**Initial Conditions and Incentives for Arab Economic Integration: Can the European Community's Success Be Emulated?**

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**Abstract**

This paper compares European Community (EC) ‘trade fundamentals’ that prevailed in the 1960s with those that apply in Arab countries today. These fundamentals differ significantly – Arab countries trade much less with each other than EC members did, and the importance of such trade in GDP varies greatly. This suggests that a viable Arab integration strategy must follow a path that differs from the preferential trade liberalization-led approach implemented by the EC. An alternative is to complement long-standing attempts to liberalize merchandise trade with an effort that revolves around service sector reforms and liberalization. This may prove to be an effective mechanism to support reforms since in principle there is a major constituency in each Arab country that has an interest in improving the performance of services – the natural resource-based and manufacturing sectors. A key condition for such an approach to be feasible is that Arab cooperation helps overcome political economy resistance to national unilateral action, or that it generates direct gains from cooperation in specific policy areas. The EC experience suggests that a services-based integration strategy will be complex and must be carefully designed and sequenced. Given the importance of service-related trade and logistics transaction costs, a first step might focus on bringing such costs down through a concerted joint effort.

## I. Introduction

Regional integration is a central element of the trade strategies being pursued by many Arab countries. All countries in the region have concluded numerous bilateral agreements reducing trade barriers on a preferential basis, and many members of the Arab League are attempting to abolish tariffs on intra-Arab trade flows altogether. Most Arab countries bordering the Mediterranean have also signed free trade agreements with the European Community (EC) that aim to eliminate tariffs on trade in goods with the EC (with the exception of agriculture) and that also embody elements of "deeper" integration – provisions that call for cooperation in trade-related regulatory areas and future negotiation to liberalize investment and services flows.

While efforts to liberalize trade between Arab countries on a preferential basis have been limited in scope, this is changing due to the implementation of the 1998 Arab League Greater Arab Free Trade Area (GAFTA), which obliges signatories to gradually eliminate tariffs by 2006 (Zarrouk, 2000). However, GAFTA is a traditional agreement that is limited to merchandise trade. In contrast to the EC treaty, the GAFTA does not imply the creation of a common market for services, investment, and other factor flows. Nor does it involve the establishment of common institutions with supra-national powers.

This paper reviews the European integration experience to draw lessons that relate to the pursuit of Arab integration. It does not address the issue of whether there is (or will be) political support for greater economic integration, it investigates instead alternative forms of regional economic integration and their incentives for Arab countries. The paper identifies the initial conditions that prevailed in the EC and describes how member states dealt with major political obstacles to integration through the design of institutions. This paper also compares EC trade fundamentals to those that apply in the current Arab context. The results show that the fundamentals differ significantly, suggesting that Arab integration will have to follow a path that goes beyond an approach based only on merchandise trade liberalization.

One alternative path identified is an integration strategy driven by the service sector. Given the importance of improving service sector performance in many Arab countries and the potential gains from regional cooperation in the regulatory domain, this

may be a more effective route toward greater integration. The EC experience suggests a services-based integration strategy will be complex and should be carefully designed and sequenced. Intra-Arab cooperation in this area could start by focusing on high logistics and trade-related transaction costs (trade facilitation), establishing focal points and benchmarks for pro-competitive regulation of key "backbone" service sectors such as transport, distribution, and communications, as well as making a concerted effort to remove entry barriers and government restrictions on competition.

## II. Key Dimensions of the EC

The basic principle guiding the formation of modern Europe has been an economic process for a fundamentally political goal: the "ever closer union among the peoples of Europe" (Treaty of Rome, Preamble, first paragraph). It is important to understand that this goal was based on a number of historical and economic factors.[1] For example, in the nineteenth century, Europe had been integrated though force of arms by Napoleon which led to a significant convergence in legislation and administrative procedures. Also relevant was how the numerous German states had combined through the mechanism of the Zollverein into a federal Germany. However, more recent history played the primary role in the formation of the EC, in particular World War II. The desire to prevent war was an overriding objective of many of those who supported European integration in the 1950s, based on their strong perception of a positive correlation between trade and peace.[2]

Before the war, European countries relied heavily on trade with each other. The collapse of trade in the 1930s and 1940s provided a strong incentive to remove the barriers that had been built. The challenge was to satisfy the political need to maintain critical national industries as well as the support of powerful interest groups while allowing greater gains from trade to be captured. As is well known, the war years were characterized by large-scale intervention in trade and "beggar-thy-neighbor" competitive

[1] What follows draws in part on Messerlin (2001). See Milward (1984; 1992) for comprehensive discussions of European economic integration.

[2] Mansfield (1994) has concluded that, controlling for other factors, there is a robust negative relationship between the volume of trade between country pairs and the probability of a war between them.

devaluations. The objective of integrating Europe provided the foundation for a mechanism to reopen European markets.

An important feature of the EC is its success managing the trade-off between *net* economic costs and political benefits for members. Europeans who were eager to create some kind of federal Europe were more ready to adopt a series of policies that were more interventionist and costly from an economic efficiency point of view, than Europeans who were merely interested in peaceful coexistence between European states. The search for balance between economic and political aspects has played a major role in EC history. Political objectives were critical in the development of the EC in the sense that costly decisions from an economic perspective were possible because of associated political gains. As a consequence of the perceived decline in political gains from European integration, a reduction in the economic costs of European unification was required to maintain the balance. Political gains from integration are subject to diminishing returns. The political idea of a perpetual peace between France and Germany was profoundly appealing to Europeans born before the 1960s. However, as of 2002, the idea of a Franco-German is was so remote that younger Europeans see no need to pay the economic costs that previous generations of Europeans were ready to pay. Such shifting balances led to efforts to expand membership and deepen integration, and they help explain why external protection has fallen over time.

***Institutions***

The basic constituent elements of the EC are well known. A major objective of the Treaty of Rome, which established the European Economic Community, was the realization of four freedoms: free internal movement of goods, services, labor and capital, including the right of establishment. Thus, the EC aims to establish a common market with a common external commercial policy. The Community is unique in that it goes beyond inter-governmental cooperation. This is reflected, among other things, in the fact that EC law has direct effect and that there are supranational institutions: an executive body (the European Commission); a political oversight body (the European Council); a judiciary (the European Court of Justice [ECJ]); and a directly elected European Parliament. Of these institutions,

the Commission and the ECJ have been the most important in the pursuit of political and economic integration.

The supranational institutions of the EC have played a major role in the process of integration. The European Commission has been the driver and guardian of the integration objective. It has the power to propose directives and regulations, which, if approved by the council and increasingly the parliament, become EC law. Since these laws have direct effect, they supersede national legislation in the area concerned. The commission is a bureaucracy, staffed by nationals of the EC who are formally independent of their governments. The European Council, comprised of the relevant Ministers of member states or Heads of State, depending on the subject matter under consideration, provides national level political oversight. The council must approve all Commission proposals, working either on the basis of unanimity or weighted voting, again depending on the topic. Over time, an increasing number of issues have become subject to voting.

The European Commission administers the common policies of the EC, including those of the two most important areas – trade and agriculture.[3] It also enforces the various treaties that have been concluded or amended over time. Of great importance is the enforcement of rules on fair competition including disciplines on state aids (subsidies) and restrictive business practices by firms, which have the effect of impeding trade and the realization of an integrated internal market. The commission has an interest in expanding its ambit through promulgation of new rules in the pursuit of integration, and also in enforcing the negotiated rules of the game. The commission, an independent European bureaucracy with its own financing (partly obtained from the revenues generated by the common external tariff), has been a defender of the European integration objective at times when member states have been less than enthusiastic (Winters, 1997). The Commission played a major role, for example, in forming a

[3] The Treaty of Rome grants the European Community (not the commission, but a complex mixture of the Council of Ministers and the commission) the exclusive competence in trade policy. However, the way the Treaty defines the scope of this common and exclusive competence is rather clumsy. Article 133 (113 in the initial Treaty of Rome) only provides a non-exhaustive list of trade policy instruments. As a result, determining what is and what is not covered required decades of rulings by the ECJ.

coalition with the private sector in the 1980s to revitalize integration through the proposal of the Single Market Program, also referred to as EC-1992.

This proved to be a powerful instrument for the realization of economic integration since it introduced the principle of mutual recognition and "competition in rules" as well as a series of concrete measures to enhance competition in service markets. This resulted in a boom in foreign direct investment (FDI) inflows and cross-border mergers and acquisitions, and induced the accession of a number of countries that determined the costs of being outside the EC had become greater than the benefits.

The European Commission plays a major role in administering various mechanisms that redistribute income and resources across groups in the EC. Any trade liberalization gives rise to losers, who, depending on their political power, may need to be compensated. Indeed, if the losers are powerful, such compensation is a precondition for liberalization to occur, unless there are other groups in society whose gains are sufficient to induce them to mobilize against those who benefit from status quo trade restrictions. The compensation required to make trade reform politically feasible can take the form of an exception to trade liberalization, long transition periods, transfers from the budget (subsidies), or issue linkage. All of these mechanisms were used in the EC. The common policies on trade and agriculture were designed carefully to maintain relatively high rates of protection for sensitive industries, complemented by transfers (subsidies) to disadvantaged regions and soft lending by the European Investment Bank for infrastructure and related types of projects.

The second major player in the integration venture has been the ECJ, which over time developed a huge case law literature interpreting the validity of national policies. As the ultimate arbiter, the ECJ's decisions are final and binding on the member states. The ECJ played a key role in the design of the Single Market Program by identifying the significant scope for the principle of mutual recognition to overcome national non-trade policies that impeded cross-border competition. More generally, it has ensured objective and consistent application and interpretation of EC law.

***Trade and Trade Policy***

The first milestone in the realization of the common market was the creation of a customs union – the adoption of a common external tariff (CET) and the liberalization of internal trade. To a very large extent, trade and trade policy constituted the glue that held the EC together.

*Trade*: In the mid-1950s, each of the six founding EC member states exported more than 25 percent of their total exports to the rest of the community and, with the exception of Italy with only 11 percent, all of them together represented more than 18 percent of intra-EC trade. Thus, all of the founding members had both a substantial stake in intra-European liberalization of trade and enough power to play a role in the process of creating the EC. Germany, the largest member country, exported almost 30 percent of its total exports to the rest of the EC, accounting for one-third of total intra-EC trade. This initial condition is of great importance in understanding the success of the EC; members not only had great political interest in cementing a binding peace, but also had great economic interest in revitalizing and further expanding intra-European trade. It is important to note that the trade involved merchandise, while trade in services, labor and capital was quite limited compared to other parts of the world.

*Trade policy*: Agreeing to a CET is a major source of difficulty for many customs unions, as illustrated by the Gulf Cooperation Council (GCC), as well as many other attempts to form a customs union (World Bank, 2000). The more unbalanced the initial tariffs across prospective members are, the harder the task becomes, unless high-protection countries are seeking to use the customs union as an instrument to liberalize trade. Sustaining the CET can be equally if not more difficult. Any common tariff will imply adjustment pressure as industries relocate. Industry interests will diverge across countries. In the nineteenth century, the American South objected strenuously to the high protective tariffs sought by US “infant” industries, which were mostly located in the North. The tariffs raised production costs in the South and implied a transfer of resources to the North, exacerbating the tensions that led to the US Civil War. Similar tensions associated with industrial agglomeration and implicit transfers helped cause the demise of the East African Common Market (World Bank, 2000). The initial conditions regarding the formation of the CET were relatively favorable. The EC created its common tariff

from four initial tariff schedules (Belgium, the Netherlands and Luxembourg were already a single customs territory, the Benelux, with a common tariff schedule). Two territories (Germany and Benelux) had rather low tariffs, and two (France and Italy) had relatively high tariffs – an ideal circumstance for using the simplest possible harmonization rule: apply the unweighted average of the four tariff schedules. This greatly facilitated agreement on the level of the external tariff, limiting disputes between EC member states to those tariff lines where duty rates were different enough to make everyone unsatisfied with the outcome of the unweighted average method. There is a non-negligible number of such cases – about 20 percent of all tariff lines (Messerlin, 2001). The General Agreement on Tariffs and Trade (GATT) helped resolve many of these conflicts by lowering tariffs across the board through multilateral negotiating rounds, thereby making the results of the averaging method palatable to the more open member states, while offering compensation to more protectionist members through better access to global export markets.

Liberalization of internal trade was accompanied by managed trade in key sectors such as coal, steel and agriculture, as well as the implementation of a common external trade policy. The latter played a major role in the EC, and to some extent became a substitute for foreign policy. The absence of other ways the EC could take international action (there being no common foreign policy) induced it to establish zones of political influence through the intensive use of discriminatory trade agreements. These agreements have had almost no economic impact on the EC. Rather, their role has been to strengthen or establish the hegemony of certain EC member states. The primary example of this over the past forty years is the role EC trade policy played in supporting the territorial expansion of the EC, which grew from the six founding members in 1957 to nine in 1973, ten in 1981, twelve in 1986, and fifteen in 1995 (not including the direct enlargement of East Germany in 1990, which had been prepared for since the community's inception and was confirmed by special trade arrangements between the former German Democratic Republic and the EC starting in the 1960s).

***Common Sectoral Policies***

European integration has been driven in part by two sectoral engines: agriculture and coal/steel. The EC has common policies in both areas where the focus of common policies is on managing production and trade. In the case of coal and steel, the 1951 Treaty of Paris establishing the European Coal and Steel Community (ECSC), the precursor of the EC, reflected a strong tradition of collusion between steel firms backed by national governments.[4] In the early 1950s intra-EC free trade in steel was impossible given German comparative advantages, therefore substituting prevailing private barriers for public management and control made a lot of political sense. But the price paid would inhibit and distort competition in this industry for the next five decades. Perhaps equally if not more important, it also provided a demonstration for other sector which were given an incentive to push for and support industrial policies that benefited them.

Although the coal and steel industries were of fundamental importance in the design and launch of the European integration effort – not least because they were seen as a major potential source of conflict between France and Germany – agriculture was equally important. In all six founding members in the early 1950s, farming constituted a significant share of the labor force and GDP. Managed trade in this sector was seen as a necessary condition to pursue integration more broadly. The Common Agricultural Policy (CAP) aimed to increase farm productivity, ensure a fair standard of living for the agricultural community, stabilize markets, and assure the availability of supplies at reasonable prices. Until the early 1990s, the CAP was essentially based on using just one instrument (price supports) to achieve all these objectives, causing steadily increasing distortions and costs. The political rationale for the CAP, as in the case of coal and steel, was that free trade, even in principle, was neither feasible nor desirable. As far as the two major players were concerned, Germany wanted access to the large French market which was highly protected (as were almost all EC markets) but could be bought off by the promise of higher prices for agricultural produce (Winters, 1997).

[4] The ECSC provisions were influenced by the "Entente Internationale de l'Acier" (International Steel Cartel), set up in 1926 by steel makers from Belgium, France, Germany, Saarland, and Luxembourg. The "Entente" reflected the prevailing view that cartels were a good mechanism to ensure market stability in the context of intra-European trade liberalization. The ECSC pricing rules (broadly similar to the US Pittsburgh basing point system abandoned in 1924 following an antitrust order) were a major element of "managed trade" in this sector.

Over time, virtually all agricultural goods were subject to common market organizations (CMOs). Until the 1992 CAP reform, the CMOs relied essentially on a set of multiple guaranteed prices determined on an annual or semiannual basis by the Council of Ministers. Because these guaranteed prices were unrelated to world prices, the CAP required import barriers to insulate the product markets from the world market. These barriers took the form of variable import levies. Adjusted on a daily basis, they raised import prices to the level prevailing in the EC. In the 1970s, export subsidies became necessary to dump surpluses into world markets in an effort to limit excess supply caused by high guaranteed prices. As of the 1980s, the CAP imposed such a budgetary burden on the Community that quantitative limits on production were imposed, voluntary set-aside programs were adopted, and subsidies were granted to low-income consumers to increase demand.

The CAP was a great success in terms of expanding output and increasing self-sufficiency in food. Indeed, it was too successful, imposing serious budgetary strains and, more importantly for the rest of the world, it imposed major costs on non-European food producers and generated decades of multilateral tension. Although the justification for the CAP has largely disappeared, agricultural reform remains highly contentious in the EC. Support for agricultural and related rural policies to support farmers remains strong and it is increasing, driven by environmental and public health concerns which, ironically, are due in part to the production-increasing incentives of the CAP.

***Domestic regulation***

It has been argued that Europe could not make much progress toward trade liberalization until "it was discovered ... that further progress depended on ... some policy of 'positive' integration ... because the removal of discriminatory policies threatened to undermine just as many entrenched interests as [policy integration] would have done." (Milward, 1984, p. 421). The rhetoric of EC policymakers and their advisors suggested that "deeper integration," – extending to domestic regulatory regimes and economic policies – was necessary to attain intra-EC free trade. Policymakers in the early 1950s such as Jelle Zijlstra, the Dutch Minister of Economic Affairs, argued that credible tariff removal required "common policies on taxes, wages, prices and employment" (Milward, 1992, pp.

188ff). Many felt that policy harmonization was required to equalize costs and that without it a customs union would not be feasible because countries would impose new forms of protectionist policies. Thus, in the late 1940s the Belgian coal mining industry argued that a common market could only be accepted if German wage and social security costs were raised to Belgian levels.[5] French officials persistently demanded policy harmonization in the social area – equal pay for both sexes, a uniform length of the working week – as a precondition for trade liberalization, given that French standards were higher than those in other countries.

Underlying these concerns were interest groups' fears of an erosion of rents or the worry that domestic policies may be used to reimpose protection. Abstracting from the common policies for coal/steel and agriculture (where managed trade and production was seen as desirable and necessary) in a number of policy areas the EC established disciplines on the ability of governments to use domestic policy instruments as a substitute for trade policy. Disciplines on enterprise behavior that impedes the realization of the common market and on government assistance – subsidies – were enforced by the Commission with varying degrees of intensity, but had an important effect on ensuring that the "conditions of competition" became more equitable over time.

A noteworthy feature of the EC has been its actions toward deeper integration through harmonization of national policies dealing with regulatory objectives. Those actions have focused on limiting the market segmenting effects of national regulations pertaining to health and safety. Progress toward harmonization was very slow, in part because adoption of a EC-wide norm required unanimity. It took fourteen years for an agreement to be reached on the composition of fruit jam and eleven for a directive on mineral water (Vogel, 1995). From 1962-1979 only nine directives on foodstuffs were adopted.

[5] In the discussion of proposals for a European customs union in the early 1950s, virtually every question that came to be addressed in the Maastricht treaty was discussed: a common European currency, monetary policy, whether there should be freedom of labor, mutual recognition of professional qualifications, a common company law, a free capital market, or common workplace and products safety standards (Milward, 1992, p. 191).

In 1979, the ECJ threw out a German ban on the sale of a French product (Cassis de Dijon) used to prepare an aperitif kir because it could not be justified on the basis of public safety or health. This established the principle that goods legally introduced into circulation in one member state could not be barred from entering and being sold in another. This principle was later incorporated into the 1987 Single European Act and the 1992 Maastricht Treaty on European Union. The "new" approach differentiated between standards that have health and safety (public interest) dimensions and those that did not. For the latter it made harmonization redundant by requiring governments to accept foreign regulations as equivalent to their own. For the former, a process of determining common minimum standards ("essential requirements") was agreed upon. Progress toward the development of these standards was made easier by a decision to accept qualified majority voting on issues affecting the functioning and completion of the single market, and defining standardization as a Single Market Program issue.

In sum, integration in the EC was strongly driven by the engine of trade in goods and all members had strong incentives to see intra-EC trade liberalized. Trade in services and factors of production (labor, capital) played only a minor role. The EC's success was partially based on an almost perfect balance of economic power. It was financed by three large countries (France, Germany and Italy) of almost equal size in terms of population and income, and two smaller countries – large and skilled enough to play the key role of mediators – Belgium and the Netherlands. These countries, which traded more than 30 percent of their total external trade with other members, had almost perfectly symmetrical large stakes in the EC endeavor. Their mutual trade dependence and relative symmetry allowed the EC to use trade liberalization as a vehicle for integration and as a result, there was no need to rely significantly on integration of services or labor markets to achieve the members' goals.

This balance was maintained in the enlargement process; the initial balances were never seriously put into question. Britain was as powerful as France or Germany, and Spain was comparable to Italy. Other new members were similar in size to the smaller founding countries. A retrospective sense of the "luck" that accompanied the birth and development of the EC during its first fifty years is best provided by the sudden, short-lived hesitations in Europe that accompanied German reunification. Britain and France

immediately showed old instinctive reactions of fear, while other member states also demonstrated concern. These reactions suggest that the EC would probably not have been founded if there had been a unified Germany.

Integration also had an overriding political objective that was strongly supported by all members – preventing another war in Europe. The EC is the child of three terrible wars (in 1870, 1914 and 1939) that were responsible for millions of deaths in the six EC founding countries. It was born in a world divided into two political and economic regimes (market-driven democracies vs. centrally-planned dictatorships). During its first thirty years it grew under the constant pressure of the Cold War.

To what extent do the economic factors, particularly the initial trade dependence conditions, that prevailed in the EC apply to the Arab context? The driving force of European integration was largely the liberalization of intra-regional trade in non-agricultural merchandise (agriculture being the subject of managed trade and EC-wide policies). Could such trade also be the basis of Arab economic integration?

## III. Merchandise Trade Fundamentals in Arab Countries

Countries in the region can be divided into three groups: relatively natural resource-poor countries (less than one-third of exports comprise natural resources), oil exporters (more than two-thirds of exports consist of natural resources – mostly fuels); and an intermediate group where exports of fuels and ores constitute between one-third and two-thirds of total exports. For completeness and purposes of comparison, data are reported for other regional countries – Cyprus, Israel, Turkey and Iran – as well as for Arab states.

### *National and Regional Small Product Markets*

The economic size of the Arab region is limited. The total GDP of Arab countries that are members of GAFTA (noted with an asterisk in Table 1) represent a little less than Spain's GDP. Only one Arab country (Egypt) has more than 60 million inhabitants. One implication of the "smallness" of many of the countries in the region is that due to differences in national laws or regulations the costs of trade and investment are higher than those for the EC (four EC member states have a population of more than 60 million, and only two member states out of fifteen have a population of less than 5 million).

**Table 1: Overview of Economies in the Middle East and North Africa: Trade Aspects, 1998**

| Countries [a] | WTO status (GATT or WTO accession year) | Population (millions) | GDP $ m [b] | GDP per capita ($ m) [b] | GDP per capita ($ m) [c] | Goods & services [b] Exports $ m | Goods & services [b] Imports $ m | Trade openness ratio (%) [d] | Shares of natural resources in total exports (%) All | Fuels | Non-fuel |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 13 | 14 | 15 |
| | Natural resource-poor countries | | | | | | | | | | |
| Israel | 1962 | 5.8 | 98,973 | 17,064 | 15,920 | 32,085 | 40,763 | 73.6 | 1.9 | 0.6 | 1.3 |
| Turkey | 1951 | 62.5 | 198,006 | 3,168 | 2,780 | 49,021 | 55,894 | 53.0 | 3.9 | 0.9 | 3.0 |
| Cyprus | 1963 | 0.8 | 8,970 | 11,649 | | 3,948 | 4,639 | 95.7 | 8.9 | 0.3 | 8.6 |
| Lebanon * | (negotiating) | 3.1 | 8,352 | 2,660 | 2,660 | | | | 11.3 | 1.4 | 9.9 |
| Morocco * | 1987 | 27.3 | 35,546 | 1,302 | 1,110 | 8,133 | 9,675 | 50.1 | 13.2 | 2.1 | 11.1 |
| Tunisia * | 1990 | 9.2 | 19,936 | 2,162 | 1,820 | 8,464 | 9,103 | 88.1 | 16.0 | 15.0 | 1.0 |
| | Intermediate countries | | | | | | | | | | |
| Jordan * | 2000 | 5.8 | 7,306 | 1,266 | 1,510 | 3,548 | 5,090 | 118.2 | 34.7 | 0.0 | 34.7 |
| Egypt * | 1970 | 62.1 | 82,710 | 1,332 | 790 | 13,932 | 19,274 | 40.1 | 53.2 | 48.5 | 4.7 |
| Bahrain * | 1993 | 0.6 | 6,184 | 10,307 | | 4,838 | 4,202 | 146.2 | 67.3 | 37.1 | 30.2 |
| | Oil-rich countries | | | | | | | | | | |
| Syria * | no | 15.0 | 69,112 | 4,623 | 1,120 | 21,498 | 21,756 | 62.6 | 81.7 | 80.7 | 1.0 |
| Oman * | no | 2.4 | 14,192 | 5,913 | 4,820 | 5,508 | 5,826 | 79.9 | 83.0 | 82.7 | 0.3 |
| UAE * | 1994 | 2.6 | 44,673 | 17,315 | 17,400 | | | 141.5 | 85.1 | 83.1 | 2.0 |
| Iraq * | no | 21.2 | | | | | | | | | |
| Iran | no | 60.7 | 187,423 | 3,088 | | 15,494 | 15,650 | 16.6 | 85.6 | 85.1 | 0.5 |
| Yemen | no | 16.5 | 5,729 | 348 | 260 | | | 91.5 | 90.0 | 89.4 | 0.6 |
| Saudi Arabia * | (negotiating) | 19.5 | 128,377 | 6,587 | 7,040 | 45,605 | 39,434 | 66.2 | 90.5 | 90.2 | 0.3 |
| Qatar * | 1994 | 0.6 | 9,193 | 16,128 | | | | 73.2 | 93.3 | 93.3 | 0.0 |
| Algeria | (negotiating) | 29.1 | 41,158 | 1,417 | 1,600 | | | | | | |
| Libya * | no | 5.8 | | | | | | NA | 96.3 | 96.3 | 0.0 |
| Kuwait * | 1963 | 2.0 | 25,523 | 12,890 | 17,390 | 11,380 | 12,217 | 92.5 | 96.7 | 96.6 | 0.1 |
| | | | | | | | | | | | |
| | Memo items | | | | | | | (avg.) | | | |
| All countries | -- | 277.9 | 950,205 | 3,190 | 2,062 | | | 80.6 | 68.3 | 66.8 | 1.5 |
| GAFTA * | -- | 222.6 | 497,991 | 2,237 | 1,799 | | | 87.5 | -- | -- | -- |

*Notes*: [a] *: Greater Arab FTA (GAFTA) Members. [b] [c] in millions of US dollars, at current exchange rates. [d] Ratio of the sum of exports and imports over GDP. Statistics for Algeria are reported for 1995. Statistics for UAE, Yemen, Qatar, Bulgaria and Poland are reported for 1997.

*Sources*: IMF, International Financial Statistics; World Bank; WTO -Trade Policy Reviews; UN COMTRADE.

The limited market size of the Arab countries is a crucial factor as to why all efforts to achieve regional economic integration since the 1950s have failed – even if one leaves aside the fact that they were conceived behind high protection with respect to the rest of the world.

There is another powerful economic force working against integration: Arab countries are relatively similar and compete more with each other for the same export markets. Most Arab countries in the sample are either oil-rich or rely heavily on oil exports. Since the fundamental motive for trade is to take advantage of differences in endowments (comparative advantage) between trading partners, their similarity suggests limited prospects for large benefits from regional economic integration. Offsetting this is the fact that Arab countries exhibit a wide range of GDP per capita, from less than US$500 (Yemen) to US$17,000 (UAE and Qatar). Such large income differences generate incentives to trade by inducing product differentiation in order to respond to different incomes and related tastes. But these differences appear too wide for the small markets to become a powerful force for significantly greater intra-regional trade. That leaves the possibility of production sharing or a processing-type of trade, where labor, energy or water-intensive parts of the production process are undertaken in countries where such factors are in relative abundance. This type of trade has become important in Central Europe, North America, and East Asia. However, for this to materialize there must be a substantial increase in the efficiency of services (reduction in transaction costs).

To summarize, the data suggest that the region is fragmented into relatively small economies and is relatively small in economic size; that many countries have similar production structures which limit their incentives to trade; and that the wide income differences in the region are unlikely to overcome the resulting trade resistance.

***Product Concentration and Differentiation***

As natural resources dominate exports of a majority of Arab countries, we have focused so far on "inter-industry" trade. This is based on specialization in production, with countries producing different products using different factor intensities. Such trade may be associated with a concentrated export structure if the country's comparative advantage in a limited range of products is very strong. Inter-industry trade is complemented by "intra-industry" trade, involving the exchange of different varieties of similar products, or the exchange of goods that form part of a production chain (importing components and exporting the processed goods). In most high-

income and newly-industrializing countries, intra-industry trade accounts for a large and growing share of total trade.

The scope for intra-industry trade is more limited for fuels than for consumer electronics, but it exists even within the oil sector, broadly defined. There are many varieties of fuels and numerous possibilities to produce differentiated oil-based industrial products such as chemicals. The potential for specialization and intra-industry trade is augmented by the fact that oil and chemical markets are oligopolistic enough to induce the few large firms operating in such markets to follow a policy of profit maximization through market segmentation and product differentiation. More generally, intra-industry trade is driven by the existence of economies of scale that make it profitable for enterprises to specialize in similar but differentiated goods and for countries to exchange them.

Various measures of the structure and composition of trade are reported in Table 2. Two indicators of product concentration in trade are reported: the number of distinct product categories exported measured at the 3-digit level of the Standard International Trade Classification (SITC),[6] and the Herfindahl-Hirschmann index (HHI).[7] As expected, oil-rich countries have concentration indices that are much higher than those of natural resource-poor countries – reflecting the concentration in oil (ores) and oil-derived exports imposed by their very strong comparative advantages in fuels. However, this generalization requires some qualification. The UAE and Saudi Arabia have relatively diverse exports, reflecting entrepôt activity as well as processing and light manufacturing activities in the UAE, and the chemical sector in Saudi Arabia. Also, the number of product categories exported increased substantially for some oil exporters such as Qatar. The shares of intermediate or resource poor Arab countries are below those of Asian comparator economies, suggesting a narrower industrial base. In a number of countries, especially Egypt, Morocco and Tunisia, there has been a significant diversification of the export base as measured by the SITC indicator. Indeed, on average, the last two decades have seen trade in the region become less concentrated. The HHI index suggests

[6] The SITC is a UN statistical classification for international trade. There are 239 different SITC items at the 3-digit level. The SITC measure of concentration is defined as the ratio between the number of 3-digit items for which exports exceed US$ 100,000 and the total number of 3-digit items (there are 239 such items). For small countries an additional criterion of at least a 0.3 percent share in total exports is used.

[7] The HHI is defined as the sum of the squares of the market share of each export item in total exports. The lower the HHI, the less concentrated the exports. The HHIs are calculated on the basis of the 3-digit level of the SITC.

that this trend is more general than the SITC measure – concentration appears to have been falling pretty much across the board. In the case of oil-rich countries, this reflects the oil price decline that occurred during this period which made the production of fuels less profitable compared to the production of oil-derivatives or other goods. But for a number of countries, especially those that are resource poor or less endowed with oil, it reflects the pursuit of domestic reforms. Egypt registered a particularly large increase in diversification, rising from 33 to 68 percent on the SITC diversification measure, while the HHI fell from 0.58 to 0.28. Similarly large reductions in the HHI occurred in Morocco and Tunisia.

**Table 2: Structure of Exports: Product Concentration and Differentiation**

| | Share of SITC items exported (%) [a] | | Index of concentration [b] | | Intra-industry trade index [b] | | Share of components in total industrial trade (%), 2000 | |
|---|---|---|---|---|---|---|---|---|
| | Natural resource-poor cont. | | | | | | | |
| | 1980 | 1997 | 1980 | 1997 | 1988 | 2000 | Imports | Exports |
| Israel | 0.84 | 0.84 | 0.26 | 0.28 | 0.64 | 0.62 | 19.5 | 19.0 |
| Turkey | 0.79 | 0.93 | 0.23 | 0.10 | 0.22 | 0.31 | 12.5 | 3.9 |
| Cyprus | 0.50 | 0.46 | 0.15 | 0.15 | 0.22 | 0.32 | 12.8 | 3.1 |
| Lebanon | 0.81 | 0.67 | 0.16 | 0.13 | 0.26 | 0.18 | 11.8 | 3.5 |
| Morocco | 0.42 | 0.66 | 0.32 | 0.18 | 0.14 | 0.24 | 19.2 | 2.5 |
| Tunisia | 0.53 | 0.75 | 0.48 | 0.21 | 0.23 | 0.29 | 14.4 | 7.4 |
| | | | | | | | | |
| | Intermediate countries | | | | | | | |
| Jordan | 0.45 | 0.47 | 0.35 | 0.27 | 0.09 | 0.16 | 18.4 | 8.5 |
| Egypt | 0.33 | 0.68 | 0.57 | 0.28 | 0.07 | 0.18 | 24.7 | 3.1 |
| Bahrain | 0.24 | 0.45 | 0.79 | 0.63 | 0.24 | 0.18 | 16.5 | 6.9 |
| | | | | | | | | |
| | Oil-rich countries | | | | | | | |
| Syria | 0.44 | 0.45 | 0.63 | 0.56 | 0.03 | 0.11 | 7.6 | 0.4 |
| Oman | 0.42 | 0.61 | 0.92 | 0.72 | 0.25 | 0.14 | 18.8 | 14.0 |
| UAE | 0.82 | 0.88 | 0.87 | 0.62 | 0.11 | 0.22 | 20.8 | 10.9 |
| Iran | 0.37 | 0.72 | 0.81 | 0.80 | 0.02 | 0.08 | 25.6 | 2.2 |
| Yemen | | | | | 0.02 | 0.03 | 19.6 | 6.7 |
| Saudi Arabia | 0.77 | 0.73 | 0.94 | 0.74 | 0.13 | 0.13 | 19.0 | 7.1 |
| Qatar | 0.01 | 0.30 | 0.93 | 0.73 | 0.04 | 0.07 | 20.4 | 3.7 |
| Libya | 0.18 | 0.12 | 0.96 | 0.77 | 0.03 | 0.04 | 21.3 | 1.6 |
| Kuwait | 0.79 | 0.65 | 0.72 | 0.56 | 0.06 | 0.07 | 17.0 | 3.9 |
| | | | | | | | | |
| | Memo items | | | | | | | |
| Malaysia | 0.85 | 0.94 | 0.30 | 0.19 | 0.58 | 0.64 | 23.1 | 22.5 |
| Korea | 0.85 | 0.92 | 0.09 | 0.14 | 0.40 | 0.57 | 17.6 | 18.3 |
| Taiwan | 0.87 | 0.93 | 0.12 | 0.12 | 0.43 | 0.57 | 17.1 | 24.3 |

*Notes*: [a] Percent of SITC items with "substantial" exports. [b] See text and footnotes for definition.
*Sources*: UNCTAD, Handbook of Trade Statistics, 1997 and 2000; UN COMTRADE.

Table 2 also presents data on the magnitude of intra-industry trade.[8] The higher the intra-industry trade (IIT) index, the more the trade of a country involves the exchange of different varieties of a similar type of product. IIT of Arab countries is far below the ratios registered by Asian comparators, which have IIT indices in the 0.60 range. Among Arab countries, Tunisia has the highest intensity of IIT (30 percent), followed by Morocco and the UAE. The magnitude of IIT has been growing rapidly in a number of other countries, however, especially Egypt and Jordan. Oil-rich countries exhibit particularly low IIT indices, reflecting their strong comparative advantages in a limited number of products. The UAE is an exception, reflecting the entrepôt trading activity of its economy.

Finally, Table 2 presents data on the share of parts and components in total manufactured exports and imports. This indicator provides information on the relative importance of "assembly" activity in total trade. A high share of components in imports combined with a low share of components in exports is observed in all Arab countries, except Oman. This compares with much higher ratios and more balanced trade for dynamic exporters in East Asia. For countries with relatively high GDP per capita (interpreted as a proxy for relatively high wages), a combination of high import share of components and low export share of components suggests a high level of assembly activities for domestic or neighboring markets, and hence a relatively high degree of effective protection against imports of final (assembled) products. Such situations are often the source of large rents for wholesalers or retailers that are able to import for local assembly. This may also prevail in countries with lower GDP per capita levels, but a low share of components in exports could also mean that these countries are used as assembly centers for the re-export of assembled goods. However, data on outward processing trade collected by the EC suggests this is not the case. Only Morocco and Tunisia are relatively large-scale users of this customs regime.

[8] The index is defined as $IIT = 1 - [\sum\sum\sum \left| X_{ijk} - M_{ijk} \right| / (X_{ijk} + M_{ijk})]$, where $X_{ijk}$ represents the exports of products from industry i from country j to country k and $M_{ijk}$ represents the imports of products from industry i by country j from country k. In this study industries are defined at the three digit level of the SITC.

To summarize, Table 2 reveals that most Arab countries tend to have relatively concentrated exports, although this has been changing rapidly for some nations (Egypt, Morocco, and Tunisia); there are low levels of intra-industry trade; and there is a high ratio of imports to exports of components. This suggests important assembly activities directed at domestic markets that are likely to require high protection against imports.

***Political Economy Implications of Intra-Arab Trade Patterns***

The geographical pattern of exports of Arab countries mirrors what has been said about export structure by product – to a large extent, it is the "corollary" in the geographical context of the economic forces at work in the production, demand, and trade patterns. As shown in Table 3, the share of exports from oil-rich countries going to other Arab countries ranges from 0.9 (Kuwait) to 13.1 percent (Oman), mirroring the production concentration of these countries (reflecting their comparative advantages in the world markets) and the fact that oil is consumed everywhere in the world. For Saudi Arabia, the largest oil producer/exporter, the share is only 7.6 percent. The core set of countries that tend to trade substantially with other Arab countries (around 20 percent or more of total exports) is limited to Jordan, Lebanon and Syria (some 34, 45 and 18 percent of total exports, respectively). With the exception of Oman, regional exports for all other Arab countries account for less than 10 percent of total exports.[9]

An important policy question concerning Arab economic integration is whether these levels of intra-regional trade are too low because of barriers to trade. The trade intensity index is an often used index of the intensity of regional trade and is helpful in determining whether the value of trade between two countries is above or below what would be expected on the basis of their importance in world trade. Identifying bilateral combinations where trade is below expected levels can also help to identify the existence of major barriers to trade.

[9] It should be noted that there is some uncertainty on the direction of trade given weak reporting by several countries.

**Table 3: Geographic Destination of Exports, 2000**

| | | Exports as % of Total Exports | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | World | All Indus. Countries | Indus. Europe | North America | Asia & Pacific | All Non-Indus. Co. | Africa | Asia | Europe | Arab nations | Latin America | Not Specified |
| Country | ($ m) | | | | | | | | | | | |
| Algeria | 20,468 | 83.4 | 66.7 | 16.5 | 0.2 | 16.6 | 1.3 | 0.8 | 6.2 | 1.1 | 8.2 | 0.0 |
| Bahrain | 5,701 | 16.8 | 6.9 | 5.6 | 4.4 | 83.2 | 3.4 | 27.4 | 0.6 | 9.7 | 0.2 | 42.1 |
| Cyprus | 953 | 39.6 | 36.9 | 2.4 | 0.2 | 60.4 | 2.5 | 2.8 | 15.6 | 26.1 | 0.3 | 11.8 |
| Egypt | 5,633 | 61.1 | 43.8 | 14.9 | 2.4 | 38.9 | 2.6 | 11.2 | 4.5 | 9.7 | 1.0 | 10.8 |
| Iran | 28,345 | 43.7 | 25.6 | 0.9 | 17.3 | 56.3 | 0.0 | 30.0 | 3.9 | 7.5 | 0.2 | 14.7 |
| Israel | 31,910 | 69.6 | 28.6 | 37.7 | 3.4 | 30.4 | 1.5 | 15.3 | 4.3 | 0.3 | 2.9 | 6.1 |
| Jordan | 1,897 | 6.8 | 2.6 | 3.4 | 0.8 | 93.2 | 3.3 | 22.0 | 1.2 | 33.8 | 0.3 | 33.9 |
| Kuwait | 17,752 | 55.9 | 14.6 | 15.2 | 26.1 | 44.1 | 0.1 | 41.8 | 0.9 | 0.9 | 0.5 | 0.0 |
| Lebanon | 715 | 36.2 | 27.0 | 8.0 | 1.3 | 63.8 | 6.7 | 4.2 | 6.9 | 45.2 | 0.6 | 1.4 |
| Libya | 12,688 | 88.2 | 88.1 | 0.0 | 0.1 | 11.8 | 2.7 | 0.5 | 7.5 | 3.3 | 0.2 | 0.1 |
| Morocco | 8,228 | 73.6 | 62.7 | 5.9 | 3.7 | 19.0 | 1.3 | 8.5 | 3.3 | 4.4 | 2.4 | 7.4 |
| Oman | 10,542 | 22.5 | 1.3 | 2.5 | 18.8 | 77.5 | 0.9 | 63.4 | 0.0 | 13.1 | 0.0 | 0.0 |
| Qatar | 11,527 | 51.0 | 1.1 | 3.7 | 46.3 | 49.0 | 0.8 | 31.9 | 0.1 | 6.3 | 0.1 | 9.8 |
| Saudi Arabia | 74,688 | 54.9 | 17.9 | 18.2 | 18.8 | 45.1 | 2.6 | 32.9 | 1.2 | 7.6 | 1.5 | 0.0 |
| Syria | 4,981 | 63.5 | 59.6 | 3.5 | 0.3 | 36.5 | 1.1 | 1.5 | 13.7 | 18.1 | 0.2 | 3.0 |
| Tunisia | 5,986 | 80.2 | 79.1 | 0.8 | 0.3 | 16.0 | 3.4 | 2.5 | 1.7 | 8.9 | 0.9 | 3.1 |
| Turkey | 27,768 | 66.4 | 53.4 | 11.9 | 1.0 | 33.6 | 3.2 | 2.9 | 11.2 | 9.5 | 1.0 | 5.6 |
| UAE | 41,068 | 42.0 | 5.1 | 2.4 | 34.5 | 58.0 | 1.7 | 32.6 | 0.8 | 9.7 | 0.2 | 13.3 |
| Yemen Rep. | 4,076 | 12.3 | 2.4 | 6.2 | 3.8 | 87.7 | 1.9 | 76.2 | 1.1 | 4.2 | 1.6 | 2.7 |
| **Total** | **314,926** | **56.3** | **28.8** | **12.5** | **15.0** | **43.4** | **1.8** | **24.4** | **3.4** | **6.9** | **1.5** | **6.1** |
| | | | | | | | | | | | | |
| **All Developing Countries** | **2,075,378** | **53.9** | **23.7** | **17.2** | **13.0** | **46.1** | **1.7** | **28.7** | **6.3** | **5.0** | **4.2** | **0.1** |

*Source*: IMF (2001), Direction of Trade Statistics Yearbook.

Table 4 reports data on the intensity of trade using a trade intensity index ranging between zero and infinity.[10] Values below unity indicate that trade between two countries is lower than expected; while values above one indicate it is relatively larger. The data suggest that intra-Arab trade flows are not consistently lower than what should be expected. The only countries that trade less than expected with other Arab countries are Algeria and Kuwait. The share of Egypt's exports to the region is about three times larger than expected. Trade intensity indices for Jordan and Lebanon are the highest, followed by Syria. Overall, the intensity index for all regional intra-trade is around 2.5 – more than double the expected level.

**Table 4: Trade Intensity Indices for Middle East and North Africa Countries' Exports, 2000**

| Country | All Industrial Countries | Industrial Countries by Region | | | Developing Countries | |
|---|---|---|---|---|---|---|
| | | Europe | N. America | Asia & Pac. | Asia | Arab |
| Algeria | 1.25 | 1.77 | 0.74 | 0.03 | 0.04 | 0.40 |
| Bahrain | 0.25 | 0.18 | 0.25 | 0.66 | 1.56 | 3.54 |
| Cyprus | 0.59 | 0.98 | 0.11 | 0.03 | 0.16 | 9.52 |
| Egypt | 0.92 | 1.16 | 0.67 | 0.36 | 0.64 | 3.52 |
| Iran | 0.66 | 0.68 | 0.04 | 2.61 | 1.71 | 2.72 |
| Israel | 1.04 | 0.76 | 1.69 | 0.51 | 0.87 | 0.12 |
| Jordan | 0.10 | 0.07 | 0.15 | 0.12 | 1.26 | 12.34 |
| Kuwait | 0.84 | 0.39 | 0.68 | 3.95 | 2.38 | 0.32 |
| Lebanon | 0.54 | 0.71 | 0.36 | 0.19 | 0.24 | 16.47 |
| Libya | 1.32 | 2.33 | 0.00 | 0.01 | 0.03 | 1.22 |
| Morocco | 1.10 | 1.66 | 0.27 | 0.56 | 0.48 | 1.60 |
| Oman | 0.34 | 0.03 | 0.11 | 2.84 | 3.62 | 4.79 |
| Qatar | 0.77 | 0.03 | 0.16 | 7.00 | 1.82 | 2.31 |
| Saudi Arabia | 0.82 | 0.47 | 0.82 | 2.84 | 1.88 | 2.77 |
| Syria | 0.95 | 1.58 | 0.16 | 0.05 | 0.09 | 6.59 |
| Tunisia | 1.20 | 2.09 | 0.04 | 0.04 | 0.14 | 3.26 |
| Turkey | 1.00 | 1.42 | 0.54 | 0.15 | 0.16 | 3.48 |
| UAE | 0.63 | 0.13 | 0.11 | 5.21 | 1.86 | 3.53 |
| Yemen Rep. | 0.18 | 0.06 | 0.28 | 0.57 | 4.34 | 1.54 |
| **Total** | **0.85** | **0.76** | **0.56** | **2.27** | **1.39** | **2.52** |

*Source*: Computations based on IMF Direction of Trade Statistics Yearbook 2001.

[10] The trade intensity index is defined as the share of one country's exports going to a partner divided by the share of world exports going to the partner. That is, $TI_{ij} = [x_{ij}/X_{it}] \div [x_{wj}/X_{wt}]$ where $x_{ij}$ and $x_{wt}$ are the value of i's exports and world exports to j, $X_{it}$ is i's total exports and $X_{wt}$ are total world exports. An index of more (less) than unity indicates a bilateral trade flow that is larger (smaller) than would be expected given the partner country's importance in world trade.

A criticism of intensity indices is that they do not control for factors such as GDP and trade costs as determinants of trade flows. A commonly used technique to incorporate such factors is the gravity model.[11] Gravity model regressions on non-oil trade for the period 1970-1998 suggest that in the 1970s, being located in the Middle East and North Africa region had no effect on bilateral trade volumes (Chang, 2000). In 1980, Arab countries' trade was actually less than predicted by the model. In 1990 and 1998 this pattern reversed, with intra-Arab exports and imports becoming larger than predicted by the model. Research by Al-Atrash and Yousef (2000) concludes that while intra-regional trade in the Maghreb countries and the Gulf Cooperation Council (GCC) states is less than predicted this is not true for the Mashreq countries. Thus, the available evidence is somewhat ambiguous regarding the question of whether intra-regional trade flows are lower than what would be expected given the levels of GDP, population, and geography.

Simple shares and trade intensity indices suggest intra-regional trade is not that low and has been expanding; the gravity regressions suggest that trade is less than what would be expected. However, there has been a noticeable change in the last ten years with trade increasing beyond what the standard gravity model would predict. (See the appendix for a brief discussion of trends in bilateral trade over the last thirty years which suggest a similar conclusion).

Two questions are particularly relevant for the prospects of trade-led Arab economic integration initiatives. First, to what extent do Arab countries that heavily export to the rest of the region (relative to their total exports) also *account* for a major share of intra-Arab exports? Second, in terms of GDP for individual Arab countries, how important are exports to other Arab nations? The first question captures the balance between the incentives of each country to attend a hypothetical regional Arab economic integration conference, and its capacity to influence the outcome of such a conference. The second question provides a very rough sense of the importance of intra-Arab trade to the national economy of each prospective member. It can be seen as a crude indicator of the strength of domestic political support for a regional Arab trade option. Despite appearances, trade policy is fundamentally a *domestic* policy – that is, a set of

[11] The gravity model explains bilateral trade between country (i) and country (j). Normally, the amount of trade is directly proportional to size (income, population, land area, etc.) and inversely proportional to the distance between trading partners i and j. It is expressed by the following equation: $T_{ij} = AY_i^{\beta 1} P_i^{\beta 2} Y_j^{\gamma 1} P_j^{\gamma 2} D_{ij}^{\delta}$ where T is the amount of trade between two trading countries, Y is the GDP of the country, P is the population, and D is the distance between the trading partners. Often additional variables such as existence of a common border or language are also included as explanatory variables.

domestic bargains between conflicting domestic interests. This perspective suggests it is important to ask whether there exists a sufficiently large domestic coalition in favor of regional trade within key Arab countries. The importance of this question is amplified when it is recognized that a country has alternatives to regional trade. Many Arab countries are already pursuing discriminatory agreements with one large industrial country or more. A significant number of countries have signed Euro-Mediterranean Partnership Agreements with the EC and, of course, many are members of the WTO and have the option of pursuing multilateral liberalization.

The Arab countries that have substantial exports to other Arab nations (more than US$1 billion) – Oman, Saudi Arabia and the UAE – are all oil exporters. These three countries account for 70 percent of total intra-Arab trade. As already mentioned, with the exception of Oman, none of these countries' intra-regional exports account for more than 10 percent of their total exports (Table 5). In the case of Oman and UAE, these exports are equivalent to 7-8 percent of GDP and go beyond oil and oil derivatives, suggesting there may be significant political support for Arab economic integration in these countries.

**Table 5: Regional Export Shares and Weight in GDP, 2000**

| Country | Value of exports to some Arab countries ($ mil) | Share in total Arab trade (%) | Exports to Arab countries as a share of total exports (%) | Exports to countries as a share of GDP (%) |
|---|---|---|---|---|
| Algeria | 224 | 1.3 | 1.1 | 0.4 |
| Bahrain | 554 | 3.3 | 6.7 | 7 |
| Egypt | 544 | 3.3 | 9.7 | 0.6 |
| Jordan | 642 | 3.9 | 33.8 | 7.7 |
| Kuwait | 154 | 0.9 | 0.9 | 0.4 |
| Lebanon | 323 | 1.9 | 45.2 | 2 |
| Libya | 425 | 2.6 | 3.3 | 1.4 |
| Morocco | 360 | 2.2 | 4.4 | 1.1 |
| Oman | 1,386 | 8.3 | 13.1 | 7 |
| Qatar | 731 | 4.4 | 6.3 | 5.1 |
| Saudi Arabia | 5,680 | 34.2 | 7.6 | 3.3 |
| Syria | 900 | 5.4 | 18.1 | 5.3 |
| Tunisia | 535 | 3.2 | 8.9 | 2.7 |
| UAE | 3,981 | 24.0 | 9.7 | 8.3 |
| Yemen Rep. | 172 | 1.0 | 4.2 | 2 |
| **Total** | **16,611** | **100.0** | **7.3** | **2.8** |

*Source*: World Bank (2002), World Development Indicators, CD-Rom; IMF (2001), Direction of Trade Statistics.

However, it should be recognized that these are not large countries in the regional context and therefore they will only have a limited capacity to push such an initiative forward. Countries with a high share of their total exports going to the Arab region such as Jordan, Lebanon and Syria, represent only a small share of total intra-Arab trade (3, 2, and 5 percent, respectively), implying that their potential influence on a regional trade process is also likely to be small.

If we look at the ratio between exports to Arab countries and GDP, in addition to Oman and the UAE there are three countries with shares above 5 percent: Bahrain, Jordan, and Syria. This suggests that these countries have an interest in the pursuit of Arab economic integration. In the case of Saudi Arabia the figure is 3.3 percent; for Tunisia 2.7 percent and for the other countries, Arab trade is less than 2 percent of GDP.

These numbers suggest that the situation is significantly different from that presiding at the creation of the EC. In the mid-1950s, all prospective EC member states exported more than 25 percent of their total exports to the rest of the Community. Intra-Arab trade shares are much lower for almost all Arab countries. Moreover, EC trade amounted to more than 3 percent of the domestic GDP for all the future EC member states (5 percent for Germany), Italy is the only exception at 2.8 percent. While the Arab trade/GDP ratios for many countries are similar, an important difference is that the variance is much higher. For a number of countries, including Egypt – which would have to be an important member of any integration initiative – the ratio is quite low. Thus, the balance between alternative trade agreements is tilted away from Arab integration.

To summarize, the available data suggest that intra-Arab trade is not less than what would be expected given fundamentals, especially for non-Maghreb countries; economies that sell a large share of their exports to the region (the potential core supporters of Arab economic integration) account for small shares of total intra-Arab trade; conversely, for countries accounting for a large share in total intra-Arab trade, such trade accounts for only a small share of their total exports; and there is a large variance in the magnitude of intra-Arab trade relative to domestic GDP for Arab countries. All this suggests that the political economy of Arab integration based on preferential merchandise trade liberalization is not propitious.

## IV. Toward a Services-Based Integration Strategy?

What are the alternatives? An obvious approach is to focus on other markets, including factor markets (labor, investment) and services.[12] To reduce domestic production and trade costs, reforms in service sector policies are needed and may have a high payoff in facilitating further liberalization of trade of goods by enhancing the ability of firms to confront increasing import competition. Service-related costs in many Arab countries are high and varied. As far as trade is concerned, logistics-related costs are often high due to government policies and regulations that result in limited competition. Public monopolies in ports and port services, combined with poor infrastructure for loading and storing goods make the costs for discharging a container two to three times higher in Alexandria than in other Mediterranean ports. Port service charges in Arab countries can reach up to 10 percent of the value of imported intermediate components (Cassing et al., 2000). Monopoly shipping and domestic policies favoring national carriers result in low-quality, low-frequency, and high-cost services. Similar observations can be made for air transportation, telecommunications and utilities. Policies restricting trade in land transport services, such as prohibitions on drivers from certain countries, arbitrary changes in documentary requirements, surcharges and discriminatory taxes, and prohibitions on obtaining cargo in the country of destination to take back to the country of origin, all impose severe costs on intra-Arab trade (Zarrouk, 2000).

More generally, inefficient services place a substantial burden on manufacturing and agricultural sectors. Services – ranging from financial intermediation and insurance to the design and marketing of products and access to high-quality, low-cost telecommunications – are a major determinant of the competitiveness of firms. Because services are often not tradable, service sector liberalization involves a mix of deregulation – the dismantlement of barriers to entry (investment) and promotion of competition – and re-regulation – establishing an improved legal environment, strengthening specialized and independent regulatory agencies. The limited tradability of services implies that FDI is an important avenue for acquiring access to best practices and new services. Given that many service activities are subject to investment restrictions (e.g., nationality requirements, restrictions on movement of personnel, limits on

[12] What follows draws in part on Hoekman and Messerlin (2002).

foreign equity shareholding), service sector reform is closely tied to privatization and the removal of licensing and related entry and operating restrictions.

Arab countries have tended to approach service reform in a piecemeal fashion. Privatization has been slower than in other parts of the world; barriers to entry often remain forbidding, both for domestic and foreign investors; and there are few independent regulatory agencies to ensure markets are contestable. Privatization proceeds generated in the Arab region constituted only 3 percent of the worldwide total in the 1990s. While the trend is increasing – rising from some US$22 million in the early 1990s to US$2 billion in 1995 to more than US$6 billion in the second half of the 1990s – the role of the state remains much greater than in other regions (ERF, 2001). Private sector participation in infrastructure is very limited. Between 1984 and 1997, projects in the region added up to only US$9 billion, compared to a worldwide total of US$650 billion for a share of just 1.4 percent.[13] Given the inefficient operation and management of state-owned and controlled utilities, there is an urgent need to adopt a sector-wide approach that includes a combination of competition, incentive regulation, and private ownership (ERF, 2001).

As mentioned, because services often cannot be traded, increasing access to domestic service markets is likely to require the entry of foreign competitors through FDI. This will not only lead to the introduction of new technologies, but it will also (and in sharp contrast to what happens with merchandise liberalization) generate demand for domestic labor. Foreign telecommunications, electricity operators, banks and retailers all need local labor. Thus, while the deregulation of entry will inevitably result in the restructuring of domestic industry, service reform has less far-reaching implications for sectoral turnover and aggregate sectoral employment than the abolition of trade barriers for merchandise. The simulation analysis undertaken by Konan (2002) suggests that reforms in services are less demanding in terms of labor adjustment than merchandise liberalization.

Service reforms can have a large indirect payoff as well – facilitating merchandise trade liberalization. Trade barriers are still high in the region, not only because of tariffs but also due

[13] Examples of recent initiatives include water supply and wastewater treatment (Oman), power (Egypt, Morocco, Tunisia, and several GCC countries), transport (a port terminal in Yemen and a container terminal in Oman; toll roads in Jordan, Lebanon, Morocco and Tunisia; port services in Morocco and Tunisia), and telecommunications (the GCC countries, Jordan, Lebanon, and Morocco). See ERF (2001).

to a variety of non-tariff measures that raise trade costs (Zarrouk, forthcoming). As a result, there remains substantial anti-export bias in many Arab countries (Galal and Fawzy, 2002 ). Therefore, traditional trade liberalization remains a priority. One reason progress in this area has been slow is that liberalization will invariably result in contraction/adjustment of domestic industries that benefit from protection, while industries in which the country has a comparative advantage will expand.[14] Many of the latter initially are likely to be small and dispersed, whereas the former are likely to be concentrated. Thus, the region faces the well-known political problem of building support for trade liberalization; those that stand to lose will often have a substantially stronger political voice as they have more information and more of an incentive to organize. Frequently it will not be known beforehand which sectors and activities will become growth areas, hence an additional lag between those who will lose and those who will gain from liberalization. This makes the early transition process politically difficult and can impede liberalization altogether.

Such political constraints to trade liberalization may be relaxed by reforms targeting the service sector, both directly by lowering trade-related transport, logistics and transaction costs, and indirectly, by reducing the cost of key inputs such as finance, telecommunications, marketing, distribution and similar services. Pro-competitive reforms that facilitate the entry of new firms can generate employment opportunities for skilled and unskilled workers who are currently employed by the government or by import-competing private manufacturing, or for those who are unemployed. Indeed, a political precondition for public sector downsizing is the need to create alternative employment opportunities.

The discussion so far has not suggested anything regarding whether a regional approach to reform makes sense. Much of what needs to be done could be pursued through unilateral actions. Indeed, in other work it has been argued that the need for reciprocal exchange of policy commitments should be less necessary for services than for merchandise trade liberalization (Hoekman and Messerlin, 2000). This is supported by recent experience in many parts of the world, especially Latin America and Eastern Europe, where great progress has been made since the late 1980s to liberalize entry and privatize the service sector. Of course, a feature of these efforts is that reforms were pursued in the context of a debt crisis or macroeconomic stabilization

[14] There are two aspects to merchandise trade liberalization efforts in the region – the preferential barrier reduction discussed earlier, and nondiscriminatory liberalization. It is the latter that is important for the region and that is the focus here.

and transition programs – something that the Arab countries have managed to avoid. However, the fact remains that there has been limited progress in addressing service-related trade costs (trade facilitation, transport) and expanding private participation in backbone infrastructure services. It is also illustrative that only Algeria, Kuwait, Tunisia, and Turkey currently have (weak) competition laws, and that efforts to adopt such legislation in Egypt, Jordan, and Morocco have proved very contentious. Thus, the status quo suggests there are political economy factors that impede pro-competitive reforms. A key question is if and how an Arab integration-based effort can help to overcome national political constraints to unilateral action.

Concerted action in the context of an Arab economic integration initiative could facilitate service reforms by: creating benchmarks and focal points; ensuring the necessary high-level attention from senior decision makers and political leaders, engagement by civil society, and a mechanism to define a reform path through a pre-commitment to achieve specific targets or outcomes. Recently, efforts to privatize services in a number of Arab countries have been revitalized. In Egypt, there are initiatives for build-operate-transfer (BOT) programs for electricity generation, transportation, and telecommunications. Regional cooperation could be part of a strategy to expand and pre-commit to further moves in this direction.

Establishment of regional regulatory agencies to oversee network services (telecommunications, electricity, railways and other critical "backbone" activities) can help to "de-balkanize" Arab markets for such services. Regional regulatory agencies could facilitate cooperation between Arab countries that are investing in and managing the physical networks through the issuance of region-wide licenses for a market that would be large enough to attract global players. More generally, a regional effort to support the creation of a common competition authority may help to identify private collusive arrangements and public policies that restrict competition in regional markets.

## V. Lessons from the EC Experience

The EC experience suggests careful consideration will be needed regarding the design and sequencing of cooperation. A central pillar of the EC integration strategy was preferential merchandise trade liberalization, a common external trade policy and common management of agriculture, but the EC also covers services and factor flows (investment and movement of

workers).[15] A number of lessons can be drawn from the merchandise trade-related dimension of EC integration – where, as previously argued, differences in intra-Arab trade dependence and relative size make it unlikely that preferential merchandise trade liberalization can act as the glue for integration efforts (also implying there may be little value in seeking to emulate the creation of a customs union and establishing the common institutions to manage this).

First, there must be an overarching vision with respect to the ultimate objective of an "ever closer union." Second, a clear path or strategy to achieve the objectives must be developed. Third, the implementation of the strategy must result in an overall balance of gains for members at any point in time. This will require flexibility and may imply a need to exclude some sectors from the liberalization objective (as agriculture was by the EC). Rather than simply exempting "difficult" sectors from the ambit of the customs union, the EC brought them under the umbrella of the integration goal through a common policy approach that was administered by the EC institutions.

To a significant extent, the joint management of these common policies became the focus of day-to-day interaction at the community level and helped make the EC a reality for national bureaucracies and stakeholders. In addition, the EC developed transfer mechanisms that redistributed income to disadvantaged groups and increased their support for integration. The supranational nature of the EC was also important in maintaining the venture over time – a self-interested bureaucracy that was given a mandate to pursue integration proved very effective at mobilizing support for new initiatives, while enforcement of the rules was pursued via the independent ECJ.

Finally, the EC experience illustrates that regional cooperation to liberalize trade and investment in services is difficult. The Common Market was limited to goods, although the manufacturing sector accounted for less than one-third of EC GDP. Most services, representing the lion's share of GDP, were left untouched by intra-EC liberalization until the 1990s. In part,

[15] Another option is to focus on liberalization of trade in factors of production, something that is not discussed in this paper. Trade in labor services has traditionally been relatively important among Arab countries, albeit hampered by significant barriers and high transaction costs (Schiff, 1996). There are close links between temporary movement of people and liberalization of trade in services. What is required in the case of labor services is primarily a relaxation of quantitative restrictions – imposed through visas, economic needs tests and investment controls.

this reflected the fact that many service providers in the EC were public monopolies (or firms to which member states granted special or exclusive rights). While these firms were subject to specific Treaty provisions on state-owned enterprises and state aids, only in the late 1980s did EC member states begin to embark on a major effort to privatize and introduce regulatory reforms for services. Following Article 52 (ex 63),[16] the EC focused primarily on only a limited number of service sectors – those perceived as constituting the infrastructure backbone of the economy: financial services, telecoms, and transport (land, air, and sea). The late 1990s witnessed painful (and not always successful) efforts to extend the list to electronic commerce, electricity and natural gas, railways, and postal services.

In the Arab context, it is very difficult to assess ex ante which sectors will be "sensitive," where a commonality of interest exists, and what is the balance of national gains and potential losses (adjustment costs). This will require detailed analysis and extensive political debate and discussion. However, a case can be made that national interests regarding service reforms should be relatively balanced. In all countries, many industries stand to benefit significantly from services liberalization and policy reform. Manufacturers and agricultural producers should have a strong interest in seeing their input costs decline and the variety and quality of services offered increased. They can therefore be expected to be a powerful force supporting regulatory reforms in services *if* a credible case can be made that the integration effort will result in such an outcome.

This is a critical issue. A necessary condition for credibility is that the Arab cooperation strategy addresses the major political economy constraints that impede national reform. One constraint is related to the large role of the State in many Arab economies. Greater participation by the private sector will require privatization and the abolition of entry restrictions for new firms. Government policies and procedures are also the cause of high transaction costs at the border (red tape). Thus, a major factor determining the relevance of any integration strategy is to what extent it will be used by governments to pre-commit to actions aimed at reducing the role of the State – the focus must be on government services as well as backbone infrastructure, both hard and soft. Two interest groups play a major role in this connection: government employees in

[16] Article 52 (ex 63), reads: "Priority for liberalization shall be given, as a general rule, to those services which directly affect production costs or the liberalization of which helps to promote trade in goods." It again illustrates the predominance of trade in goods as the focus of the EC process.

general, and more specifically, those responsible for enforcement of various regulatory policies and procedures at the border (customs) and for specific service industries (sectoral regulators).

Cross country experience suggests the latter group can be a serious constraint to the adoption of more pro-competitive policies. Sectoral ministries or regulators that oversee service industries are often more concerned with supporting domestic incumbents and maintaining the status quo and have little incentive to actively encourage new entry and greater competition, either from domestic or foreign suppliers. The bureaucratic incentives confronting sectoral regulators generally imply that little weight is put on the economy-wide dimensions of policies.

The resulting entry barriers often create significant rents for incumbents, who have a strong interest in blocking attempts to increase the contestability of “their” markets. It is important to guarantee that potential entrants are free to enter service markets, and that policies do not discriminate against foreign entrants. Entry barriers in many service activities tend to be justified by invoking market failure rationales that revolve around information asymmetries, fears of excessive entry, and the need for universal service, among others. While there is often a valid rationale for intervention (regulation), this does not generally require the creation of legal entry barriers.

The potential gains that will result from facilitating the entry and operation of more efficient service suppliers, both domestic and foreign, can help address some of the constraints listed above. Such gains include the direct effect on prices and product choices for consumers/users, as well as the beneficial impact of greater demand for domestic workers in the service sectors concerned (Markusen, Rutherford and Tarr, 2002). Fears of employment loss need to be addressed ex ante through the establishment of safety nets and transitional adjustment assistance, but what is most important is the creation of employment opportunities elsewhere in the economy following reform. A major benefit of a concerted strategy toward service sector reform is that it will, in itself, generate greater demand for labor by the private sector, whether in services or goods-producing industries.

The strategy will need to be designed to address the concerns of likely losers. The sequencing of reforms is important to make and sustain progress. One possibility is to start with a regional effort on trade facilitation (broadly defined to include key government services that influence trade transaction costs), followed by initiatives to promote more effective competition

in the regional market for network-type service industries and to liberalize entry into markets through investment (establishment).

As documented by Zarrouk (forthcoming), trade costs in the region are high, in part because of government imposed restrictions and controls at the border, and in part because of a lack of competition in port, transport and related services. This is an area that is generally recognized as a priority by the private sector. Regional cooperation in this area could help governments move forward by setting quantitative benchmarks for improvement, establishing mileposts and creating transparency and oversight mechanisms to monitor progress achieved. Cross country experience suggests that moving forward to facilitate trade by addressing regulatory and logistics restraints requires high-level engagement by political authorities, something that is difficult to sustain. A regional initiative could help ensure that the necessary attention and support is provided in due course, as the needed reforms will generally take a substantial amount of time as well as resources for training, upgrading of hardware and infrastructure, and so forth.

To the greatest extent technically possible, such initiatives should aim to reduce costs for all trade and all traders, irrespective of origin. The primary rationale for undertaking this effort in a concerted fashion is to create clear focal points and objectives, and to mobilize the high level of support that will be needed to make progress. There is no rationale for differentiating between Arab goods and those of another origin – the trade facilitation should apply on a most-favored-nation basis. Starting with trade facilitation puts pressure on only a small subset of the civil service and will benefit foreign and domestic producers equally. Red tape costs largely represent social waste; they do not generate revenue or rents. Consequently, reducing these costs can benefit the economy substantially.

A second potential area for regional cooperation is to develop mechanisms to increase the contestability of markets, especially for backbone infrastructure services. Examples of such cooperation could involve the establishment of regional regulatory agencies to oversee network services (telecommunications, electricity, railways and other critical backbone activities). Regional regulatory agencies could facilitate cooperation between Arab countries that are investing in and managing the physical networks through the issuance of region-wide licenses for a market that would be large enough to attract global players. Arab economic integration

could also be a vehicle through which regional competition disciplines are agreed upon and enforced in order to discipline private collusive arrangements and public policies that impede entry or restrict competition in regional markets.

A regional effort to liberalize backbone services could start with defining the "relevant market" in a more appropriate way. For instance, liberalizing air transport without liberalizing airport slots does not lead very far: the price of air travel will mirror both competitive pressures in terms of routes (if there are several airlines in presence, which is not necessarily the case) and monopoly rents related to airport slot monopolies. The same is true for maritime transport. Francois and Wooton (2000) estimate that the welfare gains from trade liberalization may be doubled if complementary actions are taken to increase competition in the shipping sector. These are all examples of the types of interactions that tend to be ignored by national sectoral regulators and could be addressed more efficiently in a region-wide approach.

The EC experience reveals that it is quite difficult to address regulatory differences that result in market segmentation in a cooperative manner. Perhaps the most powerful force that can be unleashed through an integration process is to increase competition through the relaxation of entry constraints – explicit barriers as opposed to implicit ones created by regulatory differences – and the application of disciplines on state aids and regional competition policies. This would require institutions like those created by the EC to monitor and challenge the behavior of governments, and to address anticompetitive practices by incumbent firms. State aids and intervention, as well as an absence of effective competition legislation, are two important factors in many Arab economies, suggesting that in terms of common institutions and disciplines the initial focus should be on those areas. Another priority for institutional cooperation and development relates to dispute settlement. As mentioned in Section III, the ECJ played a major role in advancing the integration effort in the EC. Without a mechanism to enforce liberalization commitments on FDI and entry into services, the effort will inherently be much less credible to the private sector, both in and outside the region.

The possibility of rapid movement to emulate the institutional complexity that prevails in the EC is limited. In the EC, this has grown incrementally, and the same would be true in the Arab context. Cooperation in regulatory areas and common competition policies will undoubtedly only emerge gradually. What matters most in this connection is agreement on the

vision and the actual launch of the process. This could encompass possible "half-way houses" that could be used to build support for pro-competitive reforms. One option could be a regional mechanism to increase the transparency of government policies, including assessments of the economic effects of regulations and other policies that limit competition. Such information is a necessary condition to mobilize national constituencies that are negatively affected by such policies. A number of mechanisms to generate such information are discussed in Hoekman and Mavroidis (2000).

It should be kept in mind that many of the Arab countries have concluded Euro-Mediterranean Partnership agreements with the EC. While these have only very limited commitments in the areas of services and investment, they do call for their development in future extensions of the agreements. The commitment to negotiate on these topics should provide an additional rationale for considering what can and should be done in the Arab context regarding these subjects. The same is true for the ongoing WTO Doha negotiations, which include services.

Whatever the specific features and modalities of cooperation, significant service reforms will have large economy-wide benefits (Konan, forthcoming). Such benefits will be greatest if regional reforms and disciplines are applied on a nondiscriminatory basis. In contrast to preferential liberalization of trade in goods, concerted service reforms are less likely to give rise to serious trade and investment diversion, as long as policies will often be applied equally to both foreign (non-regional) and regional suppliers. A reason for this is that regulation should be aimed at addressing market failures, and thus be applied on a nondiscriminatory basis. The same is often true, in practice, for policies affecting the major mode of contesting service markets – FDI. These generally do not distinguish between foreign investors on the basis of nationality. However, in principle this can certainly be done, and on the investment front such discrimination is pursued (on paper) in the Arab League context through an Arab rule of origin (a minimum required Arab equity ownership share). It is important that such discrimination be minimized if Arab economic integration is to be beneficial.

## VI. Concluding Remarks

Arab economic integration efforts that revolve around merchandise trade liberalization face substantial impediments: markets are generally small; strong comparative advantages in certain

products (natural resources) generate export concentration and require geographical diversification of exports beyond the region to reduce risk; and major Arab countries do not appear to have strong incentives to take the lead in pursuit of economic integration, while smaller countries that do have the incentive do not have the influence to ensure implementation. Arab countries confront an incentive structure that is quite different from what prevailed in the context of the creation of the EC in the 1950s, suggesting that emulating the EC approach – one that is based on preferential merchandise trade liberalization and the creation of a common external merchandise trade policy, leaving services reform for later – is unlikely to be a fruitful strategy for Arab countries.

For Arab economic integration to succeed there must be a sufficiently large domestic coalition that favors it over all alternatives (Galal, 2000). Given the limited magnitude and potential for intra-Arab trade and the political support for efforts to expand such trade, complementary instruments and approaches are needed. One option discussed in this paper is to focus on the services sector which includes both government and major backbone infrastructure-type services. Integration efforts that focus on services could potentially generate large gains that are much greater than those that could be obtained from preferential merchandise trade liberalization (Konan, 2002). More relevant from the perspective of achieving an integration goal is the pursuit of service reforms which could help overcome political economy resistance to unilateral reforms including further liberalization of merchandise trade on a nondiscriminatory basis. The latter is critical for many countries in the region since trade barriers are among the highest in the world outside of South Asia and consequently, anti-export bias is strong.

The European experience illustrates that for integration strategies to succeed and be sustained, powerful constituencies must see such efforts as contributing to the realization of objectives they care about. While political objectives were paramount in the EC, their realization involved the identification of economic measures that benefited all citizens in an average sense, while ensuring the concerns and interests of key “blocking” coalitions and groups were satisfied. The challenge for supporters of Arab economic integration initiatives will be to identity objectives that are supported by citizens, and mechanisms of regional cooperation that will attain those objectives. First and foremost, the decision makers must be able to make a compelling case that “going regional” will generate significant benefits that cannot be realized through unilateral action.

In doing this, care must be taken to ensure the integration mechanisms and modalities promote economic welfare. A major lesson of the EC is that the pursuit of political objectives may come at a high economic cost; the Common Agricultural Policy is an example. Therefore, an integration path that focuses on service markets should be designed so as to minimize the scope for capture by – and creation of – vested interests. In this regard there is less potential for trade diversion under a services strategy as long as regulatory reforms and removal of entry restrictions are applied on a nondiscriminatory basis. Indeed, it is important that this be the case, as discriminatory regional regulation may result in economies becoming confined to less efficient regional suppliers and standards that impede the ability of more efficient foreign firms to contest the market at a later date even if the discriminatory policy is removed (Mattoo and Fink, 2002).[17]

Any regional approach to service reforms must recognize the fact that many Arab countries have now signed agreements with the EC and that many are also engaged in negotiations on goods and services trade in the WTO. The Euro-Med agreements all include provisions calling for the development of disciplines for investment (establishment) and services trade. They also embody numerous provisions calling for the EC to provide cooperation and technical/financial assistance in trade-related regulatory areas. These agreements can and should be taken into account in the design of any Arab integration strategy. More generally, an Arab services strategy can and should be anchored in the WTO to ensure that policies are applied on a nondiscriminatory basis wherever possible. Of course, making commitments to the WTO allows concessions to be obtained from trading partners, expanding the potential gains from committing to reform. Given that the focus of negotiations at the WTO is on the depth of policy "bindings," the fruits of regional reforms can be used as a negotiating tool. Anchoring domestic liberalization in the WTO can also help Arab countries make reform more resistant to backsliding as negatively affected foreign suppliers will oppose domestic efforts to re-impose trade barriers. That said, it must be recognized that WTO negotiations on services have not progressed very far to date, general disciplines on investment and competition policies do not exist, and many of the regulatory service reform priorities remain outside the ambit of the WTO.

[17] Mattoo and Fink (2002) discuss a number of issues that affect the sequencing of preferential and multilateral liberalization of services. They point to the potential problem of negative path dependence if preferential liberalization in services occurs for network industries with sunk costs – the end result may be durable entry restrictions against more efficient non-regional suppliers.

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**Appendix: Trends in Bilateral Trade, 1960-2000**

The body of the paper describes the current pattern of trade between countries in the Middle East. It is interesting to examine whether this situation has always existed and what has happened over time. A comparison of intra-regional bilateral trade flows over the last thirty-five years suggests that there has been a significant decline in the relative importance in intra-regional trade since the early 1960s, but that there has been an increase in the last decade. A matrix of bilateral imports is reported in Appendix Table 1, with data aggregated according to the natural resource-intensity of trading partners. Table 2 does the same for exports. The region is defined as all countries, not just Arab nations.

The data reveal two different types of evolution of imports from Arab economies. On one hand, countries that are not oil-rich witnessed a decline or stability of the share of their regional trade until 1985, followed by a reversal, though it was not large enough to counterbalance the previous decline. On the other hand, oil-rich countries tend to increase trade with other Arab countries – an evolution which may reveal an income effect (oil-rich countries may have been induced to diversify their purchases because of lower oil prices, and to turn toward less expensive local sellers).

In the early 1960s, Lebanon and Jordan imported about 60 percent of all non-oil imports from the region. By 1997 this had dropped to 10-15 percent. Many countries registered an increase in the intra-regional share after 1985. The increases are substantial for Syria, Iraq, Oman, Saudi Arabia, Libya and Kuwait. The regional breakdown of exports also suggests the long-term trend is down – most countries exported less to the region in 1997 than in the early 1960s (Table 2). The exceptions with respect to non-oil trade include Egypt, Syria, Saudi Arabia, Algeria, Libya and Kuwait, which all show a recovery in the last ten to fifteen years. In the case of Syria, Egypt and Lebanon, the increase involves non-oil economies, while for Saudi Arabia the increase is in oil-rich countries (again suggesting growth of intra-industry trade in oil-related products).

**Appendix Table 1: Intra-Regional Import Pattern, 1964-97**

| | Natural resource-poor countries | | | | Intermediate countries | | | | Oil-rich countries | | | | Total regional | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1964 | 1978 | 1985 | 1997 | 1964 | 1978 | 1985 | 1997 | 1964 | 1978 | 1985 | 1997 | 1964 | 1978 | 1985 | 1997 |
| | Intra-trade as a percentage of total trade (oil included) | | | | | | | | | | | | | | | |
| Israel | 0.9 | 0.1 | 0.2 | 1.3 | 0.9 | 0.0 | 0.0 | 0.1 | 0.1 | 0.1 | 0.0 | 0.0 | 1.9 | 0.3 | 0.2 | 1.4 |
| Turkey | 1.3 | 2.2 | 1.0 | 0.8 | 1.2 | 0.9 | 0.2 | 0.9 | 9.3 | 23.5 | 31.1 | 7.6 | 11.8 | 26.6 | 32.4 | 9.3 |
| Lebanon | 3.9 | 1.4 | 5.5 | 3.6 | 2.6 | 1.6 | 1.0 | 1.1 | 18.2 | 12.7 | 0.8 | 7.7 | 24.7 | 15.6 | 7.3 | 12.4 |
| Morocco | 0.0 | 1.1 | 0.4 | 1.3 | 0.4 | 0.7 | 0.0 | 0.3 | 2.3 | 8.0 | 21.5 | 10.8 | 2.8 | 9.8 | 21.9 | 12.3 |
| Tunisia | 0.2 | 1.9 | 1.2 | 1.8 | 0.5 | 0.1 | 0.4 | 0.6 | 5.6 | 5.3 | 7.4 | 5.0 | 6.3 | 7.3 | 9.0 | 7.4 |
| Jordan | 7.5 | 6.7 | 4.2 | 4.6 | 2.3 | 1.9 | 0.5 | 1.3 | 12.9 | 15.4 | 25.8 | 21.2 | 22.6 | 24.0 | 30.5 | 27.1 |
| Egypt | 0.5 | 2.0 | 1.1 | 2.0 | 0.0 | 0.2 | 0.2 | 0.2 | 5.2 | 1.9 | 2.0 | 4.6 | 5.7 | 4.2 | 3.2 | 6.8 |
| Bahrain | 0.0 | 0.3 | 0.6 | 1.1 | 0.0 | 0.0 | 0.1 | 0.8 | 85.7 | 45.8 | 48.1 | 11.7 | 85.7 | 46.1 | 48.8 | 13.6 |
| Syria | 6.6 | 4.1 | 2.5 | 6.8 | 2.6 | 3.0 | 0.6 | 2.2 | 8.8 | 9.6 | 27.2 | 5.6 | 17.9 | 16.7 | 30.2 | 14.6 |
| Oman | 0.0 | 0.5 | 0.1 | 0.5 | 0.0 | 2.9 | 0.5 | 1.0 | 98.1 | 16.5 | 22.4 | 26.7 | 98.1 | 19.9 | 23.0 | 28.1 |
| UAE | 0.0 | 1.0 | 1.7 | 1.1 | 0.0 | 1.4 | 4.1 | 0.4 | 93.3 | 2.8 | 4.4 | 6.3 | 93.3 | 5.2 | 10.1 | 7.8 |
| Iraq | 2.8 | 1.8 | 11.7 | 5.6 | 1.4 | 0.9 | 2.2 | 15.3 | 1.8 | 0.7 | 0.1 | 3.1 | 5.9 | 3.4 | 14.0 | 24.0 |
| Iran | 1.1 | 1.5 | 11.6 | 3.1 | 0.0 | 0.7 | 0.0 | 0.1 | 3.5 | 1.0 | 0.8 | 2.0 | 4.6 | 3.2 | 12.4 | 5.2 |
| Yemen | 0.0 | 0.8 | 0.3 | 4.2 | 2.8 | 0.7 | 0.4 | 2.3 | 76.0 | 23.4 | 0.6 | 7.5 | 78.9 | 24.9 | 1.3 | 14.0 |
| Saudi Arabia | 6.2 | 1.8 | 1.8 | 10.6 | 5.7 | 0.8 | 1.2 | 0.1 | 8.0 | 1.4 | 1.9 | 23.3 | 19.9 | 4.1 | 5.0 | 34.0 |
| Qatar | 1.3 | 1.0 | 1.5 | 0.4 | 0.0 | 0.7 | 1.1 | 0.9 | 4.6 | 4.3 | 5.6 | 6.4 | 5.9 | 6.0 | 8.2 | 7.7 |
| Algeria | 2.6 | 0.3 | 2.3 | 3.9 | 0.2 | 0.1 | 0.1 | 0.5 | 0.2 | 0.2 | 0.4 | 3.4 | 3.0 | 0.7 | 2.8 | 7.8 |
| Libya | 1.4 | 3.1 | 4.5 | 9.5 | 0.7 | 0.1 | 0.0 | 2.7 | 0.9 | 0.2 | 0.1 | 1.0 | 3.0 | 3.4 | 4.6 | 13.3 |
| Kuwait | 2.8 | 2.0 | 2.2 | 2.5 | 1.3 | 1.0 | 0.6 | 1.9 | 5.4 | 1.6 | 0.1 | 11.4 | 9.6 | 4.6 | 3.0 | 15.8 |
| Yemen | 0.3 | 0.0 | 0.0 | -- | 1.0 | 4.1 | 0.5 | -- | 40.8 | 15.0 | 2.8 | -- | 42.1 | 19.1 | 3.3 | -- |
| | Intra-trade as a percentage of total trade (oil excluded) | | | | | | | | | | | | | | | |
| Israel | 0.1 | 0.1 | 0.2 | 1.4 | 1.7 | 0.0 | 0.0 | 0.1 | 0.1 | 0.2 | 0.0 | 0.0 | 1.9 | 0.3 | 0.2 | 1.5 |
| Turkey | 1.8 | 1.2 | 1.5 | 0.8 | 0.3 | 0.4 | 0.3 | 0.3 | 0.4 | 0.3 | 1.0 | 1.9 | 2.4 | 1.9 | 2.8 | 3.0 |
| Lebanon | 11.4 | 1.6 | 5.3 | 3.9 | 7.4 | 1.9 | 0.5 | 1.2 | 41.3 | 2.1 | 0.3 | 4.2 | 60.2 | 5.6 | 6.1 | 9.3 |
| Morocco | 0.0 | 1.2 | 0.5 | 1.5 | 0.4 | 0.8 | 0.1 | 0.3 | 0.5 | 0.1 | 0.4 | 3.0 | 1.0 | 2.2 | 0.9 | 4.8 |
| Tunisia | 0.4 | 2.0 | 1.1 | 1.5 | 0.7 | 0.1 | 0.4 | 0.6 | 2.5 | 0.2 | 1.9 | 1.9 | 3.6 | 2.3 | 3.4 | 4.0 |
| Jordan | 24.8 | 7.5 | 5.4 | 5.4 | 8.9 | 2.1 | 0.7 | 1.5 | 33.4 | 6.5 | 5.8 | 8.7 | 67.1 | 16.1 | 11.9 | 15.6 |
| Egypt | 0.6 | 2.1 | 1.0 | 1.8 | 0.0 | 0.2 | 0.2 | 0.2 | 4.4 | 1.8 | 1.0 | 4.1 | 4.9 | 4.1 | 2.1 | 6.1 |
| Bahrain | 0.0 | 0.5 | 1.2 | 1.1 | 0.1 | 0.1 | 0.3 | 0.8 | 31.3 | 5.8 | 3.9 | 11.8 | 31.4 | 6.3 | 5.3 | 13.8 |
| Syria | 8.1 | 4.7 | 3.5 | 7.1 | 3.2 | 3.5 | 0.8 | 2.3 | 10.0 | 0.6 | 0.7 | 5.2 | 21.3 | 8.7 | 5.0 | 14.6 |
| Oman | 0.0 | 0.6 | 0.1 | 0.5 | 0.0 | 0.6 | 0.1 | 0.5 | 96.4 | 12.9 | 22.0 | 25.9 | 0.0 | 14.1 | 22.3 | 26.9 |
| UAE | 0.0 | 1.1 | 1.8 | 1.1 | 0.0 | 0.5 | 0.7 | 0.4 | 1.2 | 0.7 | 2.8 | 6.2 | 1.2 | 2.2 | 5.2 | 7.7 |
| Iraq | 1.3 | 1.8 | 11.8 | 5.6 | 0.7 | 0.9 | 2.2 | 15.3 | 0.8 | 0.7 | 0.1 | 3.1 | 2.8 | 3.4 | 14.1 | 24.0 |
| Iran | 0.6 | 1.5 | 12.3 | 3.2 | 0.0 | 0.5 | 0.0 | 0.1 | 1.2 | 0.8 | 0.4 | 2.0 | 1.9 | 2.8 | 12.7 | 5.3 |
| Yemen | 0.0 | 0.8 | 0.3 | 4.2 | 15.5 | 0.6 | 0.4 | 1.6 | 77.0 | 22.1 | 0.6 | 7.5 | 92.5 | 23.5 | 1.4 | 13.4 |
| Saudi Arabia | 1.6 | 1.8 | 1.9 | 10.9 | 1.5 | 0.8 | 1.2 | 0.1 | 2.1 | 1.4 | 1.9 | 23.8 | 5.2 | 4.1 | 4.9 | 34.7 |
| Qatar | 0.3 | 1.0 | 1.5 | 0.4 | 0.0 | 0.7 | 1.1 | 0.9 | 0.7 | 4.3 | 5.5 | 6.4 | 1.0 | 6.0 | 8.1 | 7.7 |
| Algeria | 2.5 | 0.3 | 2.3 | 4.0 | 0.2 | 0.1 | 0.1 | 0.5 | 0.2 | 0.1 | 0.4 | 2.6 | 2.9 | 0.5 | 2.8 | 7.1 |
| Libya | 0.7 | 3.1 | 4.6 | 9.5 | 0.3 | 0.1 | 0.0 | 2.7 | 0.3 | 0.2 | 0.1 | 1.0 | 1.2 | 3.4 | 4.7 | 13.3 |
| Kuwait | 1.0 | 2.0 | 2.2 | 2.5 | 0.5 | 1.0 | 0.6 | 1.9 | 1.9 | 1.6 | 0.1 | 11.1 | 3.4 | 4.6 | 3.0 | 15.5 |
| Yemen | 0.2 | 0.1 | 0.0 | -- | 0.6 | 0.1 | 0.6 | -- | 10.8 | 1.7 | 0.0 | -- | 11.6 | 1.9 | 0.7 | -- |

*Source*: Author’s calculations based on UN COMTRADE database.

**Appendix Table 2: Intra-Regional Export Pattern, 1964-97**

| | Natural resource-poor countries | | | | Intermediate countries | | | | Oil-rich countries | | | | Total regional | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1964 | 1978 | 1985 | 1997 | 1964 | 1978 | 1985 | 1997 | 1964 | 1978 | 1985 | 1997 | 1964 | 1978 | 1985 | 1997 |
| | Intra-trade as a percentage of total trade (oil included) | | | | | | | | | | | | | | | |
| Israel | 1.9 | 1.8 | 0.6 | 1.1 | 0.0 | 0.0 | 0.2 | 0.4 | 1.5 | 2.8 | 0.0 | 1.3 | 3.3 | 4.7 | 0.8 | 2.8 |
| Turkey | 5.8 | 4.1 | 2.3 | 3.2 | 0.6 | 5.9 | 2.4 | 1.3 | 1.3 | 12.6 | 56.7 | 7.3 | 7.7 | 22.6 | 61.4 | 11.8 |
| Lebanon | 2.0 | 2.3 | 1.2 | 6.8 | 15.5 | 14.1 | 12.4 | 7.6 | 76.5 | 69.8 | 50.6 | 16.2 | 94.0 | 86.2 | 64.3 | 30.6 |
| Morocco | 0.1 | 1.1 | 3.4 | 1.5 | 0.3 | 0.2 | 0.1 | 0.2 | 2.9 | 1.8 | 6.0 | 2.8 | 3.3 | 3.1 | 9.5 | 4.4 |
| Tunisia | 0.1 | 1.3 | 1.8 | 2.0 | 1.0 | 0.1 | 0.5 | 0.5 | 7.2 | 7.5 | 7.2 | 6.6 | 8.2 | 8.9 | 9.5 | 9.1 |
| Jordan | 25.0 | 5.5 | 2.6 | 9.8 | 0.1 | 4.9 | 1.2 | 3.4 | 57.3 | 65.5 | 50.1 | 42.7 | 82.5 | 75.9 | 53.9 | 55.9 |
| Egypt | 3.4 | 3.5 | 0.6 | 9.0 | 0.6 | 1.3 | 0.3 | 0.6 | 3.7 | 8.0 | 2.3 | 6.4 | 7.7 | 12.9 | 3.2 | 15.9 |
| Bahrain | 21.3 | 0.0 | 0.3 | 1.2 | 0.4 | 0.0 | 0.4 | 1.3 | 33.5 | 16.9 | 27.4 | 5.1 | 55.2 | 16.9 | 28.1 | 7.7 |
| Syria | 29.6 | 5.6 | 2.5 | 22.9 | 6.4 | 6.6 | 1.5 | 3.0 | 13.3 | 12.9 | 7.4 | 11.2 | 49.2 | 25.2 | 11.4 | 37.2 |
| Oman | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.5 | 0.2 | 0.3 | 10.6 | 0.4 | 1.0 | 14.8 | 10.6 | 0.9 | 1.2 | 15.1 |
| UAE | 0.0 | 0.0 | 0.5 | 0.2 | 0.5 | 0.3 | 0.2 | 0.3 | 19.1 | 2.2 | 5.5 | 6.7 | 19.6 | 2.5 | 6.3 | 7.2 |
| Iraq | 3.6 | 3.8 | 11.5 | 5.3 | 0.3 | 0.2 | 1.8 | 15.9 | 5.8 | 1.6 | 0.2 | 0.0 | 9.6 | 5.7 | 13.5 | 21.1 |
| Iran | 1.7 | 2.3 | 9.1 | 3.8 | 0.1 | 0.1 | 0.0 | 0.1 | 6.8 | 0.6 | 5.8 | 0.7 | 8.6 | 2.9 | 14.9 | 4.5 |
| Yemen | 0.0 | 0.0 | 0.0 | 0.0 | 1.0 | 0.4 | 0.1 | 0.5 | 55.1 | 35.4 | 12.9 | 0.3 | 56.1 | 35.7 | 13.0 | 0.8 |
| Saudi Arabia | 2.5 | 0.7 | 2.6 | 2.7 | 4.5 | 2.7 | 6.3 | 1.3 | 1.3 | 0.9 | 0.5 | 3.2 | 8.3 | 4.4 | 9.4 | 7.2 |
| Qatar | 9.9 | 0.0 | 0.1 | 0.3 | 4.0 | 0.2 | 0.3 | 0.3 | 6.2 | 1.0 | 3.7 | 0.7 | 20.2 | 1.2 | 4.2 | 1.3 |
| Algeria | 1.3 | 0.0 | 2.3 | 6.4 | 0.3 | 0.0 | 0.0 | 0.0 | 0.2 | 0.0 | 0.1 | 1.9 | 1.9 | 0.1 | 2.5 | 8.3 |
| Libya | 0.7 | 2.6 | 5.9 | 8.4 | 1.0 | 0.0 | 0.0 | 0.7 | 0.2 | 0.1 | 2.8 | 0.4 | 2.0 | 2.8 | 8.6 | 9.5 |
| Kuwait | 0.2 | 0.3 | 1.6 | 1.5 | 1.7 | 0.5 | 0.9 | 0.2 | 4.8 | 3.3 | 3.1 | 1.7 | 6.7 | 4.1 | 5.7 | 3.4 |
| Yemen | 0.5 | 0.0 | 0.0 | -- | 0.3 | 0.1 | 0.0 | -- | 9.8 | 59.4 | 0.8 | -- | 10.6 | 59.5 | 0.8 | -- |
| | Intra-trade as a share of total trade (oil excluded) | | | | | | | | | | | | | | | |
| Israel | 2.2 | 0.2 | 0.6 | 1.1 | 0.0 | 0.0 | 0.1 | 0.3 | 1.8 | 3.0 | 0.0 | 1.4 | 3.9 | 3.2 | 0.7 | 2.7 |
| Turkey | 4.3 | 4.1 | 2.7 | 3.2 | 0.5 | 5.9 | 3.0 | 1.3 | 1.3 | 12.6 | 69.6 | 7.3 | 6.1 | 22.6 | 75.2 | 11.8 |
| Lebanon | 1.0 | 1.6 | 1.2 | 6.9 | 8.3 | 14.2 | 12.4 | 7.7 | 49.7 | 70.5 | 50.6 | 16.4 | 58.9 | 86.3 | 64.3 | 31.0 |
| Morocco | 0.1 | 1.0 | 3.1 | 1.3 | 0.2 | 0.2 | 0.1 | 0.2 | 2.4 | 1.8 | 6.1 | 2.8 | 2.7 | 3.0 | 9.3 | 4.2 |
| Tunisia | 0.0 | 1.9 | 2.6 | 2.0 | 0.7 | 0.1 | 0.7 | 0.6 | 6.4 | 11.0 | 10.4 | 7.2 | 7.2 | 13.1 | 13.6 | 9.8 |
| Jordan | 17.4 | 5.5 | 2.8 | 9.8 | 0.1 | 4.9 | 1.3 | 3.4 | 40.2 | 65.5 | 54.5 | 42.7 | 57.7 | 75.9 | 58.6 | 55.9 |
| Egypt | 5.4 | 5.7 | 1.6 | 6.0 | 1.1 | 3.5 | 1.2 | 1.1 | 6.1 | 19.3 | 10.7 | 11.8 | 12.6 | 28.5 | 13.6 | 19.0 |
| Bahrain | 0.0 | 0.0 | 1.1 | 2.0 | 0.6 | 0.0 | 1.4 | 2.0 | 74.4 | 33.6 | 36.2 | 6.5 | 75.0 | 33.7 | 38.6 | 10.5 |
| Syria | 55.1 | 3.6 | 4.3 | 28.7 | 10.5 | 19.5 | 6.5 | 10.4 | 25.7 | 38.5 | 31.8 | 31.5 | 91.3 | 61.6 | 42.6 | 70.6 |
| Oman | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 11.3 | 4.2 | 0.3 | 70.5 | 10.1 | 30.0 | 15.0 | 70.5 | 21.4 | 34.2 | 15.3 |
| UAE | 0.0 | 0.0 | 0.4 | 0.6 | 0.0 | 9.6 | 2.4 | 1.1 | 26.7 | 59.7 | 59.4 | 29.3 | 26.7 | 69.2 | 62.2 | 31.0 |
| Iraq | 7.9 | 1.0 | 2.1 | 0.5 | 2.8 | 17.0 | 18.0 | 27.0 | 36.6 | 11.5 | 11.5 | 0.1 | 47.4 | 29.6 | 31.6 | 27.5 |
| Iran | 1.6 | 0.8 | 2.6 | 3.4 | 0.2 | 1.1 | 0.9 | 0.5 | 8.4 | 8.4 | 15.4 | 4.5 | 10.2 | 10.2 | 18.9 | 8.4 |
| Yemen | 0.0 | 0.0 | 0.0 | 0.7 | 1.3 | 0.4 | 0.2 | 7.9 | 40.2 | 39.8 | 40.6 | 6.9 | 41.4 | 40.2 | 40.8 | 15.4 |
| Saudi Arabia | 19.4 | 0.6 | 2.5 | 3.8 | 56.6 | 10.9 | 5.6 | 8.9 | 9.7 | 33.4 | 5.0 | 24.0 | 85.7 | 44.8 | 13.1 | 36.7 |
| Qatar | 1.5 | 0.0 | 1.4 | 1.5 | 0.0 | 5.6 | 3.7 | 2.5 | 62.1 | 25.0 | 41.9 | 6.3 | 63.6 | 30.6 | 47.1 | 10.3 |
| Algeria | 1.4 | 0.6 | 6.2 | 16.9 | 0.3 | 0.4 | 0.0 | 0.1 | 0.3 | 1.0 | 0.1 | 9.7 | 1.9 | 2.0 | 6.3 | 26.7 |
| Libya | 1.2 | 1.7 | 14.2 | 16.9 | 1.8 | 5.1 | 0.1 | 10.6 | 11.6 | 1.5 | 1.1 | 3.7 | 14.6 | 8.3 | 15.3 | 31.3 |
| Kuwait | 4.1 | 5.5 | 0.3 | 5.3 | 25.4 | 11.9 | 7.2 | 4.0 | 57.1 | 56.7 | 35.9 | 41.5 | 86.5 | 74.1 | 43.4 | 50.8 |
| Yemen | 1.0 | 0.0 | 0.0 | -- | 0.8 | 0.2 | 0.1 | -- | 32.9 | 83.7 | 6.6 | -- | 34.7 | 83.8 | 6.7 | -- |

*Source*: Author’s calculations based on UN COMTRADE database.