THE IMPLICATIONS OF EU ENLARGEMENT FOR THE EGYPTIAN ECONOMY

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Abstract

This paper examines the implications of the recent EU enlargement for the Egyptian economy with regards to trade, capital inflows, and labor migration. The novelty of the study lies in that it analyzes all three dimensions of the economic relations, whereas the majority of other studies focus mainly on trade or investment, and only briefly address the issue of labor. The paper finds that although the enlargement will not likely lead to significant changes in the short run, its impact in the medium to long runs depends on Egypt's ability to enhance the pace and extent of economic reforms in order to minimize the cost and maximize the benefits of the EU enlargement.

ملخص

تتناول هذه الورقة دلالات توسيع الاتحاد الأوروبي في الآونة الأخيرة بالنسبة للاقتصاد المصري، وذلك فيما يتعلق بتدفقات التجارة ورأس المال وهجرة العمالة. وتتسم هذه الدراسة بأنها تتناول بالتحليل الأبعاد الثلاثة للعلاقات الاقتصادية، في حين أن معظم الدراسات الأخرى تركز أساسا على التجارة أو الاستثمار، كما تتعامل بإيجاز مع موضوع هجرة العمالة. وتخلص الورقة إلى أن آثار التوسعة على مصر سوف تكون محدودة في الأجل القصير، في حين أن آثارها الإيجابية في الأجلين المتوسط والطويل تعتمد على قدرة مصر على تعزيز وتيرة وحجم الإصلاحات الاقتصادية بما يقلل التكاليف ويعظم الاستفادة من توسيع الاتحاد الأوروبي.

1. INTRODUCTION

In 2004, the 15-member European Union was expanded to include ten new members. These countries, known as the AC-10, are Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia. For Egypt, this enlargement represents both opportunities and challenges.

On one hand, the EU enlargement could provide Egypt with access to a wider market and allow the economy to benefit from scale effects. This is especially true given that the Egypt-EU Association Agreement has been modified to include free movement of goods and services with new as well as current EU members. It could encourage Egyptian firms to become more efficient in response to increased competition from the new members (Diwan 2002). Further, it could motivate policymakers to undertake more reforms in Egypt to make the country a more attractive location for investment from the EU and elsewhere.

On the other hand, the enlargement could divert EU capital flows to the new members at the expense of Egypt. It could lead to the displacement of Egyptian exports to the EU in favor of the new members, which could have particularly negative effects for Egypt given that the EU is currently its primary export market. The impact of the enlargement on labor in Egypt is less clear, and depends on, among other things, the terms of the Association Agreement with respect to labor mobility and the initial skill mix of labor in Egypt compared to the AC-10.

In short, the likely impact of EU enlargement on Egypt is still uncertain and will likely depend on the pattern of trade between Egypt and the EU as well as that between the AC-10 and the EU. It will also depend on a number of other factors including the production structure and comparative advantage in each case, the investment environment, as well as the state of economic reforms.

In light of this uncertainty, this paper examines the implications for Egypt with regards to trade, capital inflows – mainly foreign direct investment (FDI) – and labor migration, followed by a summary of the main research findings. The novelty of the study lies in that it covers all three dimensions of the economic relations between the parties involved, whereas the majority of other studies have focused mainly on trade or investment, and only briefly addressed the issue of labor.

2. THE IMPACT OF ACCESSION ON TRADE

This section assesses the impact of the accession on trade between Egypt and the EU by calculating the indices of export similarity, trade complementarity and revealed comparative advantage (RCA) of Egypt and the AC-10. The calculations show that the index of export similarity is quite low, indicating that Egyptian exports are not similar to those of the AC-10 and are not expected to be displaced in the EU market. Also, due to the low level of trade complementarity, Egyptian exports are not likely to penetrate the market of the AC-10. Egypt is well-positioned, however, to export a wide array of products, as shown by the RCA index, provided that the pattern of demand in these countries changes.

2.1 Accession and Trade in Industrial Goods

With respect to exports of industrial goods, there are concerns regarding the competitive position of the AC-10 vis-à-vis Egypt. First, unlike Egypt, rules of origin will not apply to AC-10 exports to the EU market, which will certainly improve conditions of market access for the AC-10.

Second, the liberalization of services between the AC-10 and the EU implies that producers in these countries will have access to better quality services (Directorate for the Middle East and South Mediterranean 2003). In comparison, the Egypt-EU Association Agreement does not include provisions in this area beyond Egypt's commitments under the General Agreement on Trade in Services (GATS). Therefore, some sectors like transportation (excluding maritime) and communications will continue to be protected from competition in world markets.

Third, producers in the AC-10 have established strong ties with European companies through outward processing trade and subcontracting. As stated in Hoekman and Djankov (1998), outward processing trade, and hence exports from the AC-10 to the EU, will increase following accession. This can be explained by the AC-10's relatively more liberal trade and investment regimes, solid institutional environment, large stock of human capital, advanced industrial sector, and geographical proximity to the EU.

Fourth, some industries like textiles and clothing, and iron and steel are highly competitive in the AC-10 (Fawzy 2004). In this regard, preliminary results from a general equilibrium model indicate that following accession, greater specialization will take place whereby EU countries will specialize in high technology sectors such as machinery, equipment and transportation, while the CEEC[1] will specialize in agricultural products and clothing. As a result, the Middle East and North Africa (MENA) region could experience a decline in textiles and clothing trade, and hence, production. Preliminary estimates indicate that clothing production will decrease by 3.6 percent in Turkey, 1.6 percent in Morocco and a total of 1.1 percent for the rest of MENA, while textile production is expected to decrease by 1.5 percent in Turkey. The effect of integration is not significant in other sectors. Overall, the EU enlargement could lead to a modest welfare loss of $254 million for the MENA region (Bayar 1998).

2.2 Accession and Trade in Agricultural Goods

Trade in agricultural products between Egypt and the EU will likely be hindered by the enlargement, as the AC-10, unlike Egypt, will enjoy free access to the EU market. In addition, the Common Agricultural Policy (CAP) of the enlarged EU will protect its market through tariff and non-tariff barriers (Tovias and Chair 2003). Beyond the agricultural quotas determining Egypt's share of the EU market, Egypt will continue to be denied free access to the agricultural sector of the enlarged EU.

Finally, there is a point that warrants attention regarding both agricultural and industrial goods. As a result of EU expansion, Egypt and other MENA countries might lose their position as close trading partners with Europe. With their relatively more advanced industrial sector, better infrastructure and more skilled labor force, the CEEC has been competing with the MENA region since 1991 as the primary market for manufactured imports from the EU, the larger exporters, and the recipients of large amounts of FDI. The accession, coupled with the increasing pace of multilateral trade liberalization, implies that the MENA region might gradually lose preferential access to the EU market (Bayar 1998).

Although the above concerns are to some extent justifiable, there are several reasons why Egyptian exports to the EU may not be displaced by AC-10 exports. In fact, not much change is expected to take place in regular trade flows following accession. This can partially be explained by the fact that the bulk of trade barriers have already been removed as a result of the Europe Agreements.

[1] CEEC: Central and Eastern European Countries. This paper will use the terms AC-10 and CEEC interchangeably as the AC-10 includes 8 CEEC countries in addition to Cyprus and Malta.

The EU and the CEEC have developed closer ties since the transition process began in 1989. These ties resulted in the conclusion of a number of associative and cooperative agreements known as the Europe Agreements, which strengthened bilateral relations and led to the removal of all tariff and non-tariff barriers to trade in industrial goods. The Agreements also included provisions for free trade in services and free movement of capital. However, trade in agricultural goods was excluded, and trade flows were subject to rules of origin amounting to 60 percent of local content requirement (Togan 1996). Following the Agreements, the pace of economic integration accelerated, as reflected in increased volumes of trade and FDI flows. The EU also became the main trading partner of the CEEC, accounting for over half of their total foreign trade (Directorate General 2001).

While the Agreements helped to promote trade between the CEEC and EU, the continued success of their trade relations is primarily due to the differences in their factor endowments. The CEEC mostly specialize in goods catering to the lower segments of the market, which require lower-skilled labor and are concentrated in resource-intensive sectors, while the EU specializes in high technology products. In addition, cooperation has taken place in the transfer of knowledge and technology, and the CEEC will align their economic legislation with that of the EU (Directorate General 2001). For the EU, the conditions of market access have improved considerably.

Whether Egyptian exports will compete with those of the AC-10 in the EU market depends on the degree of similarity between Egypt's export structure to the EU compared to that of the AC-10 (Martin et al. 2002). The index of export similarity presented in Table 1 reveals a low degree of similarity, which indicates that AC-10 exports to the EU are not expected to compete with those from Egypt. In other words, there is no scope for trade diversion. Tables 2 and 3 show that in 2001 the bulk of Egypt's exports to the EU – 36.1 percent of total exports – consisted of fuels, while the majority of AC-10 exports – 48.8 percent of total exports – consisted principally of machinery and transport equipment.

Moreover, several developments may have helped enhance Egypt's competitive position and the possibility of trade creation. One such development is the Agadir Agreement between Egypt, Tunisia, Morocco, and Jordan, which will allow Egypt to benefit from the accumulation of rules of origin for exports to the EU, and may help reduce any trade losses

Egypt might experience from the elimination of rules of origin between the AC-10 and the EU.

Another development is the EU decision to increase the quotas for textiles and ready-made garments until January 2005, as well as for iron (Europa 2004). As for agricultural products, the different cultivation seasons of certain crops between Egypt and the EU will reduce the scope of competition in this area. At Egypt's request, the EU also increased the quotas for several agricultural goods to compensate for the recent removal of barriers to trade between the AC-10 and the EU.

Considering that the Egypt-EU Association Agreement will apply to the new members of the EU, will the now wider export market offset any negative impacts on Egyptian exports due to accession? The answer to this question depends on the degree of complementarity between Egyptian exports and AC-10 imports. Data presented in Table 4 show that in 2001 the trade complementarity index between Egypt and the AC-10 was low, implying that the chance of Egypt increasing its exports to the AC-10 are at present slim.

Besides, the average tariff rate for Egypt is 20.1 percent (excluding agriculture) compared to 5.2 percent for the AC-10 (Handoussa and Reiffers 2003). Despite the low level of tariffs Egypt faces in the AC-10 market, export performance has been modest. In 2001, the share of Egypt's exports to the AC-10 was a low 0.9 percent compared to 31.4 percent for the EU (Table 5). The already low tariffs on Egyptian exports in the AC-10 market suggest that not much change is expected to take place in Egyptian exports to this group of countries following accession.

However, over time the wider EU market will undoubtedly entice Egyptian producers to search for new market niches and new export opportunities. This is especially true given that the revealed comparative advantage (RCA) index presented in Table 6 shows that Egypt is well-positioned to export a range of products including food and live animals, crude materials, fuels and lubricants, and manufactured goods.

2.3 Trade in Services

Egypt is a major exporter of services among developing countries and holds a leading position in the region in some 50 service-based exports. These include transport services (with a rank of 7), travel (9), communications (4), construction (8), computer and information services (9), financial services (11), royalties and license fees (8), other business services (10), and personal, cultural and recreational services (10) (El Shinnawy forthcoming). According to the Central Bank of Egypt, exports of services increased from $3.5 billion in 1990/91 to $10.4 billion in 2002/03. The tourism sector accounts for the largest share (36 percent) of total receipts from services.

Egypt has a competitive edge over the majority of the AC-10 in services trade, as Egypt and only 3 of the AC-10 are among the top 40 exporters of commercial services worldwide. According to the World Trade Organization (2002), Egypt ranks 32nd with a share of 0.6 percent of world trade in services. As for the AC-10, Poland ranks 29th (0.8 percent), Hungary ranks 35th (0.5 percent) and the Czech Republic ranks 36th (0.5 percent). The index of revealed comparative advantage (RCA) for Egypt and the AC-10 provides more evidence as to the competitiveness of Egypt in the area of trade in services. In 2001, Egypt ranked higher than all but one of the AC-10 (Table 7). Based on such evidence, there is sufficient reason to believe that Egypt is favorably positioned in the domain of trade in services vis-à-vis the AC-10.

Egypt's edge may be lost, however, due to increased competition in the tourism sector. As indicated by Eurostat (2002), some of the AC-10 are already competing with Egypt as an attractive destinations for tourism, particularly because political instability continues to undermine the comparative advantage of the Mediterranean partners of the EU (including Egypt). By adopting the Euro sometime in the future, the exchange rate barrier will be removed and therefore European tourism to the AC-10 is expected to increase (Tovias and Chair 2003).

As argued by Ghoneim (2003), Egypt could benefit from the enlargement as the EU attempts to improve market access for services, allowing various service providers from the developing world to operate in the EU market. This could present Egyptian service providers with an opportunity to establish a presence in the EU market with respect to tourism, construction, information technology as well as other services. However, it is important to note that the AC-10 may have an advantage over Egypt due to the Lisbon Strategy, which aims to turn the EU into a highly competitive and dynamic economy by the year 2010 (Kok 2003). Such a strategy will lead to increased integration in sectors such as communications, transportation and financial services, which will likely favor the AC-10.

3. The Impact of Accession on Capital Flows

This section assesses the impact of accession on capital flows both in the short and long runs, highlighting the factors that are of essence in attracting FDI. As with the case of exports, FDI flows to Egypt from the EU are not expected to change much following accession.

3.1 In the Short Run

As shown in Table 8, FDI flows to Egypt have trended downward, while those of the AC-10 have increased, revealing that the AC-10 is seen as a more attractive destination for FDI. It is important to note that in the context of the Europe Agreements, capital has been moving freely between the EU and CEEC for some time. This indicates that, *in the short run*, flows of foreign direct investment from the EU are not expected to change much following accession. FDI flows from the EU accounted for 68.3 percent of Egypt's total capital flows in 2001/02 (Table 9).

3.2 In the Medium to Long Runs

In the medium to long runs, the impact of the accession on capital flows depends on several factors. To begin, the terms of the accession entailed deeper integration between the AC-10 and the EU, which could lead to increased capital flows compared to countries that have signed association agreements with the EU. This can be explained by the fact that it is much easier to operate in a familiar administrative and legal environment. This should send a clear message to policymakers in Egypt that in order to attract more FDI from the EU steps must be taken towards deeper integration.

The size of the market is deemed an important determinant of FDI flows as it makes it possible to take advantage of economies of scale. The EU expansion will certainly lead to a larger market, which would help attract more FDI, just as Egypt is able to conduct duty-free trade with neighboring Arab countries through the Greater Arab Free Trade Agreement (GAFTA) and with the Common Market for Eastern and Southern Africa countries (COMESA).

Openness, measured by the ratio of trade to GDP, is also among the factors that impact FDI flows. In 2001, the ratio of trade to GDP reached 81 percent for the AC-10 compared to 25 percent in the case of Egypt (Handoussa and Reiffers 2003). The openness of an economy acts as a stimulant to growth, which in turn leads to more FDI. Also, higher growth will likely lead to increased demand for exports from the EU (Directorate General 2001) and possibly from Egypt.

Privatization, yet another important factor influencing FDI, is proceeding at a slow pace in Egypt. Out of 314 companies slated for privatization, with total assets of LE104 billion and 1.08 million employees, only 190 have been privatized (CARANA 2002). Over the period 1990-2001, proceeds from privatization in Egypt amounted to $5 billion, while that of the AC-10 totaled $60 billion over just two years from 1999-2001 (Jbili and Koranchelian 2003).

A number of other determinants can influence FDI. Over the period 1998-2000, debt service to exports was 10 percent in Egypt compared to 15 percent for the AC-10. In 2001, Egypt's international reserves in terms of months of imports reached 9.7 percent versus 3.3 percent for the AC-10 (IMF 2003). With respect to the rule of law, Egypt scored 4 (out of 6) while most of the AC-10 scored 5. As for political risk, Egypt scored 64.5 (maximum 100) compared to 79.6 for the AC-10 (PRS Group 2003).

Apart from the percent of debt service to GDP and reserves in terms of months of imports, the FDI determinants examined above show that in the long run Egypt will become less attractive to FDI flows than the AC-10. To attract more FDI, it is necessary for Egypt to modify the Association Agreement to allow for deeper integration, and to give more momentum to the reform efforts taking place within the framework of Egypt's stabilization and structural adjustment program. In addition to the need to speed up both privatization and trade liberalization efforts, one area of reform that merits particular attention is market liberalization. It is worth noting that this is one of the criteria determining EU accession.

3.3 Market Liberalization

The degree of market liberalization is a major determinant of the rate of economic growth, the supply response on behalf of firms, and the attractiveness of a country to FDI flows (Diwan 2002). Although Egypt has made progress in the area of deregulation since the initiation of Egypt's Open Door Policy in 1974, some areas have yet to be addressed, such as the prices of several commodities that are still protected from market forces.[2] These include bread, fuel, sugar, edible oil, cotton and cotton products, some pharmaceutical products, utilities (water, electricity), and public transportation (USAID and Egyptian Ministry of Economy 1995). In

[2] This section draws on El Shennawy (2003b).

the case of public utilities, regulation is sometimes needed in an environment where market forces play at least a minor role in the determination of prices (Galal 1997).

The existence of minimum wage legislation in Egypt is an important issue that needs to be addressed as it contributes to imperfections in the labor market. With respect to capital markets, Egypt would be well-advised to introduce more reforms such as decreasing collateral requirements, which have traditionally been high and lead to capital market imperfections. This constraint particularly affects small-scale enterprises (World Bank 1994). The banking system is dominated by four state-owned banks, which led to limited competition and hampered the development of the banking sector (Caprio and Cull 2000). In 1999, limited competition among banks was reflected in high real interest rates which reached 7.9 percent (Mohieldin 2001).

In addition, there are barriers to entry and exit that hamper competition in other sectors of the economy. For example, the high capitalization requirement discourages small firms from entering the market (Goans 2002), while the bankruptcy law acts as a barrier to exit (Nathan Associates and Pegan 1998).

Many aspects of the economic environment in Egypt lead to high transaction costs, and therefore, to market imperfections. To mention but a few, tax collection is considered one of the main factors that discourage foreign investment and create strong preferences to work within the informal sector (Tohamy 1999). Also, dealing with customs authorities serves to increase the cost of imports (Helmy 2003; El Shennawy 2003a). Reducing transaction costs primarily requires that both the tax and custom laws be modified in order to reduce the scope for exercising opportunism by both the tax and customs officers.

Finally, how will the accession impact the economies of the AC-10 and their ability to attract FDI? In this respect, it is important to note that barriers to trade and capital mobility that existed between the AC-10 and the EU will mostly be removed following the accession. The AC-10 will apply the Common Agricultural Policy (CAP) and might join the Euro Zone in the future. Restrictions on labor mobility will also be removed, and the AC-10 will be more likely to receive additional transfers of capital from the EU. As a result of increased investment, economic growth will accelerate, resources will be allocated more efficiently, and productivity will increase. The average annual increase in the rate of economic growth in the CEEC is expected to range between 1.3 and 2.1 percent (Directorate General 2001).

The fact that the AC-10 have fulfilled the Copenhagen criteria[3] sends a clear message to foreign investors that these countries are well-positioned to receive more FDI from the EU and elsewhere. Furthermore, the accession itself is expected to have a positive effect on the macroeconomic environment of these countries. The average ratio of investment to GDP is projected to reach 26 percent, while GDP in the CEEC is expected to grow at an annual average rate of 4 percent over the period 2000-2009, with positive implications for the ability to attract FDI. In fact, foreign transfer income as a percent of GDP is expected to average 3 percent in the period 2004-2009. The accession will deepen this process further, as growth in total factor productivity (TFP) is expected to lead to an increase of 4.8 percent in GDP (Directorate General 2001).

With regards to the international rating agencies (e.g., Moody's), perceptions of the accession countries changed following the signing of the Copenhagen Treaty. The credit rating for the AC-10 improved immediately, thus rendering these countries attractive to FDI, and even more so after enhancing the quality of their institutions (Handoussa and Reiffers 2003).

Finally, it is worth noting that apart from the need to accelerate reform in several areas as mentioned earlier, increasing FDI flows from the EU to Egypt requires that the Association Agreement between Egypt and the EU be modified to allow for the free movement of capital. Moreover, increasing the amounts of FDI inflows to Egypt and other countries in the region requires more efforts to reduce political instability caused by the Palestinian-Israeli conflict.

4. The Impact of Accession on Labor Migration

This section addresses the issue of labor migration, preceded by a brief discussion of the relevant theoretical models.

The two main theoretical models explaining the factors underlying labor migration are provided by Mundell (1957) and Sjaastad (1962). According to the two models, labor migration is influenced by relative wages; given a job opportunity, workers tend to migrate in pursuit of higher wages. The migration decision is also influenced by unemployment rates in destination countries, geographical proximity, and the presence of previous immigrants.

[3] European Union membership criteria are commonly referred to as Copenhagen criteria because they were first discussed at the Copenhagen European Council in 1993. Available at: http://europa.eu.int/comm/enlargement/intro/criteria.htm

Previous immigrants help family members and friends with information about job vacancies, accommodation and transportation costs. Such “ethnic networks” help reduce the cost and risk of migration (Martin et al. 2002).

The Egypt-EU Association Agreement does not include provisions for the free movement of people. Even if it did, the above considerations make it reasonable to expect that the direction of immigration following accession will be from the AC-10 to the EU rather than between Egypt and the AC-10. Income differentials – lower wages in Egypt – and the lack of strong historical and cultural ties between Egypt and the AC-10 seem to support this hypothesis. In 2000, the number of Egyptian migrants to the EU was much larger than those to the AC-10 (Table 10). Of the total migration to European countries in 2000, 65.15 percent was destined to Germany (Table 10b). Remittances from migrants residing in the EU in 2001/2002 accounted for 10.34 percent of total remittances, while those from migrants in the Arab countries accounted for 49.83 percent (Table 11).

Restrictions on labor migration suggest a lost opportunity for Egypt to benefit from temporary immigration to the EU and the AC-10, particularly in light of the aging population in these countries. Egypt might also incur additional losses due to the possible decline in unemployment, foregone income from labor remittances and consequently less foreign reserves and less economic growth (Handoussa and Reiffers 2003).

Critics of deeper integration of labor markets argue that migration would lead to higher unemployment rates in the EU. As for the southern Mediterranean partners to the EU including Egypt, Tunisia, Morocco, and Jordan, migration might intensify the phenomenon of “brain drain” at a time when skilled labor is deemed essential to improving international competitiveness. Aside from justified concern about brain drain, skills which are not put to use or maintained through on-the-job training are apt to erode or become obsolete unless migration is possible, at least on a small scale (Diwan 2002).

Furthermore, there is a strong relationship between labor market conditions in the MENA region and political resistance to reform. For Egypt, and other regional signatories to the EU-MED agreement, a well-designed program of managed migration not only could result in increased remittances, but might also help in realizing the objectives of the agreement. First, it could create a constituency of beneficiaries from the agreement. Second, by improving labor market conditions it could help reduce the extent of socio-economic and political pressures and hence accelerate the pace of economic reforms (Diwan 2002).

A key issue here is the extent to which Egyptians and AC-10 migrants will compete for jobs in the EU if restrictions on labor migration are removed. According to Boeri et al. (2000), it is expected that 355,000 individuals will migrate from the AC-10 to the EU following the accession. Also, the more educated and productive labor force of the AC-10 will certainly reduce the opportunities for migration from Egypt (Table 12).

In the long run, opportunities for migration to the EU will increase for a number of reasons. The complementarity between population pyramids in Egypt and the enlarged EU will provide further opportunities for migration from Egypt (Directorate for Middle East and South Mediterranean 2003). Besides, the demographic structure of the AC-10 is similar to that of the EU. That is, they also suffer from declining populations, which could represent an opportunity for migration from Egypt to the enlarged EU (Table 13). Further, the accession will likely improve economic conditions in the AC-10, which might not only dampen the incentives to migrate but also serve to reverse past migration. This again signals the need to modify the Association Agreement between Egypt and the EU to allow for the free movement of people and to take advantage of immigration opportunities.

5. Conclusion

This paper explored the possible implications of EU expansion for the Egyptian economy. It finds that in the short-run, not much change in trade and capital flows or the movement of people is expected following EU enlargement. This can be explained by the fact that the bulk of change had already taken place in context of the Europe Agreements which were concluded between the AC-10 and the EU in the early and mid-90s. In addition, the index of export similarity reveals that Egypt's export structure to the EU is not similar to that of the AC-10, implying that in the short run Egypt might not face competition from AC-10 in the EU market.

In the medium to long runs, the impact of the accession on Egypt depends on the extent and pace of reforms as well as improvement in productivity. In the absence of adequate reform efforts or significant improvements in productivity, several factors – ranging from a well-educated labor force to higher productivity of the AC-10 – will combine to erode Egypt's comparative advantages which are mainly due to lower wages. Also, Egypt could face tougher competition from these countries if it diversifies its exports to include more sophisticated products currently produced by the AC-10.

However, Egypt's competitiveness can be improved if it negotiates more liberal trade in agricultural goods and less stringent rules of origin. Some of the products that Egypt could export to take advantage of a now larger European market are food and live animals, crude materials, fuels and lubricants, and manufactured goods.

With respect to FDI, Egypt is well-advised to undertake more reforms to improve its business climate and to enhance its competitive edge. Also required is deeper integration between Egypt and the EU countries, similar to that undertaken by the AC-10. This could help attract significant FDI from the EU as entrepreneurs find it easier to operate in a familiar legal framework.

Concerning labor mobility, Egypt would do well to negotiate the temporary migration of Egyptians to the EU with potential benefits to both parties. Currently, workers in the AC-10 have a comparative advantage in inexpensive skilled labor, since such labor in Egypt is relatively scarce and not cheap. But, as the economies of the AC-10 improve following accession and the adoption of additional reforms, wages are likely to rise at a time when Egypt is likely to possess more skilled labor. This could give Egypt an advantage in goods which require skilled labor.

Finally, catching up with the AC-10 requires Egypt to increase both the speed and extent of reforms that promote macroeconomic stability, accelerate institutional reform and deregulation, and achieve more openness. It is through these reforms that Egypt will be better equipped to minimize the cost and maximize the benefits inherent in the EU enlargement.

APPENDIX

Table 1. Export Similarity Indices of Egypt and the AC-10 with Respect to the EU Market, 2001

Comparator Country	Export Similarity Index (%)
Cyprus	6.8
Czech Rep.	6.3
Estonia	7.2
Hungary	6.5
Latvia	11.8
Lithuania	9.4
Malta	1.9
Poland	9.7
Slovakia	9.8
Slovenia	9.4

Note: The export similarity index was calculated using the 4-digit SITC.
Source: United Nations. PC-TAS 1997-2001.

Table 2. Egypt's Exports to the EU, 2001 (Reporter: Egypt) million US $

SITC Code	Product	Trade Value
0	Food and Live Animals	79.9
1	Beverages and Tobacco	0.1
2	Crude Materials, inedible	92.4
3	Fuels, Lubricants, etc.	473.0
4	Animal, Vegetable Oils, Fats, Wax	0.1
5	Chemicals, Related Products, Nes	142.9
6	Manufactured Goods	380.8
7	Machines, Transport Equipment	8.8
8	Miscellaneous Manufactured Articles	130.6
9	Goods not classified by kind	na
Total	**All Commodities**	**1308.7**

Source: United Nations. PC-TAS 1997-2001.

Table 3. Exports from the AC-10 to the EU, 2001 (Reporter: AC-10) million US $

SITC Code	Product	Trade Value
0	Food and Live Animals	3026.6
1	Beverages and Tobacco	232.1
2	Crude Materials, inedible	3197.9
3	Fuels, Lubricants, etc.	3107.3
4	Animal, Vegetable Oils, Fats, Wax	18.1
5	Chemicals, Related Products, Nes	3544.2
6	Manufactured Goods	17423.4
7	Machines, Transport Equipment	44267.5
8	Miscellaneous Manufactured Articles	15089.9
9	Goods not classified by kind	855.8
TOTAL	**All Commodities**	**90764.2**

Source: United Nations. PC-TAS 1997-2001.

Table 4. Trade Complementarity between Egyptian and AC-10 Imports, 2001

AC-10	Trade Complementarity Index
Cyprus	24.1
Czech Republic	18.6
Estonia	17.6
Hungary	17.2
Latvia	18
Lithuania	23.8
Malta	12.5
Poland	22.9
Slovakia	20
Slovenia	21.2

Source: Calculated by the author.

Table 5. Egypt's Exports* to the EU and the AC-10 as % of Total Exports

Partner	1993	1994	1995	1996	1997	1998	1999	2000	2001
EU	na	44.0	4.6	45.6	41.5	37.5	35.3	na	31.4
AC-10	na	1.0	0.1	0.7	0.7	0.7	0.7	na	0.9
Cyprus	na	0.4	ng	0.4	0.3	0.2	0.2	na	0.1
Czech Rep.	na	0.2	ng	0.1	0.1	0.1	0.1	na	0.1
Estonia	na	na	na	na	ng	ng	ng	na	ng
Hungary	na	0.1	ng	0.1	0.1	0.1	0.1	na	0.1
Latvia	na	na	na	Na	ng	ng	ng	na	ng
Lithuania	na	na	na	Na	ng	ng	ng	na	ng
Malta	na	ng	ng	Ng	0.1	0.1	0.2	na	0.5
Poland	na	ng	ng	Ng	ng	ng	ng	na	ng
Slovakia	na	na	ng	Ng	ng	ng	ng	na	ng
Slovenia	na	0.3	ng	0.2	0.2	0.2	0.2	na	0.2

* 1994-1996: Total exports are calculated as the sum of the 10 SITC categories (one-digit).
Source: United Nations. PC-TAS 1993-1997 & 1997-2001.

Table 6. Revealed Comparative Advantage (RCA)

SITC	Product name	Egypt's RCA	AC-10 RCA ≥ Egypt
0019	Live animals, nes	20.10	
0423	Rice, milled, semi-milled	47.25	
0461	Flour of wheat, meslin	4.28	
0541	Potatoes, fresh, chilled	28.23	CYP
0542	Legumes, dried, shelled	9.70	
0545	Oth. frsh, chll. Vegetables	2.70	CYP
0546	Vegetables frozen	8.47	CYP, CZE, SVK
0548	Veg. products, roots, tubrs	3.54	
0561	Vegetables, dried	18.80	
0566	Vegetable, unpickled frzn	3.52	
0567	Veg. prepared, presrvd, nes	1.23	HUN, POL, LTU
0571	Oranges, etc.	22.29	CYP
0572	Oth. citrus, fresh, dried	1.96	CYP
0582	Fruit, nuts prov. Preservd	5.00	
0599	Juices, other than citrus	2.31	CYP, HUN, LVA, LTU, POL
0611	Sugars, beet or cane, raw	2.43	
0612	Other beet, sugar cane	1.08	LTU, POL
0615	Molasses	70.10	
0622	Sugar confectionery	1.12	CYP, EST, CZE, POL, SVK
0741	Tea	6.90	
0752	Spices, ex. pepper, pimento	7.48	
0910	Margarine, etc.	3.83	
0985	Soups and broths	1.86	
2221	Groundnuts (peanuts)	3.91	SVK
2224	Sunflower seeds	2.92	
2225	Sesame (sesamum) seeds	5.54	HUN, SVK
2227	Safflower seeds	3.05	
2231	Copra	104.19	CZE
2450	Fuel wood, wood charcoal	8.12	
2631	Cotton, not carded, combed	54.09	LVA, HUN, EST, POL
2651	Flax, waste flax	46.38	
2658	Veg. textile fibers, nes	22.73	
2723	Natural calc. phosphates	1.07	
2731	Building, dimension stone	28.82	
2733	Sands, natrl. not mtl. Brng	21.25	
2783	Sodium chloride, etc.	11.99	
2789	Minerals, crude, nes	3.55	CYP
2821	Waste, scrap of cast iron	1.50	MLT, LVA, LTU, SVK
2911	Bone, horn, ivory, coral, etc	5.80	HUN, LTU
2922	Natural gums, resins, etc.	4.00	
2924	Plants, pharmc., perfm. Etc	19.49	
2925	Seeds, etc., for sowing	2.53	
3211	Anthracite, not agglomrtd	2.03	
3250	Coke, semi-coke, ret. Carbn	35.00	
3330	Crude petroleum	2.32	
3343	Gas oils	6.44	
3344	Fuel oils, nes	112.27	
3351	Petroleum jelly, wax etc	9.46	
3421	Propane, liquefied	18.54	
4229	Oth. fixd veg. fat, ex. Soft	7.76	
4312	Fat, oil, an, vg. Prtly, prcd	12.44	
5121	Acyclic monohydric alchl	1.78	SVK

Table 6 (cont.) Revealed Comparative Advantage (RCA)

SITC	Product name	Egypt's RCA	AC-10 RCA ≥ Egypt
5221	Carbon nes, carbon black	71.02	
5226	Oth. inorgan. bases, oxides	4.34	
5234	Sulphides, sulphates, etc.	1.84	
5235	Nitrites; nitrates	37.33	
5323	Synthetic tanning substs	2.23	
5541	Soap	4.76	
5542	Detergents, except soap	3.31	
5621	Nitrogenous chem. Fertlzr	23.91	LTU
5622	Phosphatic chem. Fertlzrs	26.88	
5711	Polyethylene	1.01	SVK, HUN, CZE
5731	Polyvinyl chloride	4.27	
5914	Disinfectant, etc. retail	1.41	SVN, MLT
5984	Mixed alkylbenzs. etc. nes	20.75	
6112	Composition leather	2.17	HUN
6113	Whole bovine skin leather	7.93	LTU
6114	Oth. bovine, equine leather	2.19	LTU
6252	Tires, pneumatic, new, bus	5.84	SVK
6332	Agglmrtd. cork, cork articles	1.11	
6354	Wood, domest. use ex. Furnt	1.75	EST, SVN, POL
6424	Paper, paperboard, cut, nes	1.49	SVK, LVA, HUN, POL, SVN
6429	Articles, pulp, paper, brd, nes	1.01	CYP, SVN, POL, HUN, CZE
6513	Cotton yarn, excl. thread	32.33	
6519	Yarn, textile fibres, nes	1.62	LVA, CZE, EST, SVK
6522	Cotton fabric, wvn, unbleached	16.60	
6545	Fabric, wvn. jute, other textiles	1.11	
6575	Twine, cordage, etc. products	2.07	
6583	Blankets, travelling rugs	1.34	LTU, SVN, LVA, CZE
6584	Household linens	23.22	
6589	Made-up articls, vtxtl. Nes	1.09	EST, POL, SVK, CZE, LTU, HUN
6592	Carpets etc. vknotted	1.62	
6593	Hand-woven rugs	2.58	HUN
6595	Carpets, etc. woven	1.12	POL, EST
6613	Building stone, worked. Etc	4.45	
6623	Refractory bricks etc.	1.41	SVK, HUN, CZE
6624	Non-refractory brick, etc	3.39	
6651	Containers, of glass	2.11	EST, CZE, POL
6652	Glassware, household etc.	4.07	CZE, SVK, SVN, POL
6659	Glass articles, nes	1.65	CZE, EST, MLT
6661	Ceramic household articles	4.00	CZE, POL
6712	Pig iron, etc. primary. Form	6.02	
6715	Other ferro-alloys	7.44	SVK
6724	Ingots of iron or steel	4.83	
6732	Flat, hot-rolled, prod. Iron	2.68	SVK, CZE, SVN
6753	Flat, hot-rolled s.steel	14.39	
6762	Bar, rod iron, stl. hot-fd	10.58	LVA
6841	Aluminum, alum. alloy, unwrght	6.74	LVA
6842	Aluminum, alum. alloy, wrk	1.69	SVN, HUN, CYP
6932	Barbed wire, etc. iron, stl	2.33	
6963	Razors, razor blades	5.90	
6974	Tbl, ktchn, h.hold art. Nes	2.44	
6978	H.hold appliances, etc. nes	3.50	
7165	Generating sets	2.11	HUN

Table 6 (cont.) Revealed Comparative Advantage (RCA)

SITC	Product name	Egypt's RCA	AC-10 RCA ≥ Egypt
7456	Spraying machinery etc.	2.10	CYP
8122	Ceramic plumbing fixtures	18.09	
8412	Suits and ensembles	3.48	MLT, SVK, SVN, LTU
8413	Jackets and blazers	2.20	MLT, LTU, HUN, LVA, POL, SVN, SVK, CZE, EST
8414	Trousers, breeches, etc.	4.21	MLT, LTU
8415	Shirts	4.51	CYP
8416	Underwear, nightwear etc.	15.42	
8422	Suits and ensembles	2.69	LVA, SVN, CYP
8424	Dresses	1.78	CYP, LTU, LVA, POL, EST
8426	Trousers, breeches etc.	2.84	LTU, CYP, POL
8427	Blouses, shirt-blouse, etc	1.11	LTU, HUN, LVA, POL, CYP,EST
8428	Underwear, nightwear etc.	1.66	HUN
8438	Underwear, nightwear etc.	7.41	
8454	T-shirts, othr. vests knit	9.42	
8932	Builders' ware, plastics	8.58	
8974	Other articles, prec. Metal	13.09	LVA
9310	Special trans not classified	2.43	

Note: AC-10: Estonia (EST), Lithuania (LTU), Latvia (LVA), Poland (POL), Slovenia (SVN), Slovakia (SVK), Hungary (HUN), Malta (MLT), Czech Republic (CZE), Cyprus (CYP).

Source: Author's calculations based on United Nations PC-TAS data, 2003.

Table 7. Revealed Comparative Advantage (RCA) in Commercial Services in Select Mediterranean Partners and the Accession Countries

Country	RCA (2001)
Mediterranean Partners	
Egypt	3.56
Jordan	2.14
Morocco	1.82
Tunisia	1.55
Accession Countries	
Cyprus	3.96
Czech Republic	0.89
Estonia	1.72
Hungary	1.04
Latvia	1.98
Lithuania	1.04
Malta	1.89
Poland	1.29
Slovakia	0.85
Slovenia	0.91

Source: Handoussa and Reiffers 2003.

Table 8. FDI Flows by Host Economy (US$ million)

Host Economy	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	% Change*
Egypt	1250	734	352	459	493	1256	598	636	887	1065	2919	1235	510	-59.2
Cyprus	70	130	82	107	83	75	119	54	76	69	121	163	163	132.9
Czech Rep	na	na	na	1003	568	862	2559	1428	1300	3718	6324	4986	4916	390.1
Estonia	na	na	na	82	162	215	202	150	267	581	305	387	538	556.1
Hungary	na	na	1462	1471	2339	1146	4453	2275	2173	2036	1944	1643	2414	65.1
Latvia	na	na	na	29	45	215	180	382	521	357	348	408	201	593.1
Lithuania	na	na	na	10	30	31	73	152	355	926	486	379	446	4360
Malta	52	46	77	40	56	152	184	277	81	267	822	652	314	503.8
Poland	11	89	291	678	1715	1875	3659	4498	4908	6365	7270	9342	8830	80172.7
Slovak Rep	na	na	na	100	168	245	195	251	220	684	390	2075	1475	1375
Slovenia	na	na	na	111	113	128	176	194	375	248	181	176	442	298.2

* % Change = percentage change over available time trend.

Source: United Nations. *World Investment Report*. 1995, 1998, and 2002.

Table 9. FDI to Egypt by Donor Economy (US$ million)

Donor Economy	1995/96	1996/97	1997/98	1998/99	1999/2000	2000/01	2001/02*	% Change**
France	18.2	9.2	62.7	3.2	62.4	0.1	208.1	1043.4
Germany	13.1	19.4	8.6	32.7	25.6	25.2	17.5	33.6
Italy	3.6	0.8	3.9	2.6	1.4	1.5	2.7	-25.0
Netherlands	na	na	na	na	0.0	0.0	0.0	0
Portugal	na	na	na	Na	486***	na	38.8	-92.0
Spain	4.2	na	na	Na	3.6	0.0	83.8	1895.2
Sweden	1.1	na	na	Na	na	na	na	na
Switzerland	7.7	12.2	5.8	19.4	22.8	5.8	2	-74.0
United Kingdom	9.5	16.7	7.9	15.7	178.7	169.4	12.3	29.5
FDI-EU	49.7	46.1	83.1	54.2	757.7	196.2	363.2	630.8
Total Inflows	627.1	769.7	1149.6	715.6	1691.2	510.1	532	-15.2
FDI-EU %	7.9	6	7.2	7.6	44.8	38.5	68.3	764.6

* Provisional.

** % Change = percentage change over available time trend.

*** Includes the proceeds from the sale of the El-Amrya Cement Co.

Notes: FDI-EU = FDI inflows from EU Countries (Austria, Belgium, Denmark, France, Finland, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, United Kingdom, and Sweden). FDI-EU% = FDI-EU as percentage of inflows to Egypt.

Source: Central Bank of Egypt.

Table 10. Total Number of Migrants from Egypt to EU Countries, 1971-2000

Year	France	Germany	United Kingdom	Italy	Spain	Greece	Austria	Portugal	Sweden	Denmark	Belgium	Finland	The Netherlands
1971		5349				1116	781						
1981	4300	8587				2415	1574	4					
1991	6300	8640				4012	4509	25					4546
1997		13595	3000	25272		6903							3105
1998		13927	4000	27286	778	6599						217	3101
1999		13976	6000	30582	919			51	596		613	220	2933
2000		13811			972			57	605	576		218	2771

Table 10a. Annual Change (%)

Year	France	Germany	United Kingdom	Italy	Spain	Greece	Austria	Portugal	Sweden	Denmark	Belgium	Finland	The Netherlands
1971													
1981		60.53				116.40	101.54						
1991	46.51	0.62				66.13	186.47	525.00					
1997		57.35				72.06							-31.70
1998		2.44	33.33	7.97	18.12	-4.40							-0.13
1999		0.35	50.00	12.08	5.77							1.38	-5.42
2000		-1.18						11.76	1.51				-5.52

Table 10b. Share of Migrants to Each Country/Total Migration (%) from the Countries Listed in the Table

Year	France	Germany	United Kingdom	Italy	Spain	Greece	Austria	Portugal	Sweden	Denmark	Belgium	Finland	The Netherlands
1971		73.82				15.40	10.78						
1981	25.47	50.86				14.30	9.32	0.02					
1991	22.47	30.82				14.31	16.08	0.09					16.21
1997		26.20	5.78	48.71	1.50	13.30							5.98
1998		24.01	6.90	47.05	1.58	11.38						0.37	5.35
1999		24.10	10.35	52.73	1.68			0.09	1.03		1.06	0.38	5.06
2000		65.15						0.27	2.85	2.72		1.03	13.07

Table 10 (cont.) Total Number of Migrants from Egypt to Other Countries, 1971-2000

Year	Switzerland	Romania	Norway	Hungary	Iceland	Slovenia	Liechtenstein	Total
1971								7246
1981					3			16883
1991					4			28036
1997					5	5		51885
1998	1624			449	5	7		57993
1999	1534	1	111	451	6	4	2	57999
2000	1591	2	131	456	5	3		21198

Table 10a. (cont.) Annual Change (%)

Year	Switzerland	Romania	Norway	Hungary	Iceland	Slovenia	Liechtenstein	Total
1971								
1981								133.00
1991					33.33			66.06
1997					25.00			85.07
1998					0.00	40		11.77
1999	-5.54			0.45	20.00	-42.86		0.01
2000	3.72	100	18.02	1.11	-16.67	-25		-63.45

Table 10b (cont.) Share of Migrants to each Country/Total Migration (%)

Year	Switzerland	Romania	Norway	Hungary	Iceland	Slovenia	Liechtenstein	Total
1971								7246
1981					0.02			16883
1991					0.01			28036
1997					0.01	0.01		51885
1998	2.80			0.77	0.01	0.01		57993
1999	2.64	0.00	0.19	0.78	0.01	0.01	0.0	57999
2000	7.51	0.01	0.62	2.15	0.02	0.01		21198

Source: Arab Labor Organization. *Statistical Bulletin of Arab Migrants in the European Countries (1971-2000)*, Arab Labor Office.

Table 11. Remittances of Egyptians Working Abroad by Country, 2001/2002

EU Country	Remittances (US$ million)	Remittances by Country/Total (%)
France	47.3	1.60
Germany	89.1	3.02
Italy	32.4	1.10
The Netherlands	12	0.41
United Kingdom	116	3.93
Greece	5.2	0.18
Spain	3.4	0.12
Total	305.4	10.34
Arab Countries		
Saudi Arabia	621.2	21.04
Kuwait	376.4	12.75
United Arab Emirates	349.4	11.83
Qatar	45.4	1.54
Bahrain	54.2	1.84
Oman	11.3	0.38
Libya	3	0.10
Lebanon	10.3	0.35
Total	1471.2	49.83
Other		
United States	955.9	32.38
Switzerland	119.9	4.06
Japan	8.6	0.29
Canada	5.9	0.20
Other Countries	85.6	2.90
Total	1175.9	39.83
Grand Total	2952.5	100.00

Source: Central Bank of Egypt. 2003. *Monthly Statistical Bulletin*, October.

Table 12. Productivity, Wage Rate and Unit Labor Cost in Egypt and Select Accession Countries, 1999

Country	Productivity	Wage Rate	Unit Labor Cost
Egypt	24,629	4,127	0.09
Czech Republic	36,628	2,896	0.11
Estonia	19,144	56,243	0.15
Hungary	44,772	2,678	1.26
Latvia	17,395	2,867	0.15
Lithuania	18,993	3,193	0.15
Slovakia*	32,078	2,243	0.10

Source: UNIDO. 2002. *Industrial Statistics Database*, CD-ROM.
*Data for Slovakia are available only for the year 1998.
Note: Productivity = Production/Employment
Wage Rate = Wages/Employment
Unit Labor Cost = Wage Rate/Productivity

Table 13. Demographic Indicators Affecting the Movement of People from Egypt and the AC-10 to the EU

Indicator	Egypt	AC	EU
Population in million (2000)	65	75	455
Population growth rate (1975-2000)	2.2	0.15	0.4
Population growth rate (2000-2015)	1.5	-0.6	0.1
Labor force growth rate (1995-2000)	2.7	0.3	9.8
Unemployment rate (2000)	9.9	12.4	6.5
Percentage of labor force to the total population (2000)	40	5.3	48.8
Percentage of population above the age of 65 to the total population	3.7	15.7	13.6
Percentage of population below the age of 15 to total population	35.4	19.27	17.4

Source: Fawzy 2004.

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