
Arab Countries, of which:	100.0	100.0	100.0	100.0	1000.0
Maghreb	16.7	63.2	7.7	14.7	0.1
GCC	56.6	7.6	71.4	44.9	59.9
Selected Mashreq	21.8	29.1	15.6	37.7	0.8
Other	4.9	0.1	5.2	2.7	39.3
<i>Source: IMF Direction of Trade Statistics, 1998 Yearbook.</i>					
1/ Country groupings are:					
Maghreb: Algeria, Libya, Mauritania, Morocco, Tunisia.					
GCC: Bahrain, Kuwait, Oman, Saudi Arabia, United Arab Emirates.					
Selected Mashreq Countries: Egypt, Jordan, Lebanon, Syria, Sudan.					
Other Countries: Djibouti, Somalia, Yemen.					

Annex, Table 3: Aggregate Intra-Arab FDI Flows

Aggregate Intra-Arab FDI Flows 1985-2002 (\$ thousands)															
To/ From:	JORDAN	EMIRATES	BAHRAIN	TUNISIA	ALGERIA	SAUDI ARABIA	SYRIA	OMAN	QATAR	KUWAIT	LEBANON	EGYPT	MOROCCO	YEMEN	TOTAL
JORDAN	*	11,815	1,541	239		35,149	43,319		5,442	13,509	20,334	37,029	859	627	172,784
EMIRATES	1,277	*	43,782	85	26	6,535,549	18,002	66,879	254,862	362,122	44,136	10,702	1,092	1,546	7,370,136
BAHRAIN	359	59,912	*	627		376,004	80	796	2,729	180,837	26,834	2,950			663,804
TUNISIA	15,844	144,204	2,832	*	5,425	405,282	3,961		20,689	359,073	8,335	4,705	100,254	192	1,489,282
ALGERIA	10,320	28,329	20,100	24,660	*	41,488	22,800		7,000	26,296	11,190	337,050		24,300	872,045
SAUDI ARABIA	9,636	157,112	149,665	3,447	4,005	*	539,722	3,120	66,358	153,349	270,627	173,039	8,090	130,809	2,005,324
SYRIA	1,021	375,386	21,688	5,455	303	372,548	*	5,757	12,662	338,258	246,057	6,695	50		1,405,458
OMAN	1,111	39,185	12,241			34,989	1,176	*	7,624	3,405	4,338	434		36,192	151,695
QATAR	624	78,740	2,833			63,925	2,343	14	*	107,711	841	280		55	270,204
KUWAIT	27,801	954	1,035	847		5,461	17,526	1,921		*	11,111	5,469	168	723	73,016
LEBANON	173	804,405	21,486	662		1,205,470	150,339	891	91,601	683,628	*				2,959,655
EGYPT	14,992	221,756	56,719	13,500	5,618	1,579,560	122,710	65,525	228,637	60,044	83,284	*	45,856		2,859,018
MOROCCO	445	76,847	65,830	22,660	16,133	171,949	26,882		2,334		8,675		*	26,444	463,050
YEMEN	1,636	15,549	223		33	197,220	10,613	14,495	64,364	3,479	12,302	37,526		*	387,302
TOTAL	057,258	2,327,193	399,975	81,180	47,857	12,635,287	1,139,668	159,398	978,459	3,549,346	815,126	686,989	160,813	236,171	*

Source: AMF

Annex, Table 4: Trade and Services Agreements, Preferential Agreements and Others

Trade and Services Agreements, Preferential Agreements and Others (Chronological)					
50s	60s	70s	80s	90s	00s
EC (Treaty of Rome) 1-Jan-58 Services agreement	EFTA (Stockholm Convention) 3-May-60 Free trade agreement	EFTA accession of Iceland 1-Mar-70 Accession to free trade agreement	SPARTECA 1-Jan-81 Preferential arrangement	MERCOSUR 29-Nov-91 Customs union	EC — South Africa 1-Jan-00 Free trade agreement
EC (Treaty of Rome) 1-Jan-58 Customs union	CACM 12-Oct-61 Customs union	EC — OCTs 1-Jan-71 Free trade agreement	LAIA 18-Mar-81 Preferential arrangement	AFTA 28-Jan-92 Preferential arrangement	EC — Morocco 1-Mar-00 Free trade agreement
	TRIPARTITE 1-Apr-68 Preferential arrangement	EC — Switzerland and Liechtenstein 1-Jan-73 Free trade agreement	CER 1-Jan-83 Free trade agreement	CEFTA 1-Mar-93 Free trade agreement	EAC 7-Jul-00 Preferential arrangement
		PTN 11-Feb-73 Preferential arrangement	CAN 25-May-88 Preferential arrangement	MSG 22-Jul-93 Preferential arrangement	SADC 1-Sep-00 Free trade agreement
		EC — Iceland 1-Apr-73 Free trade agreement	CER 1-Jan-89 Services agreement	EEA 1-Jan-94 Services agreement	United States — Jordan 17-Dec-01 Services agreement
		EC — Norway 1-Jul-73 Free trade agreement	GSTP 19-Apr-89 Preferential arrangement	NAFTA 1-Jan-94 Free trade agreement	United States — Jordan 17-Dec-01 Free trade agreement

Trade and Services Agreements, Preferential Agreements and Others (Chronological)					
50s	60s	70s	80s	90s	00s
		CARICOM 1-Aug-73 Customs union		NAFTA 1-Apr-94 Services agreement	EFTA — Jordan 1-Jan-02 Free trade agreement
		Bangkok Agreement 17-Jun-76 Preferential arrangement		COMESA 8-Dec-94 Preferential arrangement	EC — Jordan 1-May-02 Free trade agreement
		EC — Algeria 1-Jul-76 Free trade agreement		CIS 30-Dec-94 Free trade agreement	EFTA 1-Jun-02 Services agreement
		PATCRA 1-Feb-77 Free trade agreement		SAPTA 7-Dec-95 Preferential arrangement	EFTA - Singapore 1-Jan-03 Services agreement
		EC — Syria 1-Jul-77 Free trade agreement		CARICOM 1-Jul-97 Services agreement	EFTA - Singapore 1-Jan-03 Free trade agreement
				EC — Palestinian Authority 1-Jul-97 Free trade agreement	EC - Chile 1-Feb-03 Free trade agreement
				EAEC 8-Oct-97 Customs union	EC - Lebanon 1-Mar-03 Free trade agreement
				EC — Tunisia 1-Mar-98 Free trade agreement	ASEAN - China 1-Jul-03 Preferential arrangement
				CEMAC 24-Jun-99 Preferential arrangement	EU Enlargement 1-May-04 Accession to customs union

Trade and Services Agreements, Preferential Agreements and Others (Chronological)					
50s	60s	70s	80s	90s	00s
				EFTA — Palestinian Authority 1-Jul-99 Free trade agreement	EU Enlargement 1-May-04 Accession to services agreement
				EFTA — Morocco 1-Dec-99 Free trade agreement	EC - Egypt 1-Jun-04 Free trade agreement
					ECO not available Preferential arrangement
					GCC not available Preferential arrangement

Source: WTO

Annex, Table 5: Cost of Doing Business

	East Asia and Pacific	Europe and Central Asia	Latin America and Caribbean	Middle East and North Africa	OECD High income	South Asia	Sub-Saharan Africa
Starting a Business							
Number of Procedures	8	9	11	10	6	9	11
Duration (days)	52	42	70	39	25	46	63
Cost (% GNI per capita)	47.1	15.5	60.4	51.2	8	45.4	225.2
Min. Capital (% GNI per capita)	100.5	51.8	28.9	856.4	44.1	0	254.1
Difficulty of Hiring Index	20	31	44	22	26	37	53
Hiring and Firing Workers							
Rigidity of Hours Index	30	51	53	52	50	36	64
Difficulty of Firing Index	22	42	34	40	26	53	50
Rigidity of Employment Index	24	41	44	38	34	42	56
Firing Costs (weeks)	52	38	70	74	40	84	59
Registering Property							
Number of Procedures	4	6	6	6	4	5	6
Time (days)	51	133	56	54	34	55	114
Cost (% of property per capita)	4.2	3	5.6	6.8	4.8	6.1	13.1
Getting Credit							
Cost to Create Collateral (% of income per capita)	2	7.6	19.4	18.6	5.2	8	41.8
Legal Rights Index	5	5	3	3	6	3	4
Credit Inform. Index	1	2	4	2	5	1	2
Public Credit Registry Coverage (borrowers per 1000 adults)	33	6	85	20	76	1	1

	East Asia and Pacific	Europe and Central Asia	Latin America and Caribbean	Middle East and North Africa	OECD High income	South Asia	Sub-Saharan Africa
Private Bureau Coverage (borrowers per 1000 adults)	33	6	85	20	76	1	1
Protecting Investors							
Disclosure Index	3.6	2.3	2.6	5.6	2.9	2.3	2.3
Enforcing Contracts							
Number of Procedures	27	29	35	38	19	29	35
Time (days)	316	412	462	437	229	349	434
Cost (% of debt)	56.9	17.6	23.3	17.9	10.7	38.5	42.9
Closing a Business							
Time (years)	3.4	3.3	3.6	3.8	1.6	5.1	3.5
Cost (% of estate)	29.8	13.1	15.8	13	6.8	8.3	20.5
Recovery Rate (cents on the dollar)	30.4	30.5	26.6	28.6	72.2	21.4	17.1

Source: <http://rru.worldbank.org/DoingBusiness/default.aspx>

Annex, Table 6: Evolution of GDP Per region

Evolution of GDP per region							
Country/Region	GDP % of the World GDP				Annual GDP growth rate % of the World GDP		
	1962	1980	1990	2000	1962-1979	1980-1989	1990-2000
World	100	100	100	100	5.45	3.18	3.69
OECD countries	86.94	84.12	82.85	79.06	5.26	3.02	2.21
non OECD countries	13.06	15.88	17.15	20.94	6.60	3.98	4.76
EU- 15 members	32.11	34.46	31.84	28.91	5.87	2.36	1.70
USA	36.28	26.00	25.99	27.47	3.52	3.17	3.26
Americas	42.89	35.01	0.00	35.52	4.27	2.78	3.24
NAFTA	37.23	29.42	29.17	30.77	4.08	3.09	3.24
Latin America and Caribbean	6.60	6.80	5.56	5.89	5.62	1.13	3.28
MERCUSOR	3.90	4.13	3.24	3.39	5.78	0.73	3.14
CARICOM	0.10	0.08	0.07	0.07	4.33	1.97	2.05
Asia	19.28	24.56	28.58	29.76	6.88	4.75	3.10
EAP	17.88	23.41	27.12	27.89	7.04	4.71	2.98
South Asia	1.40	1.15	1.47	1.86	4.29	5.71	5.19
China	0.61	0.89	1.58	3.18	7.70	9.29	10.10
Japan	13.66	18.00	19.67	17.36	7.08	4.09	1.41
ASEAN	0.93	1.35	1.78	2.22	7.62	6.10	4.99
Sub-Saharan Africa	1.37	1.23	1.11	1.04	4.82	2.14	2.05
MENA	1.16	2.08	1.84	1.94	8.90	1.95	3.20

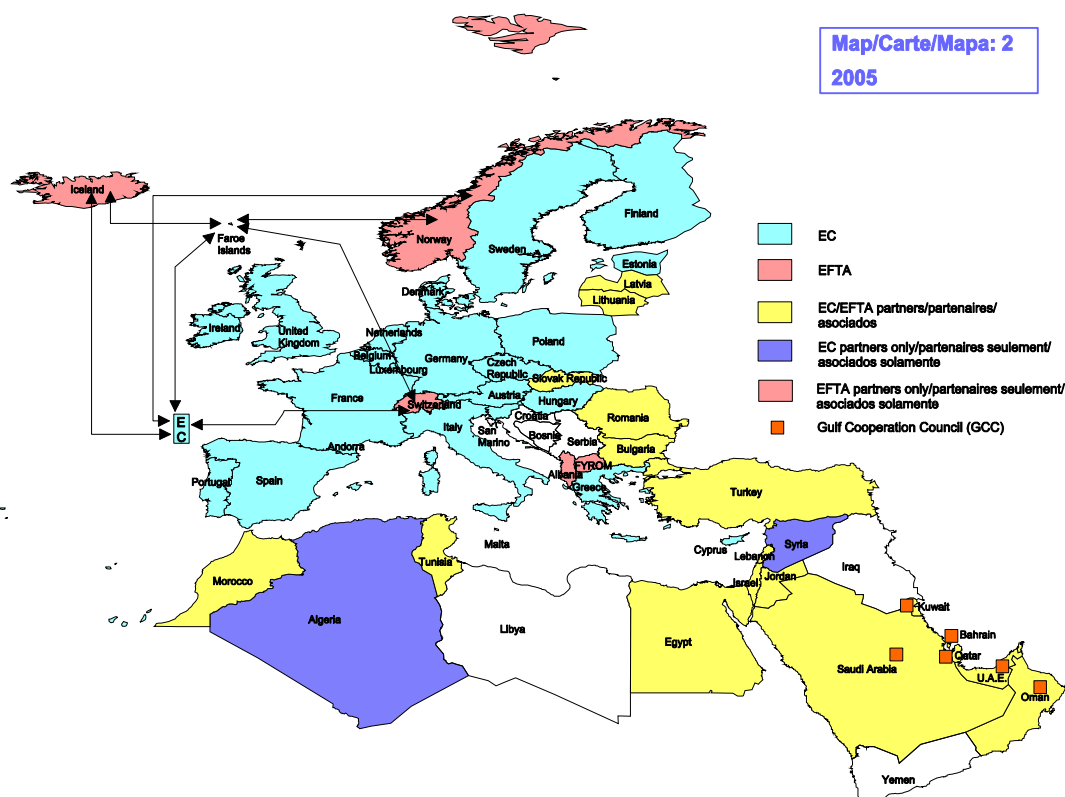
Source: Carrere and Schiff, (2003)

Annex, Table 7: Arab World Share of World's Totals

Arab World Share of World Totals			
	Arab World	World Total	Arab World as Percentage of World Total
GDP in 2001 (billions of US dollars)	632	30938.8	2.0
Population in 2001 (millions)	289.9	6134.1	4.7
Total Exports in 2000 (billion of US dollars)	243.3	7603.1	3.2
Total Imports in 2000 (billions of US Dollars)	152.5	10892.9	1.4
Number of fixed telephone lines in 2001 (millions)	21	1046	2.0
Fixed telephone density in 2001 (lines per 100 residents)	8.2	17.2	-
Number of mobile phone lines in 2001 (millions)	16	946	1.7
Mobile telephone density in 2001 (lines per 100 residents)	6.3	15.6	-
Number of personal computers in 2001 (per 10,000 residents)	2	8.4	-
FDI inflow (billions of US dollars)	6	753.4	0.8
Countries acceded to WTO as of February 2002	11	144	7.6
Countries negotiating for accession to WTO as of February 2002	5	30	16.7
Number of Tourists in 2001 (millions)	33.2	692	4.8
Tourism Revenues in 2001 (billions of US dollars)	16	463	3.6

Source: ESCWA, based on national and international sources
A dash (-) indicates that the item is not applicable

Annex, Figure 2: 2005 Expected RTAs between EC and EFTA, (Source: WTO)

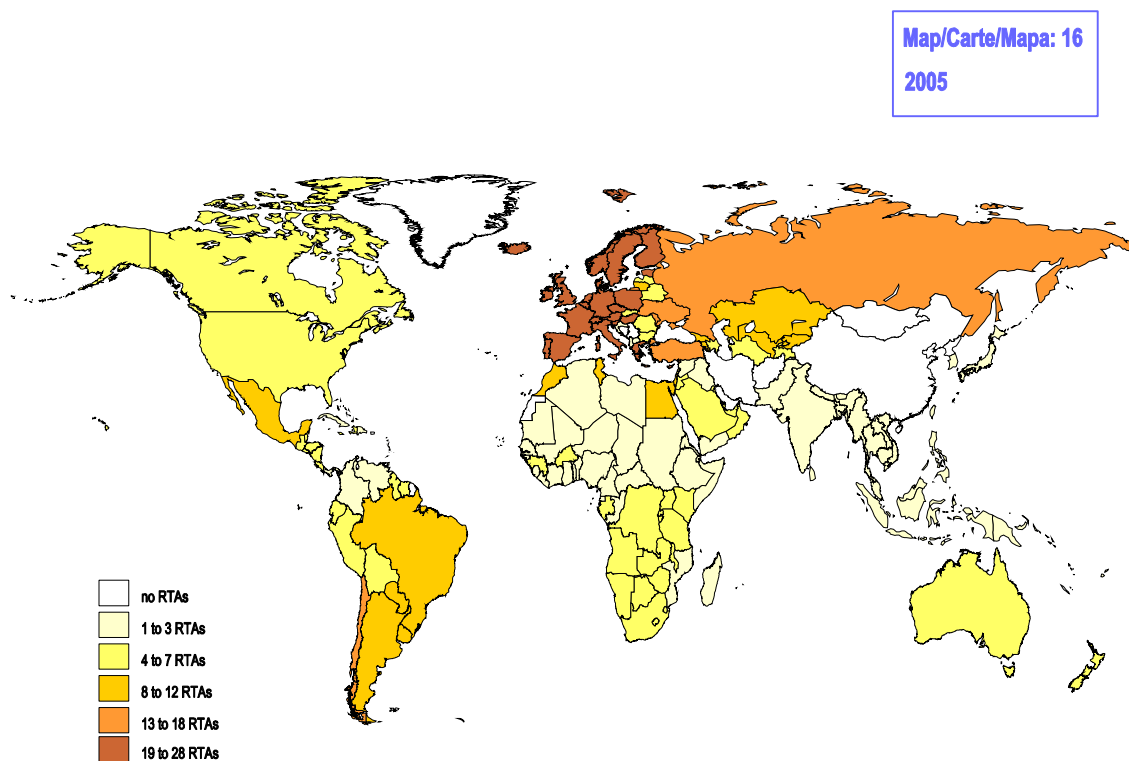


The above map shows the network of RTAs expected to be in force by 2005 between the EC and EFTA with other countries in the Euro-Mediterranean region.^{32,33} By 2005, it is expected that EFTA will have concluded RTAs with Malta, Tunisia, Jordan, Lebanon, Egypt, Albania and the Former Yugoslav Republic of Macedonia (F.Y.R.O.M). Meanwhile the EC is expected to extend its network to include Algeria, Lebanon, Egypt and Syria. RTAs between the EC and EFTA respectively and the six member countries of the Gulf Cooperation Council should be in force by 2005. The enlargement of the EC to include Cyprus, the Czech Republic, Estonia, Hungary, Poland and Slovenia, also scheduled for 2005, will have a considerable impact on the existing web of agreements in this region. The six new EC members will automatically become parties to the EC's existing network of agreements, superseding the six acceding countries' bilateral RTAs. In the medium term, a Euro-Mediterranean free-trade area may be in place by 2010.

³² Other RTAs expected to be in force by 2005 in the Euro-Mediterranean region (which do not involve the EC or EFTA) are shown in Maps 4 and 6.

³³ The EC's and EFTA's RTAs with the Palestinian Authority are not shown. Only the EC (not EFTA) has RTAs with Andorra and San Marino. Both the EC and EFTA have RTAs with Malta. The Faroe Islands are a self-governing part of Denmark, but not part of the EC. Assumes the enlargement of the EC to include Cyprus, the Czech Republic, Estonia, Hungary, Poland, and Slovenia.

Annex, Figure 3: 2005 Expected RTAs in MENA, (Source: WTO)

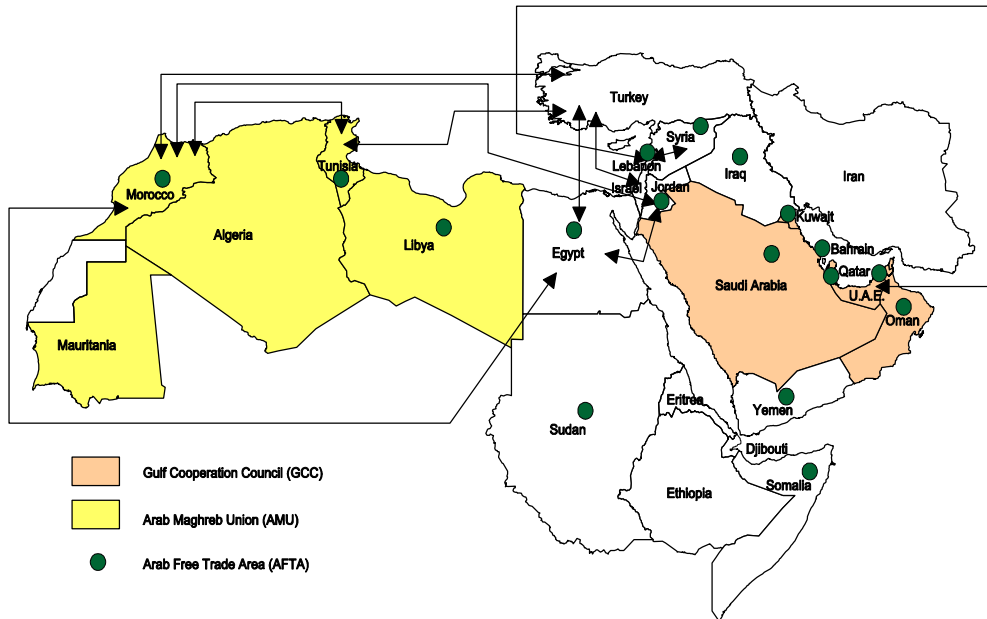


The above map shows the network of RTAs expected to be in force by 2005 in North Africa and the Middle East.³⁴ By 2005, Turkey, Morocco and Egypt are expected to extend their networks of bilateral RTAs, while the majority of countries in this sub-region should become part of the Euro-Mediterranean Free-trade area, scheduled for 2010.

³⁴ The RTAs between Israel and the Palestinian Authority, and Turkey and the Palestinian Authority are not shown. The Palestinian Authority is a member of AFTA.

Annex, Figure 4: Countries Involvement in RTAs, (Source: WTO)

Map/Carte/Mapa: 6
2005



The above map shows the expected level of involvement of individual countries/customs territories in RTAs in 2005. It also shows that a significant number of countries are likely to be involved in more RTAs by 2005.³⁵ This trend is most evident in the Americas and in Eastern Europe and Central Asia and also partly in the Euro-Mediterranean Region. By contrast, countries in Sub-Saharan Africa are not expected to conclude new regional RTAs, but to focus on the implementation, consolidation, and/or extension of existing ones.

³⁵ While 38 per cent of countries are currently involved in more than three RTAs, that percentage will rise to 59 per cent in 2005.