Foreign and Intratrade Policies of the Arab Countries

Edited
by
Said El-Naggar

International Monetary Fund

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Papers presented at a Seminar held in
Abu Dhabi, United Arab Emirates,
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Foreword

World trade has been a powerful source of growth in the entire postwar period, and the further liberalization of international trade would give invaluable impetus to economic activity. For this reason, the subject of this seminar and its significance for the Arab countries in particular is of special interest. This fourth volume of seminar proceedings published jointly by the IMF and the Arab Monetary Fund is a valuable addition to the series. The IMF is pleased to have again been associated with the Arab Monetary Fund, the Arab Fund for Economic and Social Development, and the World Bank in this seminar that addressed the issues of foreign trade and intratrade policies of the Arab countries.

Held in Abu Dhabi, United Arab Emirates, on January 27–29, 1992, the seminar brought together government officials, academic experts, and representatives of international and private organizations to discuss their experiences and to offer proposals on such topics as import substitution versus export orientation, the impact of protectionism in the industrial countries on the trade of Arab countries, the significance and implications of the Uruguay Round of Multilateral Trade Negotiations, and prospects and problems of inter-Arab trade. Professor Said El-Naggar again moderated the seminar and brought his invaluable experience to bear on managing the discussions as well as on preparing the proceedings for publication.

MICHEL CAMDESSUS
Managing Director
International Monetary Fund

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Acknowledgment

This seminar, like the three before it, was the fruit of collaborative efforts between the Arab Monetary Fund, the Arab Fund for Economic and Social Development, the International Monetary Fund, and the World Bank. The subject of this seminar has recently acquired special importance in view of the liberalization programs undertaken by most of the Arab countries. It is not an exaggeration to say that the success of economic reform in many Arab countries will hinge on their capacity to adjust their foreign trade policies to take account of far-reaching changes in the world economy as well as at home and in the Arab region.

The seminar provided an excellent opportunity for a number of high-level experts and policymakers to examine the various aspects of foreign and intratrade policies of the Arab countries. The six papers presented at the seminar are included in this publication, together with the comments of the discussants. In addition, the moderator prepared a paper which, while expressing his personal views, reflects a number of points and issues raised in the course of discussions at the seminar.

On behalf of the participants, I would like to express my thanks to Ahmed Al-Tayer, Minister of State for Finance and Industry in the United Arab Emirates, for making the keynote address. A special word of thanks is due to Osama Faquih and Abdlatif Al-Hamad and to their collaborators, for their hospitality and their tireless efforts in planning and organizing the seminar. I would like also to thank Elin Knotter of the External Relations Department of the International Monetary Fund for editing this volume and preparing it for publication.

SAID EL-NAGGAR
Moderator

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Contents

The following symbols have been used throughout this paper:

. . . to indicate that data are not available;

— to indicate that the figure is zero or less than half the final digit shown, or that the item does not exist;

– between years or months (e.g., 1991–92 or January–June) to indicate the years or months covered, including the beginning and ending years or months;

/ between years (e.g., 1991/92) to indicate a crop or fiscal (financial) year.

"Billion" means a thousand million.

Minor discrepancies between constituent figures and totals are due to rounding.

The term "country," as used in this paper, does not in all cases refer to a territorial entity that is a state as understood by international law and practice; the term also covers some territorial entities that are not states, but for which statistical data are maintained and provided internationally on a separate and independent basis.

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Inaugural Speeches

Ahmed Humaid Al-Tayer
Minister of State for Finance and Industry
United Arab Emirates

It is a pleasure for me to welcome you to Abu Dhabi at the beginning of the Seminar on Foreign and Intratrade Policies of Arab Countries. On this occasion, I would like to convey the greetings of His Highness Sheikh Zayed Bin Sultan Al-Nhayan, Head of State, and His Highness Sheikh Maktoum Ben Rashed Al-Maktoum, Deputy Head of State and Prime Minister of the United Arab Emirates.

It is also a pleasure at the onset of this speech to say that I am proud of the ongoing progress of our joint endeavor embodied in this meeting. Foreign and intratrade policies of Arab countries are currently one of the most important issues.

This seminar is held today under unfavorable conditions in the world economy. Despite international efforts to support world economic growth, the emphasis on international economic blocs has overshadowed the interest in addressing deteriorating terms of trade in developing countries.

While these blocs could be viewed as a step toward freer world trade, it remains to be seen whether they would contribute to a more open international trade system that would foster a better allocation of resources and increased competition and transfer of technology, or would rather prove to be disruptive and conducive to greater reliance on regional trade arrangements. In this decade of the nineties, the world trading system faces two of the most significant

challenges of the last forty years: first, the need to maintain multilateral commitments in managing regional trade arrangements; and second, the need to reach a successful conclusion of the Uruguay Round.

In this respect, Arab countries, in coordination with the rest of the developing countries, could play a major role in serving their own legitimate interests, because collective pressure from developing countries is necessary to achieve a better international trading system.

Of course, the profound changes in international economic conditions have had a visible impact on developing countries' economies, particularly through world trade. A review of the major indicators from the *World Economic Outlook* shows a recent deterioration in international trade growth from approximately 9 percent in 1988 to 6 percent in 1991. Concurrently there was a substantial increase in the deficit on current account of developing countries.

These indicators underscore the urgent need to liberalize trade. In particular, free trade could contribute to the acceleration of global economic growth and lay the foundation for conditions favorable to the expansion of exports of manufactured goods from developing countries, thus enabling these countries to make considerable gains in the field of industrialization.

In that connection, it has become necessary for Arab countries and their institutions concerned with developments in international trade and the world economy to urge trade blocs to eliminate trade barriers that limit access to their markets and to endeavor to reach a successful conclusion to the ongoing trade negotiations within the framework of the Uruguay Round.

Over the past few years, the Gulf Cooperation Council (GCC) countries, with liberal trade and exchange regimes, have suffered from sharp fluctuations in oil prices, highly unstable exchange rates among major currencies, as well as the negative impact of the two wars in the region.

Consequently, the GCC states have adopted several measures to support development and economic activity with a view to stimulating rates of growth and to consolidating integration efforts within the GCC area.

As we follow the efforts that Arab countries have made directly or through their specialized regional agencies for the development of

intra-Arab trade, reference should be made to the Arab Trade Financing Program—an encouraging achievement in the direction of stronger economic ties among Arab economies.

In conclusion, I would like to wish you a pleasant stay in the United Arab Emirates, and that your seminar may make a valuable contribution to the growth and development of the Arab countries.

Osama J. Faquih
Director General and Chairman of the Board
Arab Monetary Fund

On my own behalf and that of His Excellency Abdlatif Al-Hamad, Director General and Chairman of the Board of Directors of the Arab Fund for Economic and Social Development, I have the pleasure of welcoming you to this hospitable country for the Seminar on Foreign and Intratrade Policies of Arab Countries, organized by the two Funds, in cooperation with the International Monetary Fund and the World Bank.

I am proud that we have now returned after a short interruption to the tradition upheld by the two Funds of holding an annual seminar on an important financial and economic topic of interest to economic policymakers, executives, and economic entities whose activities are affected by these policies in Arab countries. During these seminars, a distinguished group of officials and experts, from inside and outside Arab countries, meets to exchange ideas and views on trade issues and problems. It is hoped that these seminars will serve as a forum to convey the participants' knowledge and expertise to Arab countries thereby assisting in the selection and adoption of the appropriate approaches and policies. This seminar is preceded by three others: Adjustment and Development in Arab Countries, Privatization and Structural Adjustment in Arab Countries, and Investment Policies in Arab Countries. This seminar addresses foreign and intratrade policies—a preeminent topic on the recent list of priori-

ties for joint Arab action. IMF and World Bank cooperation has played an important role in the success of these seminars. I would like to take this opportunity to express our deep gratitude and appreciation to these two institutions, hoping that their cooperation will continue and that it will serve our common goals.

There is no doubt that our seminar is being held at a time when trade issues are paramount on the agendas of various international forums. This is not surprising. World trade growth, one of the main contributing factors underlying the postwar international economic boom, presently faces real dangers. If misconceived national policy considerations and protectionist measures dominate international trade relations, all countries and regions will suffer greatly.

Although it has become customary for protectionist calls in industrialized countries to intensify in times of world recession and domestic economic crisis, the more worrisome developments for the future of world trade growth and expansion are, first, the failure after more than five years of negotiations to bring the Uruguay Round to a successful conclusion and, second, the increased polarization of trade in industrialized countries, as evidenced by the emergence of three giant trade blocs: the European bloc, the North American bloc, and the bloc encompassing Japan and the newly industrialized countries in Eastern Asia.

The deadline originally set for the Uruguay Round negotiations has passed. It has been extended to enable participants to reach compromises on disputed issues, because a collapse of these negotiations, accompanied by reciprocal barriers to market access among the countries, would greatly jeopardize the entire international trading system. Yet major industrialized nations have hitherto seemed unwilling to make the necessary concessions to rescue these negotiations from failure. They seem more interested in avoiding confrontations with their powerful pressure groups that stand to benefit from protection, particularly in the case of agricultural subsidies, than they are in sound economic considerations that ensure the efficient allocation of resources and higher growth rates in the longer term.

While multilateral trade negotiations are stumbling, industrialized countries are heading toward regionalization under the banner of three massive trade blocs in Europe, North America, and Asia.

The European Community (EC) is about to establish a unified market; moreover, consultations continue to be held between the

European Community and European Free Trade Association countries with a view to eliminating trade restrictions between the two groups. These developments, of course, are leading to the creation of a giant European trade bloc. The United States, Canada, and Mexico are heading toward a North American free trade area. A third trade pole has emerged; it includes Japan and the newly industrialized countries in Asia, which have enjoyed the highest growth rates. Although it is difficult at this stage to assess the repercussions of these developments on world trade, the EC's experience has shown that its establishment has brought about a rapid expansion of trade among its member countries and a slower growth in trade with the rest of the world.

While these developments have been taking place in industrialized countries and causing concern over the future of international trade, many developing countries, in contrast, have begun to abandon the protectionist and inward-looking policies they had adopted for many years, realizing that such policies led only to an impasse characterized by poor growth rates, worsening external debt positions, and deteriorating standards of living. Indeed, it is unfortunate that the developing countries that began to liberalize their trade and open their markets, enduring the short-term social and political burden of these measures, are presently facing an unfavorable international trade environment in which access to the market is becoming more difficult, thus placing the economic reforms of these countries in jeopardy.

Bearing in mind these considerations, the only alternative is a commitment to remove the barriers to the expansion of world trade. In this connection, major industrialized countries have a special responsibility in the light of their substantial weight in the world economy and their greater capacity to bear the burden of the necessary structural reforms.

I would like now to discuss the Arab countries' efforts toward, and concern about, the promotion of trade among themselves—an issue that is central to the work of this seminar. Development of intra-Arab trade has been considered—since the early days of joint Arab action during the 1950s—as a key approach to promoting Arab economic integration and development and broadening horizons toward a more efficient utilization of resources.

The steps that have been taken, however, to transform this concept into reality, that is, to realize a significant increase in intratrade, have been limited to the legal and organizational frameworks embodied in bilateral and multilateral trade agreements among Arab countries. One objective of these agreements is to promote the flows of goods and services among Arab countries through eliminating and/or reducing restrictions. Compliance with the provisions of these agreements, however, has fallen short of expectations, and thus their effectiveness in promoting intratrade has been limited.

However, interest in intratrade has continued; indeed, it has gained significant momentum during the past decade, when the development of intratrade was placed on top of the agenda of joint Arab action. Accordingly, other means were sought relating to the objective of trade liberalization and enhanced trade relations.

Based on its character and Articles of Agreement, the Arab Monetary Fund was assigned the task of finding efficient ways and means to contribute to the financing of Arab trade. In recent years, the AMF has attached great importance to this issue within the framework of its efforts to correct balance of payments imbalances in several member countries.

Its efforts, in coordination with Arab financial institutions concerned with the development of Arab trade (particularly the Arab Fund for Economic and Social Development), have borne fruit in the establishment of the Arab Trade Financing Program. It was envisaged that this structure should allow for a wide base of contributions to ensure that the program receives the appropriate flow of public and private funds needed to finance Arab trade. It was also envisaged that it should provide a comprehensive institutional framework under which all efforts to develop intra-Arab trade could be effectively coordinated.

The AMF's commitment to the success of the program was highlighted by its decision to contribute half the program's capital of $500 million. It is heartening to note that 90 percent of the program's capital was subscribed and paid in by the participating Arab financial institutions and commercial banks. This enabled the program in early 1991 to begin financing Arab trade and to plan the establishment of a modern information network that would provide accessible and reliable statistical data related to Arab trade.

In addition to financing, the program sought an appropriate arrangement with the Inter-Arab Investment Guarantee Corporation to cover Arab trade finance flows. In this connection, it should be mentioned, however, that our efforts should not be limited to the aspects of financing and guarantees, for there are additional and important difficulties owing to the lack of other services necessary to promote growth in intra-Arab trade. Experts and others concerned with trade issues have emphasized on numerous occasions and in several meetings that it is essential for Arab countries to develop these services, in the areas of transportation, communications, marketing, and commercial information.

Efforts to make the Arab producers and exporters more competitive would certainly not be completely effective if limited to intra-Arab trade financing and the removal of trade restrictions among Arab countries. Additional efforts must be made to develop and modernize the other services mentioned above.

The efforts made by Arab countries to promote intra-Arab trade do not reflect a desire to raise barriers against, or reduce trade with, the rest of the world; indeed, most Arab countries apply import duties that are considered to be among the lowest in the world. In addition, many other Arab countries began to reduce tariff rates, liberalize external trade, and open their markets, under their adjustment programs. Thus, liberalization and development of trade flows among Arab countries aim at maximizing the actual and potential capacities of Arab markets, as well as enhancing and diversifying Arab production bases. Not only would Arab countries benefit from the realization of these goals, but their trading partners would benefit as well.

As long as we continue to attach great importance to foreign and intra-Arab trade issues, we will always need to re-evaluate our previous positions objectively in light of our experience, to ensure soundness of approach and orientation. We will also always need to explore new methods to develop trade, cope with the problems, and respond to questions generated by our interaction with international and Arab trade realities.

With that in mind, you may wish to consider the following questions during this seminar:

(1) In light of the emergence of giant regional trade blocs and the rise of protectionism in industrialized countries, what stance should

Arab countries adopt regarding international trade issues? To what extent can Arab countries make their voices heard in the General Agreement on Tariffs and Trade and other pertinent forums, with a view to expressing their opinions effectively and defending their legitimate interests?

(2) With regard to intra-Arab trade, what steps could be taken to encourage Arab countries to comply more closely with the agreements aimed at eliminating intra-Arab trade restrictions? Doesn't the progress achieved so far in this area seem rather modest and disproportionate relative to the interest shown by private and official Arab circles in developing intra-Arab trade? How far can regional Arab groups, which are presently seeking trade liberalization among their respective members, lead to free intra-Arab trade?

(3) After covering the Arab trade financing needs through the Arab Trade Financing Program, what could be done to remedy the deficiencies in the other services required in Arab countries for the growth of intra-Arab trade, including transportation, communications, marketing, and trade information? To what extent can the coordination of Arab efforts in this area contribute to the enhancement of these services?

In conclusion, I hope to have shed some light on the issues with which this seminar is concerned; and, in this connection, I am looking forward to listening to your ideas and views. Once again, I would like to welcome you and to express my thanks and appreciation to the institutions that cooperated in the organization of this seminar. I would like also to thank the officials of the United Arab Emirates for their hospitality.

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Foreign and Intratrade Policies of the Arab Countries: The Basic Issues[1]

Said El-Naggar

Trade and Change in the World Economy

This is the fourth in a series of seminars dealing with economic policies of particular importance to the Arab countries. The first seminar, held in 1987, dealt with adjustment policies and development strategies; the second was concerned with privatization; and the third was on investment policies. The present seminar comes at a time when trade policy reform constitutes one of the major themes in adjustment programs. This is not difficult to explain. Foreign trade policies have a direct bearing on the allocation of resources and hence on economic growth and development. No less important is the fact that they are one of the major factors underlying international competitiveness and external equilibrium. The subject of this seminar has acquired an added significance in the light of recent developments in the world economy. These developments might be summed up as globalization, regionalization, and a rising tide of protectionism. Globalization has come about as a result of four decades of remarkable growth in world trade. Between 1950 and 1980, world exports of goods and services increased at an annual rate of 7 percent compared with a 4 percent average annual growth of

[1]The views expressed in this paper are the author's and do not necessarily represent those of the seminar.

GDP. The growth of world trade was matched by no less far-reaching developments in international finance. One of the most distinctive features of the last two decades has been the enormous growth of international capital movements. A study by the Organization for Economic Cooperation and Development (OECD) estimates international financial transactions—transactions involving a movement across national borders—at some $200 billion daily, or forty times the volume of world trade. As a result of these developments, the world economy has become characterized by a high degree of interdependence. Countries are intertwined in an extensive network of commercial and financial ties. The growing interdependence of the world economy gives rise to both positive and negative effects. On the positive side, there are now vast possibilities for a fruitful international division of labor. At the same time, all trading countries where the foreign trade sector accounts for a high proportion of total economic activity have become increasingly vulnerable to external economic shocks. This aspect was driven home to the Arab countries following the economic turbulence of the 1980s.

Alongside the trend toward globalization, the world economy seems to be going in the direction of regionalization. The completion of Europe 1992 will result in the creation of a giant trading bloc with far-reaching implications for the world economy. The same can be said about the North American free trade area comprising the United States, Canada, and Mexico. There are also indications that Southeast Asia and the Pacific Basin will see the birth of yet another giant trading bloc.

The third characteristic of the world economy is the upsurge of protectionism in the industrial countries. Underlying this development is the marked slowdown in the growth of the major industrial countries, notably the United States, coupled with relatively high unemployment and substantial external imbalances. The problem was compounded by the remarkable rise in the economic power of Japan relative to that of the major industrial countries. No less important in explaining neo-protectionism is the changing pattern of comparative advantage. The newly industrialized countries were able to acquire distinct comparative advantage, not only in the traditional labor-intensive types of products, but in a wide range of capital- and technology-intensive industries that hitherto have been the exclusive reserve of the old-established industrial countries.

Protectionism was resorted to in order to stem the tide of highly competitive imports from Japan and the newly industrialized countries.

The changing face of the world economy has important implications for the trade policies of developing countries, including the Arab countries. It was against this background that the seminar on foreign trade was convened by the Arab Monetary Fund and the Arab Fund for Economic and Social Development in cooperation with the International Monetary Fund and the World Bank. A number of issues were examined in six papers presented to the seminar. Special attention was paid to trade policies of import substitution versus export orientation, the impact of protectionism in the industrial countries on the trade of the Arab countries, the significance and implications of the Uruguay Round of Trade Negotiations, and prospects and problems of intra-Arab trade. In addition, two case studies were presented to the seminar; one on the foreign trade policy of Egypt, the other on regional economic integration among the Maghreb countries.

Import Substitution: Meaning and Implications

While developing countries have benefited in a variety of ways from the growing interdependence of the world economy, they have also suffered from the major economic disturbances of the last two decades. The decade of the 1980s, in particular, was aptly described as the lost decade. Developing countries experienced a significant setback in growth rates. In some cases, per capita incomes have actually declined. They have been adversely affected by instability of exchange rates, high nominal and real interest rates, and, above all, unprecedented deterioration in their terms of trade. At the same time, the crushing burden of external indebtedness is posing a serious threat to their growth and development prospects.

According to some economists, most of the problems faced by developing countries are inherent in the nature of their relationship with the industrial countries as long as their exports to developed countries consist essentially of primary commodities while their imports are made up of manufactured products. We know the extent to which this pattern of trade has raised serious doubts in the minds of many economists regarding its impact on growth and develop-

ment. The views of such economists as Prebisch, Myrdal, Singer, and Nurkse are too well known to warrant elaboration. Suffice it to mention that according to them this pattern of international division of labor fails to meet the development needs of developing countries. During the nineteenth century, they point out, foreign trade was truly an engine of growth. This is no longer the case in today's world. Long-term changes in the production structure of developed countries have adversely affected their demand for raw materials and primary products. Reference was made to the growing proportion of services, the decline in raw-material-intensive industries, and advances in technology in the form of synthetics competing with natural products. Moreover, it was pointed out that this pattern of international exchange between developing and developed countries has been responsible for the long-term deterioration in the former's terms of trade.

The logical consequences of those views, typical of the development doctrines of the 1960s, was a call to change the structure of trade between developed and developing countries. Through a policy of import substitution, it was argued, developing countries could embark on large-scale industrialization and do away with a colonial type of international exchange.

However, recent empirical research by Bela Balassa and others has served to show the limitations and shortcomings of development strategies based on import substitution. More often than not, import substitution policies have been associated with extremely high protective tariff and nontariff barriers, which all but eliminated foreign competition. A case in point is provided by Ahmed El-Dersh and Hanaa Kheir El-Din in their paper, "Foreign Trade Policy of Egypt." Prior to the 1986 tariff reform, import duties on finished manufactured products were extremely high. At the same time, nontariff barriers, including an outright ban on certain imports, were widely used as a means of protecting local industries. Because of pronounced tariff escalation, the rate of effective protection afforded to finished products was substantially higher than may be gauged from nominal tariffs. The situation in other developing countries was not materially different from that in Egypt. In all cases, import substitution policies have been largely responsible for serious misallocation of resources, distortion of domestic prices, overvaluation of currency, and erosion of international competitiveness.

In contrast to the poor performance of countries that have adopted a strategy of import substitution, available evidence suggests that countries that have pursued export-oriented strategies were able to attain an advanced stage of industrialization, maintain a high level of competitiveness in export markets, and achieve robust rates of growth. This conclusion is amply documented in the paper by Thalwitz and Havrylyshyn. They refer to the agreement among a large number of economists that the higher growth of exports is, in general, associated with higher economic growth, and that countries that have relied on outward-oriented polices have done better over the medium and long run than those countries that have adopted inward-looking strategies.

As a result of these findings, greater emphasis is now being placed on export-oriented strategies. It is important, however, to understand the meaning and implications of a shift from import substitution to export orientation. Import substitution policies have often been associated with a strong bias against export industries. This is due to the fact that import substitution industries have been made artificially more profitable than export industries through the imposition of high tariff and nontariff barriers on competing imports. At the same time, export industries were in many cases compelled to use locally produced inputs at prices significantly higher than world prices. This is tantamount to a tax on export sectors that, not infrequently, offset or more than offset whatever subsidies were accorded to these sectors. Stated differently, it is submitted that high protection in the import-competing sectors spells high negative effective protection in the export sectors. This point is clearly illustrated in El-Dersh and Kheir El-Din's paper. It highlights the serious handicaps under which the export industries have been operating, and goes a long way toward explaining the poor export performance of countries that opted for import substitution strategies. It follows that a shift from import substitution to export orientation means simply doing away with the anti-export bias. Under a neutral policy stance, economic resources would flow to various sectors according to their market profitability and not according to an artificially created one. Such a policy does not rule out import substitution. It distinguishes between efficient and inefficient import substitution. The former may thrive and constitute the basis

for a potential export industry. The latter is inimical to growth and development and should therefore not be encouraged.

This argument may be construed to imply a shift from a policy of high protection to one of free trade. This is not necessarily so. A certain measure of protection is unavoidable and even desirable. As pointed out by Thalwitz and Havrylyshyn, what is at issue is not the principle of protection but its degree and method. A policy of export orientation is perfectly consistent with a moderate degree of protection. Moreover, it is important to keep the domestic market fully integrated in the mainstream of the world economy and subject to the discipline of foreign competition. This can only be achieved by dismantling most quantitative restrictions and nontariff barriers and relying more on price instruments of protection such as tariffs and subsidies. Unlike quantitative restrictions, tariffs do not destroy linkages with the world economy, are quantifiable, and have the advantage of transparency.

Export Orientation: Scope and Limits

It is sometimes argued that an export-oriented strategy is feasible if it is pursued by a limited number of developing countries, but is bound to encounter great difficulties if it is followed simultaneously by a large number of these countries. There is already some resentment, it is pointed out, against imports from the four countries of the Asian rim (Hong Kong, Singapore, the Republic of Korea, and Taiwan Province of China), which have been an important factor in the rising tide of protectionism. The problem would be much more difficult if the industrial countries were to contend with cheap imports from a vastly expanded number of exporters. In other words, the call for an export-oriented strategy is based on a fallacy of composition; namely, the assumption that what is true for a small number of countries is also true if it is applied on a much larger scale.

On the face of it, the argument sounds plausible. On scrutiny, however, it is highly questionable. In the first place, this is a static argument in the sense that it assumes other things to remain equal. But a considerable increase in the exports of manufactured products

from developing countries will not leave other things unchanged. This is evident with respect to the import capacity of these countries, which will expand pari passu with the increase in exports. Looked at from the vantage point of the industrial countries, rising imports from developing countries will be matched by a parallel increase in exports to them. Thus, the capacity of the industrial countries to absorb a larger volume of imports will be significantly greater at a higher level of exports. Moreover, it should be realized that, at the present levels of trade, imports of manufactures from developing countries are still a tiny proportion of apparent consumption in the industrial countries. In 1987–88, the proportion was 3.5 percent in the United States and Canada; 3 percent in the European Community; and about 1.6 percent in Japan. These figures suggest that there is still ample room in the markets of the industrial countries before the critical threshold is crossed. Furthermore, there is no reason to assume that competition with developing countries would result in the disappearance of certain branches of manufactures. What is more likely to happen is a more sophisticated division of labor under which the same product, or parts thereof, would be produced in different countries. The experience of the European Community provides a case in point. Following the dismantling of intratrade barriers, competition among member countries has not led to the concentration of the automobile industry in one country to the exclusion of others. The automobile industry is still thriving in all producing countries, although there has been a change in the pattern of specialization so that different types, parts, and qualities are produced in different countries. This kind of intra-industry and intra-firm specialization is likely to be characteristic of the future international division of labor.

The upshot of this analysis is that there is no fallacy of composition in the case of the export-oriented strategy of development. It is valid for the four countries of the Asian rim as it is for all developing countries. Compared with import substitution strategy, it provides an appropriate framework for the optimum allocation of resources, and is more consistent with a dynamic interpretation of comparative advantage. The real problem facing the successful implementation of a thorough going export-oriented strategy on the part of developing countries is protectionism in the industrial countries.

Protectionism in the Industrial Countries

The establishment of the General Agreement on Tariffs and Trade (GATT) in the late 1940s marked the beginning of a systematic process aimed at the liberalization of world trade within a multilateral framework. Between 1947 and 1960, seven rounds of trade negotiations were completed under the aegis of GATT. The Kennedy Round, which took place in the first half of the 1960s, and the Tokyo Round, which covered the second half of the 1970s, were the most important rounds in terms of reducing the barriers to trade. As a result of this process, international trade became significantly less subject to restrictions than it was before the establishment of GATT. This is particularly true with respect to tariffs. It was estimated that the average rate of tariffs in the industrial countries was reduced from about 40 percent in 1947 to less than 10 percent following the Tokyo Round. There can be little doubt that the phenomenal growth of world trade during this period is partly ascribable to the liberalization process.

Notwithstanding progress made within the framework of the GATT, some important restrictions continued to impede the flow of world trade. This is clearly shown in the paper by Margaret R. Kelly and Bernhard Fritz-Krockow. Developing countries still encounter a wide range of protectionist measures that in some instances severely limit their access to the markets of the industrial countries. The restrictive impact of these measures is particularly felt in those sectors in which developing countries enjoy a clear comparative advantage. Such is the case as regards textiles and clothes, agricultural products, and a large number of labor-intensive manufactures. Protectionist measures in the industrial countries fall under two broad categories. The first consists of conventional measures of protection in the form of tariff and nontariff barriers. It is true that tariffs are no longer a major instrument of protection in the industrial countries. Following successive rounds of trade negotiations, most tariffs have been reduced to levels that render them insignificant as obstacles to access. Nevertheless, there are certain tariff peaks that are well out of line with the average level within any product category. Moreover, tariff escalation, typical of the tariff structure in the industrial countries, has a negative impact on the development of processing industries in the developing countries. In

most cases, raw materials are admitted duty free to markets of the industrial countries. However, when raw materials are processed, they are treated differently. Tariff rates rise with the degree of processing so that they are lowest at the early stages of processing and highest on the finished product. This type of tariff structure discourages industrialization based on locally produced raw materials. Faced with tariff escalation, developing countries are often better off exporting unprocessed raw materials rather than finished products. Furthermore, certain types of tariffs have an extremely restrictive effect. The variable levies imposed by the European Community to protect certain types of agricultural products are an example. Variable levies have the attribute of rising when the world market price falls and falling when it rises. They are used as an instrument to defend domestic prices fixed at artificially high levels. It is not difficult to see that they are far more restrictive than a regular fixed tariff as they serve to shut out the effect of a fall in world market prices.

In addition to tariff peaks, tariff escalation, and variable levies, industrial countries resort to a wide variety of nontariff barriers (NTBs), including quantitative restrictions (QRs). This is illustrated by the regime regulating international trade in textiles and clothes within the framework of the Multifibre Arrangement (MFA). It is hardly necessary to point out that textiles and clothes constitute the backbone of industrialization in developing countries. However, as early as 1962, they were excluded from the GATT rules. Contrary to these rules, international trade in textiles and clothes was made subject to an international agreement comprising practically all exporters and importers and assigning an annual quota for each participant. The agreement was supposed to be a temporary arrangement pending the incorporation of textiles and clothes into the GATT system on the same footing as other manufactured products. But the agreement has been renewed, with extended coverage, once every five years up to the present time.

The decade of the 1980s saw the emergence of a new breed of trade-restricting measures that came to take the label of neo-protectionism. Typical of such measures is the so-called voluntary export restraint (VER). Under this arrangement an exporting country "voluntarily" accepts to limit the volume or value of the exports of a certain product to a predesignated level. VERs were widely

resorted to by the United States to stem the tide of Japanese exports of automobiles, television sets, and other electronic products. They were similarly used by the European Community for the same purpose. The same treatment was administered against certain exports from the Republic of Korea, Taiwan Province of China, Hong Kong, and Singapore. Evidently, VERs belong to the category of quantitative restrictions, but they differ in that they are not part of a formal agreement of the traditional type. They have precisely the same effect as QRs but they are supposed to be entered into voluntarily by the exporting country. Because of this dual character, they were aptly described as "gray area" measures. As a quantitative restriction of international trade, they contravene the provisions of GATT. Since, however, they are presented as a voluntary arrangement, the importing country can claim to be acting within the confines of its GATT obligations. Another gray area measure is that of voluntary import expansion (VIE). This arrangement is the opposite of a VER. While a VER is designed to limit the exports of a certain product, a VIE is a device to expand the imports of another product that would otherwise not have been imported to the predesignated level. VIEs were again used by the United States as a device to expand Japanese imports of rice, beef, and telecommunication equipment. As with VERs, they do not constitute a formal contravention of the GATT rules. In essence, however, they are trade-diverting measures that violate the spirit, if not the letter, of the GATT.

A third gray area measure is the so-called orderly marketing arrangement (OMA). According to the GATT, any contracting party has the right to limit the imports of a certain product if they increase to a point deemed to be causing or threatening to cause a serious injury to home producers. This provision is known as the safeguard clause, which serves the purpose of protecting members of GATT against market disruption arising from a sudden and substantial increase in imports. During the decade of the 1980s, there was widespread use of the safeguard clause, which was not warranted by the serious injury caveat. In fact, it was often invoked to stifle legitimate competition of more efficient foreign suppliers. These are the main forms of neo-protectionism: VERs, VIEs, and OMAs, which were widely used to limit access to the markets of the major industrial countries. True, the main brunt of these measures fell on

Japan and some of the newly industrialized countries. This cannot be said, however, of the traditional forms of protection that adversely affected all developing countries. Equally important is the fact that neo-protectionism has been responsible for engendering a sense of uncertainty as regards prospects of access to the markets of the industrial countries.

The upsurge of protectionism in the industrial countries happened at a time when developing countries were urged to open up their markets and shift from the inward-looking strategies of the 1960s to a more outward-looking posture. The irony of this asymmetry was not lost on developing countries, which are obviously far less able than the industrial countries to shoulder the burden of adjustment to a more liberalized trade regime.

Significance of the Uruguay Round

The rising tide of protectionism threatened to wipe out the gains made during seven rounds of trade negotiations within the framework of GATT. Not only has it distorted the flows of international trade, but more significantly, it has reflected less than a firm commitment to the basic tenets underlying the GATT system. Multilateralism, the hallmark of the system, was gradually giving way to bilateralism and regional arrangements. The United States, which was for the better part of the postwar period the standard-bearer for a free and open international trading system, became more susceptible to protectionist pressures at home. The change in U.S. posture was reflected in the Trade and Tariff Act of 1984, which empowered the President to take retaliatory measures against countries deemed guilty of "unfair competition." The Trade Representative, who is responsible for trade negotiations on behalf of the Administration, was required to initiate investigation upon complaint from interested parties into allegations of unfair competition and make recommendations to the President. The powers of the Trade Representative were further strengthened in the Trade and Competitiveness Act of 1988. Henceforth, there was no need to wait for a complaint from interested parties. An investigation could be conducted on the initiative of the Trade Representative. Given the vital importance of the U.S. market for many trading countries, particularly Japan, China, and the four countries of the Asian rim, it was not necessary to use

these powers. The fact that the President is so empowered was enough to bring reluctant trade partners to the negotiating table. Protectionist tendencies were of course not limited to the United States. The same trend was observable in the European Community, Japan, and most of the other industrial countries.

As a result of these developments, there was a rapid erosion in the international trading system. The rules of the game that guided international action throughout the postwar period were scarcely respected, much less enforced. It was clear, however, that such a course of action was hardly sustainable. Protectionism was a costly proposition, not only for the countries against which it was administered, but also for those practicing it. Several studies have been made to estimate the cost of protectionism to countries of the OECD. Although there is a large variation in the results because of differing structures, parameter estimates, and base years, it is generally agreed that the cost is relatively high. According to a report presented to the Development Committee at its spring session in 1991, the cost of agricultural support policies alone amounts to about 2 percent of GDP, and the distortions from financing the transfers associated with these policies were quite significant. The report goes on to state that one study, for example, has estimated that the industrial countries suffer a direct welfare loss of $50 billion a year (at 1985 prices). Another study, which extends this kind of analysis to the impact of these policies on the whole economy, concludes that they cost industrial countries some $70 billion a year (at 1988 prices). The economic costs suggested by studies such as these are quite high in comparison with the relatively small contribution of agriculture to GDP in industrial countries. If account is taken of the cost related to protectionism in other sectors of the economy, the results would be far more striking.

Apart from the high cost of protectionism it also became apparent that recurrent trade disputes could easily degenerate into a full-scale trade war not only between the United States and Japan, but also between the two of them and the European Community. The damaging impact of such a development on the world economy could hardly be exaggerated.

Against this background the Uruguay Round of Multilateral Trade Negotiations was launched at the ministerial meeting held at Punta del Este on September 15–20, 1986. The Uruguay Round was to be

far more comprehensive in its coverage than previous rounds of trade negotiations. In addition to the traditional topics such as the reduction or elimination of tariff and nontariff barriers, the new round proposed dealing with issues that had never been the subject of multilateral negotiations. These include agriculture, services, trade-related intellectual property rights (TRIPs), and trade-related investment measures (TRIMs). Moreover, the new round proposed looking into ways and means of strengthening the GATT system itself. The negotiating plan envisaged a review of provisions relating to the safeguard clause, settlement of disputes, GATT surveillance of trade, and trade-related measures applied by member countries.

Although developing countries expressed reservations with respect to certain aspects of the new issues, there can be little doubt that they stand to reap substantial benefits from the successful conclusion of the Uruguay Round. The same goes, of course, for the Arab countries. In his paper on the subject, A. H. Mamdouh states that the strengthening of the system resulting from a successful conclusion of the round would secure future opportunities under a framework of equitable principles and rules and preserve the balance of rights and obligations between all developed and developing countries. More specifically, the Arab countries would benefit in their capacity as exporters of a wide range of agricultural and manufactured products. These include textiles and clothes from Morocco, Egypt, Jordan, Syria, Tunisia, and the United Arab Emirates; steel products from Algeria, Egypt, Morocco, Qatar, and Saudi Arabia; petrochemicals from a number of the Arab oil exporting countries; and processed agricultural products from Lebanon, Egypt, and the Maghreb countries. Kelly and Fritz-Krockow cite a number of specific examples showing the kind of tariff and nontariff barriers encountered by Arab exporters in the markets of the industrial countries. With respect to agricultural products (particularly citrus fruit, potatoes, dates, olive oil, onions, and wine), practically all diversified Arab exporters face significant trade restrictions in their export markets.

It was pointed out, however, that for the net food importers such as Egypt and the oil exporting countries, the liberalization of agricultural trade may prove to be a costly proposition owing to higher world prices. Evidently, the significance of this consideration varies according to the specific circumstances of each country and

the extent to which the increase in the cost of food imports is offset by a rise in the price of agricultural exports. Moreover, this kind of cost may not be that important if account is taken of the beneficial effects of higher growth rates arising from a better allocation of resources in the industrial countries.

On balance, the Arab countries, like other developing countries, have a significant stake in the success of the Uruguay Round. It should be noted, however, that only 4 Arab countries—Egypt, Kuwait, Morocco, and Tunisia—are members of GATT. That leaves 17 Arab countries—including all the oil exporting countries with the exception of Kuwait—outside GATT and the ongoing negotiations. The explanation for this state of affairs is not hard to find. At one stage developing countries as a whole were skeptical about the advantages of GATT membership. The principles of free trade, nondiscrimination, and reciprocity, to which GATT was dedicated, were seen to be inconsistent with their development requirements. While this view was arguable in the 1950s and 1960s, it is no longer so, given the fact that most Arab countries are already committed to a policy of liberalization within the framework of an adjustment program supported by the IMF and the World Bank. As to the oil exporting countries, the case for GATT membership is even stronger. Their trade regimes, as well as development strategies, have been largely outward oriented. No less important is that they have recently become significant exporters of petrochemical products, which are subject to various trade restrictions in the markets of the industrial countries. The chances of improving market access for these products as well as other products in which they are interested will be vastly improved once they become active participants in the process of multilateral negotiations.

Economic Integration and Intratrade

Economic integration among the Arab countries has been one of the principal goals of economic and political cooperation ever since the establishment of the Arab League toward the end of War World II. Reference might be made to the Economic Unity Council that included some Arab countries as far back as the late 1950s. This was followed by the establishment of the Arab Common Market, whose purpose was to eliminate intra-Arab trade barriers and eventually to

realize complete economic union with the free movement of goods, capital, and labor among member countries. While these schemes were able to make some modest contributions in terms of economic cooperation, they were far from successful in their basic objectives of economic integration. Their impact was very limited indeed, if not nonexistent. This result is hardly surprising given the vast expanse of the Arab world, the inadequacy of regional infrastructure and institutions, the different economic and social systems prevailing, the inward-looking strategy characteristic of most of them, and, last but not least, the virtual absence of complementarity between production structures. The experience of the Arab countries in this respect is not different from that of Latin America and Africa, where several integration schemes were implemented with no significant results.

The failure of economic integration at the Pan-Arab level prompted a search for alternative strategies. One approach was to seek integration through the establishment of joint projects. The decade of the 1970s witnessed a plethora of such projects in various sectors ranging from agriculture and cattle farming to shipping and mining. Some of these projects were more successful than others, but it soon became clear that whatever their benefits such projects cannot by themselves constitute a valid approach to economic integration. The limited nature of this approach gave rise to the present strategy of economic integration at the subregional level. The decade of the 1980s saw the rise of three subregional integration schemes led by the Gulf Cooperation Council (GCC), comprising the six Arab countries of the region, followed later in the decade, by the Arab Cooperation Council between Egypt, Iraq, Jordan, and Yemen; and the Maghreb Economic Union between Algeria, Libya, Mauritania, Morocco, and Tunisia. Of the three subregional schemes, the Gulf Cooperation Council and the Maghreb Union are proceeding as planned in the founding agreements. The Arab Cooperation Council on the other hand is in a state of suspension as a result of the Gulf crisis that divided its members into two warring camps.

It remains to be seen how successful is the subregional approach to economic integration compared with the Pan-Arab approach. Certain features of the Maghreb Union are enunciated in the paper by Minister Hassan Abouyoub. In contrast to the Gulf Cooperation Council, which includes a group of more or less homogeneous

countries, the Maghreb Union covers six countries that differ among themselves with respect to level of per capita income, stage of development, degree of diversification of production base, economic systems, and the inward- or outward-looking character of their strategies. These are formidable hurdles in the way of economic integration. Aware of these differences, the Maghreb countries have adopted a strategy of integration by stages, starting with selective liberalization of trade barriers, leading to a free trade area, followed by a customs union. Economic union, involving the free movement of goods as well as labor and capital, is envisaged as the final stage that is not likely to materialize before the end of the 1990s.

It is recognized that intratrade plays an important role in the process of economic integration. In the paper on intra-Arab trade, Jamal Zarrouk and others of the Arab Monetary Fund give a detailed statistical and economic analysis of the various aspects of this flow, including its value and volume, relative importance, commodity composition, tariff and nontariff barriers, and a host of other questions. The paper underscores the fact that intra-Arab trade accounts for a small proportion—some 7–8 percent—of total trade. If oil is excluded from both the intra and extra flows, the proportion is still in the 10 percent range. It is important, however, to keep these figures in proper perspective. The relative importance of intratrade of the Arab countries taken as a whole conceals the wide variations at the individual country level. For countries such as Lebanon and Jordan, trade with the rest of the Arab countries is significantly more important than these figures suggest. The export structure of both countries includes a large proportion of fresh fruits and vegetables whose primary outlet is in the markets of the GCC countries and Iraq. Similarly, the overall average fails to reflect the variations between different commodity groups. Apart from fresh fruits and vegetables, intra-Arab trade is fairly important in many categories of processed and semiprocessed products as well as a wide range of manufactures.

The situation is different with respect to oil and raw materials, including phosphates, iron ore, and cotton. In such cases, the markets of the industrial countries account for an overwhelming proportion of Arab exports. Given the great importance of oil and raw materials in the overall export structure, the share of intratrade is understandably modest. It was also pointed out that official statistics do

not take account of a good deal of trade that goes on unofficially across borders. Reference might be made to the across-the-border trade between Syria and Lebanon; Jordan and Iraq; Egypt and Sudan; Saudi Arabia and Yemen; to mention but a few examples.

With respect to the official trade between Egypt and the rest of the Arab world, the period between 1980 and 1989 might have been distorted by the Arab boycott in the wake of the Camp David accords. Most important in explaining the low level of intra-Arab trade is the fact that it continues to be subject to more or less severe restrictions in the form of tariff and nontariff barriers.

The study by Zarrouk refers to a number of agreements that have been concluded between Arab Governments with the avowed purpose of promoting intratrade. These include the 1953 agreement on transit trade, the 1964 agreement on the establishment of a free trade area, and the 1981 agreement on the promotion and development of intratrade. Those agreements were supposed to do away with the tariff and nontariff barriers impeding the flow of trade. But liberalization was carried out on the basis of agreed lists of commodities. As to be expected, and as the experience of other developing regions shows, the case-by-case approach to liberalization has failed to make a dent in the high wall of protection. It should be mentioned, however, that the level of protection varies considerably from one country to another. It is highest in Algeria, Sudan, Syria, Jordan, Iraq, Egypt, and Morocco, where the level of effective protection ranges from 75 percent to 250 percent. It is moderate or low in most of the Arab oil countries. The high level of protection in some of the Arab countries was aggravated by certain distortions in macroeconomic policies coupled with strict foreign exchange control.

There are reasons to believe that the prospects for intra-Arab trade may well be significantly better than has been the case so far. In the first place, most of the highly protected Arab countries have embarked on a comprehensive process of trade liberalization in the context of an adjustment program agreed upon with the IMF and the World Bank. In the case of the oil countries where the level of protection is generally moderate, the most important factor is the implementation of a thorough-going program of diversification. This is likely to open up significant opportunities for intratrade that do not exist when the economy is heavily dependent on oil. Last, but

not least, reference should be made to the Arab Trade Financing Program that was put into effect in 1989 under the direction of the Arab Monetary Fund. The Program marks an important shift in the strategy for the promotion of intratrade from the conclusion of ineffective liberalization agreements to the provision of badly needed financing and credit guarantees. It is hoped that the new approach, together with the other factors, will have a positive impact on the growth and development of intra-Arab trade.

3

Trade Liberalization: Policy Options from Inward-Looking to Outward-Oriented

Wilfried P. Thalwitz and Oli Havrylyshyn

I. Introduction

Many countries are currently involved in trade liberalization efforts—at three overlapping levels. First, the members of the General Agreement on Tariffs and Trade (GATT) are concluding the negotiations of the Uruguay Round on multilateral liberalization. Second, customs union, common market, or cooperation agreements are in place or are being expanded at the regional level in many parts of the world. Most of these, such as the three integration schemes among Arab countries—the Gulf Cooperation Council (GCC), the Arab Maghreb Union (AMU), and the Arab Cooperation Council (ACC)—are far less comprehensive than the European Common Market. Third, many liberalization efforts are under way at the country level, some in connection with adjustment programs supported by the IMF and the World Bank (Morocco, Tunisia, the Republic of Korea, and Poland), and others following a policy dialogue with the Bank (Brazil and Peru). In a highly integrated world economy, trade liberalization has become necessary for rapid development, but three important concerns are frequently expressed. First, that liberalizing trade threatens domestic industries and that in developing countries export expansion is constrained by protectionist

policies in other countries. Second, that liberalization reduces government control and places undue reliance on the uncertain effects of markets. Third, that it is sometimes unwise for countries to liberalize on their own because this may reduce the incentives for other countries to reciprocate.

This paper addresses these concerns and demonstrates how appropriate policies can help resolve them. The key objectives of policy are

- balancing and reconciling the goals of export expansion and of domestic industrial development.
- balancing the roles of government and market forces, both in the domestic process of liberalization and in the international negotiation of reciprocal trade agreements.

Section II briefly summarizes the historical evidence on trade policies and trade performance globally, with an illustrative sketch of the policy-performance link in the Arab countries. Section III then addresses the first policy objective, demonstrating why more liberal, outward-oriented trade policies achieve better results than restrictive inward-looking ones, both in expanding exports and in stimulating domestic industrial development. Section IV considers the second policy objective, describing the need for a reduced but active government role in trade policy, to support market forces domestically and internationally.

II. Link Between Policy and Trade Performance: Historical Evidence

General Findings

There are many trade policy options, from autarky to free trade, and the first role of government is to choose the policy that will best foster a country's economic development. Traditional economic theory favors positions as close to free trade as possible, while a competing proposition, support for infant industry, favors import substitution at an early stage of development. The historical evidence tells us a great deal about which policies are better.

Within this debate, there is broad agreement on one point:

> *Sustained* rapid export growth is good for economic growth.[1]

Almost all studies relating exports to economic growth, from Balassa (1978), to Thomas, Martin, and Nash (1990), agree that in general higher growth of exports is associated with higher economic growth. The question for trade policy is what kinds of trade regimes result in good export performance. On this issue, too, there is now wide agreement on the following proposition:

> countries that have relied on "outward-oriented" development strategies have done better over the medium and longer run than those countries that have adopted "inward-looking" strategies. (Edwards, 1989, p. 1.)

There is less agreement on the appropriate balance between government intervention and reliance on market mechanisms. Trade liberalization usually involves a movement from too much and the wrong kind of government intervention to more reliance on markets. In particular, it involves two elements: correcting the effect of intervention distortions that protect domestic industry against competition from imports and consequently result in an anti-export bias; and reducing the degree of government intervention, allowing markets and prices a greater role in affecting the economic decisions of producers.[2] But while correction of the anti-export bias follows naturally from a substantial reduction in intervention through liberalization of import restrictions and devaluation of the exchange rate, the shift to an outward orientation has often begun with the introduction of new intervention measures to compensate exporters for the high production costs they face as a result of import restrictions. Such measures typically include devaluation, duty-free and easy access to imported materials and components, export subsidies or credits, and assistance in marketing.

> Outward orientation can be achieved either by less government intervention or by different government intervention. But in the long run, the

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[1] Short bursts of exports, owing to either fortuitous circumstances of high demand for a country's raw materials or heavy subsidization of exports, are not in themselves enough to sustain the growth impetus.

[2] Krueger (1978), Bhagwati (1978), and Balassa (1971).

evidence shows that very high and continued intervention by governments is damaging to the economy and to trade performance.

Whereas on free trade itself history tells us almost nothing—apart from the experience of Hong Kong, there are no cases to analyze—the phenomenal success of East Asian countries (Japan, the newly industrialized countries, and, more recently, Thailand and perhaps Malaysia) has provoked disagreement on the appropriate role of government in achieving outward orientation.[3] Are export expansion measures that merely compensate for still remaining import restrictions sufficient, or must government restrictions and intervention also be reduced? Although it is true that Japan, Korea, and Taiwan Province of China did not immediately reduce their import restrictions when they began their export drives, they did *not* permanently maintain extensive government intervention but moved gradually to reduce it. All these countries steadily reduced their import regulations—Korea more slowly, and Singapore and Taiwan Province of China more quickly than the others—starting with decreased reliance on quotas and other quantitative controls and greater use of tariffs, and continuing with reductions in these tariffs. Furthermore, the initial levels of protection and distortions caused by government intervention, although high, were much lower in these countries before reform than in most other developing countries.[4]

Clearly, then, these East Asian success stories are not examples of a movement toward outward orientation through new government intervention alone. Rather, they first moved quickly to outward orientation and then slowly but consistently toward lessened government intervention, and in this respect their experience clearly demonstrates liberalization. Liberalization is a process that evolves over time, involving both a shift to outward orientation and a reduction of government intervention. We return later to the issue of the speed of liberalization, arguing in particular that only a few countries have been able to liberalize as gradually as Korea and without losing momentum.

[3]See Sachs (1987) and Lal and Rajapatirana (1987) for different interpretations, and Edwards (1989) for a reconciliation of the two.

[4]See Krueger (1978).

Another area of wide agreement in the liberalization debate is the need for an appropriate exchange rate policy.[5] Devaluation, by increasing the value of exports and the cost of imports, corrects the anti-export bias of an economy and contributes to both export expansion and efficient import substitution.

Some Aspects of Arab Countries' Trade Policy and Performance

Other papers for this seminar address more explicitly issues relating to the Arab countries as a group and individually, and we will not attempt to do the same here. However, it may be useful to illustrate some of the points made in the discussion so far with selective examples in the Arab country group. El-Naggar (1987) divides Arab countries into three groups: oil exporters, middle-income, and low-income. For an analysis of trade performance, the pattern of exports rather than income levels is a useful basis for grouping countries. This classification results in three groups that are nearly identical to those of El-Naggar, relabeled as oil exporters, diversified exporters, and primary exporters. (Table 1 identifies the countries in each group.) Oil exporters tend to have very low import restrictions, and generally these are tariffs rather than quantitative restrictions. The one exception is Algeria, which may be characterized as having a highly restrictive inward-looking regime.[6] However, several countries in this group do have substantial subsidy and support programs for certain sectors, in particular, agriculture and petrochemicals. The agricultural support measures in some GCC countries are similar to those in industrial countries: very limited explicit protection via tariffs or prohibitions, but considerable implicit protection using other measures.

The second group of countries, diversified exporters, have medium to low levels of restrictions, with Jordan probably lowest on this scale. Jordan has not been strongly inward-oriented or highly interventionist in the recent past, whereas the others have. However, all

[5]See Michaely, Choksi, and Papageorgiou (1989) and Thomas, Martin, and Nash (1990) for discussions of how important appropriate devaluations are in explaining successful trade liberalization experiences.

[6]Algeria is categorized as an oil exporter because oil accounts for 90 percent of its exports.

Table 1. Structure of Arab Country Exports by Export Category, 1980 and 1988
(*Percent of total exports*)

Classification	1980	1988
Oil Exporters		
Undiversified[1] (Oil > 90 percent)		
Nonfuel primary	0.7	1.3
Manufacturing	1.2	4.0
Nonfactor services	1.4	3.5
Fuel	96.6	91.1
Slight Diversification[2] (Oil < 90 percent)		
Nonfuel primary	2.4	3.6
Manufacturing	4.2	11.7
Nonfactor services	17.3	12.5
Fuel	76.1	72.3
Diversified Exporters[3]		
Nonfuel primary	21.6	18.8
Manufacturing	13.1	24.1
Nonfactor services	33.6	41.8
Fuel	31.7	15.3
Primary Exporters[4]		
Nonfuel primary	69.7	67.0
Manufacturing	1.3	3.4
Nonfactor services	27.4	28.0
Fuel	1.6	1.6

Source: World Bank data.
[1]Algeria, Libya, and Oman.
[2]Bahrain, Kuwait, Qatar, Saudi Arabia, United Arab Emirates, and Repubic of Yemen (formerly the Yemen Arab Republic and the People's Democratic Republic of Yemen).
[3]Egypt, Jordan, Morocco, Syria, and Tunisia.
[4]Mauritania, Somalia, and Sudan.

except Syria have undertaken varying degrees of liberalization or devaluation to correct some of the anti-export bias. The strongest such effort has been the adjustment and liberalization program of Morocco since 1984. Egypt undertook a devaluation in 1987 but has not yet implemented many other liberalization measures.

Finally, of the primary exporters, only Mauritania has undergone some liberalization recently.

A thorough analysis of the link between trade policy and trade performance is not proposed here, since it is particularly difficult to assess the effects of trade policy in oil exporting economies—in particular because large oil exports tend to push up the exchange rate, making other exports less competitive. But some illustrative evidence does yield suggestive conclusions (see Table 2). The apparently high growth rates of manufactured exports of inward-oriented

Table 2. Annual Growth in Arab Country Nonfuel Exports, 1980–88
(Annual growth in dollar value)

Group/Country	Total Value (Including Services)[1]	Manufactures Value	Manufactures Volume[2]
Oil Exporters			
Algeria	1.0	15.7	13.6
Libya	−2.7	8.6	11.6
Oman	7.6	3.6	−39.5
Average	2.0	9.3	−4.8
Bahrain	8.2	0.3	−2.8
Kuwait	−8.7	−15.1	−18.8
Qatar	−0.1	1.0	—
Saudi Arabia	−2.6	20.9	15.3
United Arab Emirates	6.8	15.4	12.9
Yemen Arab Republic	−5.4	12.6	10.1
Yemen, People's Dem. Rep. of	1.9	12.2	9.7
Average	0.1	6.8	3.8
Diversified Exporters			
Egypt (devaluation only)	5.5	12.6	8.0
Jordan (liberal)	3.8	8.2	5.8
Morocco (strong liberalization)	6.1	13.8	11.9
Syria (some liberalization)	4.6	8.8	6.4
Tunisia (average liberalization)	5.3	7.6	8.7
Average	5.1	10.2	8.2
Primary Exporters			
Mauritania (some liberalization)	7.7	12.0	9.5
Somalia	−9.7	5.3	3.0
Sudan	−1.7	18.5	15.5
Average	−1.2	11.2	9.3
Overall average	1.5	9.5	4.1

[1]Including exports of services. Because services are an important part of actual and potential exports in several Arab countries, and since data are available only in current prices, the totals including services are calculated in current prices.
[2]Volume rates of growth are in constant 1980 prices.

countries (Algeria, Sudan) merely reflect the very low base from which they started.[7] It is more notable that all the non-oil exporters that have been outward oriented or have undergone some degree of liberalization have experienced far higher growth rates for nonfuel exports, in particular manufacturing, than the others (Table 2).

[7]In 1990, Algeria had manufactured exports of $3 million and Sudan less than $1 million, compared with over $100 million in Egypt and Jordan, nearly $500 million in Morocco, and over $900 million in Tunisia.

Perhaps the strongest liberalizer has been Morocco, and its export growth rate has also been the highest. Indeed, if only the period since liberalization (1984) is considered, Morocco's export growth rate is even higher than shown in Table 2—about 8 percent for nonfuel exports and 16 percent for manufactures.

Although much more thorough analysis is needed to assess the effects of trade policy on performance in the Arab countries, these indicators point in the same general direction as the historical evidence for other countries: more market-based and more outward-oriented trade policies are better for export growth than more statist, inward-looking ones.

III. Export Growth and Efficient Import Substitution

The Benefits of More Liberal Trade

Less distorted and more outward-oriented regimes with less government control do much more than generate exports that pay for essential imports. They also increase imports, which introduces important competitive effects into the economy. The common perception that exports are good and imports are bad (because they hurt domestic industry) motivated the failed import substitution policies of many countries. In fact, both exports and imports are good. Exports pay for imports, but more important, the openness of trade ensures that competitive forces will push domestic producers to their most efficient *levels*. Exporters cannot export if they are not competitive, and domestic producers must approximate world costs if they are to compete with imports. Trade openness also increases the use of new technology, both in the products that are imported and among exporters who must use the best applicable technology to be competitive on world markets. Finally, liberalization brings with it a lower price for goods. The removal of import restrictions allows buyers to purchase goods at world prices plus any remaining tariff, which means, for example, not only that consumers in Morocco pay less for automobiles and electronic goods as restrictions on these items are reduced, but also that domestic producers will pay less for their inputs such as metals, chemicals, or plastic components.

Indeed, it is a happy paradox that in the long run liberalization will make domestic producers more competitive than they were

under the protected, import substitution regime. It is the lowering of input prices and the competitive push to greater efficiency that give this beneficial result. These benefits come not only from an expansion of exports but also from more openness to and competition from imports. Achieving these benefits does not require a negotiated reciprocal liberalization between a country and its trading partners. A unilateral liberalization (a move toward outward orientation plus reduced quantitative restrictions) in itself improves export performance and increases the competitive effects. This is not to say, however, that reciprocity is irrelevant; far from it. The more countries reduce barriers, the more trade is generated, and the more the efficiency gains of specialization are shared (see Section IV). To get the most from trade, countries need to combine multilateral trade negotiations with unilateral liberalization in much the same way as a merchant seeks better results both by negotiating the best price for a product and by keeping a close eye on production activities, seeking continued cost improvements there as well.

Minimizing the Transition Costs of Liberalization

Liberalization is often said to entail many costs.[8] The devaluation that accompanies liberalization raises costs and may add to inflation; workers in formerly protected industries may lose jobs as a result of import competition; and export expansion may be slow as other countries impose barriers and support their own exports. While all of these problems may accompany liberalization, they are not always as severe as feared and they can be managed by appropriate government policies.

Where devaluation is necessary (and it usually is), it will indeed raise prices, but this effect is offset by the lower prices on imported goods as import restrictions are reduced. (This effect may be blocked where domestic wholesale and retail markets are monopolistic; and therefore other complementary policies are required.) Also, since devaluation is a far less important cause of inflation than overall macroeconomic instability, an even more important complementary

[8] The following discussion draws heavily on the World Bank report by Thomas, Martin, and Nash (1990).

policy is to ensure macroeconomic stability, through fiscal and monetary restraint. On the positive side also, devaluation makes domestic producers more able to compete with imports, and, by allowing for more efficient import substitution, reduces the employment effects of increased imports. Finally, one needs to be clear about which prices are increased by devaluation and for whom. If the exchange rate was overvalued before the devaluation, the resulting foreign exchange shortages signified that not everybody could buy the imported goods; whereas some were privileged enough to receive import licenses, some paid a premium price on the black market, and some went without. Devaluation means higher prices *only* for those who previously had import privileges. Those who were unable to buy certain imports because of shortages may now be able to do so, while those who paid black market prices continue to pay those prices (or lower ones) but can buy the goods openly. To some degree, higher prices after devaluation are an illusion.

Trade liberalization will result in some worker dislocation, which may even be quite high in some localized areas or sectors. But its overall extent throughout the economy has been exaggerated, as a World Bank study of 19 countries demonstrated.[9] The study found that two factors minimize the unemployment problem. Of all the liberalization cases studied, only that of Chile in the mid-seventies showed unemployment effects as high as 10 percent. But these effects occurred only for manufactures and were offset by the very rapid employment expansion in processed agricultural exports. As liberalization measures shift the economy toward an outward orientation and reduce anti-export bias, export expansion increases employment, and in developing countries, export activities tend to be much more labor intensive than are import-substituting ones. Also, liberalization has not meant that entire factories and sectors suddenly close down and that new ones start being built up only slowly. Rather, much adjustment occurs within sectors and even within firms. While some closures do occur, the bulk of adjustment takes place by reducing production of some goods and increasing production of others, such as by switching from one kind of steel product to another. Turkey's steel industry before the liberalization of the eighties was highly

[9] Michaely, Choksi, and Papageorgiou (1989).

inefficient, but Turkey has since become the third leading steel exporter, thanks to a simple switch from large heavy steel products to simpler products such as radiators for the U.K. market.

The concern that export expansion may not come soon enough is valid but again exaggerated. A combination of devaluation and export promotion measures will help this expansion to develop more quickly. Unfortunately, barriers in importing countries are an element of the trading environment, especially for labor-intensive goods and agricultural goods, the main exports of most developing countries. But this is a problem for reciprocal negotiations at the level of the GATT, and this process requires greater and not less involvement by developing countries. No domestic trade policy measures can do much to alleviate the constraint of import barriers in developed countries. However, it is interesting to observe in this connection that as the nontariff restrictions of developed countries have increased, the most outward-oriented and least distorted economies of East Asia still come out best in export performance.

The Pace of Liberalization and Its Phasing

The desirable pace of liberalization is much debated. Any sensible answer must recognize another element besides speed, however, and that is the combination and sequencing of the many concrete policy measures that constitute liberalization.

> In general, a pace as fast as the political circumstances permit is desirable, but perhaps more important than speed is to avoid piecemeal experiments in favor of a preannounced, comprehensive, and consistent program phased in over a specified period of time.

A "fast" program of liberalization does not usually mean immediate or overnight, just as, for most proponents, "liberalization" does not mean free trade. But swift implementation is advocated because a slow pace gives opponents of liberalization (those who stand to lose from its immediate impacts, like highly protected capital-intensive industries) time to lobby for political support to reverse the process. The Bank's study of 19 countries' experience with trade liberalization shows that most reforms fail and that they fail for two reasons: the liberalization is incomplete and therefore fails to achieve the benefits that would justify it politically; and the liberalization is so gradual that political opponents have time to mount a strong

opposition.[10] Examples of such failures are Yugoslavia in the sixties, several Latin American countries over the last three decades, and Turkey in the seventies. Starting in 1980, Turkey launched a much more substantial and successful liberalization based on sustained devaluation, a large program of compensatory export promotion measures, advance notification of gradual reductions in import restrictions, and reasonable adherence to the program schedule.

There are a few cases of sustained successful liberalization over a long period, such as Korea, Greece, Spain, and Portugal. For Greece, Spain, and Portugal, the sustained success of liberalization is explained by the legal commitments they made in their accession to the European Community (EC). The anomaly of Korea's success is often attributed to the political will of its Government and the strength of its commitment to a policy of efficient economic growth based on outward orientation conditions not found in many other countries. But there is another important factor in the Korean case: its strict adherence to sound macroeconomic policies, in particular fiscal and monetary restraint, plus a stable and realistic exchange rate. The Bank study cited above concludes that such complementary policies were the single most important elements distinguishing successful liberalization episodes from unsuccessful ones.[11]

While this is not the place to elaborate the components of a comprehensive liberalization package (the two Bank studies cited do this quite thoroughly), a few points, based on experience with trade liberalization, can be made. First, trade liberalization requires macroeconomic stability and a realistic exchange rate. If these conditions are not already present, stabilization measures may need to precede liberalization. Trade liberalization steps can be announced simultaneously and can even be initiated, but liberalization can achieve little in a climate of inflation, uncertainty, and soaring public deficits. Second, other nontrade policies must also be right, in particular, regulations governing investment, price controls, and so on.

[10] Michaely, Choksi, and Papageorgiou (1989).

[11] Sachs (1987) also emphasizes the importance of macro policies in sustaining the export and growth performance of Korea.

Third, the trade measures themselves should preferably begin by eliminating quotas and similar quantitative restrictions, which can at first be replaced by tariffs. This step of creating transparency in protection has several immediate benefits. Tariffs make explicit who benefits from protection and by how much; quantitative restrictions hide this fact. This transparency makes it harder for the beneficiaries of protection to win political battles at the expense of the rest of society. Further, this switch often brings about an increase in fiscal revenues, as the implicit profit premiums arising from protection are transferred from those who hold import licenses to the government via tariffs. While reductions in tariff levels need not come at the same time, they should follow soon thereafter.

Fourth, before tariff levels are reduced, it is important to introduce export expansion measures, as defined earlier in this paper. These measures, along with devaluation, can provide early gains from liberalization by increasing exports, production, and employment, and by demonstrating that liberalization results in benefits that can offset any costs observed. A fifth important finding on which there is broad agreement is that liberalization of international financial transactions should preferably occur after most other liberalization measures to avoid speculative capital flight.

The experience with trade liberalization efforts suggests the following general proposition:

> Successful liberalization requires that the government maintain momentum and credibility.

"He who does not move forward falls backward," goes an old saying; taking small hesitant steps toward liberalization and waiting to see the results before taking the next step is a sure recipe for reversal and failure. Bold initial steps (a comprehensive preannounced program) and a reasonably fast pace both help to sustain momentum and to lend credibility to the government's intentions. Hesitation, drawn-out programs, with reversals of some measures, quickly undermine credibility and lead to a loss of momentum. The process is self-reinforcing in both directions.

What, finally, does this say about the pace of trade liberalization? In principle, if momentum and therefore credibility can be assured, the process can be very gradual. In practice, we have no cases except Korea that demonstrate that such an approach is possible.

IV. The Role of Government

We turn in this last section to the question: what does a government have to do if the objective of liberalization is to reduce government intervention? The government has a substantial role to play in the process of liberalization, in the transition from inward-looking, restrictive policies to outward-oriented, liberal ones. But even after liberalization is well under way, several critical functions remain for government in supporting a market-oriented, open, and competitive economy.

Role of Government in Managing Liberalization Process

The government's first action is to identify the objective of liberalization: given the country's current trade regime, where does it want to go? Once this goal has been identified, as well as the degree of liberalization needed to achieve it, the government's role is to formulate a program—its timing, sequencing of components, and intensity.

A second role for government is to ease the transition. This role consists of three types of activities. First, it may be appropriate to compensate those who are hurt by liberalization. True, the losers are usually those who greatly benefited from the high protection of the previous, inefficient trade regime, but they benefited because they were following the existing rules of the game, not because of malice to the rest of society. Once the rules are changed, there is some justification for assisting the new losers. The argument is particularly strong for displaced workers, who will require a safety net of unemployment compensation and similar measures. But it may even be appropriate to compensate owners of capital, by providing credit for new investments in other product lines. However, this course of action entails the risk of excessive government intervention and the temptation to try to "pick winners" in industry, a task for which economists and bureaucrats are generally not well suited. As Lieberman (1990) writes, such measures ought to be undertaken "only as a complement to policies that promote efficient, competitive supply responses by industry," such as market pricing, an increase in competition internally or through imports, or elimination of subsidies.

Another role for government in the transition is to reduce the constraints to the smooth reallocation of resources. New investments

need to be made in new places, and workers have to be trained and shifted to other sectors or other parts of the country. The government should certainly not attempt to direct all these shifts—the former socialist bloc countries have demonstrated clearly the failure of such planning. But only the government can make certain improvements, and it may be able to perform some activities better than the private sector. One is to simplify customs and tax procedures. Another is to improve infrastructure, including roads, ports, and telecommunications. Also important are improvements in the education system, particularly during the transition, in areas that quickly begin to demonstrate dynamism (such as textile engineering at a higher level and vocational and technical training in labor-intensive sectors of export strength).

Finally, during the transition, governments should engage in reciprocal negotiations in the international arena, in particular, through the GATT. While unilateral liberalization can yield significant benefits, reciprocal negotiations will certainly increase the gains from liberalization. Multilateral negotiations not only lower external barriers, allowing greater export expansion, but they also can serve an important purpose internally. Reciprocal negotiations help the government to be perceived as an arbiter balancing the interests of those who will be temporarily hurt by import competition with the interests of those who will gain from exports. While everyone gains from liberalization in the long run (import competition stimulates efficiency, export expansion creates new jobs), during the transition it helps to show that efforts are being made to ensure that no one is hurt unfairly.

Role of Government in a Liberal Economy

What role remains for the government as we approach the liberal range of policy options? First, on the role of government in an economy, what makes some economies more successful than others? In simple terms, the same things that make some individuals more successful than others: working hard, working smart, and working for the future. For the economy as a whole, this means expanding employment, investing in capital and education, striving to increase efficiency and productivity, and saving and reinvesting (wisely) a large part of GNP. But how it is done is also important. The

appropriate economic role of governments is not to decide, direct, or command, but rather to create an environment in which individuals are free and motivated to work hard, smart, and for the future, taking a direct hand only in the economic activities for which governments are better suited than individuals. That line is not easy to draw, but the burden of proof should be on governments to show why they are undertaking a given economic activity.

This very simple notion that the primary locus of economic activity is the individual acting in (and being disciplined by) the marketplace is well expressed in recent documents of the Government of Morocco, such as the "Lettre Royale du 14 Juin" of His Majesty the King. On the international aspect of economic policy, this document implies an economy open to the world market and based primarily on private initiative and the discipline of the marketplace, complemented by four types of government undertaking:[12]

- Assurance of a stable, clear, and credible legal framework for the enforcement of commercial contractual obligations in a system of justice, with recourse and access by all parties.
- Maintenance of a stable macroeconomic environment, including a realistic and stable exchange rate and fiscal and monetary stability.
- Readiness to act, if needed, after liberalization to assist those seriously hurt by any unforeseen changes (including the effects of policy).
- Direct government actions to develop the physical, human, and social infrastructure needed to spur economic growth and to increase productivity, but only in areas in which the government clearly has a comparative advantage over individual initiative.

Does this mean free trade—that is, no tariffs, no customs regulations, and no laws against dumping by foreigners? It may mean that if that is the social consensus and the government reflects that view,

[12]The concrete measures that may follow from these fundamental principles in a particular case are elaborated in Havrylyshyn and others (1990).

but it need not. A moderate level of tariffs,[13] some rules of operation on safeguards and antidumping, or similar measures are not necessarily very harmful. What are to be avoided are high tariffs, extensive use of quotas and licensing, and highly distorted patterns of protection that largely benefit some favored infant industries at a great cost to others.

In other words, what matters is that the governments perform well the four functions noted above and that any remaining trade regulations are low, clear, simple, transparent, limited, and fair in the sense that no sectors or industries enjoy greater favors than others. This means, simply, very limited and nondiscriminatory government intervention.

V. Conclusion

A country's choice of trade policy is not just a matter of selecting free trade or autarky, for there are many options in between as well. Two key aspects characterize a trade policy: the degree and type of government intervention, and the effect of this intervention on inward or outward orientation. The historical evidence on what kind of trade policy leads to the best performance, although not entirely unambiguous, does point consistently toward freer, more liberal trade.

The strongest agreement—by now virtually universal—is with the conclusion that outward-oriented regimes outperform inward-looking ones. Agreement is not as strong on how best to achieve outward orientation, whether with less, or with different kinds of, government intervention. While export expansion measures alone, even with highly restrictive import regulations, can—in theory and in fact—shift the trade regime from inward-oriented to outward-looking, two important qualifications are readily acknowledged.

[13]The industrial country average is less than 5 percent, but their level of protection is higher than tariff rates alone suggest, given the substantial increase in their use of nontariff restrictions, which is in effect a step backward in liberalization that deserves the criticism it gets. Liberalization measures in developing countries should include all possible efforts to reduce these barriers, including reciprocal negotiations and political-diplomatic pressures that publicize the extent of this "New Protectionism."

First, the measures used for imports and exports should be the simplest and clearest price-related measures available, such as tariffs, taxes, or tax exemptions for exporters; quantity control measures such as quotas or government production planning directives are to be avoided. The second, and perhaps more important, qualification is that intervention should be temporary and that the government should move consistently toward increased liberality. Thus, for example, if it starts with a highly restrictive, inward-oriented policy, its actions on the export side, such as exemptions from import regulations for exporters, are an acceptable first step, but only a first step.

If we think of liberalization as a process over time, combining a shift from inward-oriented to outward-looking policies plus a reduction in the degree of government intervention, the differences in interpretation lessen. Then not only is a quick leap to free trade a liberalization, but so also is a relatively quick change in orientation and reduced intervention or a slower two-step movement, first shifting to outward orientation and then reducing intervention. The main difference is in the timing and sequencing.

However, although the more gradual, two-step liberalization is feasible, it is difficult to implement without a loss of momentum and credibility in the drive toward the goal of more liberal trade. The very few countries that have achieved liberalization in this way and their special circumstances are a testimony to the difficulty of very gradual liberalization. That a much larger number of countries have tried gradualism and failed further emphasizes this point. This does not mean that only a strong, overnight liberalization will work. It does mean that the period of reform needs to be relatively short, and that the program needs to be announced in advance and followed as planned.

Some important roles remain for the government. For one, the government is the arbiter of society's sometimes competing interests, deciding on the policy option to be chosen and the path to be followed. For another, it may need to provide a safety net during the transition to a more liberal regime for those displaced by the reallocation of economic activity that constitutes adjustment. It also needs to act as an arbiter in the reciprocal negotiation process of the multilateral trade negotiations in the GATT. Whatever the criticisms brought against this process (and there are many), it has had

useful results. Finally, in the more liberal environment, the government retains key responsibilities to support and work with a market economy based primarily on private initiative: ensuring a system of just laws and commercial security, a sound macroeconomic environment, a system of support for the unemployed and for related assistance during unforeseen shocks, and the provision of infrastructure where the private sector does not easily operate, particularly in education, transport, and communications. In the words used so often by foreign investors—the government should do only as much as is needed to improve the investment climate, and stop short of the point where its actions undermine it.

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Comment

Rasheed O. Khalid

It is difficult to comment on a well-written paper with which you agree on all or most of its contents. So what do you do? You underline certain important aspects of the paper and point out some issues that might need elaboration and then proceed to talk about what it does not contain and perhaps should have. This is what I intend to do.

From a long-run perspective everyone would agree with the central thesis of the paper, which is that everyone gains from liberalization. This happens because import competition stimulates efficiency and export expansion creates jobs. The real issue is the path to be taken toward this objective. In other words, what is the best way to achieve this goal? The World Bank paper can profitably be expanded in that direction. I shall come to that point later. At the moment I wish to offer specific comments on certain points mentioned in the paper.

Some distinction needs to be made between the concept of "liberalization" and the idea of a strategy of outward orientation based on a vigorous pursuit of export expansion. The broad objective of economic liberalization is to allow for a more efficient and better use of resources through increased reliance on market forces. Heavy government intervention in economic matters in the former socialist countries of Eastern Europe and elsewhere in the developing world has failed to deliver the promise of economic growth and improvements in living standards of the vast majority of the populations of those countries. Accordingly, and in a process unprecedented in its scale, a large number of countries are currently engaged in comprehensive liberalization programs.

These liberalization programs are much broader than the pursuit of export expansion as a strategy for rapid economic growth. The

strategy has become fashionable because of the impressive economic performance of the newly industrialized countries of East Asia, which, relatively speaking, enjoy low resource endowment levels. The experience of these countries (the Republic of Korea, Taiwan Province of China, and, before that, Japan) has shown that a process of gradual liberalization can be successfully embarked upon after a successful export expansion drive.

Although the paper refers to the benefits of the removal of trade barriers worldwide, and to the relevance of reciprocal trade negotiations, its analysis of the gains from trade liberalization seems to be conducted largely within a unilateral context. Thus, the significance of the multilateral dimension to trade liberalization efforts in individual countries was not, I think, emphasized in a manner commensurate with its importance. While it is correct to argue that liberalization, insofar as it leads to the removal of domestic distortions, will result in efficiency gains for the country concerned, trade issues are inherently multilateral in character.

The success and continuation of trade liberalization programs currently being undertaken in a number of countries will to a great extent hinge on the presence of an international environment conducive to more open trade. One has only to look again at the experience of the newly industrialized countries of East Asia to realize how vital was the growth and expansion of world trade in the three previous decades to their remarkable success. The present calls for protectionism in industrial countries and their grouping into three major trading blocs is a cause for great concern. It is regrettable that countries that are commendably trying to open up their economies and trade—thereby risking great political and social challenges at home—are faced with an international environment in which the commitment of rich powerful countries to an open trading system appears to be waning.

The statement that "large oil exports tend to push up the exchange rate, making other exports less competitive" may require further elaboration. The exchange arrangements in the countries of the Gulf Cooperation Council, with the exception of Kuwait, are such that national currencies maintain, in practice, an unchanged relationship with the U.S. dollar. The Kuwaiti dinar is pegged to a basket of currencies that reflects Kuwait's external trade and financial relations. Over the years, however, the value of the dinar in

terms of the dollar has remained relatively stable. Perhaps an analysis of the movements of the real effective exchange rate in these countries would throw more light on this question.

Finally, there is an implicit and unstated assumption throughout the paper that an adequate, skilled, and versatile work force exists in developing countries that can be retrained and reconverted with ease. Furthermore, the impact of prolonged external shocks on liberalization reform efforts has not been explicitly recognized in the paper.

I return now to the central issue of the appropriate path for the transition to outward-oriented policies. This aspect is largely ignored in the paper; yet it is extremely important. It is a formidable task for latecomers to industrialization to break into world markets of manufactured goods. There is a strong case for granting developing countries more trade concessions, compared with what they actually face at present: a trade environment in which protectionist measures are toughest on goods in which they enjoy a comparative advantage (such as textiles). The case rests on the following assumptions: First, a fundamental asymmetric trade relation exists between these two groups of countries. The industrialized countries buy much more from among themselves than from the developing countries, and the developing countries do just the reverse. That means that a certain amount of exports from the developing countries have much greater importance for their economies than they have, in the form of imports, for the economies of industrialized countries.

Second, the developing countries will continue to provide expanding markets for imports from developed countries, especially for their capital goods. The import patterns of developing countries are distinctly biased in favor of those goods that are the main exports of industrialized countries.

Third, the potential import demand of developing countries is much greater than their actual imports. The gap arises from a general shortage of foreign exchange resources, which, admittedly, could be attributed in part to the long adherence to inward-looking policies. Thus, any degree of export expansion permitted to developing countries would lead to almost the same degree of import increase, which is in the interest of their trading partners and of world trade expansion.

Some progress—albeit at a certain cost—has no doubt been made in the past in the field of import substitution aided by import control policy. However, since the scope for import substitution is gradually reduced as development reaches more advanced stages, further progress on the foreign trade front points to the need for the expansion of manufactured exports and the opportunities inherent therein. In this connection, it is worth mentioning that regional trade arrangements and cooperation will undoubtedly contribute toward a larger market for all the countries involved. However, even if regional trade cooperation can succeed, it will solve only a small part of the problem, for it is with the developed industrialized countries that developing nations trade most.

In this context, a more liberal trade policy by industrialized countries toward exports from developing countries cannot be overemphasized. This is as important as regional trade and economic cooperation among developing countries. For it is from the developed industrialized countries that the developing countries obtain the bulk of their capital goods.

It goes without saying that an increase in the flow of external capital in the form of both loans and direct investment will be of great help. But unless external loans are provided largely in a concessionary form (a source currently tending to decrease), they cannot provide an answer to the problem for they have to be serviced and amortized or, in other words, eventually paid back by goods and services. On the other hand, direct investment could play a crucial role in the development process, by providing external finance, as well as the opportunity to benefit from advanced technology and management techniques. However, a great deal has be done, in terms of domestic economic reforms and liberalization measures, in the majority of developing countries before private foreign capital can actually be attracted. Hence, a more realistic solution would seem to rest with trade: that is, export expansion and import substitution.

It is difficult, however, to weigh the relative importance of these two elements (export expansion and import substitution) in the development process in any particular country. Historically, the United Kingdom and Japan are examples of exported growth. But Germany and the United States are examples of protected industrialization.

A more pragmatic approach to the issue of import substitution and export expansion is to try to consolidate the existing policies in an individual country and to make them more consistent and more rational to serve the purpose of development. This is not a simple task because many countries have adopted more than one kind of control—usually a combination of two or three or even more of such measures as tariffs, subsidies, multiple exchange rates, quantitative restrictions, and tax and credit incentives. In searching for a rational solution, one first has to examine the impact of these individual measures, one by one.

In concluding, I would like to say that the authors presented persuasively and clearly, but in a condensed and general form, an issue that is highly relevant to the problems currently being faced by a large and increasing number of countries around the globe. Considering who the authors are, the paper may be pointing us in the direction that World Bank thinking is fortunately being led. The impact of the paper would, I think, be greatly enhanced by an attempt to think through and to work out in some detail the optimal path to free markets and to outward-oriented economic policies.

4

Trade Policies in Industrial Countries and Their Impact on Arab Countries

Margaret R. Kelly and Bernhard Fritz-Krockow

I. Introduction

The trade and trade-related policies of industrial countries mainly affect developing countries, including Arab countries, in three ways.[1] First, policies that restrict access to industrial countries' markets limit the ability of developing countries to produce and export on the basis of their comparative advantage. Second, and related to the first, protection in industrial countries affects the level and pattern of investment worldwide; by locking resources into inefficient uses, protection reduces potential output in both industrial and developing countries. Even when a particular country does not currently face restrictions in sectors in which it bas a comparative advantage, the possibility that they could be imposed if the country became a major supplier may discourage investment. Where economic agents do not anticipate such an intensification of restrictions, investment may yield less than its expected rate of return. Third, if

[1]The Arab countries covered in this paper are the members of the Arab Monetary Fund, except for Iraq and the Republic of Yemen (formerly the Yemen Arab Republic and the People's Democratic Republic of Yemen), which are excluded owing to changes in their status as countries and/or the lack of sufficient and reliable quantitative and qualitative information.

developing countries choose to compete in industrial countries by establishing production facilities in those markets, the conditions attached to foreign investment in industrial countries, such as local content requirements, may affect the ability of foreign firms to compete with domestic firms.

Of course, the trade policies of industrial countries are not the only, or perhaps even the major, influence on the economic performance of Arab countries. Of critical importance also are external economic factors beyond the trade policies of trading partners; natural resource endowments and demographic and climatic conditions; and the domestic economic policies pursued by the countries concerned and, more broadly, the nature of their institutions. The importance of a country's own policies is clearly demonstrated by the superior performance of the dynamic Asian economies over the 1980s and, more recently, the performance of some developing countries in the Western Hemisphere that have undertaken major macroeconomic and structural reforms, including in the trade area.

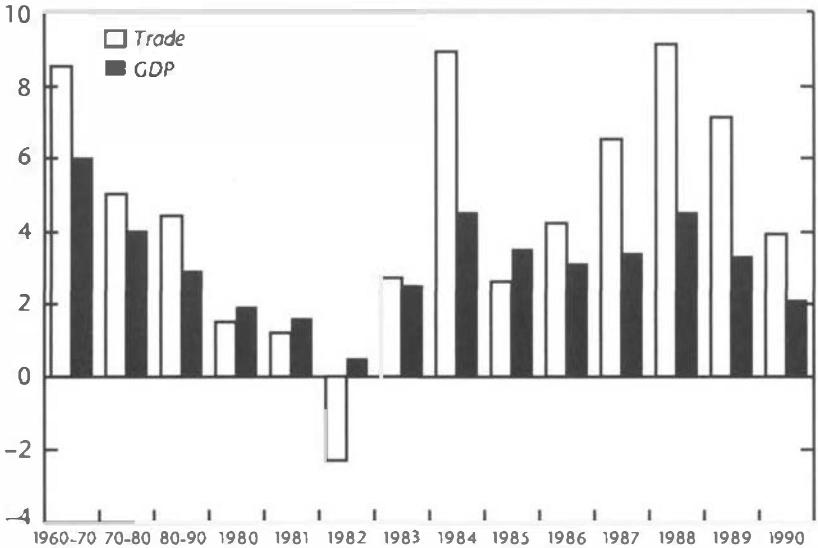
It is difficult to disentangle the effects of these various factors on economic performance, and this paper does not attempt to do so. Its main aim is to identify the specific trade and trade-related policies of industrial countries that are particularly relevant to Arab countries (see Section IV). To provide some perspective, the paper also discusses the external economic environment in which Arab countries' economic policies have been implemented over the 1980s (Section II); and provides details on the economic structure and domestic policies of Arab countries that had an important impact on their economic performance in the 1980s (Section III). Some conclusions are presented in Section V.

II. The External Environment

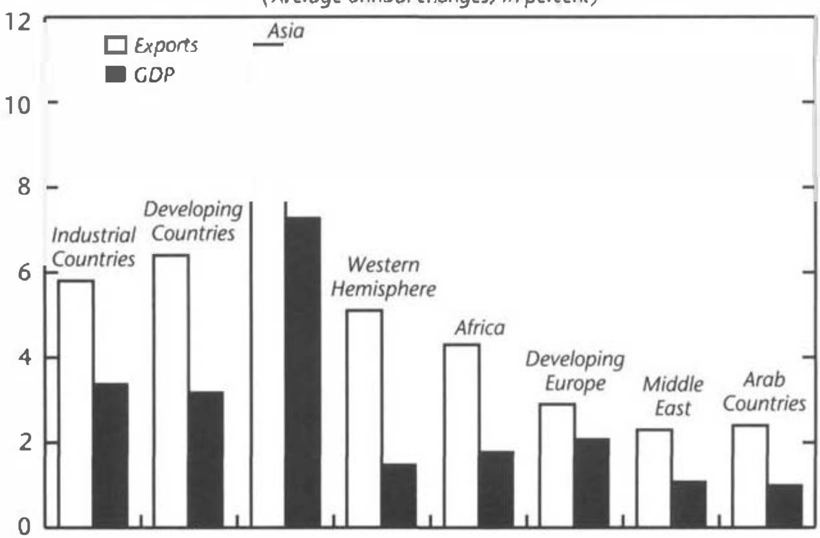
Developments in the 1980s and Current Prospects

The 1981–82 recession was followed by a long economic expansion and a further integration of the world economy through trade (Chart 1) and foreign investment. For 1983–90, the growth of output expanded on average by $3\frac{1}{2}$ percent a year in both industrial and developing countries. The growth of world trade exceeded output by 50 percent over the 1980s, an outcome that was more in line with historical trends than the relationship that prevailed during the

Chart 1. Real Trade and GDP Growth, 1960–90
(Annual changes, in percent)



Real Export and GDP Growth in Selected Regions, 1983–90
(Average annual changes, in percent)



Sources: General Agreement on Tariffs and Trade; and International Monetary Fund, *World Economic Outlook.*

period of oil price increases when the growth of trade volumes exceeded output by only 25 percent. Economic performance varied among countries, however. Among the developing countries, the Asian countries experienced the highest rates of growth in output and exports, and the Middle East and Arab countries the lowest. The performance of Arab countries is discussed in more detail below.

The post-recession period also witnessed a rapid expansion of foreign direct investment (FDI). Between 1983 and 1989, outward foreign investment by the five major industrial countries (France, Germany, Japan, the United Kingdom, and the United States) expanded at an annual rate of nearly 30 percent, or three times faster than merchandise trade flows. Relative to the rate of growth of real GDP, this was about twice the rate that would have been expected, based on historical experience, and reflected institutional and structural factors, including the deregulation and liberalization of financial markets, shifts in comparative advantage, technological advances in international communication and transportation, and efforts to circumvent protection in major world markets. Overall, the developing countries did not share equally in the expansion of FDI, and their share of FDI flows declined. The industrial countries were both the primary source and destination of FDI, and a growing proportion of that investment was related to the service sector.

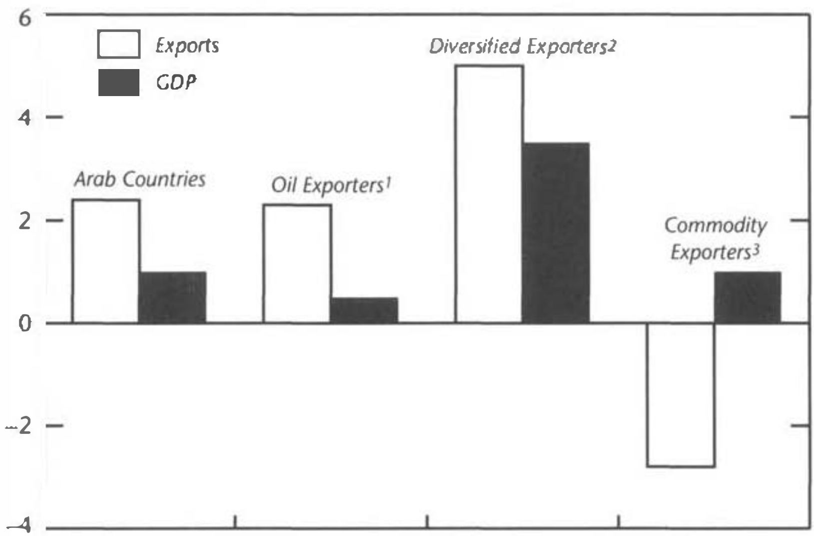
The increased integration of the world economy through trade and the globalization of investment and production increase the potential for specialization and for the growth of world welfare, but it also means that the economic policies and performance of countries have become more intertwined. Industrial countries' policies and prospects continue to have a major impact on developing countries because of their large weight in world output and because they account for about two thirds of developing country exports (Appendix Table A1). But the developing countries have also become increasingly important in the world market. While increased integration is beneficial to global welfare, it requires the ability to adapt to ongoing structural changes in the world economy. Resistance to such adjustment partly explains the resort to protectionist trade policies in industrial countries as well as attempts to control the operation of foreign companies. Since such protection tends to be concentrated in labor-intensive sectors and in agriculture—sectors in

which many developing countries have a comparative advantage—it has a correspondingly larger impact on developing countries.

The Importance of External Environment for Arab Countries

During the 1980s the average rate of growth in output and export volumes in Arab countries fell short of that in many other developing countries (see Chart 1). Economic performance varied among Arab countries, however. Diversified exporters outperformed both oil exporters and commodity exporters (Chart 2).[2] These develop-

Chart 2. Arab Regions: Real GDP and Export Growth, 1983–90
(*Average annual changes, in percent*)



Sources: General Agreement on Tariffs and Trade; and International Monetary Fund, *World Economic Outlook*.
[1]Algeria, Bahrain, Kuwait, Libya, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.
[2]Egypt, Jordan, Morocco, Syria, and Tunisia.
[3]Mauritania, Somalia, and Sudan.

[2]The countries classified as diversified exporters, commodity exporters, and oil exporters are listed in Chart 2 and discussed further in Section III.

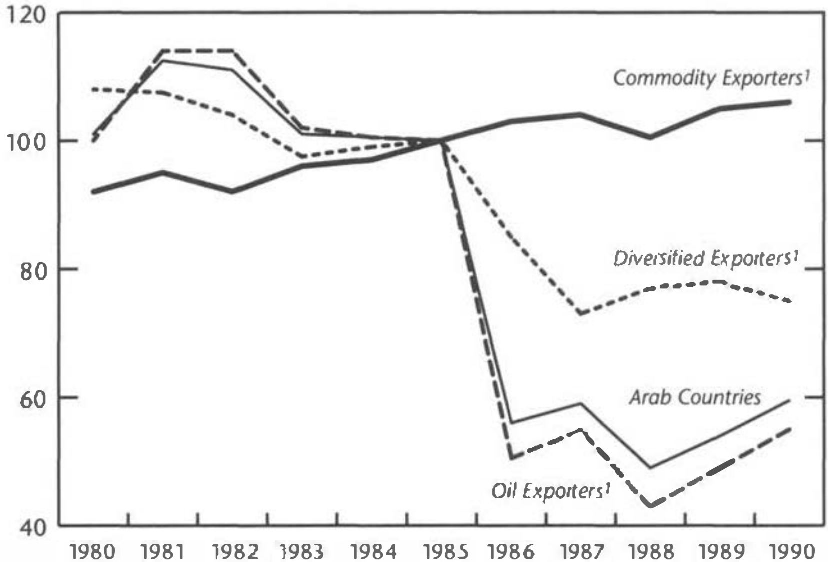
ments reflect to some extent the differential impact of the external environment on Arab countries compared with other developing countries and on different groups of Arab countries. They also reflect factors unique to the Arab countries such as their own factor endowments and economic policies.

The period of economic expansion in the industrial countries following the 1981–82 recession had a positive impact on Arab countries' exports. The strength of this impact varied according to both the importance of industrial country markets for each particular Arab country (Appendix Table A2) and the income elasticity of demand, which is relatively low for products exported by oil exporters and commodity exporters. For those Arab countries that largely trade with European countries, the growth of output and exports was somewhat curtailed by the less buoyant conditions in Europe than in the United States or Japan during this period. For the oil producing countries, exports were also dampened by oil conservation measures in industrial countries, which significantly reduced the amount of oil consumption relative to GDP, and by the expansion of alternative supplies. Of course, part of that conservation effort was a response to previous increases in the relative price of oil.

While the expansion in the industrial world had a positive impact on the economic performance of the Arab countries, movements in the terms of trade adversely affected most Arab countries (Chart 3 and Appendix Table A3). Export unit values for oil exporting Arab countries have fluctuated widely in the past, but registered a sharp decline during the 1980s, with the largest decline occurring from the mid-1980s. As a result, the terms of trade for oil exporting Arab countries declined by almost 40 percent between 1980 and 1990. Except for Sudan, the terms of trade also declined for all diversified exporters and commodity exporters in the same period because of the price declines in primary sector products. Among these countries, the deterioration was largest in Egypt and Syria, which depend on oil for 60 percent and 50 percent of their export receipts, respectively.

Interest rates on global capital markets have declined since the early 1980s. For those oil exporting Arab countries whose financial assets abroad exceed external debt, this has meant a reduction in

Chart 3. Arab Regions: Terms of Trade, 1980-90
(1985 = 100)



Source: International Monetary Fund.
[1]See footnotes to Chart 2.

investment income. For other Arab countries whose foreign debt exceeds foreign assets, the reduction in interest rates has eased their debt service burden somewhat.

III. Arab Countries' Economic Structure and Domestic Policies

The economic performance of Arab countries has also been influenced by their natural resource endowments, demographic and climatic conditions, military conflicts, and their own domestic policies. In most Arab countries a population explosion is under way, which is expected to result in a doubling of the population (currently more than 200 million) in less than 25 years.[3] In the oil producing countries, the capacity to employ an increasing population is limited

[3]See "A Survey of the Arab World," *The Economist*, Vol. 315, May 12, 1990, p. 54.

by the capital-intensive nature of oil production and the skilled labor (and hence high wages) required for downstream refinery and petrochemical industries. In addition, scarce water resources and a limited supply of arable land hamper efficient agricultural production, and the relatively high cost of domestic labor limits the scope to employ the growing population in labor-intensive manufacturing and service industries. Oil production and exports are vulnerable to fluctuations in international prices and growth in trading partners. Foreign investment is an option to reduce the vulnerability of these economies to external shocks, but FDI does not create significant employment in the capital exporting country; emigration is an option but has political limits.

Scarcity of water and arable land limits the potential for agricultural production in a number of other Arab countries. Even countries with a greater abundance of arable land are susceptible to frequent droughts. Emigration to higher-income oil producing Arab countries has been an option for lower-income countries, but such emigration (and the resulting remittances) also has limits and is vulnerable to the shifts in the demand for labor, including those caused by conflicts in the area. For the lower-income countries, however, diversification into labor-intensive manufacturing and services is an option.

Export Structure and Performance

To examine the impact of their economic structure and domestic policies on economic performance, the Arab countries are categorized into oil exporters, diversified exporters, and exporters of a few non-oil commodities.

Oil Exporters

The oil exporters comprise Algeria, Bahrain, Kuwait, the Socialist People's Libyan Arab Jamahiriya, Oman, Qatar, Saudi Arabia, and the United Arab Emirates. These countries derive 80 percent or more of their export earnings from exports of hydrocarbons and have the highest per capita incomes among the Arab countries, ranging in 1989 from $18,430 for the United Arab Emirates to $2,230 for Algeria. Most of these countries have had only moderate success in diversifying their production and export structures. Diversification has usually been oriented toward petrochemical or energy-

intensive industries, but some diversification into trade-related services has occurred[4] (Appendix Tables A3 and A4).

Diversified Exporters

The diversified exporters comprise Egypt, Jordan, Morocco, the Syrian Arab Republic, and Tunisia. These countries constitute the group of Arab middle-income countries, with per capita incomes ranging in 1989 from $1,640 for Jordan to $640 for Egypt, and they derive less than two thirds of their export earnings from their two main export product groups. While these countries have a wider-based production and export structure than the oil exporting countries, on average they still derive 53 percent of their export earnings from the two main export product groups. Non-oil exports include cotton, fresh and processed fruits and vegetables, fertilizer, textiles, clothing, and other manufactures. Tourism is an important source of earnings in countries such as Egypt, Morocco, and Tunisia. Inflows of remittances are another important source of earnings for these countries, a large share of which comes from countries other than countries of the Gulf Cooperation Council (GCC) (Appendix Tables A3 and A4).

Commodity Exporters

The commodity exporters derive two thirds or more of their export earnings from the export of one or two commodities. This group comprises Mauritania, Somalia, and Sudan, which export iron ore and fish, cotton and cattle, and cattle and bananas, respectively. They also constitute the group of Arab low-income countries, with per capita incomes in 1989 ranging from $500 in Mauritania to $170 in Somalia. These countries have had little success in diversifying their production and export structures (Appendix Tables A3 and A4).

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[4]The United Arab Emirates have built a significant re-export industry and diversified into petrochemicals, while Saudi Arabia, Kuwait, Libya, and Qatar have reduced their dependency on crude oil exports somewhat by downstream diversification into steel (Saudi Arabia and Qatar), petrochemicals (Saudi Arabia, Kuwait, and Libya), and chemicals (Qatar).

Domestic Policies

Significant differences exist among Arab countries with respect to their economic policies. Except for Algeria and Libya, most of the oil exporting countries maintain open trade and payments systems (Appendix Tables A5 and A6).[5] They have relatively low tariffs and do not impose significant barriers to international trade, except for some selective import licensing and some quantitative export restrictions to guarantee a sufficient domestic supply of certain basic goods. However, some of these countries protect their agricultural and petrochemical sectors through domestic subsidies and other support policies. With no payment restrictions on current or capital transactions, these countries are relatively well placed to attract foreign investment and, if it is profitable, to reduce their vulnerability to exogenous shocks by investing abroad. A disincentive to non-oil exports in these countries is created by the "Dutch disease"—the relative overvaluation of the currency with respect to the competitiveness of non-oil sectors of the economy.[6] Greater export diversification could be expected if they seize the opportunity provided by "dynamic" comparative advantage. Over time, the cumulative effects of investment change a country's factor endowments, for example, more capital relative to labor, and more human capital (which could result from increased investment in education) relative to less skilled labor may change the products in which these countries have a comparative advantage.

Domestic economic policies have been a major impediment to exports of other Arab countries. In a number of these countries resource allocation is distorted by controls on prices, imports, exports, and foreign exchange. These policies are sometimes an attempt to deal with balance of payments difficulties resulting from

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[5]Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates have accepted the obligations under Article VIII of the Fund's Articles of Agreement.

[6]In a Ricardian world a lack of export diversification and the Dutch disease is not a problem; each country is always better off if it produces the product in which it has a comparative advantage. Concerns about fluctuations in income and a desire to minimize risk are the main reason that export diversification might be pursued.

expansionary financial policies. Traditional exports and the emergence of a more diversified export structure have been discouraged by inward-oriented policies, including overvalued and multiple exchange rates, import and export restrictions, and the maintenance of extensive government regulations and intervention in supply, production, and marketing (Appendix Table A6). In addition, Algeria and Libya, and all the diversified and commodity exporters impose payments restrictions on current and capital transactions (Appendix Table A5).

Government regulations in several Arab countries have been directed toward ensuring domestic availability of inputs and attaining self-sufficiency in certain agricultural products or industrial inputs.[7] These regulations are enforced by parastatal production and trading monopolies and seasonal or permanent export restrictions. In most Arab countries, governments have reserved certain traditional export activities to state enterprises; these sometimes take the form of trading monopolies and sometimes production monopolies.[8] These restrictions distort the allocation of resources and create entry barriers for potential exporters.[9]

Arab countries have also imposed various restrictions on inward foreign direct investment and other capital transactions. Together with the increased state participation in production and trade, this has led to foreign capital entering a country in the form of loans to the public sector rather than foreign direct investment. Given the

[7]For example, various oil exporting countries attempt to attain self-sufficiency in basic foodstuffs, while Egypt restricts cotton exports and pays below world market prices to producers to subsidize cotton for domestic manufacturers.

[8]Monopolies apply to almost all principal exports of Arab countries, such as hydrocarbons from oil exporting countries and minerals from Morocco, Mauritania, and Jordan. They are also maintained in the oil sector, mainly for national security and fiscal revenue purposes.

[9]Algeria is an example of a country that has reversed export diversification partly as a result of government regulations. In the 1960s, it was a major exporter of agricultural products, but by 1988 agricultural exports comprised only 0.35 percent of total exports. Algeria's experience may also be explained by the Dutch disease phenomenon; with the oil booms of the 1970s, the expanding resource sector led to a contraction of the manufacturing sector through a loss of "competitiveness" caused by the appreciation of the real exchange rate.

relatively low efficiency of resource use in the public sector, these policies have tended to exacerbate foreign exchange problems in the form of debt accumulation and debt service problems (Appendix Tables A7 and A8).

Most of the diversified exporters have begun to liberalize their trade systems, although mostly by reducing government control rather than by moving toward a more neutral incentive structure. The paper by Thalwitz and Havrylyshyn (Chapter 3) suggests that this liberalization is partly responsible for increased non-oil exports, including manufacturing exports, during the 1980s. The move toward more outward-oriented policies, together with the more diversified structure of these economies would appear to explain in part the relatively better performance of these countries compared with other Arab countries during the 1980s.

IV. Industrial Countries' Trade and Trade-Related Policies

Industrial countries protect both their industrial and agricultural sectors through a variety of border and nonborder measures. The specific types of measures used to protect industry are summarized in Table 1, and the main agricultural support measures are summarized in Table 2. The impact of these policies on developing countries has been examined in two sets of papers prepared by the IMF and the World Bank.[10] These papers have found that protective measures used by industrial countries tend to affect the exports of developing countries disproportionately, but that among developing countries, exports of the newly industrialized economies are most directly affected. This section attempts to identify the extent to which these

[10] *The Impact of the Industrial Policies of Developed Countries on Developing Countries*, Prepared by the staffs of the World Bank and the International Monetary Fund for the Development Committee, Development Committee Pamphlet No. 20 (Washington, March 1989); and "The Effect of Industrial Countries' Trade, Agricultural, and Industrial Policies on Developing Countries," in *Development Issues: Presentations to the 41st Meeting of the Development Committee*, Development Committee Pamphlet No. 27 (Washington, April 30, 1991), pp. 56–77.

Table 1. Industrial Policies

Domestic Measures	Trade Measures
Subsidies	Tariffs
Cash transfers	Peaks[1]
Research and development funding	Escalation[2]
Tax concessions	Nontariff barriers
Loan guarantees and insurance	Import quotas
Subsidized credits	Voluntary export restraints (VERs)[3]
Capital grants	Tariff quotas[4]
Regional aids	Discretionary and nondiscretionary import licensing
Government procurement	Countervailing and antidumping investigations and duties[5]
National product standards	Health standards
Commodity-specific indirect taxation	Export subsidies

Source: Reproduced from Development Committee, Pamphlet No. 20 (1989), p. 6.

[1]High tariffs on selected products in a structure with otherwise low tariff rates.

[2]Progressively higher tariffs within a product category as the level of processing and value added increases.

[3]Bilaterally agreed measures to restrain export, such as orderly marketing arrangements and export management rules. VERs can be government-to-government, government-to-industry, or industry-to-industry arrangements. The distinction between different forms of VER is largely legal and terminological and has little if any bearing on their economic impact.

[4]Higher tariffs after a specified level of imports is reached.

[5]Duties equivalent to subsidy and dumping margins, respectively, on imported products.

policies of industrial countries affect Arab countries. In addition to specific impediments to trade erected by industrial countries, the economic embargo imposed by the United States on Libya since 1986 has prevented access to the U.S. market by Libya for its exports and restricts Libya's access to U.S. technology and investment.[11]

Industrial Policies

Industrial countries use a variety of measures to protect their industrial sectors. These measures include tariff peaks, tariff escalation, voluntary export restraints (VERs), the use of countervailing duties (CVDs) and antidumping duties (ADDs), and domestic subsi-

[11]Iraq has been subject to an embargo since August 1990.

Table 2. Summary of Main Agricultural Support Policies[1]

1. Market price support

Restricts the quantities or increases the price of commodities entering domestic market. Requires border measures, which are often supplemented by domestic measures and by diverting excess production to world market using export subsidies.

(a) Border measures

Import prohibitions and quotas, voluntary export restraints (VERs), tariff quotas, tariffs, variable levies (e.g., European Community (EC)), state trading arrangements (e.g., Japan), and unsubstantiated sanitary and phytosanitary standards. Export subsidies (e.g., export restitution in EC, and Export Enhancement Program and marketing loans in the United States).

(b) Domestic measures

Market intervention purchases: Commodity Credit Corporation (CCC) inventory and loan operations—United States; Common Agricultural Policy (CAP) intervention purchases—EC. Livestock Industry Promotion Corporation (LIPC) operations—Japan.

Supply control policies: set asides—United States and EC; land division programs—Japan; production quotas—United States, EC, and Japan.

2. Direct income support

Raises price and/or income received by producer without affecting domestic selling price. The most common are those related to production levels; see (a) below.

(a) Production subsidies

Commonly called deficiency payments, which are generally the difference between a target or guide price and the market price—United States, EC, and Japan.

(b) Income support or payments under supply reduction programs.

(c) Income support unrelated to production, regional, and welfare payments.

3. Other support

Includes subsidies that reduce cost of inputs, including credit, or of marketing products, or income tax exemptions; as well as government spending on infrastructure and research and development.

[1]Reproduced from Development Committee, *Development Issues: Presentations to the 41st Meeting of the Development Committee*, Pamphlet No. 27 (Washington, April 30, 1991), p. 69.

dies.[12] Sectors affected by these measures include textiles and clothing (tariff peaks and tariff escalation, VERs and other nontariff restrictions), steel (VERs, subsidies, ADDs, and CVDs), leather products and footwear (tariff peaks and escalation, VERs and other nontariff barriers), petrochemicals (tariff escalation and ADDs), machine tools and electronic products (VERs and ADDs), and coal (domestic subsidies and nontariff measures).[13] This section examines the extent to which tariff peaks and escalation and nontariff measures affect Arab countries' exports.[14]

About 50 percent of world trade in *textiles and clothing* is managed under various bilateral restraints concluded under the Multifibre Arrangement (MFA), which limits access to industrial country markets. The coverage and restrictiveness of restraints in this sector have been increased since the first VER was negotiated between the United States and Japan in the 1950s (Table 3). Textiles and clothing are also subject to tariff peaks and escalation in industrial countries. These restrictions impede the expansion in output and exports of efficient producers, tend to divert production and trade from restrained exporters to unrestrained exporters, maintain access levels for less efficient producers, and tend to increase world market prices above what they would be without such restrictions. Among Arab countries, Morocco, Egypt, Jordan, Syria, Tunisia, and the United Arab Emirates produce textiles and clothing. Egypt's exports to the United States are covered by the MFA, the exports of both Morocco and Tunisia to the EC are covered by VERs, and the United Arab Emirates' exports to both the United States and Canada are covered by VERs. In some cases the use of quantitative limits under VERs is low, implying that such restrictions are not, at this stage, a binding constraint.

[12] While CVDs and ADDs are intended as a remedy against "unfair" trading practices of other countries (such as subsidies and dumping), they are often used to harass foreign exporters and to protect domestic producers from "fair" competition.

[13] Protection of the coal sector in Germany and Spain (through domestic subsidies and quantitative import restrictions) may affect Arab countries' oil exports.

[14] In addition to measures described below, Egypt, Saudi Arabia, and the United Arab Emirates have been targeted under the "Special 301" of the U.S. 1988 Trade Bill for violation of intellectual property rights.

Currently about one third of world trade in *steel* is managed by various voluntary restraint arrangements. Requests for antidumping and countervailing duties are also frequent and subsidies are provided by some countries. Slightly more than 50 percent of the steel imports of industrial countries are subject to nontariff barriers. VERs cover imports into the United States from 19 countries and the EC, although most of these restraints are not binding.[15] The EC currently has VERs covering imports mainly from Eastern Europe and Brazil. Other EC imports are subject to a floor price mechanism; imports below the floor price can trigger antidumping action.[16] In the EC, subsidies in the steel sector are permitted only for restructuring to reduce capacity; while operating subsidies are prohibited and the Commission is enforcing EC competition policy more strictly as part of the EC 1992 program, some member states continue to provide such subsidies. In addition, regional subsidies, which are permitted under EC competition rules, may indirectly protect the EC steel industry.

Among Arab countries, Algeria, Egypt, Morocco, Qatar, and Saudi Arabia produce and export steel products. These exporters have by and large not been subject to nontariff measures in industrial countries. In 1988, the EC applied antidumping duties of 25 percent to imports from Algeria and Morocco; exports of wire rods from Egypt were investigated for dumping in 1990. Imports of specialized steel products from Saudi Arabia have been subject to countervailing duties of 3 percent in the United States since 1985.

In the *petrochemical industry*, tariff escalation is the major barrier faced by Arab countries (Table 4). In the past, petrochemical prod-

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[15]The United States initially imposed VERs in 1984 in the wake of a huge number of requests for countervailing duties lodged by the iron and steel industry. In 1989 when the VERs were to expire, President Bush announced the U.S. steel liberalization program; this involved extension of the VERs with 19 individual countries to March 1992 and the initiation of multilateral negotiations to prohibit most subsidies, eliminate or reduce tariffs, and establish a dispute settlement mechanism. The U.S. Administration has indicated that the VERs will not be renewed even if agreement on the International Steel Consensus has not been reached.

[16]The EC is involved in the International Steel Consensus negotiations with the United States and several other countries.

Table 3. Textiles and Clothing: Nontariff Barriers to Trade

Period	Agreement	Outcome
1957–62	Japanese VER with United States	Restricted export of cotton, textiles, and apparel.
1961	"Short-term agreement" (STA) (19 countries)	Importing country allowed to impose a quota unilaterally if exporting country does not provide an acceptable proposal of VER.
1962–73	"Long-term agreement" (LTA) (19 countries)	Renewal of STA plus restrictions on cotton textiles must be compatible with annual export growth of at least 5 percent for each exporting country.
1971	Japan, Hong Kong, Taiwan Province of China, and Republic of Korea voluntarily restrain their exports to United States	Combined restrictions from LTA and additional country-specific VERs restrict U.S. imports from a total of 37 countries.
1974–77	MFA I	Bilateral agreements; more fibers subject to restraints; 6 percent annual export growth is allowed.
1978–81	MFA II	Further restrictions and entry of European countries into the agreement.
1982–86	MFA III	New restrictions with unilateral quotas allowed in some cases.
1986–91	MFA IV	Agreement expanded to include silk blends and vegetable fibers.

Source: Linda Goldberg and Janusz Ordover, *Obstacles to Trade and Competition* (Paris: Organization for Economic Cooperation and Development, forthcoming 1992).

ucts have been targeted by antidumping duties in industrial countries.[17] Three of the cases during the 1980s involved exports from Arab countries—Kuwait, Libya, and Saudi Arabia: following an investigation of seven exporters to the EC market, Kuwait, along

[17]During 1980–84 there were 21 antidumping cases in the United States and 77 in the EC. As the industry underwent restructuring in these countries the number of antidumping cases dropped to 20 during 1985–87. More recently, in January 1991, Australia levied provisional antidumping duties of 11 percent on imports of low-density polyethylene (LDPE) from Qatar.

Table 4. Most-Favored-Nation Tariff Rates in EC, Japan, and United States for Selected Petrochemicals, 1988
(*In percent*)

Product	Processing Stage	EC	Japan	United States
Ethylene, propylene butylene, and butadine	Primary	...[1]	5.8	...
Methanol	Primary	13.0	4.9	18.0
Toluene and benzene	Primary	...	3.7	...
Acetic acid	Secondary	16.8	3.0	1.8
Butanols	Secondary	6.6	10.5	8.8
Diethylene glycol	Secondary	8.0	7.2	12.3
Monoethylene glycol	Secondary	13.0	12.0	12.0
Polupropylene	Secondary	12.5	17.0[2]	12.5
Styrene	Secondary	6.8	8.0	7.4
ABS plastics	Tertiary	12.5	4.6	9.4[3]
Ethyl acetate	Tertiary	11.5	5.6	3.7
Polyvinyl acetate	Tertiary	12.0	5.8	4.0
Polyvinyl chloride (PVC)	Tertiary	12.5	4.6	10.1
Vinyl acetate	Tertiary	11.5	5.6	3.8

Source: Commission of the European Communities.
[1]Zero or insignificant.
[2]Approximate. The rate is ¥32 a kilogram.
[3]Approximate. The rate is $0.7 a kilogram.

with five other exporting countries, agreed to a minimum price undertaking on urea exports to the EC; Saudi Arabia and Libya did not agree to the price undertaking, and an antidumping duty of 46 percent was imposed on EC imports from Saudi Arabia and a slightly lower duty on imports from Libya.[18] In June 1991, the European Court of Justice ruled that these duties should be annulled on the grounds that the defendants were denied access to information, which deprived them of a fair trial.

Partly in response to actual and potential access barriers in industrial countries, some petrochemical producers have diversified into offshore refining and distribution facilities. Such diversification provides a secure outlet to oil producers for some or all of their output and a hedge against protectionist measures on refined and petro-

[18]These duties covered 11 percent of Saudi Arabia's 1986 exports of petrochemicals to the EC. The price undertaking given by Kuwait covered 46 percent of its petrochemical exports to the EC.

chemical products in importing countries. In addition, it provides a hedge against fluctuating prices.[19]

Agricultural Policies

Industrial countries support their agricultural sectors (including fisheries and livestock) through various border and nonborder measures. *Market price support* schemes comprise about 80 percent of the total support provided. These schemes are supplemented by extensive *border measures* (quantitative restrictions, variable import levies, and import control by state trading entities) and by *domestic measures* (intervention purchases and supply control measures). Intervention purchases remove production from the domestic market, which is often exported later with *export subsidies. Direct income supports* and *sanitary and phytosanitary standards* in some cases also protect agriculture.

In 1990, support measures in countries of the Organization for Economic Cooperation and Development (OECD) amounted to some 2.0 percent of their GDP, ranging from 0.2 percent in Australia and New Zealand and to 4.1 percent in Norway (Table 5). The producer subsidy equivalent (PSE) of these measures ranged from low levels in Australia and New Zealand to extremely high levels in Japan, the Nordic countries, and Switzerland (Table 6).[20] In general, the countries with the highest supports tend to be the least efficient producers.

The agricultural policies of industrial countries result in reduced access for agricultural exporters to industrial countries' and third-country markets and lower world market prices. The precise impact of these measures on particular countries depends on the structure

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[19]Crude oil prices normally fall (and rise) more rapidly than prices of refined and petrochemical products. Thus, when oil prices, and therefore petrochemical feedstocks (oil and natural gas) are low, offshore production and distribution investments are relatively profitable, particularly since the cost of transporting oil is relatively low compared with the cost of transporting petrochemicals.

[20]The producer subsidy equivalent (PSE) of support policies is the transfer that would be needed to replace these policies and leave the producer no worse off. PSEs are expressed in net terms for some products (such as beef), as the costs of their inputs are inflated because of other support policies, and this effect is netted out.

Table 5. Support Measures Associated with Agricultural Policies
(In percent of GDP)

	1979–81 Average	1983–85 Average	1986	1987	1988	1989	1990 Estimate
Australia	0.4	0.5	0.5	0.3	0.2	0.2	0.2
Austria	1.7	2.6	2.8	3.2	2.7	2.2	2.4
Canada	0.9	1.7	2.2	2.2	1.9	1.4	1.4
EC-12[1]	1.6	2.5	2.9	2.8	2.5	2.1	2.2
Finland	...	...	6.8	4.9	4.8	4.3	4.3
Japan	1.7	2.8	2.8	2.8	2.4	2.3	2.1
New Zealand	0.8	2.0	3.8	0.3	0.5	0.3	0.2
Norway	...	...	3.9	4.0	3.9	3.6	4.1
Sweden	...	...	2.6	1.9	1.6	1.6	1.5
Switzerland	...	...	3.2	3.2	3.1	2.9	2.8
United States	0.8	1.9	2.1	1.8	1.4	1.4	1.3
Average OECD[2]	1.3	2.2	2.5	2.4	2.1	1.8	1.9

Sources: Organization for Economic Cooperation and Development, *Agricultural Policies, Markets and Trade: Monitoring and Outlook* (Paris: OECD), various issues; and International Monetary Fund, *International Financial Statistics* (Washington: IMF), various issues.

[1]EC-10 prior to 1986. Total transfers of EC-10 in 1986 were $97.7 billion and 3 percent of their GDP.

[2]Total transfers of OECD countries divided by GDP of OECD.

Table 6. Net Producer Subsidy Equivalents[1]
(In percent of total value of production)[2]

	1979-81 Average	1983–85 Average	1986	1987	1988	1989	1990 Estimate
Australia	9	14	16	11	9	10	11
Austria	36	37	49	48	47	39	46
Canada	24	33	49	49	42	37	41
EC-12[3]	37	35	50	49	46	41	48
Finland	...	...	68	72	73	70	72
Japan	57	65	75	76	74	71	68
New Zealand	18	24	33	14	75	5	5
Norway	...	...	76	76	76	75	77
Sweden	...	...	60	57	52	52	59
Switzerland	...	...	80	80	78	73	78
United States	16	25	42	41	34	29	30
Total	29	34	51	50	46	41	44

Source: Organization for Economic Cooperation and Development, *Agricultural Policies, Markets and Trade: Monitoring Outlook* (Paris: OECD), various issues.

[1]See footnote 20 in text.

[2]Total value of production valued at internal prices.

[3]EC-10 prior to 1986. The net PSE for EC-10 in 1986 was 52 percent.

and size of the agricultural sector and on whether the country is an actual (or potential) net exporter or a net importer of agricultural and food products. Among the Arab countries, most of the diversified exporters and commodity exporters produce and export agricultural fisheries or livestock products. With few exceptions, the oil exporting Arab countries do not have the potential to produce and export agricultural products efficiently.[21] As net food importers, the oil exporting Arab countries tend to benefit from the agricultural policies of industrial countries owing to lower world prices. The diversified exporters' access to industrial country markets in some products is restricted, and they receive lower world prices for some of their exports owing to the policies of industrial countries. For example, Morocco faces restrictions in the EC on fresh fruit and vegetables and Tunisia on oranges, potatoes, dates, and olive oil; Egypt faces tariff quotas in the EC on onions; and Jordan faces restrictions on citrus fruit. Algeria, which is classified as an oil exporter, and Tunisia face restrictions on wine exports. The commodity exporters export only limited agricultural products to industrial countries (Somalia exports bananas to Italy) and do not face any tariff or nontariff barriers on their agricultural trade except for some health and sanitary regulations. Somalia and Sudan export cattle primarily to other Arab countries, which also have health and phytosanitary regulations that may affect these exports.

Studies on the impact of agricultural trade liberalization by industrial countries show that the agricultural trade balance of the *non-oil exporting* Middle East and North African countries (which mainly include the Arab countries classified as diversified and commodity exporters) would improve. Egypt would stand to experience a particularly significant improvement in its agricultural trade balance provided it removed the far-reaching distortions in its own economy and passed through the increase in world market prices to domestic producers. The agricultural trade balance of *oil exporting countries* in the Middle East and North Africa would deteriorate owing to higher

[21]Saudi Arabia produces and exports wheat using fossil water pumped from under the desert, which will eventually run out; farmers currently receive several times the world market price for wheat.

Algeria previously exported significant quantities of agricultural products including wheat.

world prices.[22] Part of this deterioration might be offset, because higher growth related to the reallocation of resources in industrial countries as a result of liberalizing agricultural policies would likely increase the demand for goods and services produced by oil exporting countries. More generally, a substantial reduction in agricultural subsidies in industrial countries would alleviate the potential ex ante global savings shortage and pressures on world interest rates, with positive effects on investment and growth prospects in non-oil Arab countries.

Preferential Treatment

Most Arab countries benefit from the Generalized System of Preferences (GSP) provided by industrial countries to developing countries in the form of reduced or zero tariffs (Tables 7 and 8). The lower-income countries (Mauritania, Somalia, and Sudan) benefit from additional preferential treatment as least developed countries

Table 7. Trade Preferences for Arab Countries

	GSP					
Recipient Countries	EC	U.S.	Japan[1]	ACP	Maghreb and Mashreq	Least Developed Countries
Algeria	x		x		x	
Bahrain	x	[2]	x			
Egypt	x	x	x		x	
Jordan	x	x	x		x	
Kuwait	x		x			
Libya	x		x			
Mauritania	x	x	x	x		x
Morocco	x	x	x		x	
Oman	x	x	x			
Qatar	x		x			
Saudi Arabia	x		x			
Somalia	x	x	x	x		x
Sudan	x	x	x	x		x
Syrian Arab Republic	x	x	x		x	
Tunisia	x	x	x		x	
United Arab Emirates	x		x			

[1]Japan has no mechanism by which countries can be removed from the list of GSP recipient countries.
[2]Was removed in 1968; will be granted GSP status shortly.

[22]See, for example, studies reported in *Agricultural Trade Liberalization: Implications for Developing Countries*, ed. by Ian Goldin and Odin Knudsen (Paris: Organization for Economic Cooperation and Development, 1990), p. 173.

Table 8. Trade Preference Hierarchy of Arab Countries[1]

ACP, Least Developed, GSP	Mauritania, Somalia, Sudan
Maghreb, GSP	Algeria, Morocco, Tunisia
Mashreq, GSP	Egypt, Jordan, Syria
GSP	Bahrain, Libya, Oman, Qatar, Saudi Arabia, United Arab Emirates

[1]Based on the number of tariff lines benefiting from tariff concessions or absence of quantitative restrictions. The hierarchy does not necessarily reflect the relevance of the concessions for the Arab countries.

and, in the case of the EC, by their status as ACP (African, Caribbean, and Pacific) countries under the Lomé Convention. Close to 100 percent of imports from ACP countries enter the EC duty free, and only a limited number of products face quantitative restrictions. Additional preferential treatment is also provided by the EC to Maghreb (Algeria, Morocco, and Tunisia) and Mashreq (Syria, Jordan, and Egypt) countries, but "sensitive" products tend to be subject to quantitative restrictions (which vary with seasons) and minimum prices.[23]

Under most GSP schemes, "sensitive" items such as textiles, clothing, and footwear are excluded, whereas others, such as petrochemicals, receive only limited coverage.[24] The coverage of agricul-

[23]The GCC countries, which comprise Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates, are currently involved in negotiating a free trade agreement with the EC, which would affect their market access in petrochemicals, in particular.

[24]The GSP schemes of the EC, Japan, and the United States differ in country and product coverage. For example, refined oil products such as gasoline and jet fuel oil enter the EC duty free, as do most first-stage processing products based on oil or natural gas. About 5 percent of the EC's annual consumption of other petrochemicals is imported. Most of these imports enter duty free under free trade or preferential agreements with countries of the European Free Trade Association (EFTA) or the Mediterranean; part of the remainder is imported from the GCC countries, subject to GSP ceilings or tariff quotas or to MFN tariff rates. Japan's GSP scheme, by contrast, does not include refined oil products or petroleum gases, but for many petrochemical products such as methanol about 10 percent of imports of each product is distributed on a first-come, first-served basis. The U.S. scheme excludes members of the Organization of Petroleum Exporting Countries (OPEC) (except for Ecuador, Indonesia, and Venezuela) and countries with more than a specified per capita income. Petrochemicals, however, are generally included and are given duty-free access subject to certain product graduation requirements.

tural products is selective and concessions normally consist of duty reductions rather than exemptions.[25] In some countries, developing countries are graduated out of GSP schemes on certain products if their per capita income exceeds specified limits (for example, the United States and New Zealand) and/or their share of specific sector imports in the preference-giving country exceeds specified percentages (for example, the EC).

The preferential treatment received by Arab countries in the EC is reflected in their trade patterns. Diversified Arab exporters, which receive the largest preferences, ship half of their exports to the EC, against one fourth for other Arab countries. These countries would probably lose from an extension of EC preferential treatment to other non-Arab countries or a Uruguay Round agreement. Some Arab countries also benefit from financial and technical assistance not available to GSP countries. The ACP, Maghreb, and Mashreq agreements provide funds for trade financing and financial and technical cooperation. The agreements also provide incentives to promote investment.

While Arab countries benefit from preferential access to industrial country markets, the preferential arrangements among industrial countries, such as those among EC and EFTA members and the U.S.-Canada Free Trade Agreement, often outweigh preferences extended by industrial countries to developing countries.

V. Conclusions and Prospects

The relatively poor performance of output and exports of Arab countries during the 1980s, compared with other developing countries, reflects a combination of factors: external economic developments, their natural resource endowments and demographic and climatic conditions, and their own domestic economic policies. Although actual and potential access barriers to industrial countries affected the economic performance of Arab countries, they do not appear to be the major factor in their relatively poor performance.

[25]The EC's GSP scheme covers 23 agricultural products, including 8 products subject to variable levies under the Common Agricultural Policy (CAP); for the latter the preference takes a 50 percent reduction in the variable levy, within overall quotas.

The Arab countries most directly affected by industrial countries' trade policies appear to be those that are actual or potential net exporters of agricultural products and exporters of textiles and clothing. The paper by Mamdouh (Chapter 5) examines the potential for the Uruguay Round to reduce or eliminate restrictions currently faced by Arab countries in industrial countries.

Future prospects for Arab countries depend not only on industrial countries' trade policies but also more generally on their economic performance as well as that of the non-oil developing countries, and on the domestic policies of Arab countries. The *World Economic Outlook* (*WEO*) of October 1991 indicates that the growth of output and exports is expected to decline in both industrial and developing countries in 1991 but to strengthen somewhat (except in Eastern Europe and the former U.S.S.R.) in 1992, reflecting the end of uncertainties in the Middle East, the decline in oil prices, and sharply lower interest rates in some countries. For the medium term, the prospect for a continuing expansion of output (and low inflation) in industrial countries is dependent on the adoption of appropriate policies. Such policies involve a resumption of fiscal consolidation and further action on the structural front to reduce distortions and improve efficiency, particularly in the areas of labor markets and international trade.

A successful conclusion to the Uruguay Round and other multilateral trade negotiations in progress would have a sizable impact on Arab countries. It would provide increased and more *secure* access to foreign markets in both goods and services. For oil exporting countries that are likely to have net outflows of FDI and to export financial services, a successful outcome to the negotiations on trade-related investment measures (TRIMS) and financial services is of particular importance to ensure that barriers in these areas do not impede the official allocation of capital. In addition, a reduction in tariff and nontariff barriers by industrial countries and other major importing countries would provide a one-time boost to growth in these countries with flow-on effects for most Arab countries.[26] To

[26] For example, results reported in the October 1990 *WEO* suggest that the elimination of all tariff and nontariff barriers by industrial countries could raise both exports and imports of these countries by at least 5 percent; a 50 percent reduction in such barriers in the United States, the EC, and the Asia-Pacific region would raise GDP in these three regions by 5 percent.

the extent that industrial countries' restrictive trade policies have limited growth in non-oil developing countries, the successful conclusion of the Uruguay Round would provide a basis for stronger growth in both industrial and non-oil developing countries. A broad-based recovery in the non-oil world would provide new opportunities for foreign direct investment from oil exporting Arab countries.

The positive consequences of freer trade and renewed growth in the world economy will depend on the domestic policies of the Arab countries, the area over which the Arab countries have the greatest control. In oil exporting countries, the oil sector is one of the few sectors that has a comparative advantage at present exchange rates. The maintenance of open trade and payments systems and cautious financial policies should generate surpluses in those countries that can be invested abroad. Over time, the cumulative effects of investment, including in human capital, may change the products in which these countries have a comparative advantage and provide the foundation for increased growth and a more diversified export base. For the diversified exporters, the liberalization of trade and payments and other structural reforms already under way, and associated macroeconomic and exchange rate policies would best support further efficient diversification of exports of goods and services and hence sustainable growth. The commodity exporters will need to eliminate or liberalize major domestic policy distortions to benefit from the positive effects of increased world growth and trade. High-population countries need to ensure that they provide an attractive climate for foreign investment. In addition to sound domestic policies, the elimination of trade-related investment measures in these countries and the protection of intellectual property rights would do much to foster such investment. These countries do not need to await the conclusion of the Uruguay Round to address these areas and to implement sound fiscal, monetary, and financial policies.

Appendix

Table A1. Trade Shares by Country and Region, 1980, 1985, and 1989
(*Percentage points*)[1]

	Share of Total Developing Country Exports[2]			Share of Developing Country Exports in Total Imports			Share of World GDP		
	1980	1985	1989	1980	1985	1989	1980	1985	1989
Industrial Countries	68.7	61.4	62.4	31.2	24.1	22.5	67.6	69.7	73.0
United States	19.6	21.6	22.6	48.6	33.5	37.7	23.1	31.3	25.2
Japan	13.8	13.0	12.3	65.4	57.6	49.8	9.1	10.4	14.8
European Community (EC)	29.2	22.3	22.2	24.4	18.1	15.1	26.9	19.9	24.8
Other industrial	6.1	4.6	5.3	15.7	10.2	11.6	8.4	8.0	8.1
Developing Countries[2]	25.5	32.8	32.9	31.9	34.1	34.1	22.4	21.4	18.5
High-income oil exporters	8.5	8.9	5.0	23.5	28.4	22.1	2.7	2.9	1.9
Other developing	17.0	23.9	28.0	33.2	34.9	35.6	19.6	18.4	16.6
Others[3]	5.8	5.8	4.7	30.2	19.3	18.6	10.1	9.0	8.6
Total	100.0	100.0	100.0				100.0	100.0	100.0
Average				31.3	26.2	25.0			

Sources: Trade: United Nations Trade Matrix System; International Monetary Fund, *Direction of Trade*. GDP: World Bank, International Economics Department.

[1]Shares based on trade and GDP measures in current U.S. dollars.

[2]Excluding nonmember and nonreporting countries (World Bank definition).

[3]Bulgaria, Czechoslovakia, former German Democratic Republic, and former U.S.S.R.

Table A2. Arab Countries: Export Shares by Region, 1990
(In percent)

	Industrial Countries					
	Total	United States	Japan	EC	Other	Developing and Other Countries
Oil Exporters						
Algeria	88.8	21.0	1.2	63.2	3.4	11.2
Bahrain	23.8	6.4	12.3	2.5	2.6	76.2[1]
Kuwait	54.7	7.4	20.2	26.0	1.1	45.3
Libya	89.5	—	—	84.7	4.8	10.5
Oman	50.1	5.7	35.0	3.5	5.9	49.9
Qatar	64.8	1.6	60.4	2.3	0.5	35.2
Saudi Arabia	63.3	24.0	19.0	17.7	2.6	36.7
United Arab Emirates[2]	48.6	3.6	34.7	7.8	2.5	51.4
Diversified Exporters						
Egypt	67.7	8.1	2.2	54.6	2.8	32.3
Jordan	6.4	0.6	2.1	3.6	0.1	93.6[3]
Morocco	77.3	2.2	4.6	66.9	3.6	22.7
Syrian Arab Republic	38.0	1.1	0.1	34.7	2.1	62.0
Tunisia	79.3	1.0	0.3	77.2	0.8	20.7
Commodity Exporters						
Mauritania	77.6	4.5	22.3	50.8	—	22.4
Somalia	42.3	—	0.3	38.3	3.7	57.7
Sudan	46.9	2.7	5.9	37.3	1.0	53.1

Source: International Monetary Fund, *Direction of Trade*.

[1]Bahrain exports a relatively high percentage of manufactured goods to neighboring countries, in particular, Saudi Arabia.

[2]Including re-exports.

[3]Jordan's main export markets are Asia and Eastern Europe for fertilizers and minerals and Arab countries for fruits and vegetables. Also includes re-exports.

Table A3. Arab Countries: Export Indicators

	Hydrocarbons as Percent of Total Exports	Main Two Product Groups as Percent of Total Exports	Main Export Product[1]	Secondary Export Product[2]	Average Export Value Growth (U.S. dollars, 1985–90)		Terms of Trade Average Change Percentage Growth 1980–90
					Traditional Exports	Non-traditional Exports	
Oil Exporters							
Algeria	95	96	oil	—	−16.7	25.0	−4.8
Bahrain	...	...	oil	—	−9.0	42.3	0.5
Kuwait	90	92	oil	—	−10.3	−3.4	−6.0
Libya	99	100	oil	—	−20.6	—[3]	−7.7
Oman	95	97	oil	—	−13.5	1.1	−7.7
Qatar	81	88	oil	—	−17.7	17.0	−7.1
Saudi Arabia	83	87	oil	—	−8.0	40.1	−6.4
United Arab Emirates	78	80	oil	re-exports	−11.2	14.0	−3.6
Diversified Exporters							
Egypt	41	63	oil	cotton	−8.2	64.8	−2.0
Jordan	—	40	phosphates	fertilizer	7.1	2.9	−0.6
Morocco	—	51	phosphates	citrus fruit	−7.3	16.7	−2.5
Syrian Arab Republic	51	70	oil	textiles	−11.3	26.3	−12.8
Tunisia	20	40	oil	fertilizer	−9.1	28.6	−0.6
Commodity Exporters							
Mauritania	—	97	fish	iron ore	−4.7	—[3]	1.4
Somalia[4]	—	74	cattle	bananas	−24.0	−9.6	−1.7
Sudan[5]	—	66	cotton	cattle	12.0	10.4	2.4

Sources: National authorities; IMF staff estimates.
[1]Oil exports include refined products.
[2]Less than 5 percent of total exports for all oil exporters except United Arab Emirates.
[3]Less than 3 percent of total exports.
[4]1986–88.
[5]1984/85–1987/88, fiscal-year basis.

Table A4. Arab Countries: Basic Indicators

	1989 GNP Per Capita (U.S. dollars)	Average Real GDP Growth, 1985–89	Average Consumer Price Inflation, 1985–89	Average Overall Fiscal Balance, 1985–89	Average Current Account Balance, 1985–89
		(Percent)		(Percent of GDP)	
Oil Exporters					
Algeria	2,230	1.4	9.1	−3.3	0.6
Bahrain	6,610[1]	0.9[2]	−1.0	−5.3	−5.7
Kuwait	16,150	...	1.0	...	24.5
Libya	5,310	−3.1	0.2	−14.7	−1.7
Oman	5,220	−4.1	−6.6	−4.8	−0.7
Qatar	14,500[3]	0.6[4]	3.3	−15.0	0.3
Saudi Arabia	6,020	0.2	−1.3	−19.9	...
United Arab Emirates	18,430	−5.5	4.0	−10.9	15.6
Diversified Exporters					
Egypt	640	5.4	19.0	−18.9	−10.4
Jordan	1,640	−0.1	1.9	−12.5	−4.5
Morocco	880	4.8	4.9	−6.1[5]	−3.0
Syrian Arab Republic	980	2.4	31.8	−4.6	−0.3
Tunisia	1,260	2.9	7.4	−4.2	−3.7
Commodity Exporters					
Mauritania	500	3.2	9.4	−2.1	−10.1
Somalia	170	3.0	48.8	−9.4	−11.5
Sudan[6]	330	−0.1	34.7	−13.3	−9.2

Sources: World Bank, *World Development Report, 1991*; national authorities; and IMF staff estimates.
[1] 1987.
[2] Average 1985–88.
[3] 1988.
[4] Non-oil GDP.
[5] In percent of GNP.
[6] 1984/85–1988/89, fiscal-year basis.

Table A5. Arab Countries: Summary Features of Exchange and Trade System as of December 31, 1990

	Oil Exporters								Diversified Exporters					Commodity Exporters		
	Algeria	Bahrain	Kuwait	Libya	Oman	Qatar	Saudi Arabia	United Arab Emirates	Egypt	Jordan	Morocco	Syria	Tunisia	Muritania	Somalia	Sudan
Acceptance of Article status																
Article VIII		x	x		x	x	x	x								
Article XIV	x			x					x	x	x	x	x	x	x	x
Exchange arrangements																
Exchange rate determined on the basis of																
A peg	x		x	x	x					x	x	x				x
Limited flexibility with respect to single currency		x				x	x	x								
More flexible arrangements:																
Adjusted according to set of indicators																
Other managed floating									x				x	x	x	
Separate exchange rate(s) for some or all capital transactions and/or some or all invisibles									x			x			x	
More than one rate for imports									x			x			x	x
More than one rate for exports									x						x	x
Import rate(s) different from export rates									x			x			x	x
Payment arrears									x			x			x	x
Bilateral payments arrangements	x								x		x	x			x	x
Payments restrictions																
Restrictions on payments for current transactions	x			x					x	x	x	x	x	x	x	x
Restrictions on payments for capital transactions	x			x					x	x	x	x	x	x	x	x
Cost-related import restrictions																
Import surcharges				x					x	x		x			x	x
Advance import deposits				x					x	x		x			x	x
Surrender or repatriation requirement for export proceeds	x			x					x	x	x	x	x	x	x	x

Source: International Monetary Fund, *Annual Report on Exchange Arrangements and Exchange Restrictions, 1991*.

Table A6. Arab Countries: Trade Restrictions

	Imports[1]			Exports			
	Nonautomatic import licenses	Import prohibitions for protection reasons	Import monopolies	Export licenses	Foreign exchange surrender requirement	QRs for domestic supply reasons	Export monopolies
Oil Exporters							
Algeria	x	x	x	x	x		x
Bahrain	x		x				
Kuwait	x					x	
Libya	x	x	x	x	x	x	
Oman	x	x				x	
Qatar							
Saudi Arabia						x	
United Arab Emirates	x						
Diversified Exporters							
Egypt		x	x		x	x	x
Jordan	x	x			x		
Morocco	x		x	x	x		x
Syrian Arab Republic	x	x	x	x	x	x	x
Tunisia	x		x	x	x		x
Commodity Exporters							
Mauritania	x		x	x	x		x
Somalia	x		x	x	x		x
Sudan	x	x		x	x		x

Source: International Monetary Fund, *Annual Report on Exchange Arrangements and Exchange Restrictions, 1991.*
[1]Does not include import restrictions for health, cultural, or political reasons.

Table A7. Arab Countries: Capital Transactions and Debt Indicators

	Net Foreign Investment,[1] 1985–89 Average (*In percent of GDP*)	Foreign Debt Outstanding, End–1989[2] (*In percent of GDP*)	Debt Service Due, 1985–89 Average (*In percent of exports*)[3]	Net Investment Income,[4] 1985–89 Average (*In percent of exports*)[3]	Foreign Reserves in Months of Imports,[5] End–1989
Oil Exporters					
Algeria	—	37.5	59.7	−21.7	1.1
Bahrain	−0.11[6]	...	...	0.3[6]	5.4
Kuwait	−2.40	...	—	76.7	4.6
Libya	...	...	—	2.6	8.9
Oman	1.32[6]	32.8	10.8[6]	−2.6[6]	28.0
Qatar	...	...	...	...	...
Saudi Arabia	8.47[6]	...	—	44.8[6]	7.6
United Arab Emirates	—	...	...	...	...
Diversified Exporters					
Egypt	1.93	56.6	32.7	−17.8	0.2
Jordan	0.50[6]	67.6	29.0[6]	−18.0[6]	2.5
Morocco	0.21	84.5	43.1	−30.4	1.2
Syrian Arab Republic	...	...	21.5	−14.9	0.8
Tunisia	1.11	56.0	24.2	−22.2	2.3
Commodity Exporters					
Mauritania	...	...	25.6	−19.2	1.6
Somalia	−0.25[6]	...	25.1	−11.2	0.5
Sudan	−0.02[6]	...	27.5	−24.5	...

Sources: World Bank, *World Development Report, 1991*; national authorities; and IMF staff estimates.

[1] Comprises inbound and outbound capital transactions between enterprises and investors, reflecting a lasting interest on the part of the investors.

[2] Excluding net credit from the IMF.

[3] Exports of goods and services.

[4] Covers income derived from the ownership of foreign financial assets, excluding the portfolio investor's portion of the earnings of incorporated enterprises that are not formally distributed.

[5] Includes monetary gold, SDRs, reserve position in the Fund, use of Fund credit, and claims on nonresidents available to the central authorities.

[6] 1985–87 average.

Table A8. Arab Countries: Debt Reschedulings, 1979–91

	Official	Private
Oil Exporters		
Algeria		
Bahrain		
Kuwait		
Libya		
Oman		
Qatar		
Saudi Arabia		
United Arab Emirates		
Diversified Exporters		
Egypt	1987, 1991	
Jordan	1989	1989
Morocco	1983, 1985, 1987, 1988, 1990	1990
Syrian Arab Republic		
Tunisia		
Commodity Exporters		
Mauritania	1985,1986,1987,1989	
Somalia	1985,1987	
Sudan	1979, 1982, 1983, 1984	1981, 1984, 1985

Source: Paris Club agreed minutes, bank debt restructuring agreements.

Comment

Mahmoud Sakbani[1]

The topic assigned to me to discuss is the impact of industrial countries' trade policies and trade-related policies on Arab countries. We have the paper prepared by Margaret Kelly and Bernhard Fritz-Krockow of the IMF as the basis for this discussion.

Let me start first by congratulating the authors on their thoughtful and well-conceived paper. I profited from their analyses and data. I do not find any major disagreement with the thrust of their paper, though I would put emphasis on different points, and I believe thereby that I could bring a wider perspective to the discussions. In this respect, I noted with interest that out of the whole text of the paper, about half was devoted to a review of the economies of the Arab countries and their macroeconomic and trade policies. In other words, half focused on the general topic of what are appropriate or normatively sound economic policies for the Arab countries, and only half on the impact of industrial country trade and trade-related policies on the Arab countries.

I subscribe to an implicit change of emphasis as I think that the static analysis of the impact of such policies on the Arab countries is of little relevance—for reasons I will dwell upon later. Perhaps it is more important to try to gauge the probable impact of the trade policies of industrialized countries on a future diversified structure of Arab exports and imports, that is, the impact on the Arab countries once they have progressed somewhat in their development. To do this, we have to draw on the comparative experience of other

[1]The views expressed in this paper are personal, and should not be interpreted as those of the United Conference on Trade and Development (UNCTAD).

developing countries. On the other hand, raising the question of what macro and trade policies are normatively advisable for the Arab countries is both interesting and appropriate, because in my view the reasons for Arab nonperformance are largely the type of internal economic policies followed and their interaction with the prevailing sociopolitical factors. I will follow the Kelly/Fritz-Krockow sequence by first discussing the macroeconomic and trade policies of the Arab countries and then reverting to their impact. Obviously, the Arab countries, vulnerable to the external environment as they are, cannot be discussed without referring to the development environment of the 1980s, and I will therefore begin my remarks with this topic.

The External Environment and the Arab Countries

As the authors observe, the 1980s were characterized by a long economic expansion in the industrial countries, an increase in investment flows and in market integration, and a shift of income-trade relationships to ranges compatible with historical experience. However, I would like to add the following points to what the authors said:

- The distribution of growth among industrial countries was uneven, with the United States and Japan accounting for the major part of growth. Moreover, by historical standards, growth of 3.5 percent is below the levels of the previous three decades.
- The 1980s was a period of uneven performance by the developing countries, including the Arab countries. While the countries of East Asia and the Association of South East Asian Nations (ASEAN) registered remarkable performances, the rest of Asia and all of Latin America and Africa performed poorly.
- The remarkable growth of total foreign direct investment (FDI) in the 1980s masks an unremarkable, uneven incidence in the destination of such investment. Only 14 percent of the FDI of industrial countries went to developing countries; and of these, the ASEAN and East Asian countries account for the bulk of it. Moreover, and as I will discuss below, there was a negative net flow of funds to many developing country regions.
- The 1980s are characterized above all by the problem of debt and the decline in the terms of trade of developing countries.

> More than anything else, the poor performance of the Arab countries and other developing countries can be traced to these two factors.

I would have liked the authors to have gone into these aspects and to have drawn the appropriate conclusions. For my part, a study of the external environment leads me to the following conclusions:

- The macroeconomic policies of the industrial countries did not seem to attempt to ameliorate the external environment of development.
- The lending of the IMF and the World Bank Group also did not attempt to address this aspect; the vulnerability of the balance of payments of most developing countries, including the Arab countries, was not addressed by deliberate anticyclical provisions. Rather, the dominant view was to push structural reforms in each country separately. In other words, no attempt was made by the funding institutions to form a pattern of international adjustment worldwide.
- Investment funds went primarily to industrial countries. An abnormal aspect of this is the extent to which the U.S. deficit was financed from the rest of the world. If one were to superimpose on that the capital flight from developing to developed countries, one would have to say that the 1980s were characterized by large net saving by developing countries, that is, developing country savings exceeded investment for most of the decade, a situation contrary to what it should be.

Among the Arab countries, the largest share of investment flows went outside the region, and less than $70 billion was channeled to other Arab countries from all sources in all forms from 1973 to 1980. Furthermore, the capacity of Arab surplus countries to give aid and to invest externally deteriorated at the same rate as the losses they suffered in their terms of trade.

Macroeconomic and Trade Policies of Arab Countries in the 1980s

Several observations should be made about the general economic policies of Arab countries in the 1980s. First, the dominant role

assigned to the public sector not only in controlling the so-called commanding heights of the economy but in dominating the distribution of GNP on the revenue side has tied economic performance to the wisdom and effectiveness of public sector activities. On the latter, I need not qualify the evidence: the facts speak for themselves. On the former, with few exceptions, there seems to have been no effective effort to diversify the Arab economies, promote sound agricultural policies, institute industrial policies to target certain export-oriented sectors, and in some countries, even invest in human capital. In the political and sociological conditions of most Arab countries, the public sector has served, in addition to its conventional functions, extra-economic purposes: supporting a beneficiary class, providing employment to diffuse political pressures, shouldering massive armament burdens, and running public sector deficits without any market accountability.

The Arab countries have also failed, as a group, to promote conditions for secure, productive, and attractive intra-Arab investment. Whatever the reasons for this, the result has been dependence on foreign financial investments, rampant debt by those with weak balance of payments positions, and rather weak economic performance with wide gaps opening up in many countries.

A related point is the status of regional and interregional cooperation in the economic policies of the Arab countries. It seems that the poor performance of the Arab countries individually and collectively reflects, among other things, a neglect of genuine regional cooperation. This is manifest in the very low share (7 percent) of intra-Arab trade in their total trade. Neither the endowment factor nor the similarity of production structures explains this fact. If one examines the patterns of imports and exports of the Arab countries with nonregional trading partners, one has to conclude that considerable room exists for creation of intraregional trade. This is not unique to Arab countries: other developing countries share this weak interlinkage of trade and finance, and explanations are easy to find. There are major tariff restrictions among Arab countries, numerous problems of transportation, lack of information on potential partners and products, general underdevelopment of the marketing network, scarcity—at least until recently—of financing for trade and of suitable monetary and clearing arrangements, and, above all, a lack of political will to pursue agreements to facilitate trade or to

implement those agreements already signed. There is no escape from the circumstances of the world economy, and from the need for economic cooperation among developing countries (ECDC). And as one observes the increased trade and exchange, especially intraindustry trade, among developed countries, one has to conclude that something is amiss in this aspect of Arab country policies.

Because of the underdeveloped state of most Arab financial markets and the restrictive regulations, the scope of fiscal and monetary policy actions as well as microeconomic policies have proved limited. Moreover, because monetary policy in the Arab countries is typically tied to fiscal policies—and more precisely, to public finance—financial inefficiencies have added to the many problems of the banking system.

Turning to trade policies, I agree with the classification of the Arab countries proposed by the authors. On that basis I would make the following remarks. First, for the open economies (the oil exporters, except Algeria and Libya), a policy of import substitution should have been a part of their economic strategies with provisions for phasing out protectionism. The authors seem to support the line that export orientation is the only valid model that has proved itself in successful developing countries. There is no conclusive evidence for this view. The successful examples of Asian newly industrialized countries have important import substitution elements in their experience, and the poor examples in Latin America are attributable, at least in part, to the impact of debt, capital flight, and the deterioration in the terms of trade. Moreover, I can think of no sound economic argument for a categorical judgment against import substitution, as an initial phase, for countries with undiversified economic bases. Certainly, most of the oil exporters have undiversified economies. I do not, however, want anyone to jump to the conclusion that I am advocating import substitution. Quite the opposite; I am advocating a strategy of encouraging some industries to import substitutes while influencing certain dynamic industries capable of large-scale production to move into exportables. Resources should be allowed to move freely among the various sectors. Moreover, one should not lose sight of the historical fact that import substitution, while necessary to anchor the economy at some point in time, has built-in limitations in its range, in its scope, in its technological possibilities, and in its usefulness. In a word, one ought to think of a

whole spectrum of activities including, under safeguards, import substitution.

Second, the exploitation of dynamic comparative advantages in such countries is hampered by their small populations, limited markets, dependence on foreign skilled labor, and severe limits to their natural endowments. While the authors' comments are acceptable in principle, their relevance to these countries in the near future is arguable.

Third, among the relatively diversified exporters, Morocco, Jordan, and Tunisia have aimed their trade policies toward export diversification, but their development emphasis has been placed on promoting certain nontradables such as tourism, and on developing agricultural exports that benefit from preferential access to the European Community (EC) in the context of its Mediterranean policies. Hence, they have not yet reached a stage of overall diversification that permits clear judgment. Syria and Iraq, on the other hand, have been victims of a dominant public sector, massive economic regulations, inward orientation, and crushing armament efforts. No economy could endure such shackles without serious problems or boast good performance without the benefit of special circumstances. Egypt, which has sought diversification, has had to grapple with its enormous debt ($48 billion before the crisis in the Middle East), population pressures, and still slow and massive government procedures and regulations.

Two of the countries in the third category, Sudan and Somalia, have had protracted civil wars, and another is a less developed country.

Fourth, private investment in the Arab countries has generally eschewed industrial investment in favor of real estate and commercial services. This means that the productive base of the economies has remained too limited for trade policies to have had scope for effectiveness.

Fifth, the authors rightly and aptly observe that in many Arab countries, the government policies of intervention, overregulation, and inward orientation have skewed direct foreign capital toward public sector lending or direct support. Indeed, most of the bilateral aid given by the Arab surplus countries has gone to support the public budget, with the result that foreign capital has had a negligible impact on the productive base of the Arab economies.

Sixth, I have difficulty with the bland statement about opening up all markets as a viable strategy for the Arab countries. Two issues are involved: the first pertains to the problem of asymmetry in the response of demand and supply to opening up. This would lead, if not carefully managed, to balance of payments disequilibria. The second pertains to the sequence of reforms. The experience of Chile, for example, shows that liberalization and reforms should have careful sequencing, starting with macroeconomic reforms, then micro and trade reforms, and only finally opening up financial markets.

Evaluation of Impact of Industrial Country Trade Policies on Arab Countries

This topic is of limited scope for the Arab countries. Close to 80 percent of Arab exports are in oil and oil derivatives, products of low price elasticity but significant income elasticity, on which industrial country trade policies have shown little impact. Until the Arab countries have diversified exports, with a large share of manufactures in exports, the whole matter will remain of rather limited interest.

For the agricultural exporters such as Tunisia, Morocco, and, recently, Egypt, the main destination is the EC countries, which have protected agriculture. Japan and the United States are unimportant destinations for the agricultural products of the Arab countries. The EC has granted preferential access for these countries to its markets. The important question in this regard is whether such protocols will erode after 1992, and whether newcomers to the EC from Eastern Europe, for example, will be given the same advantages. I will deal with this matter later.

The trade and commercial policies of the industrial countries toward the Arab region are multilayered. It would help to divide these industrial countries into three groups: the EC, the United States, and Japan. The most important export destination and import source for the Arab countries is the EC. Japan and the United States are important for the Gulf Cooperation Council (GCC) countries, but much less so for the rest.

EC trade and trade-related policies pass through three filters: first, there is the CAP, that is, the Caribbean, Africa, and Pacific treatment articulated in the various Lomé Conventions that cover 4 Arab

countries. Second, there are the preferential access protocols of the EC granted to 12 Mediterranean countries, of which 9 are Arab countries. Third, the remainder are covered by the Generalized System of Preferences (GSP) system subject to quotas, ceilings, and local injury clauses. The least developed among the Arab countries are also beneficiaries of the provisions of the UNCTAD Paris Conference for Least Developed Countries. Japan and the United States follow the same approach as the EC in the use of the GSP and nontariff restrictions.

The GSP coverage, which is exclusively subject to unilateral decision, is constrained by nontariff measures: voluntary export restraints, variable import levies, anti-dumping provisions, orderly market arrangements, basic price systems, and so on. The data base of UNCTAD was used to depict the extent of the measures imposed, the ratio of trade covered, and the frequency of coverage, as well as for the total. Leaving aside agriculture, it is clear from these computations that textiles, steel, and shoes and other leather goods, that is, the bulk of Arab country non-oil, nonagricultural exports, are restricted by the trade policies of the industrial countries, that is, the policies of the EC, Japan, and the United States, which account for the majority of Arab exports and imports. Since agriculture is heavily protected in the EC and Japan, the trade policies of the industrial countries have a negative impact on the Arab countries in all but the oil trade. I do not set much store by the statement that some food importers have benefited from these policies; the regional dynamic impact of these policies is on the whole negative. It remains true that because the scale of Arab non-oil exports is modest and their diversity limited, the estimated losses are not large. But one should not lose sight of the *potential* impact, as the Arab countries may in future find themselves in a position similar to that of the East Asian countries at present. Nontariff barriers will then bite with the same intensity observed with respect to the manufactured exports of those countries.

Industrial country trade policies have affected several new subsectors of particular relevance to some Arab countries, that is, steel, petrochemicals, and air transport. The steel exports of Saudi Arabia, Qatar, Egypt, Morocco, and Algeria are affected. For petrochemicals, the speed with which the EC imposed trade measures should elicit high praise from all those with protectionist hearts. In these

cases, the Community used anti-dumping—its protectionist workhorse—to raise the barriers. For the air transport sector, the nontariffs take the form of environmental standards. This will be quite important in access to the EC.

Two other aspects of industrial country trade and trade-related policies should be raised. The first concerns the indirect effect of trade policies, specifically their impact on foreign direct investment, and the technological content of trade. This aspect was touched upon but not treated by the authors. The second concerns the impact of industrial country groupings on the Arab countries, in particular the impact of the post-1992 European Community and the North American free trade area (NAFTA) on the Arab countries. As custom unions and free trade zones, respectively, these groups will affect Arab country trade directly and indirectly. This aspect was not touched on in the paper. Its importance warrants, however, brief consideration.

Basically, the European Community after 1992 and the NAFTA will generate trade creation and trade diversion. While the first effect, which accrues from increased efficiency and income multipliers, is positive, the second, which accrues from increased competitiveness and access gains relative to third parties, is negative. Three scenarios of growth of EC income were constructed at 2.5, 5, and 10 percent increases in the growth of the GNP trend. The Commission of the European Communities' estimates of the overall income elasticity agree more or less with estimates made by economists such as S.G. Jones and others and with our own estimates. Using the data for all developing countries for 1979–87, the overall income elasticity was estimated at 3.5. That is, every one-point increase in the growth rate would result in a 3.5 increase in imports. This implies that the gross trade creation effect would be 17.5 percent in the middle scenario of 5 percent growth, the scenario with the highest likelihood. But this of course should be modified by the diversion effects.

According to the estimates of the EC Commission, the diversion effect will be highest in some classes of manufactures, and lowest in food and primary commodities. Although under the growth assumptions of the Commission (4.5–7.0 percent), manufactures should increase by 10 percent in the medium term, the subsectoral impact will differ depending on the product. The most significant trade

diversion is estimated to be in metal manufactures. This is followed by chemicals, office machinery, textiles, and other labor-intensive manufactures. The statistical picture seems to indicate that Arab exports of food, oil, and other energy products (not oil derivatives) would not suffer important diversion effects. On the other hand, chemicals, steel, and textiles would be affected negatively, although the order of impact is in descending order. However, it is more interesting to investigate the impact of subsectoral manufactures at the Standard International Trade Classification (SITC) two-digit level. It is all the more so, since agriculture will continue to be protected under the EC system. On this score some suggested orders of magnitude can be gleaned from recent econometric work. Griffith-Jones and Alizadeh, for example, calculated these subsectoral impacts. They found that they differ widely. Specifically, office and data equipment revealed a very high import income elasticity of 13.5, whereas electrical machinery boasted 7.7 and clothing only 2.5. In between, textiles, and manufactures of metal and leather recorded 2.5, 3.4, and 3.5, respectively. Motor vehicles, rubber, chemicals, and furniture occupied a middle range of 5.7, 5.9, 4.6, and 4.9, respectively.

On the basis of some econometric models it seems that Arab exports to the European Community, except for oil and agriculture, would stand to gain little under certain assumptions. However, the gains are significant in oil and would depend on the evolution of preferences for Arab countries and on protectionism in agriculture. These results also indicate an uneven distribution of benefits, with the bulk of the gain going to Arab oil exporters.

Nonetheless, the results clearly show that if the Arab countries can diversify their exports to certain branches of manufactures such as data processing and office equipment, paper and paperboard, electrical machinery, and motor vehicles, that is, to products of high technical content, they stand a good chance of benefiting from completion of the integrated market. The indirect effects of the EC and the NAFTA will be on private direct investment and bilateral and multilateral official flows. The budget constraints of the United States and the EC countries will force choices in aid and lending destinations between the internal uses of such funds and the external uses. In view of the political factors involved—ensuring that communism does not return and avoiding political instability in Eastern

Europe—it is likely that bilateral official aid will accord Eastern Europe first preference. Similarly, the limited resources of the international funding organizations and their control by the main industrial countries will require rationing among the competing demands and will probably result in at least diverting some funds to Eastern Europe. Because of the interest of Arab surplus countries in foreign investment, the Arab recipient countries will not necessarily attract Arab investors. Consequently, these countries will have to forge with Arab surplus countries some cooperative arrangements to redirect net Arab savings to the Arab region. In such schemes, the Arab recipient countries will have to address effectively the interests and concerns of the investors.

One last point is the potential impact of the entry of East European countries into the EC or of their being granted preferential treatment. This impact can be estimated only over the medium term and inferred basically from the degree of substitution of their products for Arab products as well as the nature of their endowment. It would be an educated guess that in agriculture, textiles, chemicals, and leather goods they will be competitors with the Arab countries. In manufactures, they will have the advantage, especially in products of high technical content. But most of all, they will be favored by investment flows because of their excellent human capital and the political considerations involved in ensuring that they do not return to communism. For these reasons, the Arab countries, like all other developing countries, will likely fare only second best.

5

The Multilateral Trading System and the Uruguay Round of Trade Negotiations: An Arab Perspective

Abdel Hamid Mamdouh

The Multilateral Trading System

The General Agreement on Tariffs and Trade

The Havana Charter, negotiated during the United Nations Conference on Trade and Employment in 1947–48, sought to establish the International Trade Organization (ITO), which was to be the third institutional pillar in the postwar international order for economic reconstruction. The ITO was to be the specialized agency that established rules and oversaw the international trading system. Owing to political factors, the Havana Charter never entered into force, leaving a vacuum in international economic relations at that time in areas such as employment, economic development, trade policy, intergovernmental commodity agreements, restrictive business practices, and settlement of disputes. That vacuum has never been entirely filled. However, one crucial gap—that of trade policy and related settlement of disputes—was filled by the General Agreement on Tariffs and Trade (GATT).

The origins of the GATT are in 1945, when it was seen as a multilateral trade agreement aimed at liberalizing world trade (after a long period of protectionism and bilateralism during the 1930s) and at providing stability, predictability, and transparency in government trade policy practices. It was agreed that such objectives could not

be achieved unless governments entered into legally binding commitments. This approach resulted in the contractual legal nature of the GATT.

The GATT is the only multilateral, legally binding, system to provide a framework of rules and procedures governing international trade. It is not truly universal, as some important countries are still not part of it, but it covers over 90 percent of world trade. It is both a treaty and an institution. The GATT system comprises the General Agreement, supplemented by separate legal instruments, such as the nontariff barrier agreements, as well as some sector-specific arrangements negotiated within the system; their implementation is supervised by the Contracting Parties to the GATT.

The GATT performs three main functions; the first is a code of conduct for foreign trade policies of its Contracting Parties, providing a balance of rights and obligations among all parties. Second, the GATT provides a forum for negotiating trade liberalization among its parties. The General Agreement provides the principles, rules, and procedures for such negotiations, while the GATT, as an institution, provides the necessary support for the negotiations. Traditional rounds of multilateral trade negotiations have been in the area of tariffs, with participating countries exchanging concessions. Third, the GATT provides for settlement of disputes between contracting parties. This function ensures the enforceability of the GATT rules.

The GATT is based on certain basic rules, expressed in legal terms in the Articles of the General Agreement. The rules are the following.

Most-Favored-Nation Treatment (MFN)

This is the cornerstone of the General Agreement, assuming the multilateral character of the trading system. The MFN rule, in Article I of the GATT, states: "... any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties." By virtue of this provision, any contracting party to the GATT cannot extend any trade concessions that discriminate between contracting parties. It also established the obligation that if a contracting party extends a trade benefit to any country, it must also extend it

immediately to all other contracting parties. The obligation has had the important effect of favoring multilateralism over bilateralism in the conduct of foreign trade.

Protection Only Through Tariffs

Customs duties are, with some exceptions, the only form of protection permitted under the GATT. Tariffs are transparent, predictable, and calculable in terms of the extent of protection they provide. They encourage the interplay of market forces, leading competition, and more efficient allocation of resources. The trade liberalization objective of the GATT is then achieved by the gradual reduction of customs tariffs. It is through successive rounds of tariff negotiations that contracting parties have reduced their tariff protection over the past four decades. Article XXVIII:b contains the GATT set of rules for such negotiations, the most important of which is that it takes place on the basis of reciprocity and mutual advantage. It follows that any concessions exchanged during such negotiations are multilateralized, under the MFN provision.

General Elimination of Quantitative Restrictions

An essential part of the GATT approach to trade liberalization is the prohibition on the use of quantitative restrictions. When the GATT came into force in 1948, the use of such measures was widespread among different countries. Unlike customs tariffs, quantitative restrictions have a seriously distortive effect on markets, blocking the price mechanism. Article XI of the General Agreement prohibits the use of quantitative restrictions. Exceptions to this general rule relate to (i) agricultural and fisheries products; (ii) situations where a contracting party suffers balance of payments difficulties; and (iii) cases of promoting the establishment of infant industry in a developing country. Each of the exceptions mentioned is invoked subject to certain conditions.

National Treatment

As a central element of the GATT, national treatment requires that once imported products cross frontier barriers they should enjoy in the domestic market treatment that is no less favorable than that accorded to any domestic like product. Article III of the GATT

reflects the rule in legal terms and defines the scope of its application to encompass internal taxes and other internal charges, as well as any laws, regulations, or requirements affecting the internal sale, offering for sale, purchase, transportation, distribution, or use of products.

Reciprocity

Reciprocity has not been defined in legal terms in the GATT, but it is reflected in some of the provisions, particularly in the Preamble and in Articles XXVIII and XXVIIIbis, which deal with tariff negotiations between contracting parties and prescribe that such negotiations shall take place on a reciprocal and mutually advantageous basis.

Differential and More Favorable Treatment for Developing Countries

This principle developed from the growing recognition after the GATT went into effect in 1948 of the need to address the increasingly important link between trade and development. The principle, introduced as Part IV of the GATT in 1964 (Articles XXXVI–XXXVIII), achieved reciprocity. Article XXXIV, paragraph 8, states "the developed contracting parties do not expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade of less-developed contracting parties." Besides Part IV of the GATT, there are other provisions that reflect this principle of differential and more favorable treatment, such as the provisions of Article XVIII of the GATT, entitled Governmental Assistance to Economic Development, and the 1979 decision by the contracting parties on "Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries," which contains what is known as the enabling clause. There are also the provisions on the treatment of developing countries in the nontariff measure agreements resulting from the Tokyo Round of multilateral trade negotiations (for example, the agreement on subsidies and countervailing measures).

Multilateral Trade Negotiations

During the past four decades the GATT has served as a forum for trade negotiations. This particular function of the GATT bas been

one of the basic elements that its founders had in mind. The Preamble of the General Agreement, after setting clearly its objectives, identifies negotiations as the means for achieving those objectives where it states:

> Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international commerce.

The provisions of Article XXVIIIbis of the GATT go even further and state clearly the legal basis on which tariff negotiations should take place.

Since the GATT came into force, seven rounds of multilateral trade negotiations have been held. The first five rounds of negotiations, the last of which was the Dillon Round (Geneva, 1960–61), dealt exclusively with tariffs. It was not until the sixth round (Kennedy Round) that negotiations started addressing a different subject, namely, anti-dumping. The seventh round, the Tokyo Round (Geneva, 1973–79), further widened the coverage of multilateral trade negotiations to cover nontariff measures, government procurement, and the agreements relating to the framework for the conduct of trade.

The common feature in all the GATT rounds of trade negotiations is that they all aim at further liberalization of international trade among its contracting parties. That was sought initially through tariff negotiations, based on GATT rules. But as the international trade environment evolved, the need to address and reconsider some of the rules of the system itself became increasingly evident. This trend changed qualitatively the mix of negotiating subjects in recent rounds, particularly the Uruguay Round, toward more emphasis on rule-making issues as against the exchange of trade concessions. Rules of the system relating to nontariff measures, unfair competition (subsidies, anti-dumping), safeguards, and those relating to the treatment of developing countries were high on the list of rule-making negotiations.

Developing Countries in the System

When the GATT first came into force, less than half of its 23 founding contracting parties were developing countries. Now more

than two thirds of GATT contracting parties are developing countries. But more important than their number in the GATT is developing country participation in the system. This has taken on a new dimension as their approach to the GATT evolved.

The participation of developing countries in the GATT system has always (not prior to 1956, I think) been governed by provisions relating "differential and more favorable treatment to developing countries." The most significant privileges that developing countries enjoy by virtue of such provisions are

- The flexibility for a developing country to impose quantitative restrictions to address balance of payments difficulties. This exception to the use of quantitative restrictions is also available to developed countries, but the criteria and conditions under which it applies for developing countries are much more flexible.
- That developed countries do not expect reciprocity from developing countries in trade negotiations to reduce tariffs and other trade barriers.

The existence of such rules, or, rather, exceptions in the system has kept developing countries' participation, in previous rounds of negotiations, at a modest level. The ability of developing countries to make tariff concessions on a large scale was always considered to be inconsistent with their import substitution philosophy during the 1960s and 1970s. The corollary to that was that developing countries could not influence the trade liberalization process to cover produce areas such as textiles, agriculture, and tropical products that are of export interest to them. The lack of substantial liberalization commitments by developing countries has led to the reluctance of developed countries to undertake meaningful commitments in return.

This situation prevailed for decades generally because most developing countries did not accept the underlying philosophy of the GATT, which is that liberalized trade promotes growth and development, and moreover their development policies did not attribute a central role to their export sectors in the development of their economies.

While this was the situation of developing countries during the 1960s and 1970s, changes started appearing during the 1980s in a way that gave the multilateral trading system a new meaning and in-

creased the importance for those countries. The most significant evolution was the rethinking, by many developing countries, of the role of trade policy in the development process and the increasing appreciation of the advantages and benefits that a dynamic outward-looking export sector could bring to a developing economy. In the 1960s it was only the Republic of Korea and Singapore that did not apply import substitution policies and followed the free market economy approach. Such countries served as examples to illustrate the imperfections of the traditional closed market philosophy and the inefficiencies that it entails.

During the 1980s an increasing number of developing countries adopted the same approach. This consequently increased the need of those countries for an open, stable, and credible multilateral trading system that provides the necessary rules and disciplines to protect the rights and obligations of its members.

The need for such a system led developing countries to take a much more active role in the Uruguay Round than they had in any previous round. Also, during that period a number of developing countries started facing debt service problems, which produced two new elements. The first is the increasing need for those countries to improve their export performance to be able to meet their financial burdens, which requires securing open export markets through negotiations. The second is the wave of unilateral liberalization adopted by those countries, which was a function both of their new approach to the role of trade policy in the development process, and of the conditionality in IMF and World Bank lending programs.

What is most relevant here about these two elements is that they led developing countries to be much more active in pursuing their interests, not only by trying to negotiate meaningful trade liberalization commitments with developed countries but also by engaging in rule-making negotiations to ensure that the disciplines of the system would reflect their interests and protect their rights. All these factors made developing countries more attached to the system than they had ever been. These changes had their implications also for the way in which developing countries operate and negotiate within the system. They traditionally operated, like in the United Nations system, as one bloc of countries having more or less the same economic and trade interests. Since their economies are not large

enough to give them any individual negotiating power, they had to operate and negotiate collectively in order to have some negotiating leverage against large negotiating partners from the developed world.

A notable trend lately in the course of the Uruguay Round has been the increased cooperation and coordination between some developing countries and developed countries, particularly small and midsized ones in various combinations. The emerging groupings are the function more of specific trade interest in different areas of negotiation than of being based on political solidarity.

It is more or less the same concept of gaining negotiating leverage through negotiating collectively, but this time it is to serve specific trade interests where the divide is not a north-south one but between small and midsized countries, whether developed or developing, on one side, and large countries on the other.

The Uruguay Round

Background

The Uruguay Round was launched against a background full of trade tensions and frustrations by both developing and developed countries. Developing countries were firmly convinced that the credibility of the multilateral system was at great risk, developed countries were not living up to their commitments toward them, and their commitment to the system itself was seriously questioned in the light of the permanent derogations they enjoyed in textiles and agriculture. They were also frustrated by the backlog of outstanding issues from the Tokyo Round in areas such as safeguards, and even with respect to their exports of manufactures, developed countries have introduced a significant number of barriers.

On the other hand, developed countries were also frustrated by the lack of commitment by developing countries. The previous seven rounds of trade negotiations had produced mainly liberalization of trade among developed countries, those that were willing to make significant concessions. Even where developing countries were committed, such as in the relatively limited area of tariff bindings, they had the flexibility to deviate from such commitments by invoking exceptions that allowed them to introduce quantitative restrictions. Developed countries were basically firmly convinced that the princi-

ple of nonreciprocity of developing countries needed to be reviewed. There was also a growing feeling that developing countries were no longer one homogeneous group of countries with similar capacities to assume commitments and therefore would all warrant the same kind of treatment. Some distinction was needed between those developing countries that are relatively developed, and should therefore participate more fully in the system, and those that are still at a relatively low level of development and therefore still warrant some flexibility. Some rethinking has even been done with respect to the latter category, on whether such flexibility is the best way to address development difficulties. Such rethinking was to a certain degree shared by some developing countries that began to adopt more outward-looking economic policies.

Apart from frustrations that ran high, some important changes also took place in the economics of international trade, the most influential of which is the role of modern technology and its impact on international trade patterns. Modern technology has considerably altered the input mix in manufactured products to the detriment of traditional raw materials. Products with high technology content have tended to be among the most rapidly growing export sectors. This trend brought a new dividing line between countries with different export capabilities.

The increasing importance of technology as a determinant of the competitive edge of exporting countries strongly influenced the international environment preceding the Uruguay Round and the agenda of negotiations. This important factor led the exporters of modern technology to pursue two important aims through negotiations. The first is to achieve a substantial degree of liberalization of different types of economic activities where they can increase their benefits from their competitive edge (such as trade in services, and disciplines on the governmental use of investment measures). The second is to secure a higher level of international protection for technology (negotiations on trade-related aspects of intellectual property rights), which in turn would also secure higher levels of revenue from the industrial use of such technology.

Also, the changes that have taken place in developing countries in adopting a new policy approach to international trade, of which the multilateral system is a central part, coupled with the increasing

trend toward trade liberalization, have led developing countries to place themselves more in the center of the system itself. They are more ready to engage in serious trade negotiations and to assume onerous commitments; they can identify their specific interests much more concretely, but they also would like to see what they can obtain in return from their developed country partners. They have not abandoned their demands for differential and more favorable treatment, but it is no longer the only basis on which they are ready to participate in multilateral trade negotiations. The emphasis of an increasing number of developing countries has shifted from that principle toward engaging in real negotiation of solid commitments.

Against this background, a strong and credible multilateral trading system was considered to be a necessity for both developed and developing countries.

A Different Round of Trade Negotiations

Since the Uruguay Round was launched in September 1986 at the ministerial meeting in Punta del Este, Uruguay, it has been viewed by the international community, and rightly so, as the most comprehensive and far-reaching international trade negotiations ever undertaken. In terms of participating countries, the list is the longest ever: 103 countries. In terms of the negotiating agenda, it is certainly unprecedented. Negotiations in the Uruguay Round take place on goods as well as on services. On goods, there are 14 subjects, which represent a wide variety of interests. On services, the subject is one that proved to be quite complex owing to the heterogeneous types of activities and transactions that it covers.

There are traditional issues in the Round that fall within three main classifications: market access issues, rule making, and systemic issues. The market access category includes negotiations on tariffs, nontariff measures, natural resource-based products, textiles, tropical products, and agriculture. The rule-making issues include negotiations on safeguards, GATT articles, multilateral trade negotiations (MTN) agreements, and arrangements and subsidies. The systemic issues include improving the settlement of disputes system of the GATT and improving the functioning of the GATT system. There is also the category of the three new issues, which includes negotiations

on the trade-related aspects of intellectual property rights, trade-related investment measures, and trade in services.

The negotiating package is wide enough to accommodate the different interests of negotiating countries. The background against which these negotiations were launched—whether it is the need for a strong and credible multilateral system by those who seek its protection or the need for a reformed system that is more relevant to the modern trade environment of high technology—had a strong influence on the negotiating agenda. It is also understood that any agreements resulting from negotiations on the new subjects, which involve different types of economic activities going far beyond mere cross-border trade in goods, will certainly be much more intrusive on national laws and regulations and will call upon governments to change such laws and regulations. This willingness to assume commitments is generated by the need for the system itself and for what it provides in terms of rules and disciplines to secure stability and predictability in markets.

Traditional Subjects for Negotiations

The negotiating agenda contains a number of traditional subjects relating to market access and rule making, and some are basically systemic issues. While it may be too time consuming to go into the fine details of each of the subjects, it may be useful to identify the main issues.

Market Access

Negotiating subjects relating to market access are tariffs, nontariff measures, natural resource-based products, textiles, tropical products, and agriculture. These subjects are of particular interest to a wide range of countries, mainly developing and the agricultural exporters among the developed countries, and their inclusion in the negotiating agenda was necessary to ensure full participation of GATT contracting parties in the Uruguay Round.

Tariffs have been the GATT's traditional and most successful field of negotiations. While it is in principle the only legal means of protection under GATT rules, it has been subject to seven previous rounds of negotiations where contracting parties exchanged reduc-

tions in their tariff rates. Those seven rounds have considerably reduced the level of tariff protection in industrialized countries. However, there are still some peaks of high tariff protection for sensitive products that are of export interest to developing countries, particularly in the areas of textiles and agriculture. In developing countries the situation is different. The general level of customs duties is higher than in developed countries, and, more important, the degree to which such duties are bound is much less. That means that such unbound duties could be increased further at any time without the need to offer any compensation to other contracting parties.

Previous successes in tariff negotiations and the recent interest in nontariff measures and new negotiating subjects may have put tariffs in the background in the Uruguay Round. However, many countries consider it to be of central importance to them that the negotiations deal effectively with the remaining problems in this area, such as tariff escalation, tariff peaks, elimination of low tariffs, and increasing the overall level of tariff bindings by developing countries. The overall objective for tariff reduction is to be no less, on average, than the reduction achieved during the Tokyo Round, which was about 30 percent.

Nontariff measures are an area that has an increasing effect on international trade owing to the relatively recent proliferation of such measures. When the GATT was negotiated and signed in 1947, quantitative restrictions were the most prevalent form of nontariff measure. Therefore, and in order to protect the benefits of negotiated tariff reductions, the founders of the GATT imposed, by virtue of Article XI, a general prohibition on quantitative restrictions. There are, of course, certain exceptions to this rule, which relate to cases of balance of payments difficulties (Articles XII and XVIII(b)), and also in Article XI for countries that limit their production of agricultural products.

In spite of such rules, and given the creativity of governments and regulators in coming up with new devices, such as voluntary export restraints, the problem of nontariff measures persisted. Ironically, the proliferation of such measures is considered to be a side effect of GATT's success in tariff liberalization.

The Tokyo Round in the 1970s represented a major effort in dealing with the problem. It resulted in agreements on subsidies and

countervailing measures, customs valuation, technical barriers to trade, import licensing procedures, and government procurement.

In the Uruguay Round, negotiators are confronted with the need for disciplines in new areas such as rules of origin and pre-shipment inspection, which have recently been cited as impediments to international trade. Countries are also exchanging concessions in the form of dismantling specific nontariff measures. Some participants tend to draw strong linkages with negotiations on tariffs because market access will be determined eventually as a result of both the tariff and nontariff treatment of a product.

Natural resource-based products are an important sector in world trade; exports of minerals (including fuels and nonferrous metals) alone reached $370 billion in 1988. The share of mining and the agricultural sector in international trade is identical, at 13.5 percent. These products are important for a wide range of countries, developing and developed. Many of them wish to go beyond their role as raw material suppliers and move into processing. The negotiating group addressed issues such as tariff escalation, government support measures, and access to supplies—particularly to fishery resources. However, the actual liberalization of trade in natural resource-based products is addressed in the negotiating groups on tariffs and nontariff measures.

Textiles and clothing is a sector that represented 9 percent of world trade in manufactures in 1988, and particularly important to developing countries, has been subject to negotiated exceptions to the GATT since 1961. The Multifibre Arrangement (MFA), under which industrial countries negotiate quotas on imports from developing countries, went into effect in 1974. The current extension of the MFA is due to expire on December 31, 1992.

The negotiating mandate in this area states that "negotiations in the area of textiles and clothing shall aim to formulate modalities that would permit the eventual integration of this sector into GATT on the basis of strengthened GATT rules and disciplines, thereby also contributing to the objective of further liberalization of trade."

Tropical products is a sector that accounted for only 3 percent of world trade in 1989. However, since it represents a precious share of developing countries' trade, tropical products were separated from agriculture so that they could have a priority status for liberalization

in multilateral negotiations. The Ministerial Declaration for the Uruguay Round has accorded tropical products "special attention," which has provided particular impetus for the negotiations on this subject. The Declaration also refers to "the fullest liberalization of trade in tropical products" as the objective in this area of negotiations.

It was agreed at the outset to pursue negotiations on seven product groups: tropical beverages (such as coffee, tea, and cocoa); spices, flowers, and plants; certain oilseeds, vegetable oil, and oil cakes (palm and coconut oil); tobacco, rice, and tropical roots; tropical fruits and nuts (bananas, pineapples, and peanuts); tropical wood and rubber; and jute and hard fibers.

Negotiations on these product groups aim at reducing or eliminating trade obstacles such as tariff escalation, quantitative restrictions, internal taxes, and sanitary regulations. Several industrial countries have maintained that the main developing country beneficiaries from such liberalization must also contribute to the negotiations by liberalization measures of their own according to their economic capacity.

The mid-term review of the Uruguay Round, conducted at ministerial level, led to a provisional package of tropical product concessions, which were largely implemented in the first half of 1989. They were mainly tariff cuts and they covered each of the product groups mentioned above.

In addition to these concessions ministers agreed to continue negotiations in this area to achieve further liberalization of trade in tropical products.

Agriculture has been a major source of tension in international trade relations owing to the escalating costs of farm support in major developed countries, the increasing use of subsidies that distort international markets, mounting surpluses, and increasing trade frictions. While the international debate on agriculture was warming up over the years, the share of agricultural products in world merchandise trade has shrunk considerably, from 46 percent in 1950 to 13.5 percent in 1988. This decline is due to the strong growth in the manufactures sector, the fall in prices of agricultural products, and also government intervention in this sector, which had a significant negative effect.

GATT rules concerning quantitative restrictions and subsidies are considerably more flexible with respect to agricultural products than

manufactures. It was generally recognized before the Uruguay Round that such rules in some respect lack precision and leave room for differing interpretations. For example, Article XVI on subsidies merely requires contracting parties to seek to avoid the use of subsidies on the export of primary products, but if they do grant them, not to do so in a manner that results in their having "more than an equitable share of world export trade" in the product concerned.

Also, the provisions of Article XI concerning quantitative restrictions are much more flexible for agricultural products, where contracting parties are allowed to impose such restrictions on any product whose production is being limited domestically.

Some contracting parties in the GATT have also enjoyed special freedom in this area by virtue of individual derogations (notably the U.S. waiver and the Swiss protocol of accession).

The seven previous rounds of negotiations have resulted in fewer tariff reductions for agricultural products than for industrial goods, and the overall degree of tariff binding is also much less.

When the Uruguay Round was launched there was no ambiguity about what needed to be addressed. The political and social difficulties for some major developed countries were also recognized. However, the urgent need for fundamental reform was clearly expressed. The Ministerial Declaration for the Uruguay Round states that

> Contracting Parties agree that there is an urgent need to bring more discipline and predictability to world agricultural trade by correcting and preventing restrictions and distortions including those related to structural surpluses so as to reduce the uncertainty, imbalances and instability in world agricultural markets.
>
> Negotiations shall aim to achieve greater liberalization of trade in agriculture and bring all measures affecting import access and export competition under strengthened and more operationally effective GATT rules and disciplines, taking into account the general principles governing the negotiations, by:
>
> (i) improving market access through, *inter alia*, the reduction of import barriers;
>
> (ii) improving the competitive environment by increasing discipline on the use of all direct and indirect subsidies and other measures affecting directly or indirectly agricultural trade, including the

phased reduction of their negative effects and dealing with their causes;

(iii) minimizing the adverse effects that sanitary and phytosanitary regulations and barriers can have on trade in agriculture, taking into account the relevant international agreements.

The mid-term review agreement in April 1989 laid down long-term guidelines as well as short-term commitments. A key objective of the long term was to "provide for substantial progressive reduction in agricultural support and protection sustained over an agreed period of time, resulting in correcting and preventing restrictions and distortions in world agricultural markets."

Rule Making

Negotiating subjects relating to rule making are those basically concerned with the review of some GATT provisions, whether in the General Agreement itself or in related instruments, which were considered by the contracting parties to warrant such a review. The four subjects falling under this category are safeguards; GATT Articles; MTN agreements and arrangements (the Tokyo Round codes); and subsidies.

Safeguards. Article XIX of the GATT allows contracting parties to impose restrictions on their imports of any product in cases where such imports have increased in an unforeseen manner and cause or threaten to cause serious injury to domestic producers of a like product. The founders of the GATT realized the political reality that governments would be unwilling to accept any far-reaching obligations to reduce their restrictions on foreign trade unless the Agreement contained a provision like Article XIX, which allows them to derogate from their commitments, an "escape clause."

Safeguard measures are not meant to deal with unfair trade practices, which find their answers in other types of measures (for example, countervailing and anti-dumping measures); they are actually meant to address situations where the trade practice involved is "fair," but, owing to a sudden increase in imports, domestic producers are being injured or threatened to be so. The purpose behind the provision is to protect domestic producers from foreign competition, an objective, some experts argue, that does not conform with the overall philosophy of trade liberalization, which should introduce

more competition leading to reallocation of resources within economies.

The challenge facing the safeguards negotiations in the Uruguay Round is to achieve a comprehensive agreement that refines the rules of Article XIX and at the same time resolves the problem of proliferating bilateral agreements restricting exports, which are known as voluntary export restraints (VERs) and orderly market arrangements (OMAs), and by which the exporting country undertakes a commitment to control the level of its exports reaching a particular market.

The major issue of contention among negotiating participants is "selectivity," and whether a safeguard measure should be taken against single suppliers or taken on a nondiscriminatory basis. Other issues that need to be resolved are the extent to which some developing countries should be exempted from safeguard actions, the duration of the safeguards measure, the need for adjustment measures by the protected industry accompanying the safeguards action, and the question of compensation for the country against which the action has been taken.

It is worth noting that reaching successful results from negotiations on this subject is considered to be a cornerstone in any effort toward strengthening the GATT system. Ministers in Punta del Este realized that when they adopted a mandate stating "A comprehensive agreement on safeguards is of particular importance to the strengthening of the GATT system and to progress in the MTNs."

GATT Articles. The Uruguay Round has provided the first opportunity, since 1955, for a comprehensive review of the Articles of the General Agreement. Some specific Articles are dealt with in other negotiating groups like safeguards (Article XIX), settlement of disputes (Articles XXII and XXIII), and subsidies (Article XVI). Thirteen of the 38 Articles of the GATT have been examined in this negotiating group. In some cases such examination was followed by substantive negotiations to refine some of the provisions. In other cases there are fundamental differences among countries as to whether negotiations are even appropriate.

While it might not be within the focus of this paper to go into the fine details of what is being discussed in this negotiating group, which in many instances involved technical issues that do not alter

any of the basic rights or obligations under the GATT, one major issue, which is highly divisive for developed and developing countries, is the balance of payments provisions. Article XVIII:B of the GATT provides an exception that gives developing countries the right to impose quantitative restrictions on their imports in case of balance of payments difficulties. Developed countries view this provision as a major loophole that allows developing countries to escape their obligations under the GATT. It has been their submission that the criteria and conditions set out in Article XVIII:B are too flexible and loose. These conditions in practice also allow developing countries to maintain permanent restrictions in the name of balance of payments difficulties while they are actually used to protect domestic industries.

Developed countries also argue that the measures used under this Article, namely sector-specific quantitative restrictions, are not appropriate for use in such situations. Instead, across-the-board price-based measures would be appropriate. In addition, a number of procedural questions arise relating to the consultation requirements for countries invoking this exception.

On the other hand, developing countries maintain that the provisions of this Article do not need any revision. The criteria and conditions specified in it, they argue, were based on the realities of developing economies where balance of payments problems are structural and long term. The Article recognizes that developing countries, when they are in the rapid process of development, tend to experience balance of payments difficulties arising mainly from the efforts to expand their internal markets as well as from the instability in their terms of trade. Developing countries argue that none of these considerations have changed since the Article was drafted. They also seem to be convinced that the measures to be used do not have to be across the board because that ignores the need to give priority to imports that are more essential for the development process.

This remains a major issue that needs to be resolved and it certainly has a high degree of political sensitivity attached to it on both sides.

MTN Agreements and Arrangements. These are the nine multilateral agreements and arrangements that resulted from the Tokyo Round of

multilateral trade negotiations, often referred to as "codes," and attempt to deal with a variety of nontariff barriers to trade. Although the majority of signatories to these codes are developed countries, they were considered widely as being a major contribution in the fight against nontariff barriers.

While some of these codes have been amended since they were agreed in 1979, it was decided when the Uruguay Round was launched that they should all be open for review during the Round with the objective of improving, clarifying, or expanding them as appropriate.

Subsidies. In the Tokyo Round an agreement was negotiated with the aim of providing disciplines for both the use of subsidies and the use of countervailing measures. In the Uruguay Round the subject was reopened with a clear recognition of the need to improve the disciplines of the subsidies code on both fronts. In the 1980s the use of subsidies in industry and even more in agriculture has substantially increased. Countervailing measures, in which some countries see a degree of abuse, have also been used considerably.

Final negotiations are taking place on a draft agreement that attempts to strike a balance between the two sides as well as ensuring the element of special and differential treatment for developing countries.

Systemic Issues

This category includes two negotiating subjects: settlement of disputes and functioning of the GATT system. They are slightly different in nature from other subjects addressed in the Uruguay Round in that they relate more to the actual functioning of the mechanics of the system. Negotiations in these areas do not endeavor to establish new rights and obligations but rather to enforce existing ones, in the case of settlement of disputes, and to secure the policy role for the GATT as an institution and improve its decision-making process, in the case of the functioning of the GATT system.

These two subjects were among the first to achieve early results in the mid-term review at the end of 1988. A set of "improvements to the GATT settlement of disputes rules and procedures" were adopted and actually implemented on a provisional basis four months later. Also, a decision was adopted to establish the "Trade Policy Review Mechanism," which provides for regular collective appreciation and

evaluation by the contracting parties of individual countries' trade policies and practices and their impact on the functioning of the multilateral trading system.

New Areas

The new issues for negotiation in the Uruguay Round, namely, investment measures, intellectual property rights, and services, distinguish this Round from the seven previous rounds of negotiations. The incorporation of these three issues into the negotiating agenda was divisive for developed countries and a group of developing countries. Developed countries led by the United States considered it necessary for new multilateral disciplines to be established for such increasingly important areas of economic activity. They also felt that the GATT is the appropriate and effective forum to deal with such questions where countries take contractual obligations that could be legally enforced through an efficient settlement of disputes system. They realized, of course, that a large number of developing countries in the GATT did not welcome such an expansion of the system. However, the trade-off was always in the interests of those developing countries in the more traditional areas, particularly where they have market access interests such as textiles and agriculture.

The misgivings that many developing countries had with respect to the new issues were based on two main concerns. The first is that developed countries would exchange concessions in the area of trade in goods for new commitments by developing countries in the area of investment, intellectual property, and trade in services, unlike the way it has always been, to exchange concessions on trade in goods for similar ones. The second is that the expansion of the system sought by industrialized countries would mean that the same rules of enforcement and settlement of disputes applied to trade in goods would also apply to the new areas, with the possibility of facing trade sanctions on their merchandise exports for any violation of rules in the new areas. They always considered investment and industrial policies to be sovereign policy areas for each government to regulate as it saw fit, and not an appropriate area for multilateral disciplines that might impinge upon such sovereignty.

The interesting feature that led developing countries to accept negotiations on such issues is that the reasons behind such acceptance

were the very same reasons for which they had initially rejected the idea. Their keen interest to negotiate the liberalization of trade in products of export interest to them, and their wish to protect themselves from the threat of unilateral trade measures taken by the United States (under Section 301) led them to accept the linkages between the new issues and the traditional negotiating issues of the GATT: bilateral trade tensions were increasing, leading in some situations to legal disputes in the GATT. A clear conclusion then was that a multilateral discipline covering such areas would protect the interests of both sides.

Trade-Related Aspects of Intellectual Property Rights

As referred to earlier, the increasing importance of technology as a determinant of international competitiveness has been the main motive for some developed countries to press for multilateral action in this field with the aim of increasing international protection for intellectual property rights. Those countries saw the need for an international set of standards that provide higher levels and wider scope of protection as well as an effective system for settlement of disputes and enforcement of such standards.

The protection of intellectual property rights (copyrights, patents, trademarks) for those countries should reflect an economic balance between the large investments devoted to research and development and the economic benefits to be gained from the commercialization of new innovations. Therefore, they believe that the lack of adequate protection in some countries deprives their companies of the fair revenue on their research and development investments.

Most developing countries, on the other hand, feel that such protection should reflect a different balance, not primarily based on considerations of international competition but rather on social considerations. Such countries, which are importers of technology, obviously see little advantage in agreeing to internationally higher levels of protection. They recognize the need for certain levels of protection of intellectual property to encourage the transfer of technology and attract foreign investments, but they see that the international harmonization of levels of protection among different countries at different stages of development would not be in their interest.

The international rules for the protection of intellectual property rights, which are largely embodied in the Paris Convention (patents, trademarks, and other forms of industrial property) and the Berne Convention (copyrights), are based on the principles of national treatment and reciprocity between member countries. They also provide for the types of intellectual property rights that have to be protected and the basic disciplines and terms of protection. However, they leave much to the discretion of each government concerning the level and scope of such protection, which results in many countries in excluding some important products such as pharmaceuticals and food products.

While the motives and objectives of developed countries are clear, developing countries found themselves facing a number of questions that they have to address.

Some are policy questions: How does the level of intellectual property right protection relate to industrial and technological development? How does the scope and level of patent protection affect the price of certain products such as pharmaceuticals? If it results in increasing prices, what are the social and political implications?

There are also negotiating questions: If countries assume new obligations in this area, what benefits could they get in other areas such as textiles, agriculture, or tropical products, and would it be possible to obtain a credible commitment from other countries, particularly the United States, to refrain from taking any unilateral trade measures, a problem that has worried many countries?

Trade-Related Investment Measures

The subject of investment measures was brought to the GATT some five years before the Uruguay Round. It was suggested by the United States that attention should be given to the effects of investment policies on international trade. This was resisted strongly by developing countries, and some developed countries were also not comfortable with the proposition. The argument was always that GATT was not legally competent to deal with investment policies.

During the preparatory stage leading to the launching of the Uruguay Round, the United States proposed a broad agenda for negotiations on investment measures that affected both foreign direct investment and international trade. That agenda included different types of performance requirements, investment incentives, restric-

tions on capital and income transfers, most-favored-nation treatment, and national treatment (including the right of establishment) for foreign investors.

In the face of strong resistance from developing countries a compromise was reached at Punta del Este. The scope of negotiations was confined to the adverse effects of investment measures and the extent to which they are addressed by the Articles of the GATT, rather than to investment policies and the broad relationships between investment, production, and trade.

Of course, investment measures can have an effect on trade. Local content export performance, trade balancing, manufacturing, and product mandating requirements are measures that can affect international trade flows. The extent to which they relate to GATT rules is, however, not the same for all. For example, a local content requirement is legally considered to be a violation of Article III of the GATT (national treatment). For an export performance requirement, that is not so; the question would be the trade effects of the measure.

This varying relationship of investment measures to GATT rules is a central question in elaborating new rules to address those measures, particularly the appropriateness of prohibiting some measures while addressing others on a case-by-case basis. Needless to say, at the heart of all this for a large number of countries is the question of the extent to which they are ready to limit their freedom to impose such measures on foreign investors through a multilateral agreement.

Developing countries argue that the use of such measures is an important instrument in the implementation of their investment policies. They believe that any disciplines in this area must take into account their development needs. They obviously have to balance concessions in this area with benefits to be achieved in other negotiating areas of interest to them.

Trade in Services

Services, for many countries, is the fastest growing economic sector and the most vigorous creator of jobs. Commercially traded services include transport, telecommunications, information services, construction, broadcasting, medical services, professional services, banking, insurance, and many others. They are basically everything except for state functions. The production of services accounts on

average for nearly 60 percent of the GDP of developed countries and for 50 percent of developing countries. The value of world trade in commercial services was estimated at about $600 billion for 1988. During 1980–90, trade in services grew at about twice the rate of merchandise trade. Owing to the poor quality of available statistics on such trade, these figures are almost certainly underestimated.

The objectives of the negotiations on trade in services are to develop a multilateral agreement (which exists currently in the form of a draft General Agreement on Trade in Services—GATS), to elaborate sectoral disciplines that may be necessary to address certain peculiarities in some sectors, and to negotiate a package of initial liberalization commitments that will enter into force at the same time as the agreement itself.

When the negotiations started in 1986, the level of understanding of the conceptual problems involved in developing a multilateral system on trade in services was poor. It did not take the negotiators long to discover that a simple transposition of GATT principles and rules to the area of services would not be possible. For example, the notion of national borders, which is central in merchandise trade measures, does not apply in the case of services. There is no border point at which tariffs or quantitative measures could be imposed. Also, the nature of services, which often require the physical proximity of the producer to the consumer, makes the transaction of supplying a service fundamentally different from supplying goods. The former requires the movement of factors of production across national boundaries in order to conclude a transaction. Consequently, the rules that need to be developed had to be different from those that are in the GATT.

The objective of the GATS is to achieve progressive liberalization of trade in services with the aim of promoting economic growth for all parties and the development of developing countries. The developing countries' concerns and interests were placed, by the negotiating mandate, at the heart of the negotiations. They have found their expression also in the provisions of the draft text of the agreement.

Developing countries understand the crucial role that the services sector of their economies has to play in development. Having a dynamic and efficient services sector is necessary for raising the productivity and competitiveness of all other sectors of the economy. Therefore they also realize that they have a fundamental interest in

these negotiations. The development of multilateral disciplines would enable them not only to secure export opportunities in some labor-intensive services but also to benefit from a more open international market, which will provide them with technologically advanced services at the most competitive prices. Those services often have backward and forward linkages with other economic activities and represent an important element in determining their competitiveness.

Current State of Play in the Uruguay Round

The original deadline to conclude the Uruguay Round was December 1990. At the end of the Trade Negotiations Committee meeting, held at ministerial level in Brussels on December 3–7, 1990, it was declared that ministers were not in a position to conclude the Uruguay Round at that point. More time was needed to reach agreement on a number of politically important issues in important negotiating areas, most notably agriculture. Other areas clearly needed more time to refine agreements that were reached, or even to reach agreement on a common basis for negotiations, such as anti-dumping and trade-related investment measures.

The negotiations were resumed at the beginning of 1991 after concentrated efforts to provide for the elements of consensus that were necessary. Another major element of uncertainty was also overcome by the extension by the U.S. Congress of the "fast-track" authority granted to the executive branch of the Government to negotiate trade agreements.

After the negotiations were suspended in Brussels, intensive consultations resulted in the resumption of the process on February 26, 1991. The breakthrough was an agreement on a negotiating approach for agriculture. A work program was also adopted with respect to other negotiating areas. The negotiating structure was also streamlined to be more efficient. No specific target date was set to conclude the negotiations; it was agreed that it would emerge from the process itself based on the real progress achieved.

Intensified negotiations have continued since then, and by the end of July 1991 a meeting of the Trade Negotiations Committee concluded that the Round was entering its decisive phase and that all the elements necessary finally to carry the Round to a successful end were at hand. It was noted that, in agriculture, textiles, market

access, and services, the combination of work done before and after Brussels enabled participants to move into the final stage of negotiations. Also in the area of rule making and the trade-related aspects of intellectual property rights, the time was ripe for the final political trade-offs. And in areas where common negotiating texts were not yet agreed, such as trade-related investment measures and antidumping, once essential political decisions were taken, agreements would fall into place fairly quickly.

The importance attached to a successful conclusion of the Uruguay Round was expressed at the highest political level, most notably by the London summit of the Group of Seven. Other statements were also made by the IMF, the World Bank, and the Organization for Economic Cooperation and Development. What all these statements, and others, had in common was that the Uruguay Round is the first priority of the world economy. It has been made clear that the political consensus behind the Round, the most important single element to the process, is intact.

Developing Countries and the Uruguay Round

As mentioned earlier, the role of developing countries in the multilateral trading system has evolved considerably owing to the evolution in their trade policies and the role of such policies in development. Their move toward more outward-oriented policies has made a successful conclusion of the Round even more important to them. Achieving higher rates of growth and the ability to overcome debt-servicing problems are closely linked to export growth rates for many developing countries. The Uruguay Round is therefore witnessing an unprecedented level of participation by those countries.

In addition to these considerations, two other important developments have taken place in parallel with the negotiations. The first is the major trend adopted by many developing countries recently toward unilateral trade liberalization. In recent years many of them have lowered their tariff rates and streamlined their tariff structures, and some have even bound their entire tariff schedules in the GATT. Many of them have also dismantled the majority of their nontariff barriers in the context of trade policy reform programs. In return for such major moves, those countries hope to see meaningful

liberalization of barriers to their exports to developed country markets, which are often of a discriminatory nature.

The second is the increasing trend toward regional arrangements among developed countries and the fear of creating trade blocs, most important of which are the Free Trade Agreement between Canada and the United States, and the creation of a single European market. Participants in such agreements argue that their objective is to liberalize trade further among them without eroding the trade opportunities of nonparticipants. Nonetheless, they are being viewed by many developing countries as a threat to trade interests and to the multilateral system.

The developing countries consider that they have gone a long way toward integrating themselves into the multilateral system and that it is now up to the major industrial countries to live up to their political statements.

Relevance and Implications for Arab Countries

Arab countries can be grouped, in terms of their exports, into three categories: the group of oil exporting countries that do not suffer from debt problems but nonetheless have structural problems that make them vulnerable to external factors, particularly oil price fluctuations. There is a group of primary product exporters that have not only structural problems but also endure minimum, and in some years, negative growth rates. And there is the group of countries with more diversified economies such as Egypt, Syria, Morocco, Tunisia, Lebanon, and Algeria, which enjoy a wider export base.

In spite of these subgroupings, Arab countries have much in common with the majority of developing countries throughout different regions of the world. They are, by virtue of the structures of their economies, excessively dependent on the outside world and vulnerable to external factors such as the prices of primary commodities and the rates of economic growth in developed countries. A number of them suffer severe debt-servicing problems. Most of them have also followed the classic industrial policy approach adopted by the majority of developing countries that was based on an export substitution strategy coupled with restrictive trade policies. Also, a number of them such as Morocco, Egypt, and Tunisia have lately

taken great steps toward establishing market economies and reforming their macroeconomic and trade policies to make them more outward oriented.

So far, many Arab countries have not felt it necessary or even attractive for them to be part of the GATT system. At present only four of them are Contracting Parties (Egypt, Kuwait, Morocco, and Tunisia). Oil exporting countries did not see the need to join the GATT because trade in their main export item has not been subject to any multilateral negotiations. But more important (and this does not apply only to oil exporting countries) is the role that most Arab countries assign to trade policy within their overall development strategy, which determines their approach to the multilateral trading system. Clearly a country that adopts an outward-oriented approach and puts strong emphasis on its export performance would see much more for it in the system than countries that adopt inward-looking strategies.

Therefore, the approach of Arab countries to the multilateral trading system, at this stage, has to be seen in the context of their policy orientation.

A number of Arab countries have joined many other developing countries in the move toward more outward-oriented policies with great emphasis on the promotion of their export sectors. For these countries, as for many other developing countries, the system represents the legal and institutional framework that will secure the future successful application of their policies. The set of legal rules could also provide them with the protection from bilateral pressures in their relations with large economic powers.

It also ensures stability and predictability in trade relations with non-Arab countries, particularly the developed ones. Such relations have proved to be of vital importance to the growth of their economies. Attempts to promote regional trade among Arab countries have not shown that the system could provide for trade opportunities that would satisfy their development needs. The similarities in the composition of their exports and imports do not allow for a wide range of trade opportunities. They would still need to secure export opportunities in developed country markets for agricultural, petrochemicals, textiles, and other primary products and depend on those countries for the supply of machinery, transport equipment, and other technologically advanced products.

If the previous assumption is followed, that is, if Arab countries do have a genuine interest in the multilateral trading system, whether those that have already decided to be part of it or others that are struggling to develop their economies, the Uruguay Round would also be of great importance to them. As a general consideration, the strengthening of the system resulting from a successful conclusion of the Round would secure future opportunities under a framework of equitable principles and rules and preserve the balance of rights and obligations between developed and developing countries.

More specifically, negotiations on agriculture are addressing one of the most important export areas for Arab countries, particularly those of the Mediterranean Basin that face barriers in a number of developed countries and suffer from the distortion in the world market of agricultural products.

Also, in some manufactured products like textiles, which are important for some Arab countries, the Uruguay Round is bound to produce important results in integrating this sector into the GATT system. There are also other products of export interest to some Arab countries, such as petrochemicals, for which they have an interest in eliminating different trade barriers in developed country markets.

Services is another area of importance. The services sector in Arab countries is growing in importance. It represents on average about 50 percent of GDP of the non-oil exporting countries. The new multilateral system in this area will most certainly have important implications for these countries.

Finally, the interest of Arab countries in the Uruguay Round and in the GATT system in general has to be seen in a wider policy perspective and the importance they assign to their export sectors in their development strategies. There is no doubt that a sound export-oriented trade policy within a strong credible multilateral trading system, together with the right macroeconomic policies, can go a long way toward creating a favorable investment climate that would encourage inflows of capital and technology necessary for successful industrial development.

Comment

Mohamed Mamoun Kurdi

I would like at the outset to express my thanks for the opportunity to participate in this seminar with a comment on the paper presented by Mr. Abdel Hamid Mamdouh.

First, I would like to thank Mr. Mamdouh for his detailed explanation of the historical background of the establishment of the General Agreement on Tariffs and Trade (GATT) and of the GATT Agreement, as well as for his concise exposition of the Uruguay Round, the concepts entailed in the negotiations, and their significance for the Arab countries.

The speaker alluded to the circumstances that blocked the ratification of the Havana Charter and the establishment of the International Trade Organization as the third institutional pillar of the international economic system in the wake of World War II. In turn, I would like to mention that the GATT Agreement has a unique legal status, since it has not yet been ratified, nor has it entered into force as an international agreement. What governs the international trade system as reflected in this highly important agreement is the interim protocol of the implementation of the agreement, the subsequent accession protocols, codes of conduct, and subsidiary agreements; this has made the international trade system highly complex, particularly as regards the resulting rights and duties of the contracting parties.

One manifestation of this legal complexity is perhaps the different levels of international commitment to the items of the General Agreement and its subsequent codes of conduct and subsidiary agreements. Whereas commitment to the items of Parts I and III of the General Agreement is fully binding, commitment to the items of Parts II and IV is discretionary; it is left to the discretion of the contracting party according to individual circumstances. The same

applies to the codes of conduct and subsidiary agreements in that they are mandatory only to the sanctioning parties. Suffice it to say that the number of contracting parties is over 100, of which less than one third have ratified some of the codes of conduct and subsidiary agreements.

Turning to the interests of the developing countries, we find that these have been attended to within the framework of Article XVIII of Part II and in all the articles of Part IV, and hence without the full commitment of the contracting parties. Quite often we hear from the developed countries that the Generalized System of Preferences, provided by those countries for access by developing countries' exports to their markets, is their full response to Part IV of the General Agreement. The developing countries should therefore set aside their aspirations and expectations as regards the method by which their developmental needs can be taken into account in the framework of the international trade system through the GATT (the basis being equality through the fundamentals of the system, namely, the most-favored-nation clause and the principle of "nondiscrimination between domestic production and similar imports").

If we consider, from a practical point of view, the experience of developing countries within the framework of the multilateral trade negotiations under the GATT, we find quite clearly that the rule-making authority lies only in the hands of those parties that influence trade in the various sectors. Because the participation of developing countries is rather modest in the different sectors, their participation in rule making is consequently modest. The ineffectiveness of the role of developing countries in the GATT is further accentuated by the fact that their trade interests are diversified, thus rendering it difficult if not impossible in practical terms for them to become an influential negotiating power, apart from the statements sometimes issued by this group without the opportunity to see them translated into reality. Here I must add that some developing countries with vital trade interests—and that are members of the GATT—have been treated by the rest of the contracting parties, particularly the developed ones, in a manner that is inconsistent with the philosophy of the General Agreement. Voluntary restrictions (practically imposed) on exports in such important sectors as textiles are the best example, namely, the Multifibre Arrangement. In short, the most important exports of developing countries' agricultural products and

raw materials have not yet received within the GATT the treatment that is needed for development to take place in the developing countries.

The author properly underlined the importance of the current round of multilateral trade negotiations, which represent a remarkable qualitative move in the international trade system by expanding the scope of the multilateral framework in many significant areas, including reductions in tariff levels and the assessment of ways to deal with trade controls outside the framework of tariffs, which in fact represent the most significant impediment facing developing countries' trade, whether relating to specifications or to other customs measures. Perhaps the most important trade issue discussed in this Round is making trade services subject to the controls of an international system.

Despite the negative aspects of past practices and the limitations of present circumstances for the developing countries in general, and the Arab countries in particular, these developments call for our attention and require evaluation, as well as a new, well-planned stance for dealing with the international trade system through the General Agreement on Tariffs and Trade.

After the collapse of communism, the move by Central and Eastern Europe as well as the newly independent states of the former U.S.S.R. toward the "free" trade system, and their adoption of market economics, it is no longer fitting or acceptable for Arab countries to remain tied to economic methodologies that historically and practically have proved sterile, incompatible, and incapable of meeting the needs of real economic development at a time when interdependence among the members of the international community, particularly in the economic sphere, has increased in depth and transparency. A look at the economic performance of the developed countries during the past two decades clearly shows the growth of the services sector of those countries' economies at the expense of the industrial production sector. It also discloses the conviction of those countries that the future requires the redeployment of industry to sites where there is a comparative advantage, while retaining the highly technological industries. An illustration of this orientation is the restructuring and rationalization of the petrochemical industry in the United States and Japan, suggesting the redeployment of this industry in its primary stage to the oil and gas producing countries,

and highlighting the opportunity available for the hydrocarbon producing Arab countries to develop the petrochemical industry. It is quite probable that the sensitivities witnessed in trade relations between Europe and the countries of the Gulf Cooperation Council (GCC) are attributable primarily to the nonacceptance of such facts by the European petrochemical industry, despite its satisfaction with the efficiency of production and the opportunities the future holds for this industry in the GCC states.

Another equally important development in the new international order is what the author referred to in the area of economic groups and trade arrangements. We have paid due attention to the measures establishing the unified European market and the establishment of the free trade area between the United States and Canada. Today we are witnessing the establishment of the European economic area as an extension of the unified European market, encompassing—along with the European Community (EC) countries—the European Free Trade Association (EFTA), the EC's mutual agreements and trade preferences, and the similar agreements concluded between the EFTA countries and those of Central and Eastern Europe. We are also seeing the EC move toward political, financial, and fiscal unity, as well as negotiations to expand the North American free trade area to include Mexico. At a later stage we will probably see further expansion of the arrangements to include other countries in Central and South America.

All these developments call for realistic and serious treatment on the part of the Arab countries. The question raised now is the impact of these developments on the multilateral trade system represented by the GATT, and the relationship between such developments and the Uruguay Round. The answer will neither be easy nor "inevitable."

There is no doubt that if the Uruguay Round fails, the international orientation toward liberalizing the international trade system will increase the complexity and confusion of the already highly complex and vulnerable system. The conclusion of this Round will give these groups a positive role, and prove—at least from my point of view—that the objective can be attained by different means, and that such means do not necessarily have contradictory ends.

This perception leads me to conclude that the trade interests of the Arab countries require involvement within the GATT multilateral

framework, without ignoring the regional arrangements and the economic and trade groupings already alluded to.

If we agree that the Arab countries will sooner or later reform their economic and trade systems and move toward the market economies; expand and diversify their productive and trade structures; increase their participation in industrial production and international trade; and increase their dependence on exports and promote a growing export base, then the significance of the Arab role in the international trade system will grow, proving that Arab reluctance to join the GATT is no longer warranted. Regardless of the diverse interests of the Arab countries, their need to exist within the multilateral framework will become clearer along with the expansion of their industrial base, the diversification of their export base, and the consequent need to facilitate the access of their exports to new and large markets.

Before I conclude my remarks, I would like to refer to the author's perception of the Arab oil producing countries' view of the GATT. For one reason or another, this view remains unchanged, but it is being re-examined and reassessed. While it is true that the oil sector is not currently subject to contractual arrangements within the framework of the GATT, it is also true that the commercial conditions faced by this sector require international attention, which cannot be gained without the active participation of the oil producing countries in the multilateral trade system.

The problem of oil is not one of tariffs but rather of trade measures hidden by other issues such as concern about the environment and its preservation, standardized specifications, and tax policies that greatly influence the demand for oil. Although there are numerous avenues for study of such concerns, the GATT remains an important channel, particularly in light of rearranging certain component items of the international trade system.

On the other hand, the diversification of the economic base of the Arab oil producing countries underlines the importance of the GATT as a channel through which the trade interests of these countries can be defended in the area of new, abundant, and nontraditional products. Quite naturally, interest in the expansion of the industrial base and the diversification of the economic structure requires a similar interest in the transfer and adaptation of technology, a matter that is

connected with the GATT's increasing interest in the protection of intellectual property rights, as well as trade in services, particularly in the area of investment.

While I do not have enough time to deal with these matters in detail, I ought to mention that the GATT represents an important channel for developing international arrangements that would respond positively to the interests of Arab countries, particularly the oil producing ones. This is especially true, since the development of such arrangements is still at the preliminary stage.

6

Trade Policies and Economic Integration Among the Arab Maghreb Union Countries

Hassan Abouyoub

The Arab world is facing challenges, which have now become worldwide, in seeking to achieve social and economic growth through a process of regional complementarity. Hence, in the wake of the pioneering experience of the Gulf Cooperation Council (GCC), the Arab Cooperation Council and the Arab Maghreb Union were established. The various courses adopted by these three groupings were based on different strategic concerns and basic objectives. These variations in strategies were in essence dictated by the nature of human and national resources that could be mobilized for the purpose of integration, in addition to demographic factors and actual or potential levels of complementarity, but nevertheless conflict directly with the perspective of unity prevalent within the Arab League, particularly the Council of Arab Economic Unity, and the various bilateral and multilateral attempts to achieve unity among Arab countries.

The purpose of this study is to analyze and evaluate the experience of the Arab Maghreb Union as an example in the area of complementarity in the Arab world, which will enable us to draw some fundamental conclusions. The study focuses on the following areas:

- The theoretical principles of various forms of complementarity.
- The basic features of the external trade policies of the Arab Maghreb Union countries.

- The strategic options for achieving integration of the Arab Maghreb Union countries.
- The impact of the establishment of the Arab Maghreb Union on the economic and trade relations of its member countries with the rest of the Arab countries in particular and with trade partners in general.

Theoretical Principles of Various Forms of Complementarity

Until the middle of this century, the prevailing belief was that free trade confined to a specific number of countries would raise world income as long as it ultimately contributed to the achievement of international free trade.

Restricted free trade may in fact have an impact on world production and consumption, which, in turn, may have a positive or negative influence, depending on the levels of effective protection applied by the trade partners in a regional grouping. Customs duties applied within the framework of a unified external tariff, for example, have a direct and measurable impact on the distribution of income. Furthermore, the gradual comprehensive or partial elimination of customs duties between partners in a customs area would inevitably have an impact on the distribution of production within the area.

The change in trade patterns between the various trade partners would result either in a change in the direction of trade or would have a positive impact on production levels. It might also lead to an increase in consumption and to an improvement in the standard of living of consumers within the country that has abandoned production of a certain commodity.

Evaluating the effects of a restricted trade area requires estimating the net benefit or loss of that area and the world as a whole, by assessing the magnitude of change in the direction of trade and the impact on production and consumption levels. As is made clear below, examining developments within countries of a certain customs union is complicated, and has to take into account changes in the internal and external environment. Furthermore, it is the future

developments in the union, as opposed to past performance, that take on added significance. Inasmuch as the share of a customs union increases in international trade, therefore, its impact on trade patterns worldwide also increases. For this reason, the European Community (EC) and the free trade area between the United States, Canada, and Mexico are still a matter of keen debate.

To complete this theoretical approach, various other factors requiring a more dynamic analysis should also be taken into consideration, such as communication structures; density of the commercial and banking networks; diversity of monetary systems; lack of full competition (presence of monopolies, etc.); and budgetary and taxation policies and nontradable factor costs. If these and other elements are not taken into account in the analysis, either the dynamics of a specific customs union would be overlooked or it would become clear that the maximum economic benefit for the union as a whole cannot be equivalent to the sum of the economic benefits accruing to each country separately. It is therefore necessary to outline the most important stages in the process of economic integration.

The first stage is the preferential area in which customs barriers are selectively reduced, in particular those that might impede the flow of trade. During this phase, a unified external tariff is not imposed. Such preferential areas are found in various forms in Africa and Latin America. With respect to Africa, reference should be made to the Lagos Plan, which aims at establishing a unified African market by the year 2000 through certain transitory stages, such as the preferential trade areas supported by the Economic Commission for Africa of the United Nations.

The second stage—the free trade area—is characterized by eliminating all trade barriers among the states concerned, without imposing a unified customs tariff vis-à-vis the rest of the world. Previous experience in this regard has shown that the elimination of nontariff barriers generally takes longer than the selective reduction of tariff barriers.

A customs union is the third stage. At this stage, a unified customs tariff vis-à-vis the rest of the world is imposed and gradually applied.

The fourth stage is the establishment of a unified market that allows for the free movement of labor and capital.

Finally, economic unity is considered to be the highest degree of regional integration. Within its framework, the states concerned place their economic sovereignty in the hands of a unified economic authority that supervises the adoption of unified policies covering monetary, tariff, tax, and other aspects.

External Trade Policies of the Arab Maghreb Union Countries: Basic Features

When the Marrakech Treaty was ratified in February 1988, on which the Arab Maghreb Union was established, the trade policies of the member states in the Union were vastly different. The states could be classified into two broad categories: countries that pursue a liberal trade policy (Morocco and Tunisia); and countries in which the government exercises a monopoly over trade (Algeria and Libya). Mauritania is unique as it is a least developed country and one in which the Government encourages private initiatives while at the same time it exercises strict control over foreign exchange.

Despite the variations in the nature of trade regulations of the five countries, they nevertheless face similar international pressures and are charactrerized by the same structural features. In this context both Algeria and Libya have started to implement—in varying degrees—structural adjustment reforms. In 1990 they adopted measures designed to lessen the Government's grip on external trade and to enable those in the private sector to carry out their transactions freely.

In this study, it is not sufficient, however, to classify states according to their external trade policies, but it is also necessary to highlight those considerations pertinent to the existence of a more active private sector, the linkages within the industrial sector, and the level of self-sufficiency in areas of food and energy, to make possible a better portrayal of the Maghreb trade policies.

The Maghreb countries share a number of characteristics that can be broadly outlined as follows:

- Narrow internal markets, which make it difficult for these countries to adopt effective import substitution strategies, while at the same time their ability to place competitive goods in the

world market is limited. Indeed, except for a few labor-intensive industries, those industries that are highly capital intensive are numbered (phosphate derivatives and liquid gas).

- National markets that enjoy levels of both tariff and nontariff protection far exceeding what the optimum allocation of resources requires.
- Excessive dependence on the international market—varying from country to country—with respect to agricultural foodstuffs, semimanufactured products, and technology.
- A significant concentration of Maghreb exports to those countries that colonized the region. This situation has arisen as a result of considerations such as exchange rate policies, cultural links, and a high level of financial dependency. Furthermore, the financing mechanisms that were laid down by the colonial powers implicitly supported their exports, which, in turn, caused a distortion in international competition within the markets of the region.
- The tariff and pricing policies adopted to curb inflationary pressures have in fact impeded the progress of traditional activities such as the agricultural sector. To correct this distortion, Morocco has implemented a series of measures aimed at adjusting the prices of its agricultural products. As a result, investment and production activities in the agricultural sector have started to improve. In general, it is possible to detect a certain degree of positive correlation between the level of subsidies on consumption and the level of food dependency in the countries concerned.
- Insufficient supply of goods for export and a lack of diversification, with primary commodities such as oil, phosphates, iron, citrus fruits, and primary products predominating. As a result, Maghreb exports enter into direct competition, rather than complementing one another, and trade between the Maghreb Union countries remains minimal. Indeed, such trade does not exceed 2 percent of the overall external trade of these countries. As will be seen later, this in turn justifies the importance of establishing a Maghreb trade area as the only means of mobilizing those capabilities of the Maghreb economies that are conducive to integration.

However, the above features do not conceal the inherent disparities that characterize the trade policies of the Arab Maghreb Union countries, some of which can be briefly outlined as follows:

- High levels of protection ranging between 45 percent to about 200 percent in Mauritania or Algeria.
- Quantitative restrictions in the form of import licenses or an administrative system for the distribution of hard currency for the import of goods, the levels of which vary between 10 percent and 100 percent for general imports.
- Taxes on production, which vary from one country to another; Morocco and Tunisia are the only two countries to succeed in introducing a value-added tax system. The lack of coordination in this regard may create large imbalances in intra-Maghreb trade.
- Varying exchange rate policies, some more realistic than others, with nonconvertible national currencies. This results in distortions in price levels and could consequently give rise to unbalanced competition among the various producers.
- Varying participation of private capital, national or foreign, in production or trade. Such participation is very much evident in Morocco and Tunisia but not in Algeria and Libya.
- Mechanisms for the control of quality, specifications, and health and plant protection, which are not unified.
- Investment incentives that vary from one country to another and that are based on varying mechanisms such as the exemption of profits from taxation and the subsidization of equipment and production costs.
- Variations in the pricing of nontradable factors of production, which, in turn, creates noticeable distortions in the prices of energy, water, and transport.

This exposition enables us to assess the magnitude of the process to establish the Maghreb economic area. It also shows that decision makers in the Maghreb Union can gain inspiration from the plan adopted by the European Community for the purpose of achieving integration gradually, although their respective environments are totally different. In this context, it should be mentioned that while there is a close resemblance rarely matched elsewhere in the cul-

tural, social, demographic, and religious characteristics of the Maghreb Union countries, the disparities in their economic characteristics cannot be ignored.

The economic indicators of the Union countries are reviewed in the appendix to this paper.

Strategic Options for Achieving Integration of Maghreb Countries

On the basis of the principles set forth in the treaty on the establishment of the Arab Maghreb Union, the salient features of a Maghreb strategy for mutual development were defined with the objective of achieving economic unity and ensuring the free movement of individuals, goods, services, and capital among the Union countries. This strategy has several stages, each of which will require a predetermined time period. It aims to achieve common interests for all parties and to provide the human and material resources necessary to achieve the Union's objectives, taking into account the level of growth in each member state. The stages for achieving complementarity among the Maghreb Union countries are as follows:

First stage. The realization of a free exchange of products of Maghreb origin by eliminating tariff and nontariff barriers before the end of 1992. This, in turn, requires implementing agreements ratified, completing the necessary procedures for those being studied, and introducing other related agreements.

Second stage. The establishment of a customs union, before the end of 1995, by unifying taxes and customs duties, imposing a unified customs tariff vis-à-vis the rest of the world, and unifying customs rules and regulations.

Third stage. The establishment of a common market among the Union countries before the end of the year 2000. This stage aims to achieve economic integration, establish a single market regime, and introduce unified arrangements within the Maghreb area. It also seeks to establish a single internal market free from customs duties and other barriers and characterized by the free movement of individuals, services, goods, and capital.

Fourth stage. Economic unity is achieved by unifying policies and economic development plans, on the basis of common objectives and with due consideration to reducing income disparities within each country and among them. General and sectoral policies must be formulated to pave the way for integration, particularly in areas of food security, human resources, energy, industry, transport, and communications as well as in the trade, financial, and monetary fields.

In addition to the strategic objectives mentioned above, the integration plan is based on specific priorities, the most important of which are

- The realization of self-sufficiency in food through cooperation in all related areas and elimination of all quantitative barriers to agricultural exchange.
- The accomplishment of a future industrial path that guarantees the achievement of integrated production by coordinating the various sectoral policies and introducing integrated industries.
- The establishment of joint energy projects to promote economic activity in the region, as well as the development of petrochemical industries.
- The implementation of programs that aim at linking the Maghreb countries and at enhancing road, railway, air, and sea transport networks as well as telecommunication networks.
- The coordination of policies relating to taxation, accounting, investment, insurance, reinsurance, and money.
- The coordination of policies in the area of human resource training and development, in line with the Maghreb strategy for mutual development.

In anticipation of realizing these objectives, a provisional trade and customs agreement has been concluded, based on the following principles: exemption from customs duties and taxes of similar effect; elimination of quantitative and administrative restrictions on a specific list of commodities, to be gradually expanded; imposition of a compensatory duty of 17.5 percent on goods benefiting from customs realignment, with the purpose of promoting sound competition among the region's producers; and establishment of a mechanism to compensate a member country for losses it may incur as a result of customs exemptions.

Impact of Establishing Arab Maghreb Union

In view of the high degree of protection in the Maghreb economies, the establishment of a Maghreb customs union constitutes a large-scale structural adjustment process that is expected to result in a more rational allocation of resources.

It is also expected that the Union will attract investment, both domestic and foreign, taking into consideration the size and quality of the Maghreb market, and it represents a good base for exports to the EC and the rest of the world.

Countries of the Union do not individually constitute an important negotiating power vis-à-vis the EC, as the latter is an instrument for negotiations with groups rather than individual countries.

The ability of the European Community to reduce trade barriers is enhanced by the ability of other groups to do the same. Moreover, through the adoption of a common external trade policy, the Union countries will be in a better negotiating position vis-à-vis the EC and will therefore be able to overcome the influence of former colonial powers.

The geographical distribution of the Union's trade will develop significantly, as it is expected that the Arab, African, and Iberian peninsular countries will constitute important partners for the Union countries. This also applies to the Asian and North American countries. In contrast, it is expected that France's share, in relative terms, will decline, as will dependency on the French market.

At the level of multilateral negotiations, Africa, by virtue of the Maghreb Union, will impove its bargaining position in negotiations with the GATT, UNCTAD, and others. In this context, it should be noted that, in general, the permanent secretariats of regional groupings have developed their bargaining positions in multilateral negotiations in a way superior to countries that negotiate singly. With the worldwide return to market mechanisms, the Maghreb Union will constitute an added vehicle for defending the interests of its members vis-à-vis the industrial world.

Finally, in the Arab world, the establishment of the Maghreb Union alongside the Gulf Cooperation Council gives a new impetus to joint Arab economic action and orients it toward more realistic and effective policies.

Appendix

Algeria

GDP: $58.25 billion (1990)
GDP by sector:

Agriculture	14 percent
Industry	49 percent
Services	37 percent

Exports: DA 48.04 billion (1990)
Main exports: oil products and natural gas
Imports: DA 43.96 billion (1988)
Main imports: cereals, other foodstuffs, equipment materials, and consumer goods
Exports to the EC: 71 percent
Imports from the EC: 61 percent.

Algeria's external trade is dominated by oil and gas exports, which constitute 90 percent of total exports. The 1986 decline in oil prices had a negative impact on the Algerian economy. External indebtedness was small in 1985 and has risen to more than $25 billion at present. Although Algeria is an agricultural country, it depends on the external market to meet more than two thirds of its requirements of agricultural and food products.

The level of customs duties in Algeria is higher than that of the rest of the Union countries. In some cases, it amounts to 100 percent for luxury products. Customs duties on equipment, however, are limited to 50 percent.

Algeria's trade relations with the EC countries are governed by a mutual trade agreement with other Maghreb Union countries and by preferential trade and customs agreements. Algeria implements the principles of the GATT and is currently negotiating its membership.

Libya

GDP: $23 billion (1990)
GDP by sector:

Agriculture	4 percent
Industry	68 percent
Services	27 percent

Exports: $6.6 billion (1987)
Main exports: oil products

Imports: $4.96 billion (1987)
Main imports: foodstuffs, manufactured products, equipment, and chemical products
Exports to the EC: 80 percent
Imports from the EC: 60 percent.

Libya's external trade, like Algeria's, depends on the export of oil products, which constitute more than 90 percent of overall exports. It imports most of what it needs, however, because of limited domestic production, which revolves mainly around the petrochemical industry. Libya is the only country in the Maghreb Union that is not party to the mutual trade agreement with the EC. It is not a member of the GATT, does not have any external indebtedness, and its customs duties are lower than those in the rest of the Union countries.

Libya has undertaken a unilateral decision to exempt all Arab products from customs duties. It is linked with the Union countries through preferential trade and customs agreements.

Mauritania

GDP: $960 million (1990)
GDP by sector:

Agriculture	19 percent
Industry	27 percent
Services	54 percent

Exports: $369.8 million (1987)
Main exports: iron ore and fish
Imports: $363.5 million (1987)
Main imports: oil products, machinery, equipment, and consumer goods
Exports to the EC: 51 percent
Imports from the EC: 60 percent.

Mauritania depends on imports to meet its needs for important commodities such as foodstuffs and equipment. Exports consist mainly of iron, copper, and fish and fish products. Mauritania is among the least developed countries in the world, benefiting therefore from preferential privileges within the framework of the Lomé Convention, which links the European Community with some countries in Africa, the Pacific, and the Caribbean. It is also part of the sub-

Saharan region. The drought that affected this region in the past few years has had a detrimental effect on the national economy as three fourths of the country's population depend on livestock (camels and goats) for their livelihood. This, in turn, made Mauritania vulnerable to serious financial difficulties and aggravated its external debt problem. Although Mauritania is linked with the rest of the Arab Maghreb Union countries through trade and customs agreements, its trade with them remains low. It trades primarily with the EC, from which it receives aid by virtue of, for instance, the STABEX System —approved by the Lomé Convention—which aims at stabilizing the level of export prices of beneficiary countries.

Mauritania applies customs duties ranging from 5 percent to 78 percent, except for automobiles, which are subject to a duty of 175 percent.

Morocco

GDP: $23 billion (1990)
GDP by sector:
Agriculture 16 percent
Industry, energy, and minerals 28 percent
Services 58 percent
Exports: $3.87 billion (1990)
Main exports: phosphates and its derivatives, citrus fruit, primary products, textiles, and fish
Imports: $6.33 billion (1990)
Main imports: equipment, oil, and semimanufactured products
Exports to the EC: 65 percent
Imports from the EC: 54 percent.

The volume of trade with the rest of the Arab Maghreb Union countries was only 3.9 percent of the total external trade of Morocco in 1990.

Morocco embarked on a liberal external trade policy with the adoption of a structural reform program in 1983. By virtue of this program, all restrictions on external trade were relaxed and the share of imports subject to control does not exceed 10 percent of the overall imports. Exports are not subject to any customs or noncus-

toms controls. Moreover, they benefit from a number of incentives such as tax exemptions, export insurance, and preferential financing.

With respect to customs policy, significant amendments were introduced into the Moroccan customs tariff whereby the maximum limit was reduced from 400 percent in 1982 to 45 percent in 1986. The average customs tariff does not exceed 18 percent. In addition to these measures, flexibility was introduced to exchange rate arrangements, and administrative procedures in areas of external trade were simplified.

Morocco is linked with the European Community by a cooperation agreement signed in 1976. It enjoys full membership in the GATT since 1987, and its trade relations with the Arab countries and some African countries are regulated by bilateral trade and customs agreements. These agreements stipulate full customs exemption for goods of national origin. Morocco also grants customs privileges to the least developed countries within the framework of the preferential system adopted by developing countries.

Tunisia

GDP: $10.75 billion (1990)

GDP by sector:

Agriculture	14 percent
Industry	30 percent
Services	56 percent
Main exports:	phosphates and its derivatives, textiles, citrus fruit, and olive oil

Main imports: cereals, equipment, chemical products, and machinery

Exports to the EC: 74 percent

Imports from the EC: 67 percent.

In 1986, Tunisia put forward a plan for liberalizing its external trade by eliminating quantitative restrictions on imports of a large category of manufactured products and equipment as well as some consumer goods. The plan aimed to achieve a level of external trade liberalization equivalent to 80 percent by 1991.

With respect to customs duties, the highest level does not exceed 43 percent.

Tunisia is linked with the Union countries through preferential trade and customs agreements as well as the mutual trade agreement with the EC. In 1990, Tunisia became a member of the GATT.

Comment

Abdel Hamid Al-Zigallaie

The paper presents valuable information on the economic indicators of the Arab Maghreb countries, their foreign trade policies, and the stages of their agreement to achieve economic unity, including the establishment of the Arab Maghreb Union. In the closing section of the paper, there is a listing of the positive consequences of establishing economic integration among the Arab Maghreb countries. The most important gains cited are improvement in the allocation of resources, attracting domestic and foreign investment, and increasing trade, particularly with the developing countries.

The paper focused on important areas. I would have liked to see more emphasis and analysis devoted to the last two sections, since they are the purpose and objective of the paper. They relate to the strategic options for achieving integration among the Union countries, and the impact that establishing the Arab Maghreb Union will have on the economic and trade relations of the Union member countries with the rest of the Arab countries and with trading partners in general. While the paper presented the stages of Maghreb complementarity and the priorities of work, there was no analysis or comment. Its discussion of the potential impact of the establishment of the Arab Maghreb Union was also quite brief and general. It was also expected that the last two sections would constitute the bulk of the study, since they examine foreign trade and its role in economic integration among the Arab Maghreb Union countries.

The paper discusses the theoretical principles of economic integration among the Arab Maghreb countries with a view to achieving economic unity, but makes no reference to current experience and provides no assessment of its progress; nor does the paper discuss the institutional aspects of integration, including those institutions responsible for managing trade among the Maghreb countries, oversee-

ing the implementation of agreements, and correcting deviations. In this regard, I would like to stress the importance of studying the various constraints to trade in these countries on intra-Arab trade flows, as well as the negative impact of the flow of foreign commodities along with the domestic commodities among the five Maghreb countries, particularly because of the weak potential for assessing and overseeing implementation of the value-added tax on domestic commodities. The paper fails to demonstrate clearly the impact of the lack of long-term industrial coordination on the volume of trade and on the allocation of investments in new projects. It therefore fails to recognize adequately the most important factor of integration, namely, the coordination of production and development plans, including joint projects. The growth of intra-Arab trade is directly associated with the growth of production, its distribution, and the division of labor within the group. To what extent have development plans and programs in the Arab Maghreb countries been coordinated? There is no evidence of any forthcoming action to establish a support system for payments clearance, not to mention the characteristics of such a system, which is regarded as one of the most significant bases for liberalizing and developing intra-Arab trade.

While the paper contains many constructive ideas, I do not agree with some of them. For example, at the beginning, it is stated that the strategies of the three Arab regional groupings directly conflict with the unity prevalent within the Arab League, particularly the Council of Arab Economic Unity. I believe that these regional groupings represent a method of action and are an addition to joint Arab endeavor. They constitute an alternative for rigidity and isolation and help to extend joint action constructively. The general legal framework of the League of Arab States, as we are aware, was based on historical and national linkages. The founding instruments of these groupings include objectives that go beyond that stage of cooperation toward deeper and more comprehensive stages of integration and union.

The paper divides the Arab Maghreb countries into two distinct classifications: countries that pursue a liberal market economy, and countries that exercise a monopoly over trade. This classification is not accurate and does not take the economic realities of these countries and their economic interdependence into consideration.

Nor does it recognize the changes in those countries as a result of implementing, in one way or another, structural adjustment policies.

In each country within this group import and export controls and procedures are in effect, though with relative variations in the degree of freedom or restriction. The extraction of, and trade in, strategic and primary commodities by all countries of this group—including oil and gas in Libya, Algeria, and Tunisia, iron ore in Mauritania, and phosphate in Morocco—are the responsibility of state public enterprises. Quite recently, some Arab Maghreb countries, such as Libya, Algeria, and Tunisia, have tended to give the private sector a greater role in economic activity. The paper states that "the gradual comprehensive or partial elimination of customs duties between partners in a customs area would inevitably have an impact on the distribution of production within the area." This statement, in my view, relates only to the negative impact of the comprehensive or partial elimination of trade restrictions, rather than considering the positive aspects as well. Moreover, the redistribution of production may lead to an overall improvement in the wealth and resources of the group, even though it might occur at the expense of production shortages in certain areas in a given country. Therefore, it is necessary to coordinate production and divide work among the countries of the group to strike a balance between the optimum exploitation of resources and equity in the distribution of profits and burdens for each party within the group, as one of the most important elements contributing to the success of integration.

The paper states that there is significant participation by the private and external sectors in production and trade in Tunisia and Morocco, but not in Algeria and Libya. In this regard I would like to mention that foreign participation is not necessarily advantageous, and in my view, the best orientation would be to replace foreign capital with Arab capital in the long run. This is related, from another perspective, to joint action to achieve progress in the area of the transfer and acquisition of technology.

The information provided on Arab Maghreb countries in the appendix of the paper is presented in a general descriptive form. It would have been more useful to analyze the data, and explain the impact on trade liberalization and the measures for economic integration among the countries of this group. It is not true that

Algeria's external indebtedness rose from a small amount to $25 billion in one year as a result of the decline in oil export prices in 1986.

On the Arab Maghreb countries' experience in trade liberalization among themselves within a framework of economic integration, it is customary to eliminate customs barriers in any grouping seeking trade liberalization and the establishment of a unified market. Trade barriers, as a matter of fact, are simple obstacles, which is why priority is always given to their removal, since administrative and quantitative restrictions are considered, to a certain extent, the most burdensome barriers to trade, and unless an agreement is made on a schedule to lift those barriers, the freedom of exchange of trade is at risk. This is clearly demonstrated in the priorities of the plan for integration in the study, which specifies "elimination of quantitative and administrative restrictions on a specific list of commodities, to be gradually expanded." In this connection, it is clear that restriction is the rule and freedom is the exception, because freedom of exchange is only for the commodities on the list. I believe that in the case of an ambitious project such as that of the Arab Maghreb countries, this list should have been for those commodities that are not freely traded and that fall under continued administrative restrictions for a specific transitional period, after which full liberalization of exchange of commodities is reached among the Arab Maghreb countries.

Another impediment facing intra-Maghreb trade is the presence of certain deficiencies in services, including banking, transportation, shipment, communications, and infrastructure. The cornerstone for building Maghreb economic integration is the achievement of an economic system and of economic policies that are consistent and convergent. The disparities in orientation and socioeconomic application in the five Maghreb countries are evident. The establishment of an integrated Maghreb economy requires that efforts be directed toward the formation of a consistent economic system and policies. To what extent have the five Maghreb countries actually followed the path of coordinating their economic systems and policies?

This discussant believes that the nature of the Arab Maghreb countries, as reflected in their limited scope, high protectionism, traditional relations with foreign markets, and diversity of economic policies, requires concentration on a number of areas, including the

convergence of economic systems and the coordination of domestic and external legislation. Without such measures, the steps already implemented would come to a standstill or even collapse. The potential of those countries would remain restricted within the narrow area of similarity and homogeneity of the present economic systems and policies in the five Arab Maghreb countries. Another area is the coordination of production and development plans in the field of industry, with a forward-looking orientation. This is a sound basis for the growth of intra-Arab trade and the achievement of equilibrium in the joint interests of the Arab Maghreb countries. To maximize Arab production, priority should also be given to cooperation in education, scientific research, acquisition of technology, training, and the exchange of technical information.

One of the aspects often disregarded within the Maghreb countries and other cooperative groups is joint work with Arab institutions and companies established with Arab capital to serve the Arab economy. I believe it is vital to cooperate with them and to give them special incentives, and, instead of duplicating the institutional structures, to benefit from the existing ones. I would also like to underline the importance of designing a program to study and correct the negative consequences of eliminating tariff and nontariff restrictions and the impact of Maghreb integration on production, distribution, operation, and the balance of payments.

7

Intra-Arab Trade: Determinants and Prospects for Expansion

Jamal Eddine Zarrouk[1]

Introduction

The promotion of trade among Arab countries has long been considered the basis for cooperation and economic integration within the League of Arab States. Though this vision had its origins in a political perspective, the development of Arab economies, especially in the fields of industrialization and foreign trade, contributed to the economic rationale for the promotion of intra-Arab trade. In fact, since the early fifties, joint Arab trade efforts have attempted to liberalize intra-Arab trade through various channels. Such channels include both multilateral and bilateral trade agreements and the recently established Arab Trade Financing Program. These vehicles were expected to allow Arab countries to achieve gains from increased trade, to take advantage of economies of scale that would enable them to produce for a regional market, and to promote competition.

However, historical evidence suggests that intra-Arab trade has expanded little during the last two decades and its share in total Arab trade has remained small. The shortcomings of intra-Arab trade performance have raised questions about its future direction. Will Arab countries pursue the promotion of intra-Arab trade by relying on multilateral liberalization while several of them are at different levels of development and have different trade regimes, or

[1]The author wishes to acknowledge the valuable contribution made to this paper by Mohamed Hamed Alhaj and Fares Ben Jradi.

will they devote their efforts to pursuing smaller-scale regional groupings that may be used as building blocks for an Arab economic community at a later stage? Should and can they do both simultaneously?

The purpose of this paper is to address some of these crucial issues. It attempts to identify the determinants of intra-Arab trade expansion during the 1970s and 1980s and to evaluate the likely trade effects of across-the-board preferential tariff reductions of Arab manufactures. It has three sections. Section I describes the main channels used by the Arab countries to promote intratrade.

Section II provides an empirical analysis of the determinants and characteristics of intra-Arab trade flows compared with total Arab trade flows and their changes as a result of trade preferential arrangements.

Section III sheds light on the extent to which inward-looking trade regimes and/or restrictive commercial practices in Arab countries have affected trading patterns among Arab countries. Then the likely intra-Arab trade gains from substantial tariff reductions and the elimination of nontariff barriers are simulated. The projected intra-Arab trade expansion is an exercise that aims at assisting Arab countries to assess the effects of across-the-board trade liberalization of manufactures of Arab origin.

The paper concludes with a summary of main findings and sets out policy recommendations for an intra-Arab trade liberalization scheme.

I. Principal Channels Available for Promoting Intra-Arab Trade

Arab countries have been able to utilize several channels to facilitate and expand their multilateral trade relations. The extent of these efforts can be observed from the number of both bilateral and multilateral trade agreements, which exceed those concluded in other related economic areas.

Arab multilateral trade agreements aim at establishing an institutional framework to remove in stages barriers to intra-Arab trade by providing preferential trade treatment, including mechanisms to finance and guarantee such trade. The Inter-Arab Investment Guarantee Corporation has expanded its work to intra-Arab export credit

guarantees, and the Arab Trade Financing Program was created as a specialized financial institution in intra-Arab trade. The following subsections present the main channels undertaken by Arab countries to expand intra-Arab trade, emphasizing their advantages and limitations to achievement of economic integration among Arab countries.

Arab Multilateral Trade Agreements

Trade agreements constitute the basis for preferential treatment among Arab countries. That several such agreements have been in effect since the early fifties reflects the desire of Arab Governments to provide a means to bring about an increase in intra-Arab trade.

The 1953 Transit Trade Agreement

Several Arab countries[2] concluded this agreement in 1953 to facilitate trade and organize its transit as a preparatory phase to establishing a common market later. In the same year, an agreement on the settlement of current payments and the movement of capital was concluded to complement this agreement, which granted full exemption of customs duties on farm products, livestock and their products, raw materials, and other selected primary products. However, the Transit Trade Agreement accorded less preferential treatment to manufacutured goods and retained quantitative restrictions on specific commodities.

Creation of an Arab Common Market

In 1964, a group of Arab countries[3] agreed to create a common market in stages to provide an advanced framework for intra-Arab trade promotion. The first phase was to establish a free trade area among the signatories of the agreement. The principal measure envisaged in the Arab common market was the elimination of tariffs and nontariffs for agricultural products as well as manufactures, according to a specific timetable. However, the decision to allow exceptions has led all the member countries to take advantage of this

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[2]Egypt, Iraq, Jordan, Lebanon, Saudi Arabia, and Syria. Kuwait ratified the agreement following its independence in 1962.

[3]Egypt, Iraq, Jordan, and Syria. Libya, Mauritania, and the People's Democratic Republic of Yemen joined later.

loophole, thus reducing the ability of the common market to realize a total liberalization of trade between its signatories.

The 1981 Agreement for Facilitation and Promotion of Intra-Arab Trade

The Agreement for the Facilitation and Promotion of Trade among member states of the Arab League[4] was signed in 1981, and entered into force in 1982. This agreement is a declaration of intent on the part of the signatories to negotiate the full elimination of tariff, nontariff, and taxes of similar effect for manufactured and semimanufactured goods. It thus complements the tariff exemptions for agricultural products that Arab countries exchanged under the 1953 agreement. Moreover, the 1981 agreement urges member countries to provide for the necessary financing of intra-Arab trade on a preferential basis. The 1981 agreement ushered in a product-by-product approach to trade liberalization, which involves negotiating agreements between a few Arab countries on individual products and then seeking to extend such agreements to all the members through the Arab League's Economic and Social Council. However, this process has turned out to be slow and cumbersome. In fact, negotiators were allowed to liberalize some manufactured products but not others. In addition, the negotiations did not lay out a time schedule for the stages to complete liberalization. Because many of the Arab manufactured products are similar, and countries are allowed to pick and choose among products, only a very few Arab manufactured products remain candidates for tariff exemptions.

Furthermore, the exchange of tariff exemptions between member countries involves losses at the start of the liberalization, including tariff revenue losses and the cost of restructuring inefficient industries in order to compete in a regional market. Because the 1981 agreement did not lay the grounds for a compensation scheme to balance the likely gains and losses resulting from liberalization, many signatories may have been discouraged from speeding up the trade liberalization process.

[4] Members of the Arab League are given in Appendix 2.

Although the above multilateral trade agreements have not in general led to the expected liberalization of intra-Arab trade, they have constituted a positive attitude toward Arab economic integration. Section II will shed further light on the effects of Arab multilateral trade agreements by looking at changes in trade patterns at both regional and subregional levels.

Mechanism for Intra-Arab Export Financing

In addition to the promotion of intra-Arab trade through the institutional framework of multilateral trade agreements, Arab countries also established an intratrade financing and guarantee mechanism. This subsection discusses the role and advantages of the Arab Trade Financing Program (ATFP) in promoting intra-Arab trade. Since the program has only recently started its activities, and data pertaining to intra-Arab trade financing are not available, the following discussion is not an attempt to evaluate the performance of such a program.

Objectives of the Arab Trade Financing Program

The Arab Trade Financing Program is the latest achievement in joint Arab economic endeavor. It was established in 1990, following a realization that financing intra-Arab trade is an essential factor in encouraging Arab exporters and importers to trade with each other on a continuous and regular basis. Thus it aims at enhancing the competitiveness of Arab exporters by providing the required export financing.

Its role is first to refinance intra-Arab trade in goods and accompanying services whenever they are of Arab origin. In most cases, a good is considered of Arab origin if it is produced or manufactured in an Arab country from raw materials or other components originating in any Arab country or if the Arab added value was 40 percent or more. Petroleum, used goods, and re-exported goods are excepted from this financing scheme.

Moreover, it provides financing through credit lines made available to the national financial agencies designated by Arab Governments. The necessary exporter/importer's guarantee should be acceptable to the program.

Finally, the program provides financing for preshipment and post-shipment credits to Arab exporters and importers through the national agencies.

Advantages of Arab Trade Financing Program

The program is unique in its specialization in intra-Arab trade financing. It seeks to mobilize resources to finance intra-Arab trade and to enable the Arab banking system to carry out its desired role in financing Arab trade.

ATFP credit coverage available for trade financing is about 85 percent of the credit provided by relevant national trade financing agencies. This coverage is the highest provided by an Arab trade financing institution, as shown in Appendix 1. In addition, the program provides financing to both Arab exporters and importers, while local commercial banks in Arab countries give loans only to exporters and at costly guarantees.

There is no doubt that financing intra-Arab trade through a regional program with its own independent resources will allow individual Arab countries to release part of their savings from financing intra-Arab trade to financing trade-related development projects instead. Thus the financing of intra-Arab exports by the program may relieve the balance of payments difficulties of some Arab countries.

Another advantage of this program is related to the inherent difficulty of risk assessment and the uncertainty surrounding future export performance. As a specialized institution directly involved in financing Arab trade, the ATFP might be able to collect information and practical experience that will allow it to assess the creditworthiness of the various trade partners. In the final analysis, this specialization can help small- or medium-scale Arab exporters and new Arab exporters in obtaining trade financing.

As mentioned previously, the program also has the advantage of refinancing pre-export credit, which the exporter can rarely obtain from a local trade financing scheme.

Because the program is a regional institution, it can group together trading risks and prorate them among several Arab countries. In addition, as it acquires a good financial position in the international market, it will be able to augment its resources by borrowing from foreign sources.

Arab Trade Financing Program and Export Credit Guarantees

Providing guarantees for financing intra-Arab trade is an activity that complements the work of the ATFP. Credit guarantees make it possible to refinance and ensure a continuity in the program. Since the program itself does not provide guarantees, it signed an agreement with the Inter-Arab Investment Guarantee Corporation to provide guarantees for the credit operations that are carried out by the program and its national agencies. In practice, the Corporation provides guarantees to national agencies to cover all their operations that are refinanced by the program.

Finally, it is worth recalling that a major characteristic of the recent trends in world trade flows is the increasing role of trade information technology and especially world trade information networks. Trade information technology has increased competition among businesses. The ATFP has taken the initiative in preparing for the establishment of a trade information network for Arab users. This system will be able to collect data and information on trade laws and regulations, preferential arrangements, and available export market opportunities in the Arab countries. These services will help Arab exporters to better reach Arab markets and to gain new comparative advantage.

II. Development Trends and Determinants of Intra-Arab Trade

This section starts with an analysis of trends in the evolution of intra-Arab trade during the 1970s and the 1980s. Subsequently, an applied study of two basic relationships is carried out: First, the effect of growth in per capita GDP on intra-Arab trade expansion, and second, the extent to which Arab trade preference agreements have increased intra-Arab trade. The section concludes with features of successful regional trade groupings among countries.

Development Trends of Intra-Arab Trade

Value and Share

The historical evidence (Table 1) indicates that the value of intra-Arab trade (exports and imports) increased about eleven times between 1972 and 1980, reaching $22.5 billion in 1980, compared

Table 1. Developments in Value and Share of Intra-Arab Trade in Arab Total Trade,[1] Selected Years, 1972–90

	1972	1980	1981	1985	Average 1981–85	1986	1989	1990	Average 1986–90	Average 1980–89
					(Millions of U.S. dollars)					
Intra-Arab trade	1,996.0	22,508.3	27,663.2	15,895.4	19,867.4	13,027.4	17,606.9	16,833.6	15,467.9	18,235.1
Intra-Arab exports	874.6	11,446.0	13,993.4	7,183.7	9,779.3	6,341.7	8,853.0	8,450.3	7,713.3	9,045.8
Intra-Arab imports	1,121.4	11,062.3	13,669.8	8,711.7	10,088.1	6,685.7	8,753.9	8,383.4	7,754.6	9,189.3
Total Arab trade	27,332.5	345,194.6	350,921.6	206,911.4	269,784.7	168,373.4	212,759.0	251,944.2	200,719.2	244,577.4
Total exports	16,704.2	234,321.9	216,850.9	107,959.4	147,991.7	79,769.7	116,181.3	141,246.5	104,154.3	135,380.6
Total imports	10,628.3	110,872.7	134,070.7	98,952.0	121,793.0	88,603.6	96,577.7	110,697.7	96,565.6	109,196.8
Intra-Arab trade as percentage of total trade	7.3	6.5	7.9	7.7	7.3	7.7	8.3	6.7	7.8	7.5
Intra-Arab exports as percentage of total exports	5.2	4.9	6.5	6.6	6.6	7.9	7.6	6.0	7.6	6.7
Intra-Arab imports as percentage of total imports	10.6	10.0	10.2	8.8	8.3	7.6	9.0	7.6	8.0	8.4

Source: International Monetary Fund, *Direction of Trade Statistics, 1991.*
[1]Arab total trade of member countries of the Arab Monetary Fund.

with $2 billion in 1972. Then it started declining with the fall in world oil prices, averaging $20 billion between 1981 and 1985, and $15 billion between 1985 and 1990. During the decade of the 1980s, the average value of intra-Arab trade leveled out at about $15 billion, of which intra-Arab exports alone accounted for $9 billion.

As regards the share of intra-Arab trade in total trade, it did not increase significantly during the 1970s and 1980s, averaging around 7.5 percent during the decade of the 1980s. Intra-Arab exports as a percentage of total exports accounted for about 7 percent and intra-Arab imports for more than 8 percent of the total imports during the same period.

These trends show that the importance of intra-Arab trade in total trade, either viewed from the export or the import side, has been largely insignificant.

Share of Intra-Arab Trade in Total Arab Trade with Major Regional Groupings

A summary of the shares of Arab trade distributed by selected regional trading blocs that are main Arab trading partners is presented in Table 2. In addition, detailed membership of the regional trading blocs grouped into associations between industrial and developing countries is shown in Appendix 2.

Table 2 indicates that Arab exports to the major regional trading associations have accounted for about 60 percent of total exports during the 1980s. Arab imports from these trading associations constituted about 70 percent of total imports during the same decade. This sizable share of Arab trade with the world's major trading associations reflects the increasing importance of the regional trend in Arab trade with its principal trading partners. It also suggests the likely benefits that regional trading associations stand to gain from strengthening the bargaining power of their members to assure greater market access.

As regards Arab trade with the world's major regional trading blocs whose members are industrial countries, the Arab countries exported about 48 percent of total exports and imported about 59 percent of the total imports during 1980–89. These figures suggest that Arab countries are a large export market for the industrial member countries of these trading associations. The capital and engineering goods that predominate in Arab imports from the indus-

Table 2. Developments in Direction of Arab Trade by Major Regional Trading Blocs

	Exports (as Percentage of Total Arab Exports)					Imports (as Percentage of Total Arab Imports)				
Trading Blocs	1980	1985	1989	1990	1980–89	1980	1985	1989	1990	1980–89
A. Developed Countries' Regional Trading Blocs										
European Community (EC)	33.5	36.2	29.0	31.8	34.2	37.4	40.2	42.0	45.9	41.5
North American Free Trade Area (FTA)	15.6	7.6	12.3	13.5	11.3	11.5	10.5	12.9	12.9	12.1
European Free Trade Association (EFTA)	2.2	0.9	1.2	1.6	1.4	3.2	4.3	4.8	4.7	4.2
New Zealand-Australian Free Trade Area (NAFTA)	1.0	1.0	1.0	1.2	1.1	1.0	1.6	1.5	1.7	1.5
Total (A)	52.3	45.7	43.5	48.1	48.0	53.1	56.6	61.2	65.2	59.3
B. Developing Countries' Regional Trading Blocs										
Arab Countries (Intra-Arab)	4.9	6.6	7.6	6.0	6.7	10.0	8.8	9.0	7.6	8.4
Association of South East Asian Nations (ASEAN)	2.1	1.9	2.2	2.3	2.2	0.6	1.0	2.3	2.6	1.0
Latin American Integration Association (LAIA)	2.0	3.5	2.7	2.4	3.2	0.7	1.8	1.6	1.5	1.4
Total (B)	9.0	12.0	12.5	10.7	12.1	11.3	11.6	12.9	11.7	10.8
Total (A)+(B)	61.3	57.7	56.0	58.8	60.1	64.4	68.2	74.1	76.9	70.1
C. Rest of the World	38.7	42.3	44.0	41.2	39.9	35.6	31.8	25.9	23.1	29.9

Source: International Monetary Fund, *Direction of Trade Statistics*, 1991.

trial countries incorporate higher value added than the primary and semimanufactured goods that predominate in Arab countries' exports to them.

As to Arab trade with the regional trading associations whose members are developing countries, Arab countries exported about 12 percent of total Arab exports and imported around 11 percent of the total imports during 1980–89, indicating that the regional trading associations in developing countries are export as well import markets for Arab countries.

Intra-Arab trade was the largest among the regional trading associations whose members are developing countries during 1980–89. In addition, the 8 percent intra-Arab import share and the 7 percent intra-Arab export share in total imports and exports, respectively, suggest that Arab countries are import markets for each other more than for other developing countries.

Trends in Non-Oil Intra-Arab Trade

The Arab countries as a group are oil exporting countries in the first place. But changes in the commodity structure of Arab exports took place during the 1980s. The data in Table 3 show that non-oil Arab exports as a percentage of total oil and non-oil exports have steadily increased from about 11 percent in 1980 to 14 percent in 1985, and then to 42 percent in 1989. This growing share of non-oil Arab exports can be explained by Arab countries' efforts toward industrialization and diversification of their exports away from oil.[5]

Regarding trends in non-oil intra-Arab trade in the 1980s, the data in Table 3 indicate that non-oil intra-Arab exports as a percentage of non-oil Arab total exports have fluctuated sharply. While the share of non-oil Arab exports increased steadily during the period 1980–89, the share of non-oil intra-Arab exports did not follow the same upward trend during the same period. After peaking at about 39 percent in 1980, the share of non-oil intra-Arab exports fell to about 26 percent in 1985 and then 14 percent in 1989. The declining share

[5]The growing non-oil Arab exports may result from falling oil export shares caused by the decline in oil prices during the 1980s. However, as will be elaborated later in this section, the predominant push for change in the commodity structure of non-oil Arab exports was industrialization, which shifted Arab production progressively from primary goods to manufactures.

Table 3. Developments in Shares of Non-Oil Intra-Arab Trade
(*In percent*)

	1972	1979	1980	1985	1987	1988	1989
Non-oil Arab exports as percentage of total exports	16.3	15.2	10.9	14.4	22.3	27.8	42.1
Non-oil Arab imports as percentage of total imports	97.9	97.2	96.3	95.7	95.7	97.7	97.3
Non-oil intra-Arab exports as share of non-oil Arab total exports	24.5	20.0	39.3	25.8	20.7	21.5	14.1
Non-oil intra-Arab imports as share of non-oil Arab total imports	8.6	5.8	7.0	5.6	5.9	6.1	6.8
Non-oil intra-Arab trade as share of non-oil Arab total trade	11.9	9.3	12.2	8.6	9.0	9.5	9.2

Source: Intra-Arab data are constructed from various statistical publications of the Arab Monetary Fund and from other national sources.

of non-oil intra-Arab exports underlies the impact of changes in the economic activity of Arab countries, which may have been severe on non-oil intra-Arab exports. To shed light on this impact, a comparative study of trends in the growth rates of non-oil intra-Arab export volume and Arab real output follows.

Comparative Trends in Growth of Non-Oil Intra-Arab Export Volume and Arab Real Output

To study comparative trends in Arab real output and non-oil intra-Arab export growth rates, four indicators were used: the annual average growth rates of non-oil intra-Arab volume of exports, and of both non-oil Arab real GDP[6] and per capita real GDP. The latter are both proxies for real output growth. Moreover, the study covered three periods: 1974–81; 1982–89; and 1986–89, which is considered a recession period for the Arab economies. Table 4 shows the results for the average of the three periods.

For 1974–81, similar upward trends were observed in all four growth rates. However, growth in the volume of both non-oil

[6]The basic data for non-oil Arab GDP are estimated by subtracting the mining contribution from GDP.

Table 4. Comparison of Annual Average Growth Rates of Non-Oil Arab Trade Volume, GDP, and Per Capita Real GDP
(*In percent*)

	1974–81	1982–89	1986–89
Non-oil intra-Arab exports	14.1	0.5	14.8
Non-oil total Arab exports	14.9	13.0	24.2
Arab per capita real GDP	15.8	−4.0	−0.7
Non-oil Arab real GDP	11.3	−3.9	−0.07

Sources: International Monetary Fund, *International Financial Statistics*; and Arab Monetary Fund data base.

intra-Arab and non-oil Arab exports exceeded non-oil Arab real GDP and per capita Arab GDP growth.

For 1982–89, Arab real GDP fell dramatically, as did per capita real GDP, as a result of the worldwide recession of 1980–83. Thus both non-oil Arab real GDP growth and per capita real GDP growth became negative. Likewise, growth in the volume of non-oil intra-Arab exports fell to almost zero. However, the volume of non-oil Arab exports continued to grow at an annual average rate of 13 percent, similar to that during the first period.

Finally, during 1986–89, growth in both non-oil Arab real GDP and per capita real GDP improved slightly but remained negative. While growth in the volume of non-oil intra-Arab exports was much stronger, reaching an annual average rate of 14.8 percent, growth in the volume of non-oil Arab exports was at a record annual average rate of 24 percent.

Whereas this analysis of trends highlights the strong association during the 1980s between growth in Arab real GDP and growth in the volume of non-oil intra-Arab exports, the association between Arab real GDP and the volume of non-oil Arab exports was weak. This finding seems natural and predictable, given that Arab countries, which are exporters as well as importers among each other, have experienced a decline in income and an impact from the international recession that lasted well after 1982, when many other countries started economic recovery.

Changes in Commodity Structure of Non-Oil Intra-Arab Trade

This section discusses the evolution of the commodity composition of non-oil intra-Arab exports and imports contrasted with that of non-oil total Arab exports and imports. The basic data used for the

analysis are from the UNCTAD data base. Commodities are grouped into 10 categories of goods and 4 main product groups. The 10 categories of goods are adapted from the GATT classification by broad factor-intensity groupings. For instance, food, agricultural products, minerals, and ores are considered to be primary goods. Consumer goods comprising textiles, clothing, and household equipment are in general labor intensive. Capital and engineering goods that include machinery, transport equipment, and office machinery are more capital-intensive and skill-intensive goods. The data analysis focuses on two years: 1981 is the earliest year for which Arab trade data in the Standard International Trade Classification (SITC) are available, and the most recent yearly data are available for 1988.

Table 5 shows the percentage composition of non-oil intra-Arab and total Arab exports, and Table 6, the percentage composition of non-oil imports, for 1981 and 1988.

Changes in Commodity Structure of Non-Oil Intra-Arab Exports

The percentage composition shown in Table 5 indicates that shifts in the structure of non-oil intra-Arab exports occurred during the period 1981–88. First, the relative importance of intra-Arab exports of primary goods decreased in 1988. The share of primary goods in non-oil intra-Arab exports fell from 41 percent in 1981 to 33 percent in 1988. Looking at the export basket of this product group, the share of food, accounting for 34 percent of non-oil intra-Arab exports in 1981, fell to 24 percent in 1988.

Second, the share of manufactured goods ranked highest in non-oil intra-Arab exports, reaching 35 percent in 1988 from 21 percent in 1981. In this product group, the share of chemical exports was highest in 1988 and double the 11 percent share of 1981. Subsequently, the share of consumer goods exports, ranking third in the percentage composition of non-oil intra-Arab exports, remained constant in 1988, at about the same 20 percent share as in 1981. Among consumer goods, textile exports increased from 7 percent in 1981 to 12 percent in 1988. Finally, the share of exports of capital and engineering goods fell from 18 percent in 1981 to 11 percent in 1988.

This historical evidence suggests that structural changes in the composition of intra-Arab exports took place during the 1981–88 period. These changes may have resulted from industrialization and diversification efforts by the Arab countries and materialized in the

Table 5. Developments in Product Composition of Arab Non-Oil Exports
(*In percent*)

	Product Composition of Non-Oil Exports			
	Intra-Arab		Total Arab	
	1981	1988	1981	1988
Primary Products	41.3	33.5	51.3	42.2
Food	34.3	23.9	19.2	17.4
Nonfood agriculture	5.6	1.5	13.8	18.4
Metals, minerals	1.3	8.1	18.3	18.4
Industrial Goods	20.7	35.4	22.8	23.5
Chemicals	11.0	21.6	18.9	18.1
Iron, steel	0.8	2.3	1.2	1.3
Semimanufactures	8.9	11.5	2.8	4.2
Capital Goods	17.7	11.2	5.5	3.6
Machinery and transport equipment	17.7	11.2	5.5	3.6
Consumer Goods	20.2	20.0	19.5	30.5
Textiles	6.9	11.7	8.5	15.4
Clothing	7.6	4.0	9.0	12.4
Other consumer goods	5.7	4.3	2.0	2.7
Other Commodities Not Classified Elsewhere	0.2	0.0	0.9	0.1
Total	100.0	100.0	100.0	100.0

Note. The product shares in Tables 5 and 6 are compiled from the COMTRADE data base. The commodity trade data were available only for Algeria, Egypt, Jordan, Morocco, Oman, Saudi Arabia, Syria, and Tunisia.
Source: UNCTAD, COMTRADE data base, 1990.

development of new industries such as petrochemicals, which made up more than one third of non-oil intra-Arab exports in 1988.

The general model for changes in the commodity structure of developing countries' exports hypothesizes that the evolution of comparative advantage rests on the introduction of new technology and know-how or skills. Developing countries that acquire technology through imports will first move to export semimanufactured and labor-intensive products such as consumer goods, comprising textiles and clothing. Then, at a later stage, developing countries' exports will shift to more capital-intensive and skill-intensive goods.

As far as Arab countries as a group are concerned, by acquiring textile and clothing technologies, countries like Egypt, Morocco, Syria, and Tunisia gained a comparative advantage in exporting such labor-intensive consumer goods. In addition, the resource-rich and capital-rich countries of the Gulf Cooperation Council (GCC) succeeded in developing petrochemical industries to the extent that they

Table 6. Developments in Product Composition of Arab Non-Oil Imports
(*In percent*)

	Product Composition of Non-Oil Imports			
	Intra-Arab		Total Arab	
	1981	1988	1981	1988
Primary Products	40.1	35.4	23.9	34.4
Food	29.1	25.9	19.6	25.0
Nonfood agriculture	3.7	2.4	2.5	6.0
Metals, minerals	7.3	7.2	1.8	3.4
Industrial Goods	27.3	40.1	26.3	30.1
Chemicals	10.1	22.1	6.7	13.1
Iron, steel	4.1	5.4	5.7	6.6
Semimanufactures	13.1	12.6	13.9	10.3
Capital Goods	13.7	11.1	34.8	27.2
Machinery and transport equipment	13.7	11.1	34.8	27.6
Consumer Goods	18.0	13.4	13.7	7.8
Textiles	2.2	2.8	3.9	3.7
Clothing	2.6	2.4	1.8	1.9
Other consumer goods	13.2	8.2	8.0	2.2
Other Commodities Not Classified Elsewhere	0.9	0.0	1.3	0.4
Total	100.0	100.0	100.0	100.0

Note. By definition, intra-Arab imports equal intra-Arab exports plus transport and insurance. However, intra-Arab import figures turned out to be widely different from intra-Arab export figures, after approximated costs of transport and insurance were added. It appears that many of the discrepancies can be explained also by the different recording dates for imports and exports, and different product classifications between Arab countries. Hence, the product shares of Table 6 are compiled for illustration of overall trends in intra-Arab commodity trade patterns only; they are not intended for data cross checking.
Source: UNCTAD, COMTRADE data base, 1990.

acquired new comparative advantage in exporting petrochemicals. As a result, the share of petrochemicals in total Arab exports expanded.

Table 5 indicates that the commodity structure of non-oil Arab exports has evolved differently from the commodity structure of non-oil intra-Arab exports. Thus, while the share of consumer goods in non-oil total Arab exports increased sharply, from 19.5 percent in 1981 to 30.5 percent in 1988, the share of consumer goods in non-oil intra-Arab exports remained constant. One explanation for this difference is that many Arab countries have had protected import-competing industries producing similar consumer goods. This protection may have prevented an increase in the share of consumer goods in intra-Arab exports.

Another difference in the evolution of the commodity structure of non-oil intra-Arab exports and non-oil total Arab exports concerns changes in the share of petrochemicals. While this share in the former increased sharply between 1981 and 1988, the share in the latter fell slightly over the same period. Protection policies in developed countries may have prevented GCC countries, in particular, from increasing petrochemical exports. But these trade barriers in developed countries coincided with the increase in Arab demand for petrochemicals for agricultural uses and as inputs in manufacturing, inducing an increase in the share of petrochemical products in intra-Arab exports.

Commodity Composition of Non-Oil Intra-Arab Imports

Intra-Arab imports equal by definition intra-Arab exports after adjustment for transportation and insurance. However, in practice, discrepancies may occur between these figures. Different recording dates and product classifications account for many of these discrepancies. Thus, the difference between the two sets of intra-Arab trade data is reflected in the compiled percentage commodity composition of intra-Arab imports. It can be shown from Table 6 that although the product shares in intra-Arab imports are different from those in intra-Arab exports, they still follow similar overall trends.

According to the general model, shifts in the commodity composition of developing countries' imports rest on factors such as import substitution policies, industrial capacity expansion, and the stage of development. Regarding Arab countries, the results in Table 6 highlight some similarities with, but also differences from the developing countries' model. Also, there are similarities and differences in the changing commodity structure of non-oil intra-Arab and Arab imports.

First, the share of primary goods, comprising food in intra-Arab imports declined, while the share in total Arab imports increased over the period. This result confirms other international findings on the increasing reliance of Arab countries as a group on foreign sources of food supplies. In addition, the share of industrial goods rose owing to the sharp increase in intra-Arab imports of petrochemicals between 1981 and 1988. Moreover, the share of consumer goods in both intra-Arab and total Arab imports declined over the period.

This decline may have been triggered by import substitution policies and infant industry protection in many Arab countries.

Finally, the share of capital goods in both intra-Arab and Arab imports also fell. This may have resulted on the one hand from the completion of large-scale development projects in a number of Arab countries, especially the GCC countries, and on the other from the revised development policies and reforms in heavy industries in a number of Maghreb and Mashreq countries.

Determinants of Non-Oil Intra-Arab Trade

The previous analysis of intra-Arab trade trends highlights historical evidence that the non-oil intra-Arab trade volume has been influenced by Arab real output. Also, as indicated in the data compiled on the commodity structure of non-oil intra-Arab trade, evidence suggests that Arab countries acquired new comparative advantage in manufactured goods, comprising petrochemicals, and consumer goods, including textiles and clothing. This section presents an applied study to test two basic relationships: first, between changes in non-oil intra-Arab trade and per capita GDP growth, and, second, comparing the increases in internal trade as a share of GDP before the application of preferential trade agreements with the increases after the application of such agreements. The section concludes by noting the features of successful regional trade associations in world trade.

Effects of Per Capita GDP Growth on Non-Oil Intra-Arab Trade

To test the effect of growth on changes in non-oil internal trade (imports and exports), per capita real GDP growth was used as a proxy to take into account the impacts of output and population growth. Also, the effect of per capita GDP growth was separately tested on two other variables: changes in non-oil external trade, excluding intratrade, and changes in non-oil overall trade. Thus, three types of elasticities[7] were measured to explain the impact of

[7]The elasticities were separately measured by regressing change in the intra-Arab trade volume, change in the external (non-Arab) trade volume, and change in the overall trade volume on per capita real GDP growth. A set of dummy variables was introduced in each of the three regression equations to explain the changes in elasticities after the application of the preferential trade agreements.

per capita GDP growth on changes in trade shares: first, the internal elasticity, which measures the percentage change in intratrade in response to per capita real GDP growth; second, the external elasticity, which measures the percentage change in external (excluding intratrade) trade in response to per capita real GDP growth; and finally, the overall elasticity, which measures the percentage change in total trade in response to per capita real GDP growth. These elasticities were estimated for three selected Arab regional trade groupings, namely, the members of the League of Arab States, the Arab Common Market (ACM), and the Arab countries of the GCC (see Appendix 2). Tables 7–9 present the estimated elasticities for the three selected regional trade groupings, covering two selected average periods.

Table 7 summarizes the results of the relative effect of Arab per capita GDP growth on changes in trade shares of Arab countries as a group during two selected periods. The estimated internal intra-Arab elasticity shows that, on average, a 1 percent growth of per capita GDP was accompanied by a 1.15 percent increase in the volume of intra-Arab trade during the period preceding the conclusion of the 1981 Agreement for the Facilitation and Promotion of Intra-Arab Trade. Moreover, this intratrade elasticity also did not change during 1982–89, after the application of the agreement. The dummy variable accounting for the changes in internal elasticity was not statistically significant.

Table 7. Changes in Income Elasticities for Non-Oil Trade of Arab Countries
(*In percent*)

Per Capita Income Elasticity/	Period I 1972–81	Period II 1982-89
Internal	1.15	1.15
Intra-Arab non-oil trade	(7.39)	
External	1.13	1.17
Arab non-oil trade		
(excluding intra-Arab)	(8.56)	(4.73)
Overall	1.13	1.17
Total Arab non-oil trade	(8.89)	(4.02)

Note. For Tables 7–9, the figures in parentheses for Period I are t-statistics, which measure the statistical significance of the estimated elasticities. The t-values in parentheses for Period II measure the statistical significance of the estimated dummies. If the coefficient of a dummy variable differs significantly from zero, it is added to the respective income elasticity. The regression estimation is in log-linear form.

Table 8. Changes in Income Elasticities for Non-Oil Trade of GCC Countries
(*In percent*)

Per Capita Income Elasticity/	Period I 1974–81	Period II 1982–89
Internal	0.98	0.93
Intra-GCC non-oil trade	(4.36)	(3.61)
External	1.14	1.22
GCC non-oil trade (excluding intra-GCC)	(5.82)	(6.39)
Overall	1.12	1.20
Total GCC non-oil trade	(6.31)	(5.83)

The estimated external elasticity, which equaled the overall elasticity for the Arab countries, was close in magnitude to the internal intra-Arab elasticity during both periods.

Table 8 summarizes the results of the effects of GCC per capita GDP growth on changes in GCC trade shares. These results suggest that the percentage increase of intra-GCC trade volume in response to a 1 percent growth in per capita real GDP was 0.93 percent. At the same time, both percentage changes of the external and the overall trade volumes in response to a 1 percent growth in per capita GDP were greater than 1 during the two selected periods of 1974–81, preceding the creation of the GCC free trade area, and 1982–89, after its creation.

Table 9 presents the results of the effect of ACM per capita GDP growth on changes in ACM trade shares. They show that the percentage increase of intra-ACM trade volume to a 1 percent growth of per capita GDP was 0.51 percent. However, both percentage changes of the ACM external and overall trade volumes were greater than 1 during the two selected periods: the 1961–65 period, before ACM creation, and the 1966–72 period, after it.

Thus these summary data suggest that increases in the intra-Arab trade volume were more sensitive to growth in per capita real GDP than the increases in both the intra-GCC and the intra-ACM trade volumes, before as well as after the application of trade preference agreements. The low internal elasticities within the GCC and the ACM groupings can be explained by several factors, one of which is the existence of limited and undiversified production bases in each of

Table 9. Changes in Income Elasticities for Non-Oil Trade of Arab Common Market (ACM)
(*In percent*)

Per Capita Income Elasticity /	Period I 1961–65	Period II 1966–72
Internal	0.57	0.51
Intra-ACM non-oil trade	(1.41)	(1.77)
External	1.41	1.11
ACM non-oil trade (excluding intra-ACM)	(4.41)	(1.29)
Overall	1.12	1.09
Total ACM non-oil trade	(4.47)	(1.41)

these regional groupings, which fail to make the members of the grouping one another's best customers.

In contrast, the production base in the Arab countries as a group is relatively larger and more diversified, thus allowing for economies of scale. Therefore, changes in intra-Arab trade seem to relate better and respond more strongly to growth in combined Arab output than do changes in both intra-GCC trade and intra-ACM trade to their respective real output growth.

Multilateral Trade Agreements and Patterns of Non-Oil Intra-Arab Trade

To shed further light on how Arab trading patterns have changed with the establishment of regional associations, data on the increase in non-oil internal trade (exports and imports as a share of GDP) were compiled for the League of Arab States, the GCC, and the ACM. Moreover, as noted above, the study of internal trade increases was related to two selected periods, as indicated in the tables.

Tables 10–12 show the calculated increases in intratrade as a percentage of GDP. Also, increases in two other trade shares were measured: increases in external trade as a share of GDP, and increases in total trade as a share of GDP. Table 10 presents increases in non-oil Arab trade shares as a percentage of GDP. Intra-Arab trade as a share of the Arab countries' combined GDP increased by 0.15 percent between 1974 and 1981, and then fell to 0.05 percent between 1982 and 1989, showing no net increase after the conclusion of the 1981 Arab trade preference agreement. In contrast, external trade (trade with outside Arab countries) as a ratio of Arab combined GDP declined even more than internal trade.

Table 10. Changes in Non-Oil Trade Patterns of Arab Countries
(*As percent of combined Arab GDP*)

	Total Increases		
	Period I 1974-81	Period II 1982-89	Change in Period II from Period I
Total increases in intra-Arab trade	0.15	0.05	−0.1
Total increases in Arab external trade	7.58	−1.19	−6.39
Total increases in Arab overall trade	7.73	−1.14	−6.59

Note. For Tables 10–12, the above measures of trade increases have been used as a crude test for the effect of trade policy on a country's trade patterns. (World Bank, *World Development Report, 1991*; and Schott (1989).)

Sources: International Monetary Fund, *Direction of Trade Statistics*; Arab Monetary Fund, statistical data base.

Table 11 presents the estimates for the GCC, which show that internal trade as a share of the combined GDP of the GCC members rose by 0.57 percent, from 0.36 percent between 1974 and 1981 to 0.93 percent between 1982 and 1989. Thus, it appears that growth of internal trade,[8] although slow, did occur after the GCC free trade agreement was signed. The increase in the GCC's external trade as a share of the combined GDP was higher, however, than the increase in internal trade. It seems plausible that the increase in external trade was due to the low trade barriers of the GCC countries against nonmembers and to the limited GCC industrial production base. Also the implementation of the GCC free trade agreement needed more time to evolve as a framework for allocation of production and increased trade. In addition, the new GCC industries, especially petrochemicals, produce more than the domestic markets can absorb. However, in the future, the GCC producers may benefit from their larger markets through orienting their production to the needs of the GCC high per capita income market. Finally, Table 12 indicates that increases in internal trade as a share of the ACM members' GDP

[8] The improvement in the process of collecting and classifying foreign trade data of GCC members in the 1980s, especially the revised classification into exports and re-exports, may have influenced the small increases in intratrade in the 1980s, compared with the increases in the 1970s, which, in most cases, were not based on data classified into exports and re-exports.

Table 11. Changes in Non-Oil Trade Patterns of GCC Countries
(As percent of combined GCC GDP)

	Total Increases		
	Period I 1974–81	Period II 1982–89	Change in Period II from Period I
Total increases in intra-GCC trade	0.36	0.93	0.57
Total increases in GCC external trade (excluding intra-GCC)	4.65	8.24	3.59
Total increases in GCC overall trade	5.00	9.17	4.17

Table 12. Changes in Non-Oil Trade Patterns of Arab Common Market (ACM)
(As percent of combined ACM GDP)

	Total Increases		
	Period I 1956–61	Period II 1966–72	Change in Period II from Period I
Total increases in intra-ACM trade	−0.73	0.07	0.8
Total increases in ACM external trade	−2.14	3.33	5.47
Total increases in ACM overall trade	−2.87	3.26	6.13

were insignificant after the ACM was created. However, the increase in external trade as a share of the combined ACM's GDP was higher than the increase in internal trade, following the similar trading pattern with the GCC.

The results discussed above suggest that in general the implementation of trade preference agreements was not conducive to a rapid increase in internal trade of the selected three Arab regional groupings. They frequently produced similar products, thwarting the opportunity to gain from trade based on economies of scale and product differentiation. In addition, import substitution and infant industry policies pursued by members of the associations made it difficult to free intraregional trade.

Another insight to be gained from the results is the expansion of external trade of the GCC and the ACM, which was much more rapid than the increase in internal trade. It is possible that this

increase was due in part to the low trade barriers imposed by the member countries of the GCC, especially against nonmembers. Moreover, foreign producers may have benefited from increased trade opportunities in larger regional GCC and ACM markets on the basis of economies of scale.

Finally, the summary data for the increase of intra-Arab trade confirm the discussion in the first section that the product-by-product scheme intended in the 1981 agreement failed to contribute to a rapid increase in Arab internal trade. In practice, the list approach to liberalize intra-Arab trade has so far succeeded in identifying a handful of candidates for liberalization. The apparent reluctance of Arab countries to come forward with a complete preferential scheme covering all industrial products of Arab origin has limited the scope for potential gains from intra-Arab trade liberalization.

Intraregional Trade Performance in Selected Regional Trade Groupings

The historical evidence suggested in Table 13 shows that in general regional trade groupings did not increase intraregional trade significantly during the last two decades.[9] However, some features of the regional trade groupings that expanded their intratrade more successfully than the others are worth mentioning.

Outward-oriented economic groupings have been more successful than inward-oriented ones in promoting intratrade. Among the regional groupings of industrial countries, the EC, which has a strong outward orientation, enjoyed the greatest internal trade share as a percentage of total exports, with 55 percent in 1980 and 60 percent in 1989 (Table 13). Among the regional groupings of developing countries, ASEAN, which is an outward-oriented regional association, had the highest internal trade shares, with 17 percent in 1980 and 18 percent in 1989. Intra-ASEAN trade is likely to increase as a result of the new free trade agreement concluded between its members in July 1991, which is expected to replace the current trade preference agreement that has been in place since 1960.

[9]This evidence corroborates the one reached in the World Bank's *World Development Report, 1991*.

Table 13. Comparative Intraunion Export Shares in Total Exports, 1980–89
(In percent)

	1980	1985	1989
A. Developed Countries' Regional Trading Groups[1]			
European Community (EC)	55.7	54.4	59.8
North American Free Trade Area (FTA)	26.5	38.0	33.8
European Free Trade Association (EFTA)	14.8	13.6	13.9
New Zealand-Australian Free Trade Area (NAFTA)	6.4	7.0	7.8
B. Developing Countries' Regional Trading Groups[1]			
Arab Countries (Intra-Arab)	4.8	6.3	8.0
Arab Common Market (ACM)	1.8	0.9	0.7
Gulf Cooperation Council (GCC)	3.0	4.6	5.8
Maghreb Arab Union (MAU)	0.3	1.0	2.3
Association of South East Asian Nations (ASEAN)	16.9	18.4	17.8
Latin American Integration Association (LAIA)	13.7	8.4	10.8

Source: International Monetary Fund, *Direction of Trade Statistics, 1991.*
[1]The member countries of each are listed in Appendix 2.

The regional trade groupings formed through across-the-board liberalization hold the largest share in internal trade. This is true of most regional trading associations among industrial countries that were grouped into either free trade areas or customs unions. However, most of the regional trade groupings among developing countries were formed through trade preferential agreements using a list of liberalized products to promote intratrade.

Finally, among the most important factors limiting the promotion of internal trade among developing countries are the members' small industrial production bases, their similar factor endowments (which have often led to producing similar products), inadequate infrastructure, restrictions on intraregional factor mobility, and intraregional conflicts.

III. Extent of Restrictive Trade Practices and Potential Gains from Liberalization of Intra-Arab Trade

The conclusions in Section II indicate that Arab countries acquired comparative advantage in manufactured goods at the expense of

primary goods, whose share in intra-Arab exports declined. In general, the development efforts toward industrialization and export diversification in many Arab countries have been among the main factors leading to these gains in comparative advantage.

However, the evolving difference in the commodity structures of intra-Arab exports and total Arab exports can be explained by the existence of high tariff and nontariff barriers that can lead to significant distortions in the commodity structure of Arab imports. Such high levels of protection in Arab markets may have prompted Arab exporters to look for trade opportunities for their products in less protected, non-Arab markets. To test this hypothesis, the first part of this section analyzes the extent of the restrictive trade practices in Arab countries. Then an attempt is made to measure the likely increases in intra-Arab trade as a result of across-the-board liberalization of tariff and nontariff barriers.

Tariff and Nontariff Barriers in Arab Countries

Restrictive trade practices, whether in the form of tariff or nontariff barriers, influence efficiency of resource allocation in the Arab countries. Extensive use of these practices distorts production and consumption, pushes up inflation, and weakens the international competitiveness of domestic industries. Because Arab production is less diversified than, say, the industrial or newly industrializing countries (NICs), restrictive trade practices in the Arab countries reduce trade opportunities more dramatically for Arab exporters than for the exporters of industrial countries or NICs. Even trade preferences for Arab products are still applied selectively on a few manufactured products.

Features of Tariff Barriers in Arab Countries

Disparities in level of tariffs. Levels of tariffs in the Arab countries are relatively high. In addition, extreme disparities exist, with some countries having high and others very low duties. Table 14 summarizes the levels of weighted and unweighted average tariffs in the individual Arab countries. These can be classified into low-tariff countries, namely, the countries of the GCC, and high-tariff countries, the remainder. For instance, the highest official unweighted average tariff imposed in Sudan is 250 percent; in Syria, 150 percent; in Egypt, 120 percent; and in Mauritania, 175 percent. Also, among

Table 14. Weighted[1] and Unweighted Average Tariff in Arab Countries
(*In percent*)

	Weighted			Unweighted		
Country	1981	1988	1990	Low	High	Tariff Year
Jordan	12.4	14.8	8.6	0.0	130.0	
United Arab Emirates	1.2	0.6	0.4	0.0	4.0	
Bahrain	1.7	3.4	3.0	5.0	10.0	
Tunisia	20.0	21.0	14.0	0.0	75.0	(1986)
Algeria	19.1	26.0	23.0	7.0	100.0	
Saudi Arabia	2.5	8.0	11.0	15.0	30.0	(1988)
Sudan	42.0	37.0	43.0	0.0	250.0	
Syria	12.4	15.1	11.0	10.0	150.0	
Somalia	35.0	23.2	10.9	0.0	100.0	
Iraq				5.0	150.0	
Oman	1.5	3.5	2.5	4.0	20.0	
Qatar	1.8	2.6	5.0	4.0	20.0	
Kuwait	3.5	7.0		18.0	25.0	
Lebanon			17.5	0.0	90.0	
Libya	15.4	16.5	27.0	0.7	100.0	
Egypt	35.3	29.0	18.0	2.5	120.0	(1990)
Morocco	31.2	19.0	16.0	5.0	45.0	(1987)
Mauritania	17.0	17.0	33.0	0.0	175.0	
Yemen	26.0	27.0			100.0	
Average (all Arab countries)	11.0	12.0	11.0			
Average (developing countries)				34.0[2]	81.0[3]	(1987)[4]

Sources: Weighted tariff averages: Arab Monetary Fund, statistical data base; unweighted tariff averages: UNCTAD, *Trade Control Measures in Developing Countries, 1988;* International Monetary Fund, *Annual Report on Exchange Arrangements and Exchange Restrictions,* various issues.

[1]Weighted tariff average is obtained by dividing the values of import duties by the total import values.

[2]Tariff average is based on 82 individual countries.

[3]The highest tariff average is found in South Asian region.

[4]Unweighted tariff average in developing countries was obtained from World Bank, *World Development Report, 1991.*

the high-tariff countries, there are disparities in the levels of high and low tariffs. These differences are due to the various objectives of tariffs pursued in the Arab countries, which can be one or a mix of the following: to generate government revenues, protect national and infant industries, minimize distortion in consumption by reducing tariffs or granting exemption of certain basic commodities, and impose high tariffs on luxury goods. Table 14 also shows the level of

weighted average tariffs in the individual Arab countries, which are used as indicators of changes in the structure of tariffs. The summary data show that a sharp reduction in the weighted tariffs of Jordan, Tunisia, and Egypt took place in 1990 as a result of their tariff and trade policy reforms.

Tariff escalation. As in many developed and developing countries, Arab countries impose higher tariffs on products at a higher stage of processing. This tariff escalation is illustrated by the data in Table 15, which reports both low and high levels of tariffs on each product category. The tariff rates on primary goods range between zero and a low rate in most Arab countries. Then the tariff rates are higher on intermediate and finished goods. They are highest on consumer products, comprising textiles and clothing and processed food. In addition, there is a wide dispersion in the level of tariffs on consumer goods across Arab countries. For example, tariff rates on processed food range from 5 percent in Bahrain to 100 percent in Yemen, and to 200 percent in Sudan. The tariff rates on textiles and clothing range from 4 percent in the United Arab Emirates to 100 percent in Yemen, Syria, and Algeria, and to 175 percent in Mauritania.

Effects of Tariff Barriers on Intra-Arab Trade

Although intra-Arab trade preference agreements cover raw materials and agricultural products, most of the manufactured goods of Arab origin are excluded from the preference scheme. Thus they are subject to the escalating tariffs mentioned above.

The high levels of tariffs on manufactures in most Arab countries have often resulted in high levels of protection for manufacturing sectors. Such protection discourages Arab exports of manufactures from flowing to Arab markets. Instead, trade in manufactures may continue to rely on the traditional markets of developed countries, where trading opportunities still exist despite the prevailing protection. To support this view, a comparison of protection levels in industrial countries with those in Arab countries (Table 15) shows that average levels of protection in industrial countries are much lower than the levels of protection presently found in most Arab countries, both on primary goods as well as on manufactures. The lower average levels of protection in industrial countries, coupled with the national industry protection in Arab countries, may be an important factor in boosting the export share of such goods in total

Table 15. Tariff Escalation on Imports of Arab Countries

Country	Foodstuff and Agricultural Materials		Chemicals		Processed Food		Textiles and Clothing		Machinery and Equipment	
	Low	High	Low	High	Low	High	Low	High	Low	High
Jordan	0.0	23.0	0.0	28.0	20.0	85.0	20.0	85.0	0.0	25.0
United Arab Emirates	0.0	4.0		4.0		4.0		4.0		4.0
Bahrain	0.0	5.0	0.0	5.0	5.0	10.0	5.0	10.0	5.0	10.0
Tunisia	0.0	25.0	6.5	25.0	10.0	75.0	10.0	75.0	6.5	25.0
Algeria	0.0	40.0	0.0	25.0	5.0	100.0	5.0	100.0	40.0	50.0
Saudi Arabia	0.0	12.0	12.0	20.0	12.0	20.0	12.0	12.0	12.0	20.0
Sudan	15.0	125.0	10.0	80.0	20.0	200.0	10.0	80.0	75.0	175.0
Syria	1.0	30.0	1.0	40.0	50.0	100.0	50.0	100.0	1.0	40.0
Somalia	2.0	10.0			20.0	30.0	20.0	30.0		
Iraq										
Oman	0.0	5.0		5.0		5.0		5.0		5.0
Qatar	0.0	4.0	4.0	20.0		4.0		4.0		4.0
Kuwait	0.0	4.0	4.0	20.0	15.0	25.0	0.0	15.0	0.0	20.0
Lebanon	0.0	50.0	0.0	28.0	18.0	90.0	18.0	90.0	7.0	90.0
Libya										
Egypt	0.0	30.0	0.0	30.0	10.0	100.0	7.0	80.0	7.0	30.0
Morocco	0.0	25.9	0.0	17.4	34.9	45.9	2.5	45.0	12.5	23.6
Mauritania	0.0	5.0	5.0			175.0		175.0		175.0
Yemen	0.0	40.0	0.0	25.0	50.0	100.0	50.0	100.0		50.0
Average developing countries	0.0	75.0	0.0	100.0	5.0	150.0	8.7	150.0	0.0	34.0
Average developed countries	0.8	9.4	0.1	4.9	4.4	20.0	1.7	75.6	0.4	11.5
Average (EC)	0.0	12.4	0.0	17.5	...	24.0	0.0	17.0	0.4	15.0

Sources: UNCTAD, *Trade Control Measures in Developing Countries, 1988*; International Monetary Fund, *Annual Report on Exchange Arrangements and Exchange Restrictions*, various issues; IMF-World Bank Study, *The Impact of Industrial Countries' Trade, Agricultural and Industrial Policies on Developing Countries*, 1990; and World Bank, *World Development Report, 1991*.

Arab exports and in causing its share in intra-Arab exports to stagnate.

However, the low overall level of tariffs on manufactures does not necessarily mean that trading opportunities in manufactures, including consumer goods, are more accessible in the developed than in the Arab countries. One reason is the relatively inelastic demand for imports of manufactures in Arab countries, in contrast with the highly elastic demand for such goods in developed countries. Another is the heavy reliance of developed countries on nontariff measures to restrict trade in manufactures with the developing countries. Nevertheless, both industrial and developing countries

have at present recourse to nontariff measures. The extent of nontariff barriers in the Arab countries is presented below.

Nontariff Barriers in Arab Countries

Nontariff barriers are different from tariffs. While tariffs have a direct effect on import costs, nontariff barriers are measures aimed at restricting imports (or exports) through administrative decisions. Nontariff barriers are in general highly restrictive measures imposed on quantities. They are extensively used by most Arab countries to restrict foreign trade. Nontariff barriers frequently used in Arab countries are presented in Appendix 3. They range from prohibition of import of certain commodities to government monopoly over imports, monetary and financial measures, import licensing, quotas, and additional fiscal charges on imports (paratariffs).

Import licensing and quotas. Import licensing, and, in some cases, quotas are used in Arab countries to restrict imports. Appendix 3 indicates that import licenses are required for almost all imports in 10 Arab countries,[10] although in some of these countries annual import certificates and licenses may be granted to manufacturers to import intermediate products and raw materials. Also, import licenses may be granted only for commodity lists determined by the competent authorities in 8 Arab countries.[11] In Saudi Arabia, Qatar, and Kuwait, import licenses are required only for statistical purposes and for notification to customs officials. An import license is not required in the United Arab Emirates. Overall import licensing in Arab countries is a restrictive measure often used by Arab Governments to allocate foreign exchange to correct balance of payments difficulties, and to protect national production from foreign competition.

Government monopoly over imports. Government agencies often have a monopoly over imports of primary commodities, including oil products, raw materials, minerals, cereals, and other agricultural products. The extent of government agencies' monopoly over imports ranges from 75 percent to 95 percent of the total imports in Algeria, Syria, Iraq, and Libya, and between 25 and 70 percent of the total

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[10] Jordan, Algeria, Sudan, Syria, Somalia, Iraq, Oman, Libya, Mauritania, and Yemen.

[11] Bahrain, Tunisia, Saudi Arabia, Qatar, Kuwait, Lebanon, Egypt, and Morocco.

imports in Jordan, Tunisia, Sudan, Somalia, Egypt, Mauritania, and Yemen.

Government monopoly over imports in general, and imports of manufactured goods in particular, is a restrictive trade practice, because it reduces competition between Arab exporters, which is necessary to create viable, internationally competitive industries and to take advantage of economies of scale by producing for regional markets. In addition, government monopoly over imports of manufactured goods distorts relative prices in favor of production for domestic markets. This monopoly also helps impose high economic costs, because it encourages rent-seeking from informal activities in parallel markets.

Monetary restrictions on imports. The required advance import deposit of certain amounts of money is another important restrictive measure imposed by many Arab countries to limit imports. Appendix 3 indicates that 12 Arab countries require advance deposits for imports. These deposits range from 10 percent to 100 percent of the c.i.f. value. A few Arab countries require that this percentage be deposited in foreign currencies. Likewise, such monetary restrictions influence foreign trade in general and intratrade in particular, because they tend to freeze intra-Arab patterns.

Paratariff in Arab countries. Paratariff restrictions are generally additional fiscal charges levied on imports (or exports) with an effect similar to tariffs, because they are used to restrict demand for imports and to discriminate in favor of domestic production. Appendix 3 presents the additional charges levied on imports in individual Arab countries. They are usually imposed as a percentage of the customs duties or as a percentage of the c.i.f. value.

Paratariffs may reach double the tariffs levied on imported goods. Overall paratariffs are relatively high and replicate in Arab countries. Also, the methods of their calculation are not transparent and confusion often surrounds their administration.

Potential Gains from Liberalization of Intra-Arab Trade

In an attempt to quantify the likely trade gains from substantial tariff reductions and the elimination of nontariff barriers on manufactured goods of Arab origin, two types of gains from trade liberalization are estimated. First, there are static gains, which may be realized in the short term, namely, those that will result from a

change in relative prices immediately after the removal of the trade barriers. Second, there are dynamic gains, which are long-term gains as a result of increases in production, services, investment, and growth.

Static Gains

Concept of trade creation and diversion. Measuring the likely expansion of intra-Arab trade depends on quantifying two familiar effects of a multilateral across-the-board trade liberalization. Trade creation, which takes place following tariff cuts, is somewhat similar to increases in the quantity of imported goods because they are cheaper. However, trade creation usually depends also on both the supply and the demand conditions. For example, high tariff reductions on products with low import-demand elasticities may lead to a smaller trade expansion than low reductions on products with high import-demand elasticities.

Trade diversion results from a shift of imports from relatively low-cost foreign producers' nonbeneficiaries to higher-cost producers who are beneficiaries of tariff exemptions. It is considered a discriminatory measure against nonbeneficiary countries, which may lead to a reduced economic welfare that outweighs the gains from trade creation, if the exchange of tariff exemptions was accompanied by the imposition of new, high tariff barriers against relatively low-cost nonbeneficiaries. Where trade diversion is high, and even higher than trade creation, there will be a loss of efficiency that increases the likelihood that losses from the trade preference will exceed gains.

Assumptions for measuring static gains. The methodology of measuring static trade gains from across-the-board liberalization is based on the familiar concept of trade creation and trade diversion.[12] Moreover, to quantify these two concepts, a number of assumptions have to be taken into account. First, measuring trade creation and trade diver-

[12]This method is used in calculating trade gains resulting from reduced tariffs by several international organizations in the field of trade negotiations such as UNCTAD, which has used this method to help developing countries project net increases in trade when they exchange tariff exemptions during the Uruguay Round negotiations (Laird and Yeats (1986)).

sion assumes the elimination of nontariff barriers and other administrative measures to allow for direct effects of tariff cuts. Second, it is assumed that world prices are constant. Third, because of the extreme disparities in the levels of tariffs on manufactures in Arab countries, an unweighted average tariff rate calculated by the World Bank[13] for the Middle East and North African countries was used as a basic rate for tariff concessions. In addition, across-the-board tariff cuts were proposed as a liberalization formula. Fourth, demand elasticity of intra-Arab imports of manufactures was estimated, applying a general model for estimating price elasticity.[14]

Finally, it is suggested that Arab countries would reach an agreement on the division of gains as a result of trade liberalization between them. Such agreement would encourage the members to apply tariff exemptions on intra-Arab manufactures in full.

Estimating results of trade gains. The results of the empirical evidence on the trade expansion effects of tariff cuts are summarized in Table 16. They are shown under two tariff margin cuts: 50 percent and 100 percent. An agreement that incorporated full (100 percent) concessional tariffs on intra-Arab imports of manufactures could expand intra-Arab trade by $400–500 million annually. These likely increases make up 1 percent of non-oil total Arab exports or 9 percent of non-oil intra-Arab exports annually. In the case of 50 percent concessional tariffs on intra-Arab imports, the likely intra-Arab trade expansion could reach about $200 million, that is, $\frac{1}{2}$ of 1 percent of non-oil total Arab exports or 4.5 percent of non-oil intra-Arab exports annually.

These results show that the likely intra-Arab trade expansion is relatively insignificant. Two major statistical factors explain this modest potential trade expansion: the estimated price-inelastic demand for intra-Arab imports of manufactures, and the influence of tariff-cutting rates. Regarding the weak demand for imports as a result of the tariff reduction, previous studies[15] showed that demand conditions usually change at different stages of processing. There-

[13] World Bank, *World Development Report, 1991.*

[14] Relation of demand on intraimports of manufactured goods to the relative prices and real income during 1972–89 was estimated in a log-linear form so that the coefficient can be directly interpreted as elasticity.

[15] Finger and Olechowski (1987).

Table 16. Projected Increases in Intra-Arab Trade from Across-the-Board Tariff Reductions on Manufactures of Arab Origin[1]

	Tariff Reductions	
	100 percent	50 percent
Unweighted tariff average[2]	26	26
Value of actual intra-Arab imports of manufactures, 1989 (*million U.S. dollars*)	4,420	4,420
Elasticity of demand for intra-Arab imports of manufactures (*percent*)[3]	−0.521	−0.521
	(*million U.S. dollars*)	
Projected trade creation	495	247
Projected trade diversion	88	49
Net trade creation	407	198
Net trade creation as percentage of intra-Arab non-oil exports	9 percent	4.5 percent
Net trade creation as percentage of Arab non-oil exports	1 percent	0.5 percent

[1]These projections were estimated using the SMART system and other restrictive assumptions discussed in the text of this paper. (The SMART system was developed by the staff of the World Bank and UNCTAD.)
[2]Estimated for the Middle East and North Africa by the World Bank (*World Development Report, 1991*).
[3]Intra-Arab import elasticity of demand was estimated by running a log-linear model of the effect of relative prices and real income on import volume during 1972–89. All data are annual and drawn from Arab Monetary Fund statistical data base.

fore, import demand elasticities normally increase with processing, and the potential trade expansion will be higher for goods at a higher stage of fabrication. Potential intra-Arab trade expansion will be relatively larger for fabricated, as opposed to primary commodities and semifinished goods. Thus, in assessing the influence of tariffs, consideration must be given to demand conditions to draw meaningful results about their effects on intra-Arab structure.

With regard to the level of tariff-cutting rates, the extent of their depth also affects potential trade expansion. As shown in Table 16, full cuts of 100 percent lead to higher potential intra-Arab trade increases than do 50 percent cuts. This result confirms the benefits drawn from full liberalization of intra-Arab trade in manufactures as opposed to partial tariff concessions. Although it is practically difficult to reach a full tariff exemption agreement on manufactures, an overall tariff-cutting formula based on tariffs and nontariff barrier reductions, and coupled with provisions such as duty-free reentry of domestically produced commodities that have undergone processing in another Arab location, will usher in further intra-Arab

trade expansion. In this respect, the garment industry can be a significant example.

Dynamic Gains

Dynamic gains need longer to materialize. They occur as a result of liberalization of production factors and reallocation of resources in the context of a regional industrialization, allowing the competitive process to determine the allocation of production.

Measuring dynamic gains is very difficult, since it requires estimating a complex model that extends to the structural characteristics of Arab economies. Such a work is not within the scope of this paper. However, in order to convey some indications of potential dynamic gains from intra-Arab trade liberalization, an attempt has been made to measure them under highly simplified assumptions, as follows:

- Real growth would rise between 2–5 percent annually during the first five years immediately after the liberalization (the average annual growth rate would be 3 percent during this period);
- Annual average real growth rate would reach 5 percent during the second five years after the liberalization;
- Import-demand elasticity would increase from its currently estimated rate of 1.15 percent to 1.3 percent for the first five years following the liberalization, to reach 1.5 percent during the second five-year period. Finally, the initial value of non-oil intra-Arab imports would be $7 billion, which is close to their level in 1989.

Under these assumptions, intra-Arab exports of manufactures would grow at an annual average rate of 3.9 percent of non-oil total intra-Arab exports during the first five years following the liberalization, and at a rate of 7.5 percent during the second five years thereafter.

Therefore, intra-Arab trade could increase by as much as $1.5 billion at the end of the first five years of liberalization, and by $5.2 billion at the end of ten years. These estimates are based on low growth assumption, contrasted with the higher potential growth that would result from intra-Arab trade liberalization itself. Also, the estimates of potential gains from liberalization of intra-Arab trade, whether static or dynamic, are only examples to assist policymakers

in the Arab countries in evaluating the results of a full intra-Arab liberalization of manufactures. Of course, this is not the final word in this field and the assumptions used here are greatly simplified.

Conclusions

This paper studied the main features and the determinants of non-oil intra-Arab trade trends, using historical and statistical evidence. Its main focus was to assess the effectiveness of trade promotion by studying three major Arab regional groupings: the members of the League of Arab States, the Gulf Cooperation Council, and the Arab Common Market.

The main findings can be summarized as follows:

First, the annual average value of non-oil intra-Arab trade reached about $18 billion, that is, 7.5 percent of non-oil total Arab trade during the 1980s. The annual average value of intra-Arab exports accounted for about $9 billion, while the annual average value of non-oil intra-Arab exports was $5.7 billion, or 64 percent of intra-Arab exports during the last decade. These historical trends show that intra-Arab trade's contribution to total Arab trade was insignificant.

Second, a comparison of the share of intra-Arab trade in total Arab trade by major regional trade associations shows that Arab export and import markets are the largest destination of Arab trade with developing countries.

Third, as far as non-oil intra-Arab trade is concerned, there has been a strong relationship between growth in the volume of intra-Arab trade viewed from the export side, and growth in Arab combined real GDP and per capita real GDP, compared with a much weaker relationship of growth in the volume of total Arab trade with growth of Arab output.

Fourth, regarding the commodity structure of intra-Arab exports and imports, the composition for 10 categories of goods excluding oil for the longest available period—1981–88—shows that the composition of intra-Arab exports has changed. There has been quite a strong surge in the share of industrial goods, comprising chemicals and semimanufactures, and a decline in the relative importance of primary goods. Moreover, a comparison of changes in the commodity structure of intra-Arab exports with those of total Arab exports indicates that although the share of consumer goods in total Arab

exports increased sharply, the share of such goods in intra-Arab exports remained constant in 1981–88. One main explanation for this is that many Arab countries have applied high levels of protection for emerging infant industries and national production. This protection may have prevented an increase in the share of consumer goods in intra-Arab exports.

To the extent that import substitution policies to encourage national production have often resulted in high levels of protection for domestic industries—leading to a detachment of production decisions from market signals—Arab countries that followed inward-oriented import substitution policies have failed to expand intra-Arab trade.

Fifth, a study of the effect of GDP growth on intra-Arab and external trade shows that intra-Arab trade volume was more sensitive to growth in per capita real GDP than were the intra-GCC and intra-ACM trade volumes. This result was in part due to the limited and undiversified production base in each of the GCC and ACM groupings as opposed to a larger and more diversified industrial production base in Arab countries as a group. Moreover, the Arab countries that are principal trading partners to the members of the GCC and the ACM are often nonmembers of these associations. Thus, intra-Arab trade provides better trading opportunities to Arab countries as a whole than do intra-GCC and intra-ACM trade to their members.

Sixth, the results of the study on how Arab trading patterns have changed with the 1981 Agreement for the Facilitation and Promotion of Intra-Arab Trade and the establishment of the GCC and the ACM groups show clear evidence that neither the Arab trade preference agreement nor the two associations were conducive to a rapid increase in internal trade. For the Arab countries, the product-by-product scheme adopted for intra-Arab trade liberalization failed to contribute to a rapid increase in Arab internal trade.

The apparent reluctance of Arab countries to come forward with a complete preferential scheme covering all products of Arab origin has limited the scope for potential gains from intra-Arab trade liberalization.

Seventh, restrictive trade practices in individual Arab countries are also impediments to intra-Arab trade expansion. The summary data on tariff and nontariff measures indicate that many Arab

countries impose high levels of tariffs. In addition, Arab countries apply tariff escalation, that is, higher tariffs on products at a higher stage of processing. The range of tariff rates is highest on consumer goods, in which Arab countries acquired new comparative advantage in world markets. Furthermore, there are divergences in the level of trade liberalization in individual Arab countries. For instance, the GCC countries impose relatively low levels of protection on foreign trade, while the remaining Arab countries still have high levels. These disparities could cause difficulties in motivating low-tariff and nontariff countries to exchange concessions with high-tariff and nontariff countries that are commensurate with the likely gains.

Eighth, an attempt was made to measure potential static and dynamic gains from across-the-board liberalization of tariff and nontariff barriers. For static gains, an agreement that leads to full (100 percent) concessional tariff cuts on intra-Arab imports on manufactures could expand intra-Arab trade by between $400–500 million in the first year after the agreement. These likely increases represent 1 percent of non-oil total Arab exports or 9 percent of non-oil intra-Arab exports.

Dynamic gains usually need longer to materialize. They would result from the liberalization of production factors within a larger regional market and the reallocation of resources in the context of a regional industrialization. Measuring such dynamic gains is very difficult, since it requires estimating a complex model of structural changes in Arab production, investment, and services. However, an attempt was made to provide "hypothetical" dynamic gains based on highly simplified assumptions.

Finally, the study presents strong reasons for the Arab countries to take effective measures for a multilateral trade liberalization scheme, covering all products of Arab origin and allowing for tariff and nontariff barriers to be phased out in stages. Such a trade liberalization scheme provides a significant contribution to the implementation of the 1981 Agreement for the Facilitation and Promotion of Intra-Arab Trade.

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Appendix 1

Comparative Terms and Structure of Trade Financing: ATFP Versus Trade Financing Schemes in Selected Arab Countries

Country or Scheme	Financing Scheme	Interest Rate	Maturity Period	(Maximum) Credit Coverage	Required Guarantees
Jordan	Postshipment loans	10–11.5 percent	(Longest period) short-term loans up to 80 days	Up to 80 percent	Insurance and guarantees required
Algeria	Preshipment	5 percent	180 days and up to three years for nontraditional exports	Up to 80 percent	Insurance and guarantees required
	Postshipment	8 percent			
Iraq	Preshipment	5 percent net	Up to 90 days	Up to 80 percent	Insurance and guarantees required
Egypt	Preshipment Postshipment	11–14 percent	180 days–1 year	70 percent	Insurance and guarantees required
Morocco	Preshipment Postshipment	9 percent LIBOR+margin	Up to one year traditional exports and up to five years for capital and equipment	70–85 percent	Insurance and guarantees required
Arab Trade Financing Program (ATFP)	Financing through line of credit contract with national agencies—rediscounting of trade financing instruments from national agencies preshipment and postshipment	LIBOR+ 0.25 percent	Short-term: 180 days and up to 365 days	Up to 85 percent of the eligible credit extended by the national agencies	ATFP Board of Directors shall decide nature of necessary guarantees

Source: Arab Trade Financing Program, 1991 (Abu Dhabi, United Arab Emirates).

Appendix 2
Membership of Selected Regional Trading Blocs

Trading Blocs	Type of Association	Year Formed	Member Nations
1) Arab countries	Preferential trade agreement	1981	Algeria, Bahrain, Djibouti, Egypt, Iraq, Jordan, Kuwait, Lebanon, Libya, Mauritania, Morocco, Oman, Qatar, Saudi Arabia, Somalia, Sudan, Syria, Tunisia, United Arab Emirates, Yemen
Arab Common Market	Free trade area	1964	Egypt, Iraq, Jordan, Libya, Mauritania, Syria, Yemen
Gulf Cooperation Council	Free trade area	1981	Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates
Maghreb Arab Union	Cooperation for a future customs union	1989	Algeria, Libya, Mauritania, Morocco, Tunisia
2) European Community (EC)	Economic association	1972	Belgium-Luxembourg, Denmark, France, Germany, Greece, Ireland, Italy, Netherlands, Portugal, Spain, United Kingdom
	Unified market	1992	
3) U.S.-Canada (FTA)	Free trade area	1989	United States, Canada
4) European Free Trade Association (EFTA)	Free trade area	1960	Austria, Finland, Iceland, Norway, Sweden, Switzerland
5) New Zealand-Australia Free Trade Area (NAFTA)	Free trade area	1965	Australia, New Zealand
6) Latin American Free Trade Area (LAIA)	Preferential trade agreement	1980	Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Paraguay, Peru, Uruguay, Venezuela
7) ASEAN	Preferential trade agreement	1967	Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand
	Free trade area	1991	

Appendix 3
The Extent of Nontariff Barriers in Arab Countries

Country	Prohibited Imports	Government Monopoly Over Imports	Advance Import Deposit	Import Quota Licenses	Additional Fiscal Charges on Imports
Jordan	Certain agricultural products during crop year, alcoholic beverages, second-hand cars and buses, and certain consumer goods and luxury consumables	Petroleum products, ores, and metals	30 and up to 70 percent of c.i.f. value	Import license requirement on all imports if their c.i.f. value exceeds JD 100	13 percent of c.i.f. value
United Arab Emirates	Few commodities for health and security reasons	Government procurements[1]	No	No	No
Bahrain	Cultured pearls and few other commodities for health and security reasons	Rice, sugar, government procurements[1]	No	Import licenses are required for arms and ammunition and alcoholic beverages	2 percent of c.i.f. value on fats and fresh fruits
Tunisia	List of commodities issued by Ministry of Economy	Cereals, petroleum products, foodstuffs, tobacco products (25 percent of total imports)	No	Import regime; annual import certificates, traders' quotas (industrial imports may be imported freely)	Imports are subject to 14 percent and up to 70 percent VAT and in some cases to consumption tax of the c.i.f. value
Algeria	List of commodities issued by Ministry of National Economy	Government grants concessions to public enterprises and specific groups	Imports valued at less than $2 million must be paid for in cash or with credit of up to 90 days	No	25 percent and up to 100 percent

Appendix 3 *(continued)*

Country	Prohibited Imports	Government Monopoly Over Imports	Advance Import Deposit	Import Quotas Licenses	Additional Fiscal Charges on Imports
Saudi Arabia	45 prohibited products for health and security reasons	Government procurements[1]	No	No	10.3 percent on the customs value of imported product[2]
Sudan	List of commodities issued by Ministry of Trade and Cooperation	Petroleum products, cereals, pharmaceuticals, agricultural produce	10 percent and up to 100 percent of the c.i.f. value in foreign currency	Import licenses are required for all private imports	Various additional charges on imports; 10 percent defense tax on all imports except for selected products
Syria	List of commodities issued by Ministry of Economy and Foreign Trade	agricultural goods, iron, steel, tobacco, paper, agricultural machinery, industrial goods (80 percent of all imports)	100 percent of c.i.f. value based on official exchange rate	All imports except those valued at less than LS 2,000; certain imports from ACM[3] are exempt from license	2 percent "license fee" on all imports except those by Government; 20 percent unified import surcharge
Somalia	List of commodities including those prohibited for safety and social policy	Petroleum products, pharmaceuticals, explosives, jewelry, minerals, and other products of necessity	100 percent of c.i.f. value in foreign currency	Import license for all imports except prohibited items	80 percent surcharge on alcoholic beverages, 12 percent on consumer goods, 25 percent on livestock
Iraq	List of commodities, including food preparations, alcoholic and nonalcoholic beverages, chemicals, and textile fabrics	Imports are normally handled by socialized sector	100 percent of c.i.f. value in foreign currency	Licenses for all private imports	0.5 percent and up to 0.75 percent on imports of capital goods
Oman	Few commodities for reasons of health, security, or public policy	Government procurements[1]	For nonauthorized imports	Licenses are required for all imports	No

Qatar	Pork and its derivatives, other commodities for reasons of health or security	Government procurements[1]	No	Alcoholic beverages, firearms, ammunition, and certain drugs	No
Kuwait	Certain steel and asbestos pipes, pork or foodstuffs containing pork, alcoholic beverages, and used vehicles, gas cylinders, and portable phones	Government procurements[1]	No	Licenses are required for all commercial imports other than fresh fruits and vegetables; licenses are issued freely to registered Kuwaiti merchants and companies	No
Lebanon	Narcotics, arms, ammunitions, and similar products are either prohibited or reserved for Government	Wheat, citrus fruits, apples, olive oil, peanuts	Foreign exchange may be obtained freely for licensed imports	Imports of certain other agricultural products and all seeds, certain finished goods, sanitary ceramic wares, insulated electric and telephone wires, cables made of copper	7 percent and up to 90 percent of surcharges on all imports
Libya	Consumer goods and luxury consumables	Imports included in annual commodity budget are undertaken exclusively by state-owned exterprises (90 percent of all imports)	All imports require central bank approval	All imports require exchange permits	10 percent on customs duty
Egypt	210 prohibited products, the majority of which are consumer and luxury goods	Foodstuffs, agricultural raw material, ores and metals (38 percent of all imports)	35 percent prior import deposit in domestic or foreign currency to be financed from importer's own resources	Licenses on all non-prohibited imports	12.5 percent on the c.i.f. value

Appendix 3 *(concluded)*

Country	Prohibited Imports	Government Monopoly Over Imports	Advance Import Deposit	Import Quota Licenses	Additional Fiscal Charges on Imports
Morocco	Category of imports in List "C"	Agricultural produce, petroleum products, ores and metals, and chemicals (15 percent of all imports)	Minimum import prices	Licenses are required for products in List "B" (11 percent of all imports)	12.5 percent VAT of the c.i.f. value
Mauritania	Few goods for reasons of health or public policy	Tea, sugar, rice, other	All imports must receive foreign exchange approval from central bank; advance payments for all private imports	Licenses are required for all private imports	Additional charges of up to 10 percent on the c.i.f. value
Yemen	Used machinery and equipment for resale, other commodities for health or public policy reasons	Petroleum products, medical imports, foodstuffs	Foreign exchange is provided to priority categories	Licenses are required on all private imports	1 percent tax for reconstruction; 100 percent surcharge on imports transported over land routes without licenses

Sources: International Monetary Fund, *Exchange Arrangements and Exchange Restrictions*, 1987–91; UNCTAD, *Control Measures of Developing Countries*, 1988; GATT, *Trade Policy Review: Morocco, 1991*.

1 Government procurements are required to give preference to goods of national origin and those produced within the Gulf Cooperation Council (GCC), provided that the prices of these goods are within specified margins of the prices of imported substitutes; the margins are 10 percent for goods locally produced and 5 percent for goods produced within the member countries of the GCC.

2 Harbor and service charges: 10 percent of customs value of goods. Tax on conformity certificate: 0.3 percent of customs value of goods.

3 *Annual Report on Arab Common Market*.

Comment

Tayseer Abdel Jaber

Studying the various forms and mechanisms of Arab cooperation aimed at achieving economic integration is not a new endeavor, but a continuation of awareness of the concerns and problems of the Arab nation, and an attempt to find means conducive to its growth and integration. The first physical expression of this awareness was the establishment in 1945 of the League of Arab States. Later, it was reflected in a number of bilateral and multilateral agreements and arrangements, notably—on the economic side—the ratification in 1953 of the agreement to facilitate exchange of trade and organize transit trade among some Arab countries, the Agreement for Arab Economic Unity of 1957, the decision to establish the Arab Common Market in 1964, the ratification in 1981 of an agreement to facilitate and develop trade exchanges among Arab countries, and the establishment of three Arab economic cooperation councils during 1981–89.

Of all the different modalities of Arab economic cooperation, the development of intra-Arab trade and the identification of the related problems has consumed the major part of the literature and seized the attention of Arab Governments as well as regional specialized organizations. The paper prepared for this seminar by the Arab Monetary Fund, "Intra-Arab Trade: Determinants and Prospects for Expansion," complements the study papers and research work previously conducted in this field. It is a comprehensive paper that discusses the issue from various perspectives, and, on the whole, is a commendable scientific effort. However, I have some remarks on its contents.

In discussing the rationale behind liberalizing Arab trade, the paper states that the economies of Arab countries are similar. This description, in my view, is highly simplistic. With the exception of

the economies of the GCC countries, which can be said to be similar, those of the Arab countries are more complementary than similar. There is a remarkable disparity among them as regards the distribution of natural resources, population, wealth, and environment, factors that are on the whole considered to justify complementarity and that assist in achieving such complementarity among their economies.

I also have some remarks on the outcome of the assessment of the aggregate, foreign, and intra-Arab trade of the Arab countries. The paper does not show whether the figures on aggregate, foreign, and intra-Arab trade are reported in real or nominal terms. If they are in nominal terms and per capita income is in real terms, the results of the regression are inaccurate and can only be used if a variable is introduced to represent the impact of prices on the value of trade, and thus act as another independent variable in addition to real per capita income.

Neutralizing the population effect on income by using per capita income in the sample assessed by the paper should have been accomplished on the trade variable by using the per capita trade ratio rather than aggregate trade. Alternatively, the size of the population should have been used as another variable in addition to per capita income, so long as the size of the population affects the total volume of trade. Disregarding this factor influences the significance of the results, since it overestimates income elasticity for demand on trade.

The paper acknowledges the use of dummy variables in running the regression for trade and per capita income during the two periods under review, to assess the impact of the Agreement for the Facilitation and Promotion of Intra-Arab Trade after its ratification. In this regard, I have two remarks:

First, it is necessary to use the dummy variable only in the second period (1982–89), since the agreement was not in effect during the first. Second, the paper does not indicate the coefficient of the dummy variable, so the impact of ratifying the agreement is not known.

The second period (1982–89) is not a normal period for measuring the relationship between the volume of intra-Arab trade and per capita income because the two variables tended to move downward. This is another cause for reservations about the paper's assessments

of the impact of internal elasticity on the demand for internal trade during that period. The same applies to the rest of the elasticity results in Tables 7 and 9. More research is thus needed in this area.

The paper made an assessment of the prospective static and dynamic gains from the liberalization of intra-Arab trade. The results are considered by the author of the paper as indicators to assist trade policymakers in the Arab countries. The paper, however, does not adequately preserve the theoretical background of the method used, so that it is not possible to refer to the information, thus making it difficult to accept the results. I therefore suggest greater coverage of the method of calculation.

The paper suggests that Arab and regional cooperation agreements have not led to the promotion of intra-Arab trade agreements. With the exception of intra-Arab trade, Arab foreign trade benefited from the regional trade liberalization agreements within the framework of the GCC and Arab Common Market countries more than intra-Arab trade benefited from those groupings. This conclusion has no theoretical or practical basis. The theory of complementarity does not speak about the benefits gained by countries outside the trade groupings as a result of intratrade liberalization of such groupings. From a practical point of view, there is no evidence that foreign Arab trade, except intra-Arab trade, gained from Arab cooperation agreements.

The paper concludes:

- The contribution of intra-Arab trade to overall Arab trade is marginal.
- Economic activity in the Arab countries has a greater impact on intra-Arab non-oil trade than on the growth of total Arab exports.
- The share of non-oil Arab manufactured exports during the 1980s has increased to more than one third of the value of intra-Arab exports at the expense of a diminishing share of basic commodities. The share of consumption commodities has also not increased in total intra-Arab exports owing to the adoption of import substitution and the protection given to infant industries in most Arab countries.
- With the exception of oil, intra-Arab trade for all Arab countries is more important than it is within the regional groupings selected, namely the GCC and the Arab Common Market.

- Neither the Arab nor the regional cooperation agreements could promote intra-Arab trade, but they were useful to foreign Arab trade.
- The paper discusses the reasons behind the weak intra-Arab trade from *two* standpoints: the first is that the 1981 Agreement on the Facilitation and Promotion of Intra-Arab Trade depends on commodity lists on which agreement is difficult to reach. Furthermore, the agreement does not provide for a compensation mechanism or for equity in the share of gains, opportunities, and costs as a result of liberalizing intra-Arab trade. This has led a number of Arab countries to refrain from the immediate liberalizing of their trade. Second, there are restrictive trade policies in the Arab countries.
- Arab countries are able to achieve trade gains through expanding their intra-Arab trade by eliminating or reducing tariffs.

In light of these results, the paper finds that there are strong motives for the Arab countries to take effective measures to liberalize completely their intra-Arab trade away from tariff and nontariff restrictions. This can make a positive contribution toward achieving the broad objectives of the Agreement on the Facilitation and Promotion of Intra-Arab Trade and to reforming the international trade system.

Despite the important conclusions of the paper on the current situation and the problems of intra-Arab trade, requiring a comprehensive liberalization of such trade from tariff and nontariff restrictions in order to increase the volume of Arab trade, I believe that the issue has other dimensions that call for more than just the liberalization of tariff and other trade restrictions.

Looking at the basic characteristics of joint Arab action, it seems that, prior to the 1970s, the efforts made to liberalize and smooth the flow of intra-Arab trade were too ambitious and too comprehensive. Cooperation projects lacked the flexibility necessary to accommodate the disparities among the countries concerned, on the one hand, and changing circumstances on the other. Such projects were put forward on the basis of either full acceptance or full rejection. In other words, countries that were potential parties to such arrangements were not given the option to accept the terms and conditions

of only those projects they were prepared to accept. This was one of the main factors that hampered the efficacy of the Arab Common Market and the growth of its membership despite the efforts of the Council of Arab Economic Unity to develop the market over 25 years. Elasticity is a basic element in joint action, as evidenced by the successful economic integration experience all over the world, such as the European Economic Community (EEC) and its accommodation of the individual circumstances of each member country. Furthermore, the decisions issued by the technical bodies emanating from the different organizations of joint Arab action were not binding on the member countries; such decisions depended on the political considerations involved. The experience of regional economic cooperation over the period largely depended on the relationship between governments, and hence reflected the economic and social philosophy of the more influential countries in the region without attempting to seek participation by the beneficiary grass roots (farmers, craftsmen, and traders) in strengthening and developing Arab cooperation, whether in determining the objectives of such organizations or in selecting the means to achieve those objectives.

Experience gained from the period indicates that when the industrial and agricultural sectors are underdeveloped in Arab countries, production structures are limited, and coordination of development policies is lacking, adopting trade liberalization as a method of joint Arab action will fall short of its objectives even with the best of intentions to achieve such liberalization.

In the wake of world oil price adjustments during 1973-74 and the accumulation of financial resources by some Arab countries, the interests of Arab joint action expanded from the mere liberalization of trade to other new spheres. Interest in joint Arab projects appeared the most promising means of promoting Arab integration. Capital transfers from surplus oil Arab countries to non-oil Arab countries were encouraged as was the transfer of Arab labor in the opposite direction. A number of important institutions to enhance Arab cooperation were established during the period, such as the Saudi Arabian Monetary Agency (SAMA), the Arab Fund for Economic and Social Development (AFESD), and the Inter-Arab Investment Guarantee Corporation (IAIGC). This interest in trade liberalization was maintained, and in 1981 the member countries of the

League of Arab States signed the Agreement on the Facilitation and Promotion of Trade among its members.

The results of Arab joint action in the 1960s were not encouraging; there was a lack of flexibility in dealing with the individual Arab member countries, and the growing disparities in wealth between the Arab oil countries and the rest of the Arab countries in the 1970s created different standards of living, consumption patterns, and development patterns between the two groups. These compelling factors led to the emergence of the need for subregional cooperation, which took shape through the establishment of the Gulf Cooperation Council (GCC) in 1981.

The establishment of the GCC was a novel and unique experience in the area of Arab cooperation, as it was the first multilateral arrangement outside the framework of the League of Arab States and the Council of Arab Economic Unity. Eight years later in 1989 the Arab Cooperation Council was established encompassing Iraq, Jordan, Yemen, and Egypt, followed by the establishment of the Union of Maghreb Countries comprising Tunisia, Algeria, Morocco, Libya, and Mauritania. The same period witnessed the resurgence of interest in bilateral trade agreements, and a number of such agreements were signed between the People's Democratic Republic of Yemen and Oman in November 1989, Iraq and Egypt in 1988, Egypt and the United Arab Emirates in July 1988, a Trade and Cooperation Agreement between Egypt and Sudan in February 1987, Iraq and Morocco in November 1987, and Tunis and Jordan in December 1986. The interest in bilateral agreements was behind the success achieved by such agreements in promoting intra-Arab trade more than through regional groupings such as the Arab Common Market. Bilateral agreements focus directly on the interests of the two contracting countries, and the liabilities ensuing from such agreements are limited compared with those from regional groupings with broad objectives that often exceed the ability and desires of member countries.

This significance of bilateral over multilateral agreements in shaping intra-Arab trade can be illustrated by the figures provided by the United Nations Economic and Social Commission for Western Asia (ESCWA) in 1987 on the geographical share of the intra-Arab trade of its member countries as a whole and of each individual country.

The ESCWA found that the bulk of trade was confined to the first three trading partners. At the level of the whole region, 58 percent of the export trade share involved the first trading partner, 72 percent the first and second partners combined, and 81 percent the first three partners. On the import side, the shares were 58 percent for the first partner, and 75 percent and 83 percent for the first two and the first three, respectively. At the level of the member countries, the share of intra-Arab exports of the first three partners exceeded 80 percent in six countries, namely, Bahrain, Egypt, Oman, Saudi Arabia, Syria, and the United Arab Emirates, 90 percent in the case of Iraq, and 100 percent in two countries (at that time), the Yemen Arab Republic and the People's Democratic Republic of Yemen. On the import side, the share of the first three partners was over 80 percent in five countries, namely, Egypt, Iraq, Jordan, Syria, and the United Arab Emirates and over 90 percent in Bahrain and Oman.

In light of the failure of regional organizations to promote intra-Arab trade, attributable in part to their indifference to the various aspirations and potential of individual Arab member countries, there is a need to adopt a new method of looking for ways and means by which intra-Arab trade can be developed and its problems solved. Such ways and means begin with a study of intra-Arab potential and constraints in the member countries of each organization, and later on among the different organizations.

Similarities among the GCC economies, for example, make them competitive rather than complementary. They are all largely outward-oriented economies, depending on exports of one basic commodity—oil—and importing almost all their needs for goods and services. They are characterized by small populations, an abundance of financial resources, and high income levels, and hence high standards of living leading to advanced patterns of consumption that cannot easily be met by domestic products from within the GCC or other Arab countries. Their financial potential has made it possible to apply sophisticated development methods in those economies, making them significant markets for manufacturing industries, equipment, heavy machinery, and advanced electronic goods, which are produced on a limited basis in Arab countries and therefore are imported from the industrial countries. Except for petrochemical

industries, where most GCC countries enjoy a comparative advantage, expansion in the areas of agriculture and industry at a reasonable cost is hampered by the nature of the desert land, the scarcity of raw materials needed for industry, and the shortage of labor.

The GCC's efforts in promoting means of cooperation among its member countries by liberalizing factors of production, eliminating tariffs, unifying tariffs for transactions with other countries, establishing joint projects, and facilitating the movement of commodities cannot lead to a meaningful increase in the volume of intra-GCC trade because the economic nature of its member countries does not make it possible for economic integration measures or the elimination of trade and tariff controls to increase intra-Arab trade significantly. If oil exports and re-exports are excluded, there is little to be imported from one country to the other. The figures for 1987 demonstrate that even when re-export figures, which represented a high degree of GCC intra-trade, are taken into account, the ratio of individual country imports from these countries as a whole were as follows: Bahrain, 1.2 percent; Kuwait, 2.1 percent; Qatar, 3.4 percent; Saudi Arabia, 1.6 percent; and the United Arab Emirates, 4.5 percent.

However, despite the low prospects of intra-GCC trade development on the one hand, and the limited potential of these states to export to the rest of the Arab countries on the other (except for oil, petrochemicals, and re-exported goods), the importance of the region for intra-Arab trade should not be underestimated. On the contrary, the GCC countries represent a sizable economic and financial power in the Arab world, as a source of financial flows and an important market for goods and services. Such a market provides a great opportunity to absorb products from the Arab countries that have the potential to develop their agricultural and industrial production and have a comparative advantage over the rest of the GCC countries' trading partners from outside the Arab region. This is due to geographic proximity, the low cost of production resulting from cheap labor, and the availability of raw materials at low cost. They enjoy that comparative advantage particularly for bulky commodities that are commercially not suited for long-distance transportation, such as cement, mineral water, rubber, plastic materials, and iron structures. Nevertheless, the small volume of GCC imports

from the rest of the Arab countries (at 3.3 percent of total GCC imports during 1984–87) clearly reflects the prevalence of constraints against access of other Arab countries' commodities to GCC markets, due largely to the nature of demand in GCC markets or to the trade practices therein. In part, those constraints have their sources in the other Arab countries.

Most of the Arab countries outside the framework of the GCC belong to the Arab Cooperation Council or the Arab Maghreb Union. It is difficult to assess their position on the basis of their membership in those organizations because of the short period of time since their founding and the repercussions of the Middle East crisis on their effectiveness, particularly in the case of the ACC. Assessment of the impact of Arab joint action on those countries as a whole leads to the conclusion that the opportunities for integration among those countries have not been exploited in a manner conducive to increasing their intra-Arab trade, for the following reasons.

The objectives of trade promotion and liberalization were not accompanied by measures to coordinate their development policies. Instead of making the full use of comparative advantage in certain factors of production to establish an integrated export-oriented industry, each country sought industrialization for the sake of import substitution. This resulted in the emergence of a small number of similar industries, leading to high protectionist measures taken by other Arab countries to protect their domestic industry.

Except for fruit and vegetable growing, which required special care and effort in the export process, the agricultural policies in the non-GCC countries failed to produce the basic food commodities and animal products in sufficient quantities to be included in their intra-Arab trade. In fact, they rely more heavily on imports of such commodities from outside the Arab region.

As the oil price surge receded and balance of payments pressures increased, the diminishing financial resources of these countries in general affected their ability to provide direct financing for their imports. Because of the unavailability of export financing programs in the Arab countries, these countries had to increase their imports from non-Arab countries that could afford procurement with delayed payment.

The expansionary expenditure policies that continued for many years in these countries led to significant economic distortions, reflected in higher prices and a drop in the value of their local currencies. This boosted the costs of production, thereby negatively affecting demand for their products.

Disparities in the level of economic development in the Arab countries posed a risk that one country, or a limited number of countries, might get the lion's share of gains at the expense of the less developed ones. This concern, and the absence of a compensatory mechanism to help the disadvantaged countries adjust for the results of integration, made most of the Arab countries reluctant to commit themselves to the decisions on intra-Arab trade liberalization.

The political rather than economic orientation of the decisions on Arab economic cooperation and trade liberalization is another factor. Relations among Arab Governments are fragile and unstable. Therefore, a deterioration in those relations would jeopardize decisions on cooperation and be detrimental to gains already made. The importance of this factor is such that it is necessary to separate Arab trade and economic cooperation efforts, on the one hand, and the impact of political relations on the other. This can be achieved by two measures. First, countries should avoid rash commitments that are made in response to temporary conditions or motivated by self-interest. Second, popular participation must be emphasized in identifying the objectives and means of achieving Arab trade and economic cooperation, to prevent noncompliance with or blocking of cooperation decisions. Solving the problems relating to the liberalization and promotion of intra-Arab trade requires, therefore, that efforts be made on many fronts. It is also clear that easing tariff and other trade constraints represent only one aspect of that endeavor.

In conclusion, two points must be stressed: First, the importance of intra-Arab trade becomes clearer when petroleum and its by-products are excluded. The Arab markets are the natural and basic outlets of the exports of a number of countries in the region, such as Lebanon and Jordan, for manufactured and agricultural commodities. Their exports to Arab countries, particularly to those in Western Asia, constitute a high percentage of their total exports.

Second, Arab countries have attempted all approaches to promoting cooperation and integration among themselves and to increasing

trade flows, but have failed where other groups achieved success. This indicates that the cause of failure lies not in the methods adopted, but in the lack of real commitment, for reasons that are entirely economic. The establishment of the Single European Market at the end of this year may be an incentive to the Arab countries to enhance cooperation among themselves to deal with the repercussions, which will inevitably appear if the current Arab economic situation continues to prevail.

8

Foreign Trade Policy of Egypt, 1986–91

Hanaa Kheir El-Din and Ahmed El-Dersh

The main purpose of this study is to examine the most important components of foreign trade policy in Egypt and to assess their impact on production performance and on export incentives. It will focus on distortions resulting from the trade policy adopted by Egypt during the eighties, starting in 1986. Trade distortions resulting from other policies such as price controls and investment incentives in various activities are very serious. However, the analysis is confined only to distortions arising from trade policies, namely, the tariff structure, various nontariff barriers, and the exchange rate system.

The next section provides a historic overview of Egypt's trade policies since the mid-nineteenth century, followed by a review of the current economic situation in Egypt. Then the main elements of current Egyptian foreign trade policy are examined, and the likely impact of this policy and the resulting distortions are analyzed. The final section summarizes the findings and presents the main conclusions that emerge from the study.

Historic Overview

After the collapse of Mohamed Ali's attempt to develop Egypt into an autarkic industrial economy around 1840 and the abolition of government monopolies in trade and production, and until 1930, Egypt was forced to adopt a regime of almost perfectly free trade. "The country landed on the road leading to an export oriented economy. [It was] integrated as an agricultural unit in the world-

wide economic system."[1] During almost a century of free trade, the Egyptian cotton economy was developed to a high level, but practically no industrialization took place. Direct controls were virtually nonexistent, with one important exception from 1916 onward: a ban on imports of cotton.[2] However, the Government played a major role in economic development because of its responsibilities in irrigation and in other public works.

A new attempt at industrialization began in the interwar period, stimulated by the interruption of maritime transport during the First World War, the accumulation of savings, and the increased profitability of import substitution. This attempt was led by Bank Misr (founded in 1920), which initiated the development of such nontraditional activities in the Egyptian economy as printing, cotton ginning, paper, navigation, cotton spinning and weaving, insurance, and cinema.

In 1930, Egypt gained fiscal autonomy, and immediately used its newly acquired freedom to establish the first tariff structure to protect its infant industry and raise government revenue. As a result, the few existing industries expanded, and a number of new ones were established during the 1930s: in cement, kerosene, and petroleum products.

The next major stimulus to industrialization was provided during the Second World War when Egypt was cut off from foreign supplies. This protection, coupled with increased expenditures by the allied forces, encouraged the growth of such economic activities as repairs, metal manufacturing, and construction. During the war, controls on foreign trade, supplies of necessities, prices, rents, and foreign exchange were introduced. After the war, and until 1959, the protectionist policies were continued; further industries such as nitrogenous fertilizers were established.[3]

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[1]Charles Issawi, *Egypt in Revolution: An Economic Analysis* (London; New York: Oxford University Press, 1963), p. 24.

[2]Bert Hansen and Karim A. Nashashibi, *Foreign Trade Regimes and Economic Development: Egypt* (New York: National Bureau of Economic Research, 1975), pp. 3–4.

[3]Khalid Ikram, *Egypt: Economic Management in a Period of Transition* (Baltimore, Maryland: Johns Hopkins University Press, 1980) pp. 13–15.

Until 1961, increased tariff protection, import licensing, and the imposition of other taxes and duties on imports provided additional encouragement to industry. During this period, Egypt also held substantial—though largely blocked—sterling reserves in London. Foreign trade and exchange policies consisted of stabilizing the balance of payments and the domestic economy under the constraints set by the speed at which the British Government would agree to release the blocked sterling reserves.[4]

By 1962, foreign exchange reserves were exhausted, and Egypt entered a period of permanent and severe foreign exchange shortage. Concurrently, the wave of nationalizations in 1961 and the introduction of Arab Socialism and the National Charter presented in 1962 extended the scope of government controls; what had been emergency measures before 1961 became the normal institutions of the country. The economic infrastructure, the majority of heavy and medium-sized industries and mining, and banks and insurance companies were taken over by the public sector. The entire import trade and three fourths of the export trade were made public. Private ownership and control were restricted to internal trade, land, buildings, construction, and light industry.[5] Severe import controls were imposed during the sixties. Egypt sometimes had recourse to subsidies to promote exports of selected manufactured goods such as textiles. However, the industrial strategy was heavily oriented toward encouraging import substitution activities. The performance of industry between 1961 and 1973 was dependent on the administration of the foreign exchange budget and on import quotas and controls, since the foreign trade regime during that period was completely centralized.

Although the early 1970s brought liberalization, the system of foreign exchange budgeting and import administration was not abolished. Nevertheless, import procedures for the private sector have changed several times since 1973. However, Egyptian trade policy still involved a variety of regulatory instruments: import licensing, tariffs, surcharges, guarantee deposits, and the prohibition of imports have all been, and some still are, utilized.

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[4] Hansen and Nashashibi (cited in fn. 2), pp. 4–8.

[5] Ikram (cited in fn. 3), pp. 20–23.

In question is the extent to which Egyptian trade policies affect resource allocation and growth, understating the cost of import substitution and overstating the cost of potential export activities. With extensive price controls, domestic market prices are not affected by foreign trade policies. With a large public sector in which investment decisions are made by the government and with direct intervention in production decisions, the allocation of resources does not reflect domestic market prices. A system of deliberate intervention in resource allocation through direct controls and commands may conceivably attain efficiency in production, investment, and growth—or may create more inefficiency than would result from a given trade policy under a market system. However, in a private enterprise economy, the impact of foreign trade policy can be assessed through the price distortions it causes, assuming that private producers adjust to the distorted prices.

In general, Egyptian economic policies have not been conducive to export expansion. The import substitution orientation, even after the liberalization of the economy started in 1974, is indicated by the fact that merchandise exports (other than petroleum) fluctuated around an average of 5 percent of GDP during 1977-89, compared with an average of about 11 percent for Turkey, 11.5 percent for Spain, 13 percent for Greece, and over 30 percent for the Republic of Korea, as shown in Table 1.

Current Economic Situation

The second half of the 1980s was a difficult time for Egypt's economy, when export prices for oil dropped by over $12 a barrel between December 1985 and March 1986.

- Real economic growth decelerated sharply from an average of 5 percent a year in the mid-1980s to near stagnation.
- Inflation remained in the 20–30 percent range.
- Pressures accumulated in the balance of payments: arrears built up, despite efforts at adjustment and the debt relief provided by Paris Club members and other creditors in 1987.
- Annual budget deficits of close to 20 percent of GDP constrained the economy.

The main elements behind these economic difficulties were, first, the growing external debt service burden and unfavorable external developments, such as the precipitous fall in oil prices and in other

Table 1. Share of Exports and Imports in GDP
(*In percent*)

	Egypt		Greece		Korea, Rep. of		Spain		Turkey	
	Exports/ GDP	Imports/ GDP	Exports/ GDP	Imports/ GDP	Exports/ GDP	Imports/ GDP	Exports/ GDP	Imports GDP	Exports/ GDP	Imports/ GDP
1977	6.9	25.7	10.5	26.1	28.4	30.6	8.5	14.8	3.6	12.2
1981	4.7[1]	35.4[1]	11.6	24.1	30.9	38.0	10.9	17.1	8.3	15.6
1985	2.6[1]	23.9[1]	13.6	26.7	35.1	36.1	14.5	18.0	15.1	21.6
1989	6.2[1]	25.7[1]	16.0	29.7	29.3	28.8	11.7	18.8	16.7[2]	20.4[2]
Average	5.1	27.7	12.9	26.7	30.9	33.4	11.4	17.2	10.9	17.5

Source: International Monetary Fund, *International Financial Statistics*, various issues.
[1]Relates to fiscal years ended June 30.
[2]1988.

related sources of foreign exchange (workers' remittances and Suez Canal tolls), recession in the world economy in general, and the sharp decline in the flow of aid.

Second, structural weaknesses and expansionary financial policies helped to maintain a high level of domestic demand, which, in turn, exerted strong pressures on prices and the balance of payments. These financial policies included controls on many aspects of production and investment; administered pricing, leading to severe price distortions (such as procurement prices for cotton, energy prices, prices of basic consumer goods, exchange rates, and interest rates); public sector monopolies in the production and distribution of major products and services; a restrictive import regime that provided a high degree of protection and prevented the development of an efficient tradable goods sector; a fragmented exchange system and overvaluation of the exchange rate; and sharply negative interest rates in real terms, thus providing a strong incentive to borrow in domestic currency and encouraging dollarization of the economy.

Low interest rates combined with low domestic energy prices and overvalued exchange rates encouraged inefficient investment, placed pressures on the balance of payments, and led to a shift from domestic currency holdings to foreign currency.

Starting in June 1986, Egypt embarked on a fundamental reform of its economy, aimed at introducing market forces as a major determinant of resource allocation in the economy. However, these reforms were fragmented and did not reflect an overall strategy for increasing efficiency, reducing the debt burden, and promoting growth. The excessive caution of the Government and the alleged concern about the well-being of Egyptians, particularly low-income groups, delayed these reforms.

With mounting economic difficulties,[6] the reform gathered momentum, policy measures became bolder, more encompassing, and had a wider impact on economic processes in Egypt. These developments culminated in the program of stabilization and structural reform that gained the support of the International Monetary Fund and the World Bank and was the basis of the stand-by arrangement

[6] Experience of other developing countries suggests that "an atmosphere of crisis has sometimes been the policital stimulus for reform." See World Bank, *World Development Report, 1987*, p. 96.

signed with the IMF in May 1991. The objectives of this program were to achieve, as rapidly as possible, a sustainable macroeconomic equilibrium through a number of stabilization measures; to set the stage for renewed economic growth in the medium and long term through a fundamental restructuring of the economy; and to alleviate the impact of economic reforms on the low-income groups through improvements in social policies.

The key elements of the stabilization program include measures such as unification and depreciation of the exchange rate; increasing domestic energy prices and implementing a general sales tax to reduce the overall budget deficit; and increasing interest rates and adopting a noninflationary credit and monetary policy, opening the banking and financial sector to market forces, and strengthening the Central Bank's supervisory capacity.

The structural adjustment program includes the macroeconomic framework; public enterprise reform and reordering of public investment priorities; price liberalization in the industrial, agricultural, energy, and transport sectors; liberalization of foreign trade policy by narrowing the range of tariff rates, reducing tariff preferences and exemptions, and by reducing in phases nontariff barriers on both exports and imports; and development of the private sector and regulatory reforms. These policies are expected to work in a mutually reinforcing way to reduce fiscal and external deficits, raise domestic savings, and induce efficiency changes that will restore growth to the economy.

The fundamental dual objective to be achieved by liberalizing foreign trade is to expand exports and to replace imports through pursuing two complementary lines of action: establishing competitive export channels and creating efficient import replacement capabilities. The economy would thus become self-reliant, in the sense of maintaining a high rate of investment and a high rate of growth of real national income in the future, while continuing to service external debt and reduce dependence on external borrowing.

Components of Foreign Trade Policy Since 1986

The elements of trade policy to be considered are the tariff structure, various nontariff barriers, export incentives, and the exchange rate system.

The abolition in 1986 of "import rationalization committees" that implied an import licensing system was a major turning point in Egypt's attempt to liberalize[7] its foreign trade policy. It was accompanied by a major restructuring of tariffs as well as the foreign exchange system. Yet the foreign trade system was still characterized by a considerable number of nontariff barriers and a high degree of protection for domestic output, mainly in the industrial sector.

Tariff Structure

The tariff structure is one of the main economic policy tools. Its importance lies in the fact that it can achieve a number of economic and social objectives depending on the country's stage of development. Following the nationalization of almost all export-import enterprises in 1961, a new tariff structure was established in 1962, and it was revised in 1975, in accordance with the new policy of "opening up the economy." Furthermore, in 1980 a complete reform of the tariff structure was made.

With a few exceptions, the 1980 tariff structure was quite rational, with tariff rates increasing with the stage of production. However, a number of problems have arisen with this structure. One was valuing duties at the official exchange rate, implying an effective reduction of customs duties by 15 percent and 40 percent depending on the rate of exchange applied to imports—commercial bank rate, "own" exchange rate, or otherwise. Another was that investors were frequently misled owing to distortions in the relative price structures resulting from the wide variation in the rates of customs duties within broad commodity groups.

On August 21, 1986, a new tariff plan (Presidential Decree No. 351) was issued that attempted to reform the tariff structure and to create the right incentives for domestic producers. It intended to

- Simplify the tariff categories by reducing them from 43 to 10 categories, increasing from a rate of 5 percent to a rate of 160 percent (except for food imports, subject to a 1 percent tax);

[7]Liberalization means "any policy action that reduces the restrictiveness of controls—it may be their complete removal, or the replacement of a restrictive set of controls with a less restrictive one." (Ann O. Krueger, *Perspectives on Trade and Development* (Chicago: University of Chicago Press, 1989), p. 184.)

- Eliminate dues and import surcharges associated with the tariff;
- Introduce a rationale into the tariff structure, taxing raw materials and basic foodstuffs very lightly, intermediate and capital goods moderately, and consumer durables and luxury items steeply to encourage production;
- Give tariff discounts that increase with the proportion of domestic components used in the finished product, to encourage local assembly industries (a discount of up to 75 percent);
- Rationalize imports; and
- Adjust the exchange rate used in valuing imports for tariff computation purposes, to reflect its true market value.

Comparing the effect of the 1986 tariff reform on the structure of nominal protection with that of the 1980 tariff structure, the weighted average rate of nominal protection on productive activities decreased from 48.1 percent to 47.5 percent, coupled with a reduction of its standard deviation from 52.1 percent to 47.0 percent. However, if the effect of the accompanying devaluation of the Egyptian pound for tariff computation purposes from $1.414 per LE 1 to $0.735 per LE 1 (that is, from 70.7 piasters per $1 to 136 piasters per $1) was taken into consideration, the weighted average nominal tariff rate on the dollar value of imports would increase from 34.0 percent to 64.6 percent. Thus, it appears that the 1986 tariff revisions were primarily intended to substitute price restrictions on imports for the quantitative restrictions abolished in August 1986. This signified a step toward alleviating administrative restrictions and allowing effective play of the price mechanism.[8]

In spite of wide variations in the commercial banks' rate of exchange, the exchange rate for tariff valuation purposes was kept fairly constant until 1989, when an across-the-board reduction in tariff rates of 30 percent was enacted. Meanwhile the exchange rate used for valuation of imports for tariff purposes became the free market rate, which at that time was LE 2.6 per $1 ($0.385 per LE 1).

[8]H. Kheir El-Din and others, *Evaluation of the Protection System in Egypt* (Center for Economic and Financial Research and Studies, Cairo University, 1989), pp. 24–26.

These changes were made to avoid increasing the tariff burden resulting from the devaluation of the Egyptian pound.

For tariff exemptions and preferences, the 1986 tariff law had skimmed down the number of such exemptions and confined them to certain agencies and certain purposes clearly specified in the law. Since 1987, tariff exemptions have been scrutinized, streamlined, and restructured. The vast majority of exemptions were eliminated. Exemptions that represented about 49 percent of potential tariff revenue in 1986 fell to about 17 percent in 1990. A study of tariff incidence (calculated as the ratio of tariff collection to imports), using 1988 import figures, notes that the tariff range was narrowed, in 1989, to 0.7-120 percent; with 80 percent of the tariff lines having rates not exceeding 35 percent and only 1.2 percent exceeding 80 percent. Furthermore, the study suggests that legal tariff rates of up to 30 percent are almost equal to observed tariff incidences, while at higher rates, the tariff incidence is much lower than the corresponding legal tariff rates. This raises the question of why tariff exonerations are more common at higher than at lower tariffs.[9] Tariff preferences, which imply reductions in tariff rates when imports are made by certain agencies, covered about 90 tariff lines.

Finally, as part of the structural adjustment program, the tariff structure was further streamlined and restructured in 1991 (Presidential Decree No. 178 for 1991, issued on May 21, 1991). The range of tariffs was narrowed from 0.7-120 percent to 1-100 percent. Some exceptions were made from the lower limit that include a few basic foodstuffs, and some from the upper limit that include luxury cars, vans, cosmetics, tobacco, and alcoholic beverages. Thirty of 90 tariff lines with tariff preferences were eliminated—usually referred to as "footnotes" to the tariff schedules.

Nontariff Barriers (NTBs)

After the implementation of the new import control regime in 1986 and the abolition of the "import rationalization committees," which had previously licensed private sector imports, the quotas and

[9]Julio Nogues, "On the Design of a Trade Liberalization Program for Egypt" (unpublished; World Bank, January 1990), p. 9.

quantitative restrictions on imports were dismantled and replaced by an explicit "banned list" of imports. All commodities not listed could be imported without prior permission. The abolition of the import licensing system was an important step toward economic liberalization. However, Egypt still manages a complex system of nontariff barriers representing quantitative, qualitative, and administrative restrictions on imports and/or exports of a considerable number of products.

Nontariff Barriers on Imports

NTBs on imports cover, in addition to import bans, the suspension of letters of credit, prior governmental approval, special conditions, availability of servicing facilities, quality control, and foreign exchange budgeting and allocation.

Import bans. When first introduced, on August 21, 1986, they included about 210 tariff lines of the Brussels trade nomenclature, comprising 548 commodities half of which were consumer nondurable goods. In 1987 and 1989 more items were added to the list of import bans. In early 1990, the number of banned tariff lines reached 225 and covered approximately 571 commodities. These bans were not absolute. Imports of banned goods were allowed for specific purposes in recognition of the importance of some activities in the economy or to satisfy some real needs that could not otherwise be met, such as the needs of the tourism sector, local assembly industries, temporary admission system, and turnkey projects. The system was flexible enough to accommodate such needs and was less restrictive than it appeared. The purpose of these permanent import bans was basically to protect the domestic output of industries that could satisfy local demand. Starting in May 1990 a number of commodities and/or commodity groups were taken off the list of bans until it was restricted to 105 commodity groups in May 1991.

Letters of credit suspensions (LCSs). This restriction was first applied in 1988 in the form of directives from the Ministry of Economy and Foreign Trade to banks via the Central Bank to stop opening letters of credit for some commodities. In March 1989, and in the following months, as a result of the acute shortage of foreign exchange, more items were added to the list of LCSs to reach 77 commodity and commodity groups by the end of 1989.

In some cases, commodities included in the list of bans were also included in the LCS list, making the design of import policies appear uncoordinated. This can be explained by the fact that considerable amounts of banned commodities were allowed into the country for the reasons given earlier, but, under the pressure of mounting shortages of foreign exchange, instructions were given to banks to suspend temporarily opening letters of credit for some commodities. This kind of restriction was announced as temporary and was not considered by policymakers a permanent feature of Egypt's foreign trade system. In fact, starting in May 1990, a series of directives to the Central Bank gradually reduced the list of LCSs, until it was eliminated, except for a very few items that were transferred to the list of permanent bans.

Prior approval by specified authorities. Tariff lines also exist whose imports are conditional on the approval of different ministries and government agencies as to quality, quantity, and price. Most of these conditional imports are subject to health, standard, defense, and quality considerations. However, approvals granted on the basis of quantity may be for protectionist purposes.

The list of tariff lines with conditional imports once comprised about 80 entries. In 1987, the list was restricted to 47 tariff lines, to which further items were added to reach 56 by the end of 1989. However, the process of dismantling this NTB was implemented in May 1991, when the new Executive Regulations for the Administration of Imports and Exports (ERAIE) removed 41 of the total 56 entries.

Furthermore, enterprises established under Investment Law 43 for 1974 (amended by Law 230 for 1989) are required to obtain annual approvals from the Investment Authority to import their required inputs. These approvals are granted according to their productive capacities.

Finally, projects established under the Tourism Law—mainly hotels and other tourist establishments—are required to obtain Ministry of Tourism approval to import their needs for different inputs. Commodities imported under this system are supposed to be used solely by these establishments, that is, they are not permitted to trade in such commodities.

Special conditions. The single most important product in this category was cement; the special condition was that imported cement

had to be subjected to a laboratory test to check that it conformed with international specifications. Specifications have also to be met for used motor vehicles and equipment. These conditions vary between products and are applied mainly to motor vehicles and capital goods. However, some imports of consumer goods as well as intermediate goods have to satisfy specified conditions. By May 1991, when the new ERAIE went into effect, this list was reduced.

Servicing facilities requirements. To import a number of commodities, the foreign exporter should have an Egyptian commercial agent, an appropriate service center approved by the Ministry of Industry in Egypt, and a guarantee to provide spare parts. The list covered mainly household appliances, tractors, and transport equipment.

The declared objective of this NTB is to protect local consumers or users of such products. However, since the adequacy of these servicing facilities is determined by the Government, this restriction could become a protectionist measure to domestic producers by restricting the brands that these facilities would be allowed to operate in Egypt. This NTB was eliminated by the new ERAIE in May 1991.

Public import monopolies. Imports from bilateral agreement countries were confined to public sector foreign trade companies (general and specialized trading companies). Furthermore, imports of a list of commodities were confined to the above-mentioned companies, and the list covered wheat, flour, unpacked tea, edible oils, animal fats, tobacco, coal, petroleum and its products, military production inputs, and weapons. The ERAIE has recently permitted private sector companies, Law 43 companies, and cooperatives to import from bilateral agreement countries all products agreed upon without exception,[10] and the import of commodities such as sugar and petroleum products (previously restricted to the public sector) was also opened to the private sector.

Quality control. The list of commodities subject to quality control covered about 65 tariff lines, most of which are foodstuffs. Some wood and basic metal products are also affected by this NTB. This

[10]Previously, private sector entities could not import from bilateral agreement countries wood, paper, paper pulp, and cardboard, which remained the monopoly of public sector foreign trade companies.

restriction on imported foodstuffs is quite justified. In 1989, imported automobile parts and durable consumer goods were added to the list. The ERAIE maintained this NTB on transport equipment. The likely explanation for this NTB is to limit imports of these products by adding bureaucratic ties to the process in addition to consumer protection.

Prior import deposits. Importers are required to deposit an amount equivalent to the value of imports: 35 percent is deposited when the importer applies for a letter of credit, and the remaining 65 percent when the letter of credit is actually open. (These percentages apply to trading entities, but when imports are made by production entities, they become 15 percent and 85 percent respectively.) On average these deposits are frozen for about three months, and they pay no interest. Therefore, assuming that the real interest rate is zero and that the actual inflation rate is about 25 percent, the system of prior import deposits is approximately equivalent to a 6 percent tariff surcharge. This obviously adds to the protectionist bias of the trade regime. Another liberalization measure introduced by the ERAIE was to reduce such deposits from 35 percent to 20 percent for imports by trading entities, and from 15 percent to 10 percent for production entities. In addition, interest can be paid on these deposits.

Foreign exchange budgeting and allocation. An annual foreign exchange budget allocates expected foreign exchange receipts from the Central Bank pool and the free banking pool to various uses. If the foreign exchange earnings available to the Central Bank are in excess supply, the balance is used to repay debt. Foreign exchange at the free banking pool is allocated—at the free banking rate—to different government bodies. The past needs of these government bodies represent a major criterion for this allocation. When excess demand appears, rationing is enforced by additional measures: tighter foreign exchange allocated to the public sector, suspension of letters of credit, and attempts to adjust the exchange rate. The private sector was allowed under this system to retain its export earnings for a maximum period of one year. Unused balances, after this time, were to be sold to commercial banks at the free banking rate. Private sector units needing foreign exchange had to resort to the parallel market where exchange rates command a premium. This

system of foreign exchange allocation, therefore, discriminated against the private sector.

The new ERAIE did not include a foreign exchange budget or a reference to the allocation of foreign exchange to public sector enterprises. The new foreign exchange regime, together with reform of the public sector law, is supposed to eliminate such discrimination.

Nontariff Barriers on Exports

Exports in Egypt were subject to taxes, some explicit and other implicit in nature, in addition to a number of NTBs such as export bans, export quotas, prior approvals, and quality control.

Cotton growers in Egypt are subject to an implicit tax, whose amount is the difference between cotton farmgate prices and prices at which cottons are exported. Farmgate prices had barely reached, until recently, 40-50 percent of export prices. This has been the main reason behind the deterioration in the production and export of cotton. Meanwhile, the local spinning industry receives an implicit subsidy as its cotton buying prices are only fractions of world market prices.

On the other hand, some exports are subject to an explicit export tax, such as that imposed on raw hides and skins. The objective is to protect the shoe and leather industry.

Quantitative and qualitative restrictions on exports are also represented:

Export prohibitions. The list of export prohibitions covered 20 commodities, most of which were foodstuffs and fodder, raw hides and skins, waste paper and paperboard, low-grade cotton (scarto and sekkina), and scrap metals (iron, copper, aluminum, and lead). Egypt imports food products and fodder in addition to selling them at subsidized prices. These prohibitions are thus imposed to prevent smugglers from exporting these subsidized products. In general, these export prohibitions are not enforced to protect domestic industries, except those on raw hides and on scrap metals. Export bans of hides and skins provide significant protection to downstream leather tanning and other processing activities. The list of export prohibitions has been reduced, under the ERAIE, to 6 items, which still include raw hides, waste paper, and scrap metal.

Export quotas. The list of goods subject to export quotas included 17 items, most of which were foodstuffs, as well as cotton waste and

various yarn waste. The rationale behind this restriction on foodstuffs is their relatively short local supply. On the other hand, the export quota on cotton waste and yarn waste appears to be imposed for protectionist purposes. Annual quotas were usually decided by consultation between the Ministry of Economy and Foreign Trade and other ministries concerned—mainly the Ministry of Supply and Internal Trade and the Ministries of Agriculture and Industry—taking into account the local conditions of supply and demand for such commodities.

The ERAIE scaled down export products subject to annual quantitative quotas to only 4 items: raw and waste wool, tanned skins, cotton and cotton yarn waste, and newspaper waste.

Export prior approvals. Prior export approvals granted by different agencies, including the Ministries of Supply, Industry, Health, Agriculture, and Defense, were required for 37 export items. Most of these approvals were not imposed for protectionist purposes except for tanned leather. The new ERAIE reduced this list to only 1 item: yarn and gauze made of cotton or manmade fibers.

Prior approval by General Authority for Supervision of Exports and Imports and quality control. The exportation of a list of commodity groups required prior approval by the General Authority for Supervision of Exports and Imports to verify the quality and specifications of items that included fresh, frozen, and canned vegetables and fruits, citrus fruits, juices, eggs, honey, biscuits, and roasted peanuts. Another list including exports of flowers, medical herbs, fresh fruits and vegetables, dried vegetables, aromatic oils, and dried beans imposed obligatory quality control for public sector companies while this was left optional for the private sector. The ERAIE canceled this discrimination and maintained quality control requirements only for foodstuffs.

Public export monopoly for selected products to agreement countries. Whereas exports of fresh oranges and onions remained the monopoly of some public sector foreign trade companies until May 1991, the new ERAIE eliminated this discrimination, and allowed the private sector to export these commodities to agreement countries.

Export Incentives

These incentives cover the drawback and temporary admissions systems and the removal of discrimination between public and private sectors in foreign trade.

Drawback and temporary admissions systems. A commonly practiced form of assistance for exporters is to remove the burden of tariffs and possibly the domestic indirect taxes on materials used in manufacturing export products that add to their cost. Relief from paying such duties takes two basic forms: refunding taxes and duties previously paid on materials used in manufacturing a product when it is exported (drawback); and allowing duty-free imported materials intended for use in manufacturing products for export (temporary admission).

It is certainly more advantageous for the exporter to be exempt from paying duties than to pay them initially and then to get a refund, or drawback, later, because he does not have to lock up his funds, for however short a time, in any refundable tariffs. However, schemes of temporary admissions also have their limitations. As part of the Government's attempt to liberalize trade and promote exports, both schemes were expanded and improved. Procedures for refunding drawbacks have been considerably simplified. Refunds can now be made within a week.

Alleviating restrictions on private sector trading activities. Removing discrimination between the public and private sectors in effecting foreign trade transactions is undertaken gradually. Upon the approval of the Minister of Economy and Foreign Trade, private sector companies, Law 43 companies, and cooperatives are permitted to conclude offset trade deals with companies and entities in countries with which Egypt has trade and payments agreements, provided that these transactions include commodities appearing in the commodity lists annexed to these agreements. Thus past reliance on public trading companies is being reduced through increased participation by the private sector in foreign trade.

Foreign Exchange System

Although the Egyptian exchange system has been highly liberalized since 1976, it was still complex and a multiple rate system until October 1991. In the early 1980s there were at least six exchange rates. The number was narrowed to four in 1986, then in 1987 was officially brought down to two rates: the Central Bank pool rate and the free banking pool rate. Both these rates were overvalued and the quantity of foreign exchange demanded exceeded the quantity supplied at these overvalued rates. This legal excess demand, together

with the considerable demand for illegal transaction purposes, has traditionally supported a third "parallel" market for foreign exchange.

The Central Bank pool dealt with exports of petroleum, raw cotton, and rice, the Sumed pipeline revenues, and Suez Canal dues. It also financed imports of basic foodstuffs (wheat, flour, edible oils, tea, and sugar), insecticides and fertilizers, a large number of public sector capital transactions, and transactions through bilateral payments agreements. Since January 1, 1979, the exchange rate of most transactions has not been altered, and the buying rate was set at LE 0.7 per $1. However, some transactions under bilateral trade agreements were effected at special exchange rates. In August 1989, the Egyptian pound was devalued at the Central Bank to LE 1.1 per $1 and further, to LE 2.00 per $1 in July 1990. This rate remained highly overvalued, however, and had the effect of understating the pound cost of imports of subsidized foodstuffs in the government budget.

The free banking rate used to be fixed daily by a government-appointed committee of private and public sector bankers. This rate was determined according to a combination of market conditions and other nonmarket factors. In opening this market, in May 1987, the rate was initially set at LE 2.165 per $1, which represented a 37 percent devaluation of the Egyptian pound. Banks could purchase foreign exchange, at that rate, from all sources other than those confined to the Central Bank pool. Major sources for this pool were tourist expenditures in Egypt, remittances from Egyptians working abroad, and revenues from exports of commodities other than those earmarked to the Central Bank pool. Banks were authorized to sell foreign exchange from the pool to finance imports, repatriation of foreign companies' profits, and, to a lesser extent, private foreign debt servicing. The exchange rate in this pool was not a perfect substitute for a freely determined market rate and hence failed to reflect market forces realistically. This must have affected the competitive position of Egyptian exports detrimentally in international markets and aggravated the problem of foreign exchange shortage.

In addition to these pools, there was the parallel market (or black market) for foreign exchange, where some transactions were consid-

ered legal: trading through private foreign currency accounts in banks, whereas trading outside bank accounts was deemed illegal. This market was the direct result of certain types of demand for foreign exchange that could not be satisfied through the commercial bank pool. Rates in that market did respond generally to forces of supply and demand. It had as a floor the free banking rate but had been distorted by occasional police intervention in the market.

As mentioned earlier, the exchange rate for customs valuation purposes had been devalued in 1986 to the level of the commercial bank rate (LE 1.36 per $1); however, it was not allowed to be devalued at the same pace and was still LE 1.89 per $1 in July 1989 when it was abolished. The free banking rate was to be applied for customs valuation and that rate was reviewed monthly. An across-the-board reduction of 30 percent in the tariff rate and a 35 percent cut in the consumption tax on imports were then announced to offset the inflationary impact of applying the depreciated customs valuation rate.

To simplify the exchange system and ensure a competitive exchange rate, the prevailing system was replaced in February 1991 by a dual exchange system consisting of a primary market and a secondary (or free) market for a transitional period, at the end of which the two markets would be unified. Transactions in the primary market were restricted to the Central Bank and its authorized branches. Receipts in this market were foreign currency proceeds of public and private sector exports of goods. Payments formerly included in the Central Bank pool continued to be settled through this market.

The exchange rate for the entire system was determined in the secondary (or free) market. The exchange rate in the primary market was maintained, on a daily basis, within 5 percent of the most recent seven working days of the average rate in the free market, which has been fluctuating around LE 3.3 per $1.

An essential feature of this system was the permission granted to nonbank foreign exchange dealers to operate in competition with banks in the free market, provided they satisfied certain conditions. A number of supporting steps in this system have also been implemented, including abolition of import accounts and of the requirements that letters of credit be opened for imports.

Finally, in October 1991, unification of the two markets was announced, thus ending a long history of multiple foreign exchange rates and fragmentation of the exchange market.

Impact of Trade Policy on Resource Allocation and Export Performance

Analysis of the elements of trade policy in Egypt has shown their complexity and diversity. The Government's constant interference in regulation of trade has favored the production of substitutes for imports protected by tariffs, bans, and other NTBs. Furthermore, trade policy has implied an anti-export bias enhanced by the overvaluation of the Egyptian pound vis-à-vis foreign currencies. The next section assesses the coverage of NTBs as an indicator of their importance as potential instruments for protection. It further discusses effective protection resulting from the tariff structure and the exchange rate. The extent of anti-export bias implied by some of these policy instruments is also examined.

Coverage of Nontariff Barriers

NTBs have been widely used in Egypt during the period under study as balance of payments instruments to bring imports into line with foreign exchange availability and as protective instruments to shield domestic production from foreign competition. Their protective effect on output of both imports and exports was investigated by studying the production coverage of various NTBs.

This coverage was calculated twice: using NTBs as described in Ministerial Decrees 1036/78 and 333/86 and their amendments until March 1990 and then using NTBs as amended by the new ERAIE of May 1991. The methodology requires knowledge of NTBs applied on various imports and exports and the domestic value of production of comparable products. Ideally, the production statistics should be as disaggregated as the information on NTBs. In our case, the values of production were generally more disaggregated than the information on NTBs. The source of these values was "Industrial Production by Commodity, 1987/88."[11] The production coverage of individual

[11]A Central Agency for Public Mobilization and Statistics (CAPMAS) publication, Document No. 71-12611/90, June 1990.

NTBs by sector and for total industrial production was assessed. However, 3 out of the 17 activities covered in the CAPMAS publication were disregarded: mining and quarrying, petroleum products and coal, and miscellaneous manufactures. Whether the output of the first two activities is protected is somewhat irrelevant for studying Egyptian foreign trade policy, since the activities are highly regulated and dependent on political decisions on the rate of extraction, expected domestic consumption, and foreign exchange requirements. In addition, the degree of protection of miscellaneous manufactures is not meaningful owing to the great heterogeneity of this activity.

Production Coverage of NTBs on Imports

It is clear from Table 2 that various NTBs have different degrees of restrictiveness and different coverage. Import bans in 1990 covered a large proportion of the industrial activities considered (52.1 percent); this figure was reduced to 40.7 percent after May 1991, but it is still very restrictive. Although their impact on private sector activities was greater than on the public sector before 1991, the ERAIE has lifted the impact of these bans on the private sector considerably (from 64 percent to around 33 percent). Their effect on the public sector was only slightly changed (from 47.5 percent to 43.7 percent). The coverage of letters of credit suspensions (8.8 percent) was much lower than that of permanent bans. Furthermore,

Table 2. Production Coverage of Various NTBs on Imports Before and After May 1991 ERAIE

	Incidence (*in percent*)					
	Before ERAIE			After ERAIE		
NTB	Public sector	Private sector	Total	Public sector	Private sector	Total
Permanent bans	47.49	64.04	52.09	43.66	32.92	40.67
Letters of credit suspensions	9.16	7.92	8.82	—	—	—
Prior approvals	12.38	9.51	11.58	—	—	—
Special conditions	8.41	2.60	6.80	0.56	0.51	0.55
Servicing requirements	6.87	1.53	5.38	—	—	—
Quality control	13.61	21.42	15.78	19.99	21.98	20.55
Total incidence	70.67	78.26	72.78	54.51	54.32	54.50

its impact on the public sector was stronger than on private activities. This NTB was eventually abolished by the new ERAIE. Other NTBs were much less important than permanent bans. The public sector enterprises seem to have benefited more from these NTBs than the private sector. The ERAIE has practically lifted all these barriers except that requiring submission to quality control tests, the coverage of which increased from 15.8 percent to 20.6 percent, with a heavier incidence in the private sector, leading to the question whether the partial lifting of permanent bans (the most criticized of NTBs) has not been partly compensated by increasing the coverage of quality control requirements.

The total incidence of NTBs on imports has decreased as a result of the ERAIE from 72.8 percent to 54.5 percent of production in the industrial activities under consideration, and has tended to give equal treatment to both public and private sectors. Overall, eliminating double counting[12] and adding the incidence of other NTBs to import bans, the production coverage of import restrictions rises from 52.1 percent to 72.8 percent before the ERAIE and from 40.7 percent to 54.5 percent thereafter. NTBs serve different purposes: whereas import bans are primarily protectionist, many of the other NTBs could be justified by health, defense, standard, and quality regulations, and others (LCSs) could be explained by foreign exchange shortages. More detailed analysis may be required to disentangle the protectionist elements in NTBs other than import bans.

Finally, Table 3 provides a summary of the production coverage, by activity, of NTBs considered here. There is a wide disparity between activities. Before the new ERAIE, total production coverage of NTBs on imports exceeded 90 percent in seven activities: food products; beverages and tobacco; clothing and ready-made fabrics; wood, furniture, and fixtures; footwear; leather, leather goods, and furs; and transport. The incidence of NTBs on food products was considerably reduced after the ERAIE; it was also somewhat reduced for transport, but remained higher than 90 percent for the other five activities. The coverage of NTBs varied between about 40 percent and 90 percent for six of the activities considered: spinning and

[12]The sum of incidences of individual NTBs in Table 2 (100.45 percent and 61.77 percent) is much higher than total incidences given. This clearly shows that some commodities are subject to more than one NTB.

Table 3. Production Coverage of Various NTBs on Imports by Activity Before and After May 1991 ERAIE

	Incidence (*in percent*)					
	Before ERAIE			After ERAIE		
NTB	Public sector	Private sector	Total	Public sector	Private sector	Total
Food products	99.04	97.72	98.53	58.70	59.31	58.94
Beverages and tobacco	100.00	100.00	100.00	96.12	66.85	93.66
Spinning and weaving	34.95	56.65	39.83	30.58	45.28	34.16
Clothing and ready-made fabrics	100.00	100.00	100.00	100.00	98.97	99.47
Wood, furniture, and fixtures	91.82	99.88	97.74	91.23	99.83	97.55
Paper and paper products	49.62	59.46	53.05	16.08	32.78	21.89
Printing	99.89	57.13	67.88	—	—	—
Footwear	100.00	100.00	100.00	100.00	100.00	100.00
Leather, leather goods, and furs	89.78	98.90	94.82	89.78	98.80	94.82
Rubber products	—	—	—	—	—	—
Chemicals and chemical products	61.70	88.25	68.53	30.76	35.19	31.90
Nonmetallic products (except coal and petroleum)	87.94	72.39	82.48	77.52	69.17	74.59
Basic metallic industries	56.70	51.61	55.68	44.27	42.64	43.94
Means of transport	97.43	99.62	97.47	84.12	37.67	83.16
Total incidence	70.67	78.26	72.78	54.51	54.32	54.50

weaving; paper and paper products; printing; chemicals and chemical products; nonmetallic products; and basic metallic industries. Only rubber products were, before the ERAIE, completely free from NTBs.

After the ERAIE, NTBs on printing were also completely removed, with the coverage for the remaining activities being reduced to the range of 30–85 percent, except for the five activities previously mentioned, which remained highly protected. In general, even though the coverage of NTBs in Egypt has been reduced, it still remains high, thus artificially increasing the relative attractiveness of production in activities highly shielded by NTBs on imports.

Production Coverage of NTBs on Exports

Table 4 presents estimates of the production coverage of individual NTBs on exports before and after the ERAIE. The sources of

Table 4. Production Coverage of Various NTBs on Exports Before and After May 1991 ERAIE

	Incidence (*in percent*)					
	Before ERAIE			After ERAIE		
NTB	Public sector	Private sector	Total	Public sector	Private sector	Total
Prohibitions	8.54	3.13	7.04	0.11	0.001	0.08
Quotas	0.38	0.66	0.46	0.19	0.35	0.23
Prior approvals	9.99	3.08	8.07	—	—	—
Quality and other controls	3.24	1.89	2.87	2.97	1.46	2.55
Total incidence	21.95	8.27	18.15	3.30	1.87	2.90

data and the methodology used are the same as those used to calculate the incidence of NTBs on imports.

It appears that NTBs weighed more heavily on the public sector than on the private sector—their incidence covered 21.95 percent and 8.27 percent, respectively, of their production. The ERAIE reduced the total impact of these restrictions considerably, from 18.15 percent to 2.90 percent. The most important of these NTBs—in terms of production coverage—were export prohibitions and the requirement of obtaining prior approvals to export. However, after the ERAIE, quality control restrictions became relatively more important as other NTBs on exports were lifted.

Examining the distribution of NTBs by activity in Table 5 indicates that food products and leather and leather products were the most heavily constrained by NTBs on exports. For food products, these restrictions were not intended to protect domestic industry, as Egypt imports many foodstuffs. Rather, they were dictated by the need to avoid exporting or re-exporting food products, and thus increasing the domestic shortages.

Export restrictions on leather and leather products (particularly on tanned leather)[13] significantly protect downstream leather processing activities and the shoe industry, which is additionally pro-

[13]Exports of raw hides are also prohibited, bur their impact is not represented here as they are not included in the activities considered. This prohibition, in turn, provides substantial protection to the tanning activity.

Table 5. Production Coverage of Various NTBs on Exports by Activity Before and After May 1991 ERAIE

	Incidence (*in percent*)					
	Before ERAIE			After ERAIE		
NTB	Public sector	Private sector	Total	Public sector	Private sector	Total
Food products	72.44	16.42	50.78	14.11	4.09	10.23
Spinning and weaving	1.30	0.89	1.20	0.40	0.74	0.49
Leather, leather products, and furs	81.98	50.44	64.56	81.98	50.44	64.56
Chemicals and chemical products	24.20	9.89	20.67	—	—	—
Basic metallic industries	14.29	6.95	12.81	0.0005	0.013	0.003
Total incidence	21.95	8.27	18.15	3.30	1.87	2.90

tected from foreign competition by import bans. Restrictions on the exports of basic metallic industries (scrap metals) and of spinning and weaving (cotton waste) are also for protectionist purposes, but were considerably reduced under the ERAIE.

Effective Protection

To identify the overall effects of the policy on the structure of the relative incentives provided to various activities, the effect of such policies on the prices of both final products and intermediate inputs should be taken into account. Import tariffs, NTBs, and multiple and overvalued exchange rates affect considerably the structure of incentives offered to producers. While a tariff or an NTB imposed on an imported product would raise its domestic price (thus protecting the domestic substitute), any tariffs or NTBs on the inputs used to produce this substitute would reduce the extent of protection, as the production cost would rise. Conversely, while overvaluation of the exchange rate applied to an import would reduce its domestic price (thus discouraging production of its domestic substitute), overvaluing the exchange rates applied to imported inputs increases the protection to this domestic substitute by reducing its production cost. Accordingly, analysis of the degree of protection to a certain activity should not be confined to the nominal rate of protection (NRP), that is, to the difference between the domestic and international price of

its output, but should be extended to the value added obtained under the prevailing trade policy compared with what could have been achieved without such a system.

The effective rate of protection (ERP) of an economic activity sums up the overall impact of the policies applied on the incentive structure. It may be defined as the percentage excess of domestic value added obtained under a set of policies over the value added that would have been realized without these existing policies or international market value added.[14]

In Egypt, estimating the effective rate of protection with relative accuracy is extremely difficult. The main methodological problems are with the treatment of import bans and other NTBs, with the extensive system of price controls, subsidies, and indirect taxes, and with marked quality differences between domestic and imported products. With these difficulties in mind, we discuss the effective protection on various commodity-producing activities and implied in the 1986 tariff structure that prevailed until 1991.[15] A comparison with former tariff structures is also undertaken, along with an attempt to assess the additional impact of both NTBs and the prevailing exchange rate system. The analysis draws upon the results of a study on the evaluation of the protection system in Egypt.[16]

Table 6 reports the results of the estimates of effective rates of protection, along with the nominal protection accorded to various activities. Effective rates of protection do not seem to be highly correlated with the nominal rates as reflected by the estimated rank correlation coefficient of 0.51, in the sense that a relatively high nominal rate of protection is not necessarily associated with a relatively high effective rate of protection.

Calculations showed that in almost all cases the effective protection granted to the activities considered is higher than the nominal,

[14] Bela Balassa and Associates, *The Structure of Protection in Developing Countries* (Baltimore, Maryland: Johns Hopkins University Press, 1971).

[15] As previously mentioned, a 30 percent across-the-board reduction in tariff rates was undertaken in 1989, along with a devaluation of the exchange rate used to value customs tariffs, leaving the tariff burden on various activities unchanged until the 1991 reforms.

[16] See Kheir El-Din and others (cited in fn. 8), pp. 114–20.

Table 6. Protection Rates for Selected Activities in 1986 Tariff Structure Compared with Previous Tariff Structures
(*In percent*)

Activity	Protection Rate: Nominal 1986	Protection Rate: Effective 1986	Protection Rate: Effective 1980	Protection Rate: Effective 1959
Agriculture	31	38	41	...
Animal production	12	113	11	...
Food processing	8	17	5	21
Beverages	110	262	295	210
Tobacco processing	195	(59)	15	100
Cotton ginning	—	(68)	(68)	...
Spinning and weaving	34	788	NIVA[1]	92
Final wear	109	348	862	67
Leather and products (excluding footwear)	16	35	68	80
Footwear	51	160	35	...
Wood and wood products (excluding furniture)	42	40	(6)	32
Wooden and metallic furniture	110	296	607	22
Paper and printing	16	36	29	33
Chemicals	15	75	61	32
Rubber, plastic, and products	28	563	1221	59
Porcelain, china, and ceramics	75	214	336	
Glass products	36	54	68	34
Other nonmetallic products	6	1	14	
Steel, iron, and metallic products	17	120	192	43[2]
Tools and machinery	28	39	58	23
Transport	60	628	473	47
Average	47	176	215	...

Sources: Estimates for 1980 and 1986 are from Kheir El-Din and others (cited in fn. 8), pp. 115 and 121. Estimates for 1959 are from Robert Mabro and Samir Radwan, *The Industrialization of Egypt, 1939–1973: Policy and Performance* (Oxford: Clarendon Press, 1976), p. 61.
[1]NIVA: Negative international value added. This indicates an infinitely large protection.
[2]The estimates given in Mabro and Radwan were 43 for iron and steel and 41 for basic metals.

except for two activities—tobacco processing and cotton ginning. For ginning, discrimination against this activity should be even higher than the estimates, which did not reflect the effect of keeping the domestic price of cotton lower than its export price, nor recognize the effect of the overvalued exchange rate for the pound at which cotton exports (and thus cotton production at world prices) were estimated. If these effects had been taken into consideration, the effective rate of protection would have fallen even lower and

would have indicated that competitive producers were actually discouraged from engaging in cotton growing and ginning activities.

Ten activities have very high rates of effective protection. The effective protection granted to the remaining nine activities is not extremely high, ranging from 1 percent to 75 percent. In particular, it appears that customs tariffs provide little effective protection to agricultural crops.

Thus, Table 6 indicates that the effective protection extended by the tariff structure alone tended to favor highly consumer goods, whether durable or nondurable, in addition to steel and iron and transport. It moderately protected intermediate goods and tools and machinery, while it actually discriminated against the more traditional manufacturing activity of cotton ginning.

The effect of the 1986 tariff revisions was to reduce the extent of effective protection in the economy. The economy-wide average rate of effective protection declined from 215 percent in 1980 to 176 percent in 1986. Thus it appears that the 1986 tariff revisions were intended to reduce the extent of protection granted to production activities. Bearing in mind that these revisions were coupled with the removal of all additional taxes on imports (which ranged between 15 percent and 20 percent) and with the devaluation of the pound for tariff computations from 70.7 piastres to 136 piastres per $1—from $1.414 to $0.735 per LE 1, a 48 percent devaluation—this tariff reform implied a step toward liberalization and substitution of market mechanisms for direct administrative interventions more than a genuine reduction of effective protection to domestic activities.

However, comparing the effective rate of protection implied by the tariff structure prevailing until 1991 with that granted to various activities in 1959—prior to the central planning era when most production activities were controlled by the Government and the public sector and when the economy was inward oriented toward import substitution—it appears that domestic production activities are still highly protected by the tariff structure. Out of 16 activities for which the effective rate of protection estimates for 1959 could be found and matched with the more recent ones, only 1 activity seems to have obtained significantly less protection than in 1959—the tobacco processing industry—where high tariffs in the present tariff structure on imported tobacco inputs drastically reduce the domestic

value added generated in this industry. Three other activities (food processing, leather and leather products excluding footwear, and other nonmetallic products) also appear to enjoy less protection currently than in 1959; however, the difference does not seem to be large. The remaining 12 activities have been sheltered by a higher degree of effective protection, with some of them enjoying effective rates of protection ranging from threefold to 13-fold their level before central planning.

Currency overvaluation can lead to significant discrimination against domestic production. However, except for cotton spinning, which received cotton inputs at the highly overvalued rate of exchange prevailing at the Central Bank, adjustment for overvaluation did not greatly alter the structure of effective protection in various industrial activities. It tended to emphasize discrimination against some activities and to lessen the degree of protection given to others, but did not alter the relative position of most activities,[17] because the exchange rate adjustment applied to the same degree to both outputs and inputs—except for spinning.

Overvaluation of the currency has been a major source of discrimination against export crops—cotton and rice[18]—which financed the Central Bank pool and later the primary market—until unification of the foreign exchange system in October 1991.

Finally, adjustment for overvaluation least affects the private sector, as their foreign exchange requirements were mostly obtained from the parallel market and thus did not benefit as much as public sector activities from the protectionist impact of importing their inputs at the relatively overvalued exchange rate prevailing in the free banking pool.

Table 7 sums up the estimated nominal rate of protection and the effective rate of protection for a number of industrial activities along with the respective production coverage of NTBs and of import bans before and after the new ERAIE. Nominal rates of protection implied in the tariff structure were not highly correlated with the incidence of both NTBs and of import prohibitions, as reflected by

[17] Kheir El-Din and others (cited in fn. 8), Chapter V.

[18] Ibid., p. 113.

Table 7. NRP, ERP, and Production Coverage of NTBs and Import Bans for Selected Activities Before and After ERAIE

			Incidence (*in percent*)[1]			
			Before ERAIE		After ERAIE	
Activity	NRP[2]	ERP[2]	NTBs	Bans	NTBs	Bans
Food processing	8	17	98.53	52.90	58.94	9.63
Spinning and weaving	34	788	39.83	37.95	34.16	34.16
Final wear	109	348	99.24	99.24	99.47	99.47
Leather and products	16	35	94.82	94.82	94.82	94.82
Footwear	51	160	100.00	100.00	100.00	100.00
Chemicals	15	75	68.53	27.95	31.90	31.87
Rubber	28	563	—	—	—	—
Basic metals	17	120	55.68	53.17	43.94	38.54
Transport	60	628	97.47	96.03	83.16	81.72

[1]For the production coverage of NTBs, see Table 3.
[2]NRP and ERP have been taken from Table 6.

the estimated rank correlation coefficients of 0.30 and 0.60 for the period prior to the new ERAIE and of 0.45 and 0.60 thereafter. Furthermore, all these coefficients were not significant or had a low significance, which did not exceed the 90 percent confidence level. However, the rank correlation coefficients between the effective rate of protection and the incidence of both NTBs and import bans revealed a significant correlation between the effective rate of protection and import prohibitions before the new ERAIE. The estimated rank correlation coefficient reached 0.84 and was significant at the 99 percent confidence level. The rank correlation coefficients between the effective rate of protection and the impact of NTBs before the ERAIE (-0.29) and between the effective rate of protection and the incidence of both NTBs (-0.15) and import bans (0.07) after the ERAIE were all small and insignificant. These observations point to the fact that—except for import prohibitions before the new ERAIE—NTBs on imports did not generally affect various production activities in the same way as did the tariff structure. Activities that received a high degree of effective protection from the tariff structure were not necessarily the most sheltered by NTBs on imports or by import prohibitions.

Finally, the effect of reducing the dispersion of tariff rates in the revised 1991 tariff on the structure of effective protection has not yet

been thoroughly investigated. However, if we remember that the tariff rates in the Egyptian tariff structure have generally increased with the stage of production—with raw materials taxed at lower rates than intermediate goods, and these two categories less protected than final consumer goods—the degree of effective protection granted to various activities would be expected in general to decline if the dispersion of tariff rates is reduced. The protectionist impact of the tariff structure would be reduced and the domestic production would be opened to increased foreign competition.

Anti-Export Bias in Trade Policy

A domestic producer has the choice of selling the output in the domestic or the export market. This decision largely depends on the relative profitability of the domestic versus the export market, which, in turn, depends upon the prices. Domestic prices are affected by foreign trade policies. If the policies pursued render production for the domestic market more profitable than production for export markets, they are said to discriminate against exports and to entail an anti-export bias.

Egypt, like all industrial and developing countries, has protected its manufacturing industries that produce for the domestic market. It has traditionally protected import-substituting industries over exports, and industry over agriculture, principally by imposing high protective tariffs on imported commodities. Some essential foods and raw materials are exempted from tariffs, but most imported inputs and final products are subject to import taxes that are usually high. These taxes increase costs of production and hinder export expansion. They further raise domestic prices, thus raising the financial profitability of domestic sales compared with export sales.

Since the liberalization policy was adopted in 1974, Egypt has encouraged economic activity through a complex system of incentives. Domestic investments have been encouraged through tax deductions, low-cost credits for specific sectors, and tariff reductions and exemptions on imported machinery and material inputs. Until 1986, domestic production was further assisted through import licensing, quantitative restrictions on imports, and an overvalued exchange rate. However, these measures discouraged exports by raising the

profitability of production for domestic markets over foreign markets.

In August 1986, Egypt made a move toward a more liberal trade regime. Successive policy reforms consisted of dismantling quotas and quantitative restrictions on imports, comprehensive tariff revision and unification, and successive devaluations and reductions of the multiple exchange rates until unification was accomplished.

These steps toward liberalization were significant. However, the acute foreign exchange shortages resulted in increasing recourse to various nontariff barriers such as import prohibitions and suspensions of letters of credit to reduce demands for foreign exchange. Some of these NTBs had explicit protectionist intentions, others were used for "rationalizing" foreign exchange use, for health, defense, or other considerations. They all resulted in increasing domestic prices and the profitability of production for the domestic market and in further discouraging exports. Some incentives were provided to exports, including allowing industrial exporters to retain 100 percent of their export earnings. Thus, they eliminated the bias against exports caused by converting export proceeds at a lower exchange rate (the official bank rate) than that applied to financing imports of intermediate inputs and debt service (the parallel market rate). Also, institutional changes involving simplification of export and import procedures were initiated, the duty drawback and the temporary admissions systems were revised, and discrimination against the private sector in foreign trade was removed, allowing it to engage in various export activities.

These expanded incentives, coupled with the devaluation and the subsequent adjustments were intended to increase the competitiveness of exports. These reforms altered the structure of economic incentives, but still failed to eliminate the bias against exports.[19] The extent of the economy-wide average bias against exports decreased from 36.6 percent before the August 1986 tariff reform to 34.3 percent thereafter. However, it did not decrease uniformly across all activities. A few activities actually experienced an increased bias

[19]For the measurement of the extent of tariff-induced bias against exports, see Balassa and Associates (cited in fn. 14), pp. 331–32.

against their potential exports (animal production, food processing, tobacco processing, footwear, wood and wooden products (excluding furniture), paper and printing, and chemical products (excluding petroleum refineries)). The anti-export bias declined in all other activities. Sectors enjoying the largest decrease in this bias were sectors with high export potential: spinning and weaving, final wear, furniture, ceramics, china and porcelain, and glass and products.[20]

The latest tariff reform in 1991 further tended to reduce the margin between domestic and export selling prices, helping to reduce the bias against exports. This tendency was further enhanced by the new ERAIE—which considerably simplified export procedures as well as eliminating a large portion of NTBs on imports—and by the successive devaluations and the unification of the exchange rate. Whether these measures will significantly stimulate exports remains to be seen.

Concluding Remarks

Examination of Egypt's trade policy since the mid-eighties has shown that, first, NTBs on imports have been used widely for various purposes. Import bans were primarily directed toward protecting domestic industries. However, while many of the other NTBs could be justified by health, defense, standard, and quality regulations, others were used as balance of payments instruments to counter acute shortages of foreign exchange. In spite of serious attempts at phasing out NTBs on imports, their production coverage remained very high (exceeding 80 percent) in several activities, which were mainly import-substituting activities. The new ERAIE significantly reduced NTBs on imports. There is evidence, however, that an acceptable NTB (quality control) has been substituted for another more restrictive and criticized one (import prohibitions).

NTBs on exports have also been used, but to a lesser extent. Most were not intended to have protectionist effects, with a few exceptions that provided considerable protection to downstream activities.

Although the incidence of NTBs on imports was higher for the private sector, the new ERAIE tended to give equal treatment to

[20]See Kheir El-Din and others (cited in fn. 8), pp. 124–26.

both public and private sectors in terms of import restrictions, whereas export regulations remained more constraining on the public sector, even after the new ERAIE.

The effective protection given by the tariff structure has in general been higher than implied by nominal tariffs on outputs, indicating that tariffs on outputs were generally higher than on inputs. Effective protection has tended to favor consumer goods activities—whether durable or nondurable—in addition to the steel and iron industry and the transport industry. The intermediate goods industry and tools and machinery were moderately protected, while the more traditional manufacturing activities were actually discriminated against.

The tariff reform of 1986 coupled with the devaluation of the pound for tariff valuation and the ensuing modifications implied a step toward liberalization and the substitution of market mechanisms for direct administrative interventions more than a genuine reduction of effective protection to domestic activities. However, decreasing the range of tariff rates in the 1991 customs tariff revision is likely to reduce somewhat the effective rate of protection granted to various activities.

There is evidence of significant correlation between the production coverage of import bans and the effective rate of protection in some industrial activities, showing that the latter has been reinforced by import prohibitions.

In spite of successive measures to increase export incentives, the tariff structure continued to show a significant bias against exports (estimated at 34.3 percent in the tariff structure prevailing until 1991). This bias has been considerably eased on some export sectors with high export potentials. The latest 1991 tariff revision has further tended to reduce the spread between domestic and export selling prices, thus helping to reduce the bias against exports.

Successive devaluations of the exchange rate and the reduction of multiple rates until unification in October 1991 had little impact on the structure of protection, as it applied similarly to both outputs and inputs. However, the impact on the spinning industry and on major export crops (cotton and rice) was highly significant. These devaluations—an attempt to unify the banking rate with the parallel rate—had a greater impact on the public than on the private sector,

as the latter was less protected by the overvaluation of the exchange rate and imported its production requirements predominantly at the parallel market rate.

The series of corrective measures that Egypt implemented aimed at reducing high customs tariffs, phasing out most nontariff barriers to imports, dismantling restrictions on exports, simplifying the exchange rate system and ensuring a competitive exchange rate, and treating public and private trading activities equally have had a positive impact on external trade performance. Encouraging signs can be recognized:

- Exchange rates have stabilized, and the difference between the free banking rate and the parallel rate had become marginal even before the recent unification.
- Nontraditional exports—especially engineering products and cotton manufactures—have positively responded to the exchange rate devaluation since 1987.
- A declining trend in the rate of expansion of commodity imports has been noted in spite of alleviation of NTBs.

The balance of payments outlook has improved somewhat. However, in spite of these signs of improvement, the trade performance and the pattern of resource allocation have not altered fundamentally, which may be partly explained by the following:

- NTBs, although pervasive, did not effectively constrain imports, and large quantities of banned imports continued to flow into the economy.
- The tariff structure played a secondary role in determining the domestic price level and in affecting the structure of relative incentives, which were mainly determined by government controls and direct intervention. Tariffs in Egypt have primarily been a source of government revenue.
- The effect of overvaluation of the Egyptian pound on the structure of incentives in the economy has been relatively limited, except for cotton spinning, cotton weaving, and other manufactures.

Furthermore, successive attempts at liberalizing the trade regime and the ensuing corrective measures were undertaken timidly and in

piecemeal fashion. In addition, trade policy in Egypt is not the major determinant of trade performance or of the pattern of resource allocation, both of which are still controlled by various government regulations and interventions and by institutional, legislative, political, and social considerations. It is still too early to judge whether the recently enacted trade policy reform, started in 1991, will effectively and fundamentally alter trade performance and help establish competitive export channels and efficient import-substituting capacities. But awareness of the need to reform on various economic and noneconomic fronts at the same time is an encouraging indicator of potential improvement.

Comments

Abadalla Al-Kuwaiz and Nasser Al-Kaoud

The authors of the paper, Hanaa Kheir El-Din and Ahmed El-Dersh, deserve to be commended for their effort in preparing it, and for its content, which is a valuable contribution to our seminar. It provides a comprehensive survey and analysis of Egypt's foreign trade policies.

Our comment provides a brief summary of the paper, and then a number of general remarks.

The paper deals with the foreign trade policy of Egypt, providing a historic overview of its foreign trade policies since the mid-1800s, referring to the various stages and the basic features of each stage (1840–1930, between World War I and World War II, during World War II, from the end of World War II through the 1950s, between the 1960s and the early 1970s, then up to the early 1980s).

The paper then presents the current economic situation in Egypt beginning with the second half of the 1980s, the difficulties encountered by the Egyptian economy and the factors behind them during that period, and the reforms adopted by Egypt since June 1986 aimed at introducing market forces to determine resource allocation, which led to Egypt's agreement with the International Monetary Fund in 1991 on a structural reform program and a stabilization program. The paper presents the key elements of the two programs.

The components of Egypt's trade policy since 1986 are presented in detail, including a description of the tariff structure, the nontariff barriers, the foreign exchange system, and the changes introduced in those components up to October 1991.

In the section entitled "The Impact of Trade Policy on Resource Allocation and Export Performance," comparisons are provided for production coverage of various customs tariff and tariff barriers before and after 1991 (the date of the new Executive Regulations for

the Administration of Imports and Exports (ERAIE)). The levels of effective protection rates provided by tariff for 1959, 1980, and 1986 are shown.

This section also discusses the aspects of anti-export bias in trade policy and the measures taken since 1974 to remedy the situation, giving incentives to exports.

While the paper presents a detailed description of the tariff structure and nontariff barriers in Egypt, it is made at the expense of the analytical side, which is characterized by generalizations in its findings.

As an example, one section deals with the analysis of trade policy, resource allocation, and export performance. But it does not discuss these areas directly by linking them to a theoretical framework. It presents only the production coverage of tariff and nontariff barriers, the proportion of production subject to these barriers, the effective rates of protection, and aspects of anti-export bias in trade policy. The paper does not provide any qualitative analysis or quantitative assessment of the impact of changes in tariff and nontariff barriers and in the exchange rate on the composition and volume of exports and resource allocation.

In a number of instances, the paper mentions that economic decision makers use the tariff (or export duties) or the exchange rate, among other instruments, to influence production rates or government revenue, without providing an appraisal of these two instruments or indicating a preference for one over the other. Even if we confine our discussion to customs duties, we find no reference in the paper to the impact different tariff levels had during the period under review on industrial growth in particular, or on the growth of government revenue or of national income in general. Furthermore, if we consider only the governmental objective of increasing government revenue, we find that such an objective can be reached through increasing the rates of customs duties (or export duties), or as a result of increased tax revenues based on increased production resulting from a reduction of customs duties on production inputs or a reduction of export duties (the so-called Laffer Curve), or what we can call the theory of Ibn-Khaldun (named after Arab thinker Ibn-Khaldun) on the impact of taxes. No such analysis is evident in the paper.

It is well known that Egypt often resorts to swap arrangements in its trade relations as an instrument of its foreign trade policy. It would have been useful if the authors had elaborated on the position of this instrument in Egypt's trade policy.

In a seminar like this, the paper is expected to include an analysis of the composition and volume of Egypt's foreign and intra-Arab trade, and the impact on these two areas of the changes in tariff and nontariff barriers. The outcome of the general conclusions—on the positive response of nontraditional exports to a reduction in the exchange rate, or the deceleration of increases in imports of commodities resulting from adjustment measures—is not adequate.

The list of nontariff barriers to imports includes import prohibitions, the suspension of letters of credit, prior approval by specified authorities, special conditions for imports, servicing facilities requirements, and quality controls. These barriers are presented in the paper as if they were of equal impact or justification. The paper refers to replacing one barrier by another, for example, an import ban for quality controls. Quality controls or the requirement of servicing facilities should have been justified in a different way.

The issues contained in the paper are numerous, scattered, and lack cohesion, which reflects on the unity of the paper.

It seems that many of the nontariff barriers resulted from the limited role given to the private sector and the nonadoption of market economics. It is therefore important for the economy to be oriented more toward market forces, the allocation of resources, and privatization because of the major role they play in the liberalization of Egypt's trade policy.

The paper repeatedly states that Egypt's trade policy has targeted import substitution and shown a bias against exports, leading thereby to a diminishing share of imports in GDP. But Table 1 shows that the ratio of Egyptian imports to GDP in 1977 is the same as for 1989. I wish the paper could give an explanation for this.

The paper presents the structural reform program and the stabilization program without adequate evaluation or assessment of their applicability.

Comparisons between the production coverage of tariff and nontariff barriers can be more meaningful if they include data from other countries.

In calculating effective and nominal rates of protection, the paper draws upon the results of another study by one of the authors (Hanaa Kheir El-Din), making the method adopted for calculating the rates or arriving at those results ambiguous for the readers of the paper presented at this seminar. For example, there is no reference in the paper to any evidence supporting the concluding remark on the existence of a significant correlation between the production coverage of import prohibitions and the effective rate of protection. The analyses contained in the paper also do not support the concluding remark that successive exchange rate devaluations had little impact on the structure of protection. The overall bias against exports in the economy is assessed to have fallen from 36.6 percent before August 1986 to 34.3 percent thereafter. It is unclear how this assessment was calculated.

The study provides no explanation of a number of the concluding remarks, which are included as a supplement or marginal notes and not as conclusions drawn from the text of the paper.

Lyn Squire

The authors deserve to be commended for having written an informative, competent, and very timely assessment of Egypt's trade policies and the reform recently initiated by the Government.

Underlying the paper, especially in the early part, there is the argument that only with protection of the industrial sector will manufacturing develop in a country. For example, it is contended that the country's first industrialization in the 1930s only took place because a tariff was imposed that had protective effects. This may well be true in the case of Egypt during the last hundred years, but the general proposition that industrialization only occurs with protection is demonstrably untrue. Fortunately, this erroneous contention does not affect the remainder of the paper.

One significant contribution that the paper makes is in the measurement of the production coverage of nontariff barriers (NTBs) in

Egypt. The estimated coverage, including only manufacturing, is strikingly large. Earlier analysis, initiated along somewhat similar lines by Hanaa Kheir El-Din, shows a more modest coverage of NTBs. Without getting into a detailed comparison of the two different data sets and estimates, one nevertheless must question whether the more recent estimates presented in the paper overestimate NTB protection. The current estimates are undertaken at a highly aggregated, two-digit, level, while the earlier estimates were undertaken at a more disaggregated four-digit level. Aggregation introduces an upward bias in the coverage estimates; if there is evidence of an NTB for a given product group, all of the production in that product group is considered to be protected by that NTB. Nevertheless, the point made by the authors is well taken and correct: Egyptian manufacturing has in the past enjoyed considerable NTB protection and continues to do so, even after the rather courageous steps toward trade policy reform taken in 1991.

The use of the concept of effective protection to analyze the effects of the Egyptian incentive system is appropriate and potentially quite useful. The problem stems from the way in which rates of effective protection are calculated. The authors have relied on work that makes the estimates on the basis of *tariff* protection. In an economy in which there are significant policy-induced price distortions reflecting the overall incentive system, one cannot attribute much importance to effective tariff protection. Effective tariff protection is not the same as effective protection. For Egypt, the price distortions have been considerable, including, as the authors document, extensive NTBs. Tariffs cannot explain, or measure, the differences between international and domestic prices. Yet the extent to which those differences are allowed to exist reflects the system of incentives. Accordingly, one must be very careful in not reading too much into the authors' estimates of effective tariff protection. One hopes that with the reforms initiated so far by the Government some initiative will be exercised to undertake a comprehensive and policy-oriented study of the incentive system, including the measurement of effective protection based upon direct domestic and international price comparisons.

In analyzing the trade policy liberalization, and particularly the reduction of NTBs, taking place during 1991, the authors conclude that there has been some substitution between more acceptable

NTBs (such as quality control) for more restrictive NTBs (such as bans). In the strict sense this cannot be true, since both were reduced significantly during 1991, although proportionally bans were reduced less dramatically. One must conclude that this was so because the Government has found it politically more difficult to reduce the bans. In addition, looking at the reduction in bans that has taken place so far, it is evident that the greatest cuts were not in manufacturing but in agriculture, and for the private sector, rather than for the public sector. Again, the Government seems to have found it difficult to reduce protection for manufacturing and for the public sector itself. This of course raises questions as to the future success and direction of the reform effort.

While the paper very ably describes the policy reforms that have taken place during 1991, there is little said about where they are likely to go in the future. The reader is left with the question of whether these reforms have been a one-step operation or whether they are part of a larger program of trade reform to unfold sometime in the future. If the latter is true, what is the nature of the future reforms? What can be expected and when? Moreover, if there is a blueprint for a reform program that the Egyptian Government has in mind, why is such a direction not forcefully announced and indicated by the Government?

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