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Trade Integration as a Way Forward for the Arab World

A Regional Agenda

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Abstract

The current political turmoil for more open and participative societies in many Arab countries coupled with the emergence of new growth poles around the world could create the conditions for a big push toward greater regional and global trade integration of the Arab world. Further integrating Arab countries among themselves and opening up the region to the rest of the world are two complementary avenues to improve market access, promote behind-the-border regulatory reforms, facilitate cooperation on regional public goods, foster the emergence of an "Arab factory" through regional supply chains and productions networks, and eventually create the conditions for more and better paid jobs for the growing Arab workforce. A more ambitious trade agenda in the context of the Pan-Arab Free Trade Area would be a good place to start. Although difficult and challenging, and requiring a good dosage of flexibility and variable geometry, such an agenda would consist of (1) completing the free movement of goods within the Pan-Arab Free Trade Area, notably through the elimination of unnecessary non-tariff barriers; (2) implementing a regional initiative to liberalize services trade, including identifying a number of pilot service sectors for early regional liberalization; and (3) strengthening the rules and discipline applicable to regional trade and other policies of common interest.

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Trade Integration as a Way Forward for the Arab World: A Regional Agenda

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Introduction

The second Arab Economic, Social and Development Summit that was held in Sharm El-Sheikh, Egypt in January 2011 took place against the backdrop of an Arab world in turmoil that keeps losing ground in the globalized world economy. Although countries in the Middle East and North Africa (MENA) region have made progress in recent years in exploiting comparative advantage, the share of the MENA region in total world exports of non-oil goods has remained under 1 percent for more than 30 years, and despite doubling its services exports, MENA's share in total services trade has also stagnated at around 2.8 percent during 1990–2006.[2] These outcomes reveal serious competitiveness issues and suggest that the region has missed opportunities to integrate into the world economy, increase growth, and create new productive jobs. The Summit came when widespread popular protests in many Arab countries cropped up over lack of civil and political liberties, economic opportunities—including high unemployment—and rampant corruption, and turned into political upheavals.

Yet, with the emergence of formidable global competitors such as China, India, and Brazil, a more open Arab world may have an historical opportunity to tap new poles of growth through greater regional and global integration. A new, fast-evolving multi-polar world economy is emerging, in which some developing countries are becoming economic powers and others are moving towards becoming additional poles of growth (Zoellick 2010). MENA's productivity is comparable to that of many middle-income countries of Latin America and surpasses that of Sub-Saharan Africa. However, a comparison with high growth East Asian countries and other emerging countries shows large gaps in total factor and labor productivity. Further integrating Arab countries among themselves and opening up the region to the rest of the world are two complementary avenues to gradually close the region's productivity gap. In improving market access for exporters, promoting behind-the-border regulatory reforms, facilitating cooperation on regional public goods (e.g., infrastructure), and creating the conditions for the emergence of an "Arab factory" through regional supply chains and productions networks, regional trade agreements are a powerful tool for transformational changes (Chauffour and Maur 2010). Deeper regional integration could help address some key economic challenges that face the region, such as economic diversification and creating jobs for an expanding workforce.

The 2011 Arab Economic Summit was another missed opportunity to advance the trade agenda in the Arab world. Contrary to what had been anticipated after the first Arab Economic Summit in Kuwait in 2009, the Sharm El-Sheikh Summit did not make any major leap forward on trade integration, and the Summit Declaration only reiterated the objective of establishing the

[2] For a recent discussion of economic developments in the MENA region, see World Bank (2010), MENA Regional Economic Update: Recovering from the Crisis.

Arab Common Market in 2020 and undertaking fresh partnerships with a number of emerging countries, including China, India, Turkey, and Russia. To be sure, nowhere in the world is regional integration a painless and easy process. And the Arab world is no exception. Everywhere it requires leadership, resolution, and patience, including with temporary reversals. Above all, each regional integration process is unique in its historical and political context.

Historical circumstances may begin to be reaped in the Arab world for a big push toward greater regional and global integration. Until now, the region has suffered from discretionary and arbitrary implementation of policies, and from lack of government credibility to really change a deeply rooted status quo of privileges and unequal treatment of investors. While the current political turmoil in the Arab region could end up further entrenching those privileges or creating new ones, it could also create the conditions for more open, non-discriminatory, and rule-based economies. In this scenario, the Arab world could start reaping the full benefits of global and regional integration. And as far as regional integration is concerned, completing the Pan-Arab Free Trade Area (PAFTA) would be a good place to start.[3] This would essentially consist in (1) completing the free movement of goods within PAFTA, notably through the elimination of unnecessary non-tariff measures; (2) implementing the regional initiative to liberalize services trade, including identifying a number of services sectors for early regional liberalization (e.g., trade facilitation & transport, banking & finance, and communication & information); and (3) strengthening the institutional rules and discipline applicable to regional trade and other policies of common interest.

Completing the free movement of goods within PAFTA, notably through the elimination of unnecessary non-tariff measures (NTMs), and integrating better the region into global supply chains and production networks would create the conditions for the emergence of the "Arab factory". A concerted effort to streamline all unnecessary NTMs in PAFTA countries will remove one of the major remaining bottlenecks to intra-regional trade in goods. This would involve reviewing the substance of existing NTMs, streamlining them using methodologies experimented in other regional agreements around the world, including a guillotine approach when appropriate, and establishing regulatory impact assessments to improve the process through which new NTMs are created. To facilitate the integration of the region into global supply chains and production networks, countries in the region could unilaterally reduce their most favored nation (MFN) tariffs, especially tariff peaks, to the level of the most competitive regions of the world (e.g., East Asia). Such unilateral liberalization has proven to be a successful strategy in a number of emerging trading partners that are now sustainable growth poles.

[3] The preferential integration of many Arab countries with the EU, the US and other important trading partners is equally strategic but is not the focus of this paper.

Liberalizing services trade within PAFTA and beyond is the next low-hanging fruit to boost regional integration, due in particular to the positive spillover effects of more open services trade on trade in goods. In line with the 2009 Kuwait Arab Economic Summit Declaration, the Arab world should embark on a concrete plan to freeing services trade among Arab countries and beyond. This plan would involve developing a regional strategy for trade in services integration, establishing forums (or "services knowledge platforms") to address knowledge gaps and facilitate the political economy of reform, conducting regional Regulatory Services Audits, and negotiating a pan-Arab agreement in services. To pave the way for services liberalization, a number of pilot services sectors could be identified for early regional liberalization. Key candidate sectors for such early liberalization include (1) trade facilitation & transport, given the importance of facilitating trade in key corridors and improving trade facilitation and logistics services inside the Arab region, including Customs and border agencies; (2) banking & finance, to immediately promote banking sector competition, encourage further access to credit and intra-Arab investment, and facilitate capital movement among Arab countries; and (3) information & communication, in order to enhance the competitive potentials of technology enterprises, develop legislative frameworks related to this sector, and encourage the private sector to attract investment.

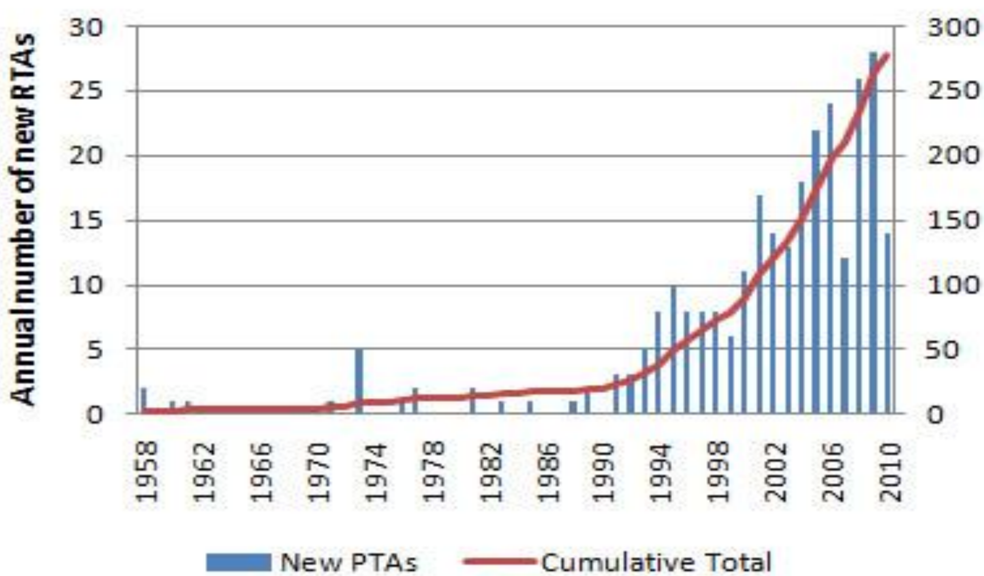
A meaningful and credible pan-Arab free trade area requires that regional trade and other policies of common interest be subject to clear, non-discriminatory and transparent binding rules and discipline.[4] A major institutional overhaul to strengthen the rules and discipline applicable to PAFTA and other regional institutions would provide additional credibility to the regional integration plans. This would involve strengthening or agreeing on a new set of basic principles for the governance of PAFTA, including prohibitions of NTMs unless they fulfill a set of basics principles, such as non discrimination and necessity, effective national treatment provisions in services trade, and effective framework to guarantee the free movement of labor within the region. An approach would be to strengthen the mandate of the General Secretariat of the League of Arab States (the Secretariat) to monitor the implementation of members' liberalization commitments, including the dismantlement of NTMs and the liberalization of services. Regardless of the approach, regular monitoring of implementation commitments is important for policymakers to be able to assess the effects of the agreement. This would also involve creating a permanent and independent dispute settlement mechanism to oversee enforcement, including measures to ensure compliance.

[4] These rules and discipline would need to be made consistent with the other treaty obligations that a number of Arab countries have with the EU, the US and other trading partners.

1. The Arab World in an Increasingly Integrated World

Regional integration is a reality that is fast reshaping the world. Integration is happening rapidly throughout the world – and much of it is regional in nature: transoceanic integration in post-WW2, North-South integration since 1970s, now a very swift trans-Eurasian integration – the integration of the super-continental space anchored by the EU, Russia, China, Japan and India. Sixty years after the founding of the GATT the global trading landscape has changed beyond recognition. While membership of the WTO continues to grow,[5] participation in preferential trade agreements (PTAs) is expanding at an unprecedented rate. As of end-2010, 278 PTAs have been notified by the WTO members and are currently in force (Figure 1).[6] As a consequence, a growing proportion of world trade is, or has the potential to be, conducted under preferential terms rather than under the non-discriminatory regime of the WTO. In addition, trade conducted under preferential rules is increasingly subject to a plethora of cross-cutting regulatory rules and discipline, which multiply the potential channels of regional policy convergence and integration.

Figure 1. PTAs notified to the GATT/WTO (1958-2010), in force, by year of entry into force

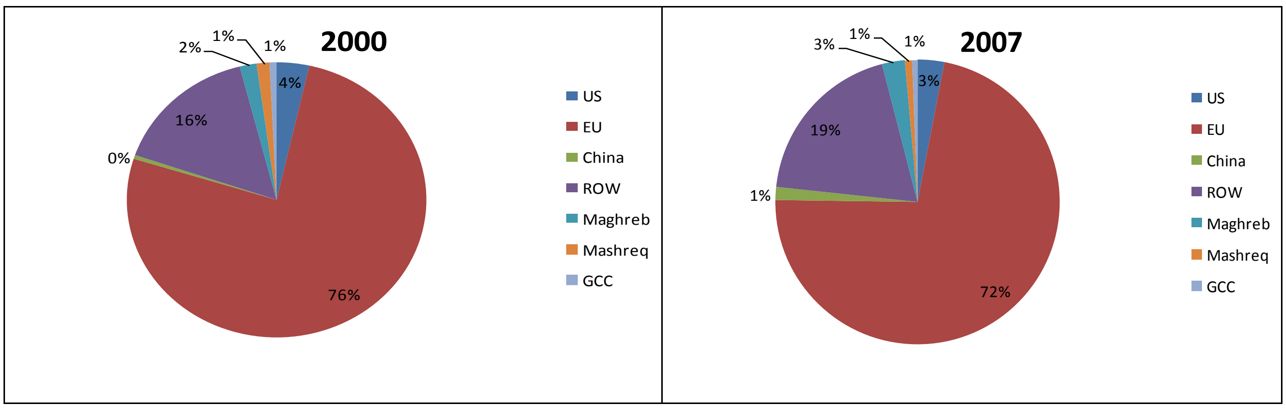


Source: WTO Secretariat

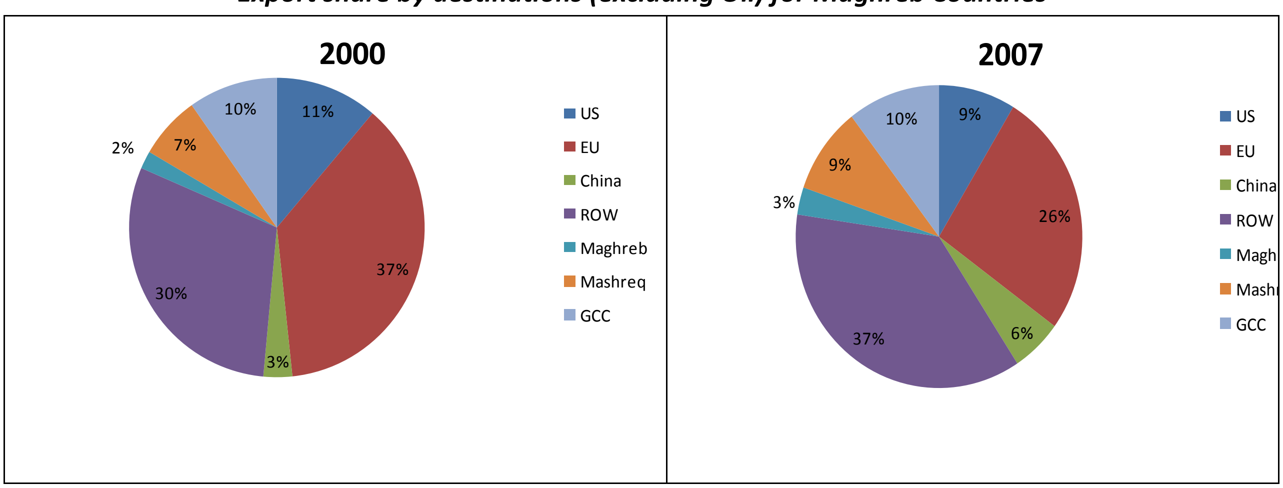
[5] As of end 2010, the WTO counted 153 members with 30 countries in the process of accession, including six Arab countries (Algeria, Lebanon, Libya, Syria, and Yemen) as well as Iraq and Iran in the MENA region.
[6] This figure does not include the hundred PTAs which are currently in force but have not (or not yet) been notified to the WTO. The new World Bank Global PTA Database (GPTAD) provides information on some of these non-notified PTAs. It is available at http://wits.worldbank.org/gptad/

The Arab world has yet to reap the full benefits of trade integration. Integration has been a goal for the Arab World since the establishment of the Arab League in 1945. However, for a variety of (mainly political) reasons, that goal has remained elusive for a long time (Aluwaisheg 2004). For many Arab countries, regional trade accounts for less than 10 percent of total trade. At less than 5 percent, the Maghreb countries had the lowest share of intra-regional non-oil merchandise trade (Figure 2). And this share only marginally increased since 2000. Intra-regional trade in the Mashreq and Gulf Cooperation Council (GCC) represents a somewhat larger share of trade. In the case of Syria and Yemen, regional markets account for more than half of all non-oil exports; for Bahrain, Lebanon, Oman, and the UAE it is in the 35-40 percent range; while it is more than 25 percent for Egypt, Jordan, Kuwait, and Saudi Arabia. Recent political developments in the region toward more open and participative societies may create the conditions for improved political collaboration in support of regionalism.

Figure 2. Export share by destinations (excluding Oil) for Maghreb Countries



Export share by destinations (excluding Oil) for Maghreb Countries



Source: Comtrade

The Pan-Arab Free Trade Area (PAFTA) and other regional trade agreements (e.g., Agadir Agreement) do not appear to have created significant intra-regional trade.[7] Notwithstanding its own version of the "spaghetti" bowl of overlapping PTAs (Box 1), the Arab world is less integrated than many other regions. Early studies on the question of whether intra-regional trade flows are lower than what would be expected given levels of GDP, population and geography are somewhat ambiguous.[8] Simple shares and trade intensity indices suggest intra-regional trade is not that low and has been expanding; yet gravity models usually found that trade is less than what would be expected. A more recent update of the gravity model suggests that there has been a noticeable change in the last few years, with trade now being larger than what the standard gravity model would predict (Abedini and Péridy 2008). Yet in a world where trade is fast growing one would expect more intra-regional trade regardless of regional agreements. In the case of GCC, the increased integration seems to reflect the progress made in converging on common norms and policies in some regulatory areas and in integrating both factor and product markets.

The Arab world is more integrated through labor mobility and to some extent infrastructure links than through trade and investment. Regional economic and socio-political developments since the early 1970s, especially the oil price shocks of 1973 and 1979, the oil price reversal in the mid-1980s, and the two Gulf wars of 1991 and 2003 triggered large migration movements and displacements of population. Migration policies have also been relaxed in a number of countries. Currently, GCC nationals can move freely among the member countries, and there is a waiver of visa requirements for expatriates with valid visas in other Gulf countries. It is estimated that some 4.5 million migrants from MENA countries live in the GCC and other Arab countries.[9] Integration via infrastructure links is also developing in the region. Cross-border initiatives involving gas pipelines, electricity networks, telecommunications, and road links are increasing in number. Yet, the benefits from such initiatives will be modest unless countries in the region commit to undertake the liberalizing reforms pending in their respective domestic infrastructure markets.

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[7] The Pan-Arab Free Trade Agreement (PAFTA) was negotiated under the auspices of the Arab League's Economic and Social Council and came into force in 1997. PAFTA aims to enhance economic integration among its 17 Arab member countries through the establishment of a regional Free Trade Area that would eliminate tariffs, quotas and other barriers to trade. Under PAFTA, all tariffs on goods of Arab origin were to be removed by January 1, 2005. More recently, PAFTA signatories have expended integration efforts to trade and investment in services as well as to increase efforts to deal with non-tariff measures that restrict trade flows.

[8] For a recent review, see Hoekman, B. and Sekkat K. (2009). Deeper Integration of Goods, Services, Capital, and Labor Markets: A Policy Research Agenda for the MENA Region, World Bank, Mimeo.

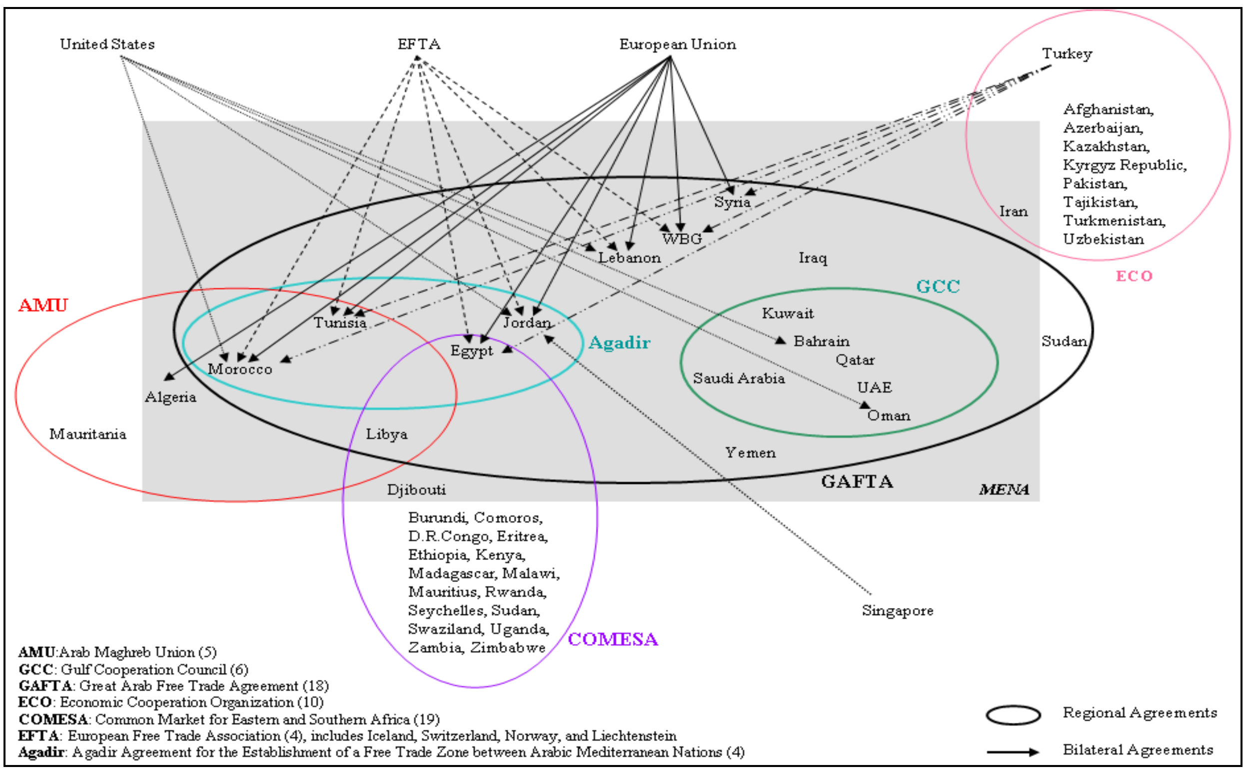
[9] MENA Economic Developments and Prospects: Regional Integration for Global Competitiveness, (2008), World Bank.

Box 1. PTAs involving the Arab World

The idea of regional integration among Arab countries has been pursued for decades. Efforts to integrate the Arab world regionally date back to the 1950s, earlier than in any other developing region. Examples are the 1957 Arab Economic Unity agreement and the 1964 initiative by Egypt, Iraq, Jordan, and Syria to form an Arab Common Market. Today, the key plurilateral trade agreements are the Agadir Agreement between Egypt, Jordan, Morocco and Tunisia which has been in force since 2007, the Gulf Cooperation Council (GCC) Customs Union in force since 2003 and the Pan-Arab Free Trade Agreement (PAFTA) in force since 1998 which includes members of the GCC and Agadir as well as other members of the Arab League. In addition, the Arab Maghreb Union (AMU) includes Agadir parties Tunisia and Morocco, and Algeria, Libya and Mauritania.

Arab countries also belong to a crossing network of intra-regional bilateral trade agreements. For instance, Jordan has agreements with Bahrain, Egypt, Israel, Morocco, the Palestinian Authority, Sudan, Syria, Tunisia, and the United Arab Emirates and is negotiating with the GCC; Tunisia has agreements with Egypt, Iraq, Jordan, Libya, and Morocco; and Egypt has agreements with Iraq, Jordan, Lebanon, Libya, Morocco, the Palestinian Authority, Syria and Tunisia.

Links with countries outside the region are also expanding. Several countries are part of the EuroMed process of agreements with the EU and EFTA. In addition the United States has negotiated agreements with several countries in the region: Bahrain, Jordan, Lebanon, Oman and Morocco and is currently negotiating with the United Arab Emirates. While individual members of the GCC have signed agreements with or are negotiating with the United States, the GCC as a group is also negotiating with a large number of partners across the world. Its agreement with Lebanon is in force, agreements have been signed with EFTA, Singapore and Syria and its extensive negotiating agenda includes Australia, China, the EU, India, Iran, Japan, Jordan, Korea, MERCOSUR, New Zealand, Pakistan, and Turkey.



Source: MENA Economic Developments and Prospects: Regional Integration for Global Competitiveness, (2008), World Bank.

The lack of trade integration is as much a cause as a consequence of the region's economic difficulties. Low trade integration could be the result of poor production complementarities and other exogenous factors. Indeed, a number of Arab countries have similar resource endowments, production capabilities, and export structure. They may find it difficult to use regional integration as a means to establish patterns of specialization and diversification. The lack of intra-regional trade is also to some degree policy driven. As recently analyzed, public sector governance and participation, accountability and transparency, and rents and privileges remain key impediments to private sector development in the region.[10] The very same causes also impede the region's capacity to export. Without improved rule of law, participation, and governance, trading across borders is difficult and trade cannot sustainably flourish. In turn, the lack of integration and exposure to new technologies, innovation, and ideas hamper more rapid progress in the region and help explain many economic and social shortcomings: poor resources utilization, insufficient human capital, gender inequality, high unemployment, oversized governments, unfavorable investment climate, limited foreign investment, and eventually lackluster private sector performance.[11]

Historical experiences of successful regional integration offer avenues for the Arab world. Gains from regional integration could be very significant, as recently demonstrated by the performance of countries in Central and Eastern Europe and East Asia. Whether Arab countries refer to the centralized EU model of integration or the decentralized ASEAN model, they have much to learn from these successful models of regional economic integration (Akhtar 2009). Yet, worldwide there are very few regional cooperative institutions that function effectively due to the common unwillingness of governments to share sovereignty and the weakness of national and regional administrative capacities. Strong political will and solid institutions are therefore key to success. Strengthening and making regional Arab institutions, including the General Secretariat of the League of Arab States, more effective and efficient would be an important step toward promoting intra-regional cooperation (see below).

The Arab world needs to invent its own model of integration based on its circumstances and conditions. While regional integration can be a significant driver of a country's better overall performance, as in the case of Central Europe and Eastern Europe or South East Asia, it can also be the reverse: in Central Asia autocratic and corrupt regimes may reinforce each other with poor governance and limited economic reform. The Arab world's approach to regional integration should be anchored on the region's evolving realities and circumstances—including the current political and social upheavals in many Arab countries for more voice and representation, economic opportunities, and openness more generally.

[10] From Privilege to Competition: Unlocking Private-Led Growth, (2009) MENA development Report, World Bank.
[11] Arab Human Development Report 2002, UNDP and Arab World Competitiveness Report 2005, World Economic Forum.

- **A first circumstance is that the Arab world could take better advantage of a shared heritage and common identity, especially in this historical time of political rebellions.** There are at least three Arab worlds; each with its own idiosyncrasies and prospects. The Maghreb countries are predominantly oriented toward the EU;[12] while Mashreq countries have a more diverse reach. The GCC countries are more globally integrated, although overwhelmingly through oil and gas. The Arab world is also somewhat more integrated in terms of investment (from GCC) and labor (into GCC but other regions too) than trade. In terms of sub-regional integration, the three groups are at different stages of economic convergence. While the GCC are moving from a customs union to developing a common market with a possible monetary union on the horizon, the other two sub-regions remain are divided with longstanding political disputes and/or conflicts. In each sub-region, countries are also at various stages of progress towards establishing liberal democracies and open market economies. Yet Arab peoples have more in common in terms of culture, identity and sense of belonging than many other regional trading blocs. The current social and political upheavals could help cement a collective future based on common values, including economic freedom and civil and political liberties.

- **A second circumstance is that the Arab world needs stronger regional powers to drive regional cooperation.** The development of efficient and effective regional cooperative institutions appears to be critically driven by the initiative and interests of major regional powers: France and Germany were critical in the early stages of the EU; Japan nurtured the "flying geese" model of development in East Asia and took the leadership to foster regional cooperation; the US drove NAFTA; Russian and Chinese interests may drive the regional integration of Central Asia. However, like in many other regions of the world, it is not clear which power(s) in the Arab world could lead and drive regional cooperation. There is no natural "hub" or anchor country – as is the case for Mexico and Central America (the US) – nor is there a subset of "equals" (large countries) that have an interest in cooperation – as was the case in the EU Regionalism (Hoekman and Messerlin 2003). Yet most Arab countries understand that they are now part of a regional architecture. That they have an interest in healthy, dynamic, flexible regional systems for finance, trade, movement of ideas and people, the environment-- and strong regional institutions. Given its history, size, and geography, Egypt may have a particular leading role to play after its current transition.

- **A third circumstance is that the emergence of a new, fast-evolving multi-polar world economy could help trigger the exceptional conditions that are often required for regional integration.** Again the example of East Asia and Eastern and Central Europe illustrates the

[12] Excluding oil, the share of the EU in Maghreb export was 72 percent in 2007 (down from 76 percent in 2000). Trade with Mashreq countries has remained marginal at 1 percent during the period.

historical conditions that unleash the integration process: the collapse of Japan after WWII and the discredit of a political system in Eastern Europe. In the absence of such historical conditions, regional integration tends to be a deeply protracted political process. The current political adjustment in the region coupled with the rebalancing of the world economy offer unique opportunities for the Arab world. The move towards multiple poles of growth is accelerating as middle classes grow in developing countries, billions of people join the world economy, and new patterns of integration combine regional intensification with global openness. For the Arab world, the rise of China, ASEAN and India offers great opportunities beside energy (Pigato 2009). Arab countries are an important source of capital for the rest of the world, and increasingly a business-service hub between Asia – East and South – and Euro-Africa. The Maghreb can soon be part of a Euro-Med integration linked to both the Mideast and Africa. The prospects of a Union for the Mediterranean encompassing 43 countries from Europe and the Mediterranean basin could become more favorable with the appropriate democratic transitions in North Africa, the Middle East and the Balkans.

With appropriate flexibility and variable geometry, building on PAFTA to tackle border and behind-the-border barriers to trade and investment is the surest path for integrating the Arab world. By removing barriers to trade among Arab countries, PAFTA would allow firms to obtain access to a larger regional market and, like in East Asia production networks in which hubs are increasingly sourcing intermediate inputs from the lowest cost spoke thereby increasing the scope for economies of scale to be realized, while consumers benefit from the price-reducing and variety-increasing effects of greater competition (Baumann and Ng 2011). PAFTA also helps to reduce the negative effects of the patchwork of overlapping trade agreements that has emerged – reducing the potential for trade diversion and negative hub-and-spoke effects associated with agreements signed by Arab countries with the EU and the United States (among others), and extending the benefits of free trade agreements between subsets of Arab countries (e.g., Agadir and GCC). PAFTA could also be critical in promoting innovation and trade diversification. A comparative analysis of dynamic exports of the Arab countries shows that for most Arab countries the number of dynamic products is higher in intra-regional trade than in exports to the EU (Zarrouk 2000). This indicates that the dynamic Arab products maintain differentiated export niches in intra-regional trade and suggests that there is scope for expanding intra-regional trade in processing activities.

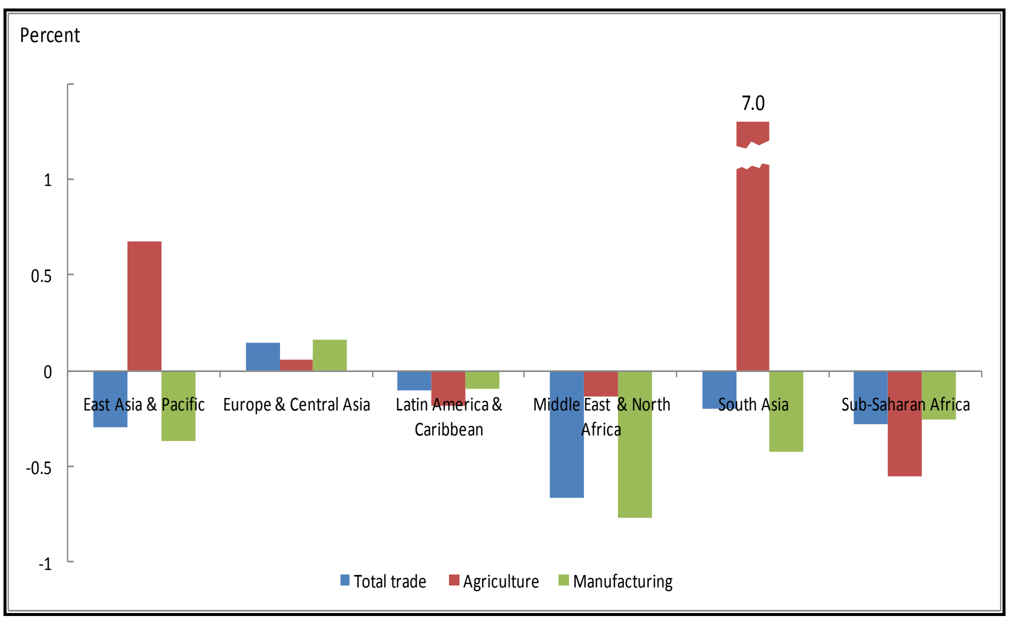
2. The Status of Goods and Services Liberalization in the Arab World

Despite progress, the dismantling of intra-regional barriers to trade in goods and services remains an unfinished agenda. PAFTA aims to enhance economic integration among its 17 Arab member countries through the establishment of a regional Free Trade Area (FTA) that would eliminate tariffs, quotas and other barriers to trade. Under PAFTA, all tariffs on goods of Arab origin were to be removed by January 1, 2005. Obstacles still hindering the full implementation of the great Arab FTA were to be cleared before 2010 and the freeing of service trade among Arab countries was expected to accelerate.[13] However, little is known about the extent to which the provisions of PAFTA and subsequent official declarations have been implemented.

2.1 Goods – A largely completed agenda

Significant progress has been made in reducing barriers to trade in goods within PAFTA. Over the last decade, preferential liberalization under PAFTA and other PTAs has been complemented with reductions in MFN tariffs. As a result, the average uniform tariff equivalent of all tariffs (ad valorem and specific) for the region fell from 14.7 percent to 6.7 percent between 2002 and 2007. Despite mounting protectionist pressures during the global economic crisis, tariffs in the MENA region decreased by another 0.8 percentage points during 2008-09. The MENA region was actually the region where tariffs decreased the most during the financial crisis, especially on manufacturing goods (Figure 3). This improvement has been confirmed by private sector operators. In 2001, tariffs were ranked as one of the most important barriers to intra-regional trade in a survey of firms in the region (Zarrouk 2001). In a follow-up survey conducted in 2009, they were ranked last (Hoekman and Zarrouk 2009). A majority of respondent companies reported that tariffs on intra-regional trade have largely been removed, and that there has been a marked improvement in customs clearance-related procedures.

Figure 3. Changes in tariffs regions, 2008–09

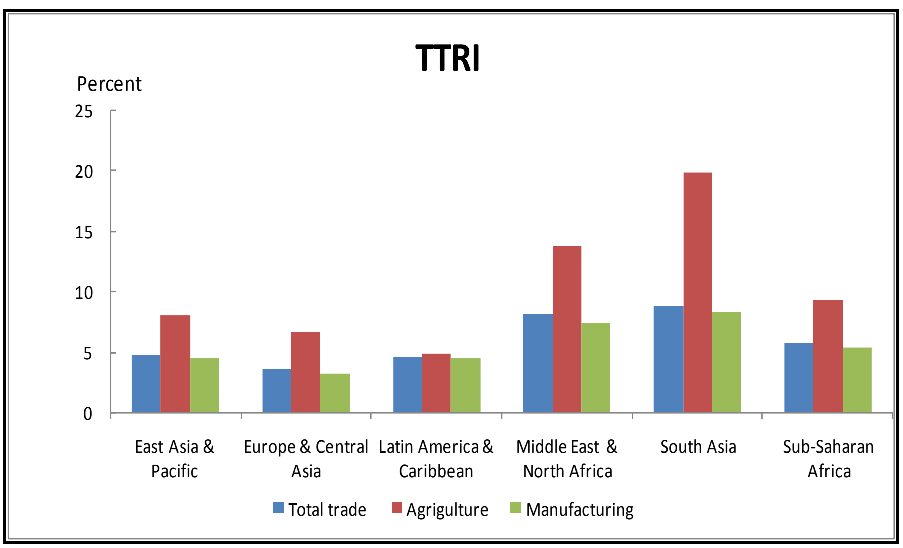


Source: World Bank and UNCTAD staff estimates.

[13] Kuwait Declaration of the Arab Economic Summit, January 19-20, 2009.

The external tariff liberalization agenda has yet to be completed. Notwithstanding the progress made in the last decade, the level of tariff protection in the MENA region vis-à-vis the rest of the world remains relatively high by international standards. According to the Tariff-only Trade Restrictiveness Index (TTRI),[14] only the South Asia region had a level of tariff restrictiveness higher than the MENA region in 2008 (Figure 4). The MENA region compares unfavorably with its main competitors in Eastern Europe and Central Asia, Latin America and the Caribbean, and East Asia and the Pacific—the new dynamic poles of the world economy. In particular, agriculture in the Arab world is still relatively heavily protected by high tariffs. Further external liberalization is all the more important as some countries may be adversely affected by trade diversion and the economic size of the Arab world is limited. Arab countries that are members of the PAFTA represents a little less than Spain's GDP. With relatively small domestic markets, trade and investment liberalization become key to integrate the region into production sharing or processing-type of trade, where each country specializes in its areas of comparative advantage and factor endowment to serve bigger markets. As discussed below, a pre-condition for this to materialize, however, is a substantial increase in the efficiency of logistics and other trade services.

Figure 4. Tariff-only Trade Restrictiveness Index (TTRI) by region, 2008



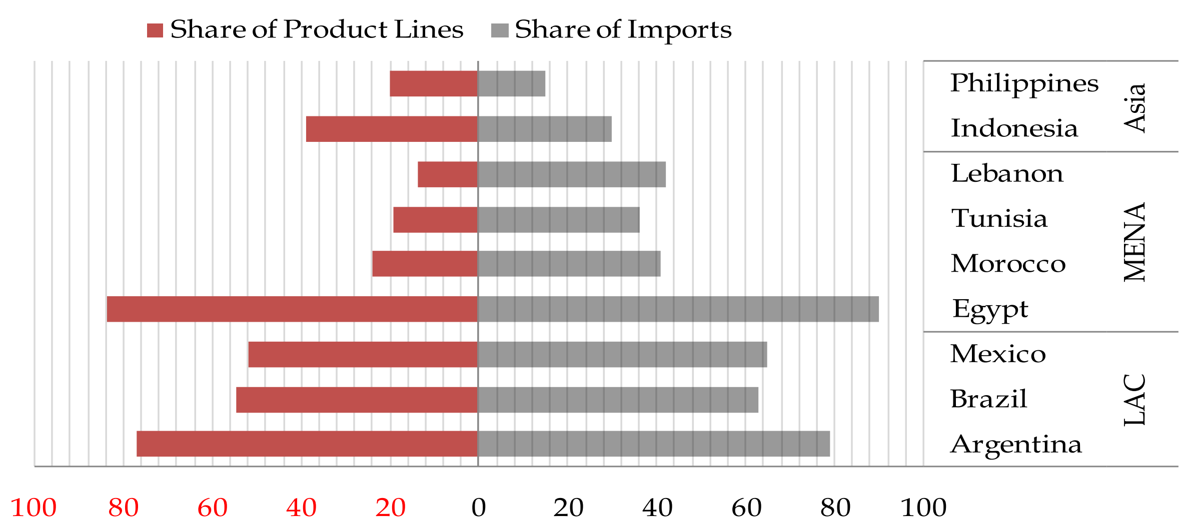
Source: World Bank and UNCTAD staff estimates.

Non-tariff measures (NTMs) have become the most important barriers to trade in the Arab world. While there has been tariff liberalization under the PAFTA, NTMs—including straightforward border closures—continue to impede regional integration. These include

[14] The TTRI is calculated as a weighted sum of ad valorem tariffs and ad valorem equivalent of specific duties, where the weights are import volumes and import demand elasticities.

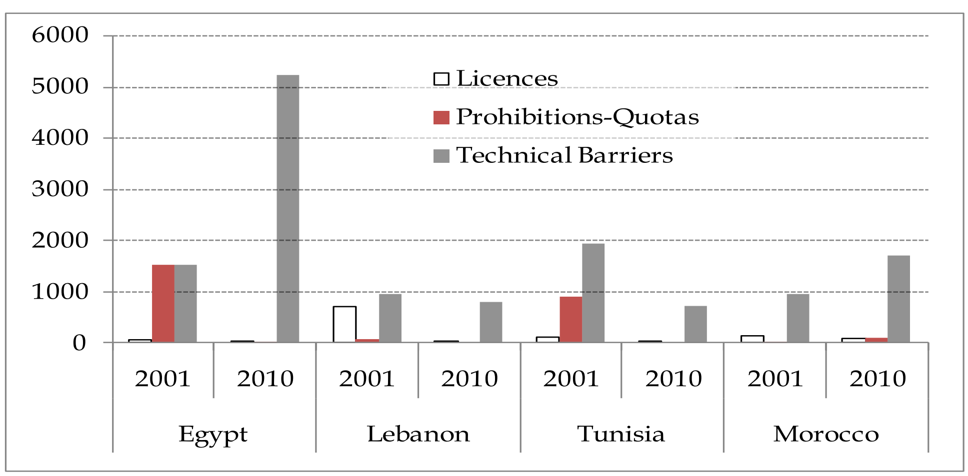
excessive delays resulted from lengthy processes of clearance and inspection, the number of documents and signatures needed to process a trade transaction, and the frequency of problems with customs and other government authorities. Based on selected evidence, the incidence of NTMs in the MENA region would seem to be higher or at least similarly comparable to that of other regions at similar income levels Figure 5. Also, the nature of NTMs has tended to shift away from old-style command-and-control to product standards and technical requirements ("technical barriers"), as shown in Figure 6.

Figure 5. Simple and trade-weighted NTM coverage ratios



Source: Gourdon 2011.

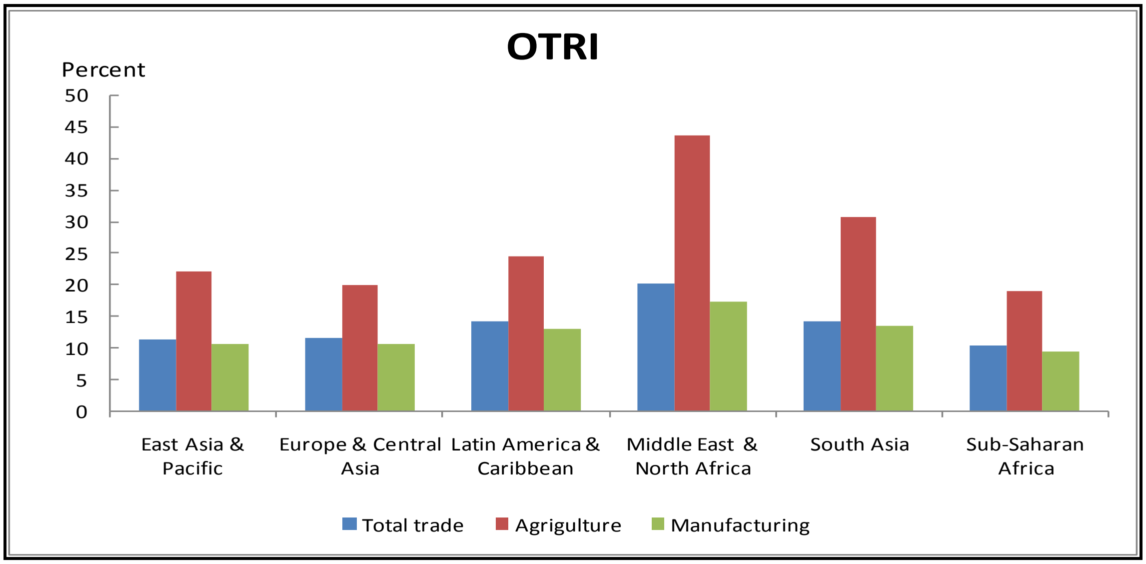
Figure 6. Shifting nature of non-tariff measures in the MENA region



Source: Gourdon 2011

When NTMs are included to the calculation of the overall trade restrictiveness index (OTRI),[15] the MENA region comes across as the most restrictive region in the world, driven by their high NTMs on agriculture goods (Figure 7). According to the firms surveys mentioned above, transport-related infrastructure and real trade costs (i.e., trade facilitation) have become the most important constraint to trade in the region. This confirms recent analytical studies that conclude that the magnitude of Arab trade flows is significantly lower than it would otherwise be as a result of high real trade costs (Dennis 2006, Harb 2007, and Peridy 2007).

Figure 7. Overall Trade Restrictiveness Index by region, 2008

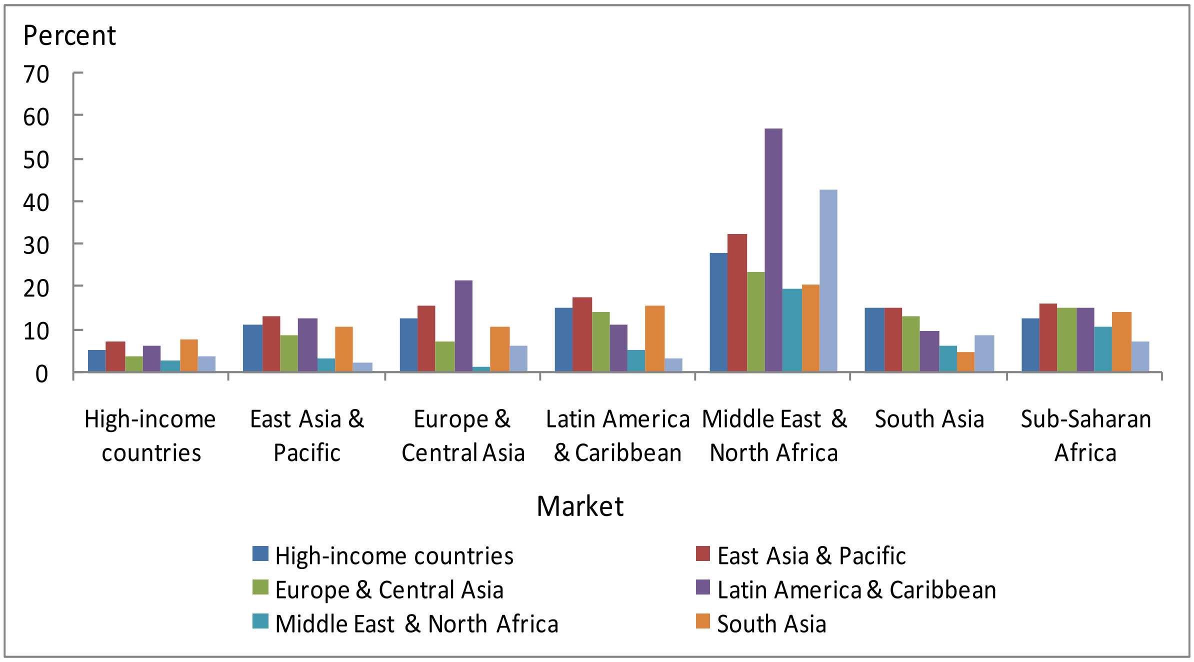


Source: World Bank and UNCTAD staff estimates.

Limited access to Arab markets for world exporters tends to insulate the region. The level of trade policy restrictions confronting exporters from a country in other markets can be measured by the Market Access Overall Trade Restrictiveness Index (MA-OTRI). This index measures the uniform tariff faced by exporters in all the external markets that is consistent with the current aggregate export of a country. Given trade preferences and the composition of goods exported, most countries have good market access in the market of high-income countries (Figure 8). Market access in the MENA region is quite restrictive, particularly among exporters from the Latin American and Sub-Sahara Africa countries. In fact the market access of Sub-Sahara African exporters in the MENA region has deteriorated in 2008. It was about 17 percent in 2007, and it jumped to more than 40 percent in 2008. Likewise, MA-OTRI for Latin American exporters to the Middle East and North Africa increased from 40 percent to 57 percent.

[15] The OTRI adds nontariff measures to the TTRI to calculate an overall trade restrictiveness index.

__Figure 8. Market Access Overall Trade Restrictiveness Index, by exporters and markets, 2008__



Source: World Bank and UNCTAD staff estimates.

The pervasiveness of NTMs is compounded by relatively poor regional trade logistic performance. Data on the performance of logistics services and on the internal costs associated with shipping goods from the factory gate to the port, and from ports to retail outlets suggest that traders confront significant hurdles in the region, with only the UAE being among the world's better performers. The *Doing Business* "cost of trading" data indicate that the costs associated with completing the procedures to export or import a 20-foot container (document and administrative fees for customs clearance and technical control, terminal handling charges and inland transport) remain high in the region (Figure 9).[16] Only Bahrain, Egypt, Qatar, Saudi Arabia, and the UAE were among the 30 top performers in 2009. Similarly, the Logistics Performance Index (LPI) reveals a great deal of variance and significant performance bottlenecks within many Arab countries (Figure 10).[17] Performance in the mostly high income Gulf states is noticeably stronger, but still well below their income group average. The standout performer is the UAE, ranked 24th in the world in the 2010 LPI, with a score comparable to that of Korea.

[16] The cost measure does not include tariffs or trade taxes. Only official costs are recorded. Inland transport costs are based on distance to the shipping port. The methodology, surveys and data are available at http://www.doingbusiness.org.

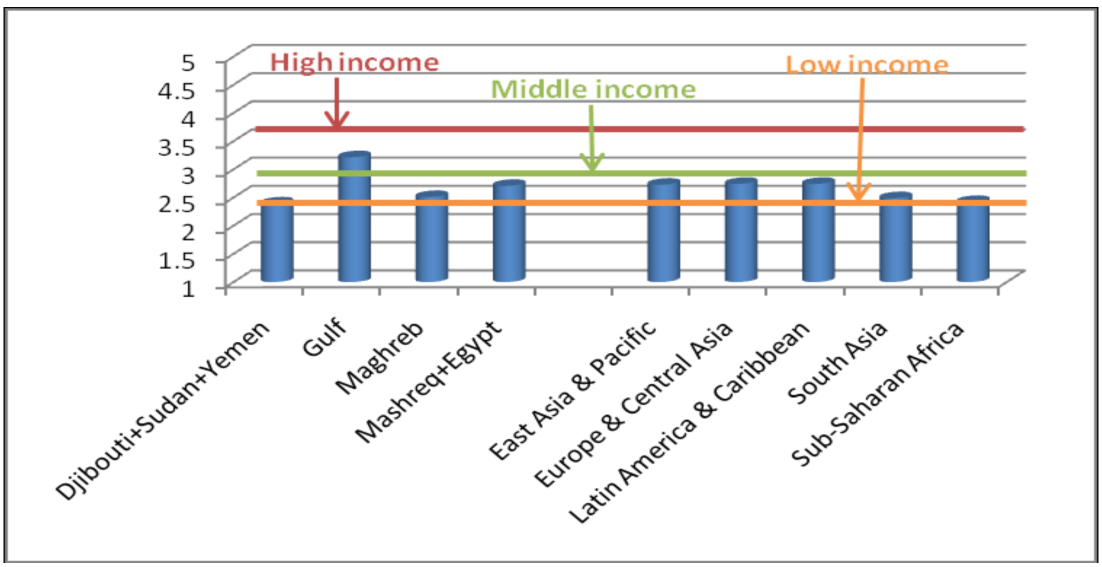
[17] The Logistics Performance Index (LPI) is based on a worldwide survey of operators on the ground (global freight forwarders and express carriers), providing feedback on the logistics "friendliness" of the countries in which they operate and those with which they trade. The methodology, surveys and data are available at http://www.worldbank.org/lpi.

Figure 9. Trading Across Arab Borders

Country	Rank	Country	Rank	Country	Rank
GCC	**52**	**Resources Rich**	**117**	**Resources Poor**	**59**
Bahrain	21	Algeria	118	Djibouti	35
Kuwait	104	Egypt, Arab Rep.	24	Jordan	74
Oman	119	Iran, Islamic Rep.	142	Lebanon	83
Qatar	36	Iraq	178	Morocco	64
Saudi Arabia	16	Syrian Arab Republic	111	Tunisia	38
United Arab Emirates	14	Yemen, Rep.	126		

Source: Doing Business (2009)

Figure 10. LPI scores in the Arab world versus other regions

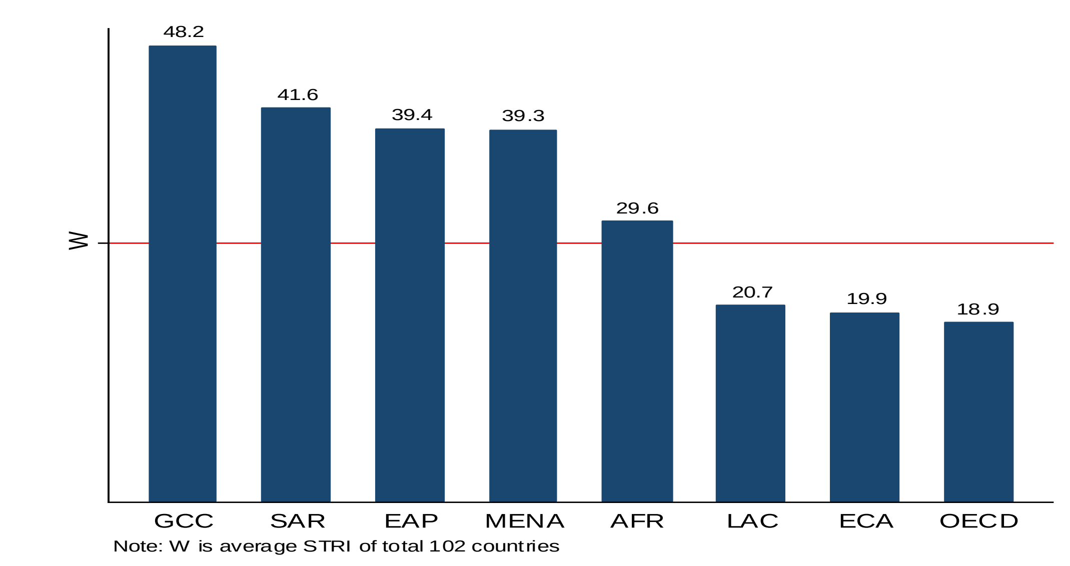


Source: LPI 2010, World Bank

2.2 Services – A largely unfinished agenda

Services trade among Arab countries remains largely unopened and unexploited. Despite the importance of the services sector and services exports for many Arab countries (e.g., tourism, transport and other commercial services), the region is characterized by its high level of services trade restrictiveness. According to the World Bank's Services Trade Restrictiveness Index (STRI), which contains detailed and comparable information on policy and regulatory measures affecting international trade in services,[18] the most restrictive policies are observed in the GCC countries such as Qatar, Kuwait, and Saudi Arabia, and in other Middle East countries, including Egypt and Tunisia (Figure 11). In contrast, policies are relatively liberal in Latin America, Eastern Europe and the OECD countries, with Sub-Saharan Africa somewhere in between the restrictive and the more liberal regions.

Figure 11. Services Trade Restrictiveness Index, by Region, 2007/08



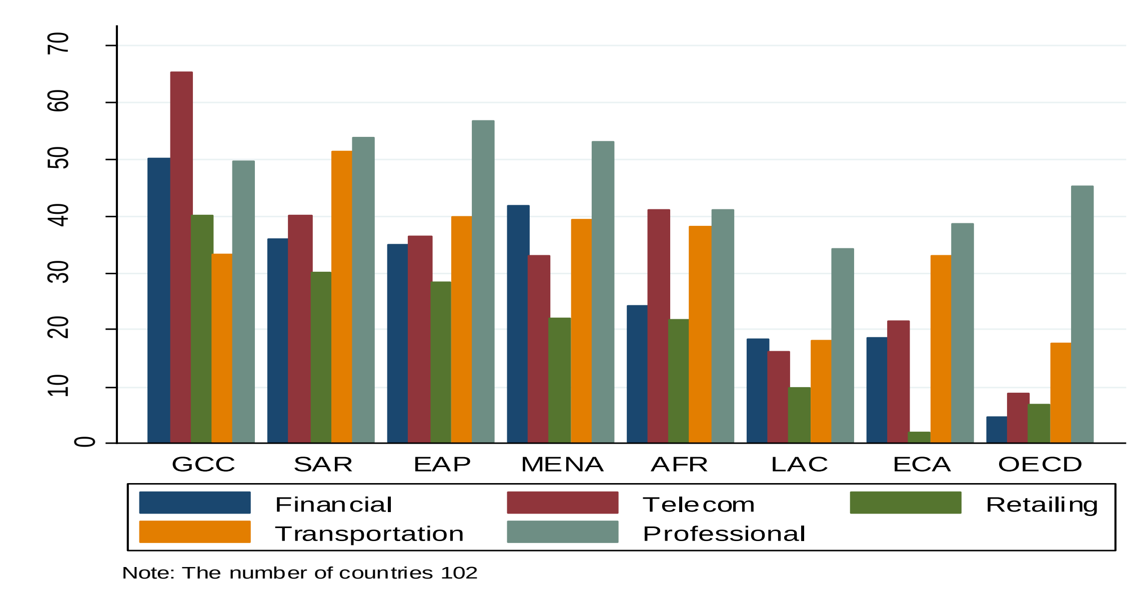
Source: Borchert, Gootiiz and Mattoo (2010)

Restrictiveness in service trade is prevalent in all major services sectors. The breakdown of the STRI by major service sector shows the highest barriers to trade in the MENA region appearing in professional services, financial services, and transport services (Figure 12). Even though the markets for most services are now more competitive worldwide, they remain far from being truly contestable in most countries. In telecommunications, governments continue to limit the number of providers and the extent of foreign ownership. In both banking and insurance, the allocation of new licenses often remains opaque and highly discretionary. In retail, a range of domestic regulations, such as pervasive zoning laws, severely impede entry in both developing and industrial countries. Transport and professional services remain a bastion of protectionism. In maritime transport, even though international shipping is today quite open, entry into cabotage and auxiliary services such as cargo handling is in many countries restricted. In air transport, most countries across all income groups restrict investment in the supply of international and domestic air passenger services. Within professional services, accounting and the practice of foreign law tend to be more open than auditing and the practice

[18] The STRI database contains information from a total of 102 countries, of which 78 are developing countries and 24 OECD countries; the country coverage represents all world regions and income levels.

of domestic law. Overall, in the sectors and modes of supply covered by the index, the restrictions on foreign investment are far less stringent than the restrictions on the supply of services by foreign professionals (Gootiiz and Mattoo 2009).

Figure 12. Restrictiveness of Services Trade Policies, by Region and Sector, 2007/08



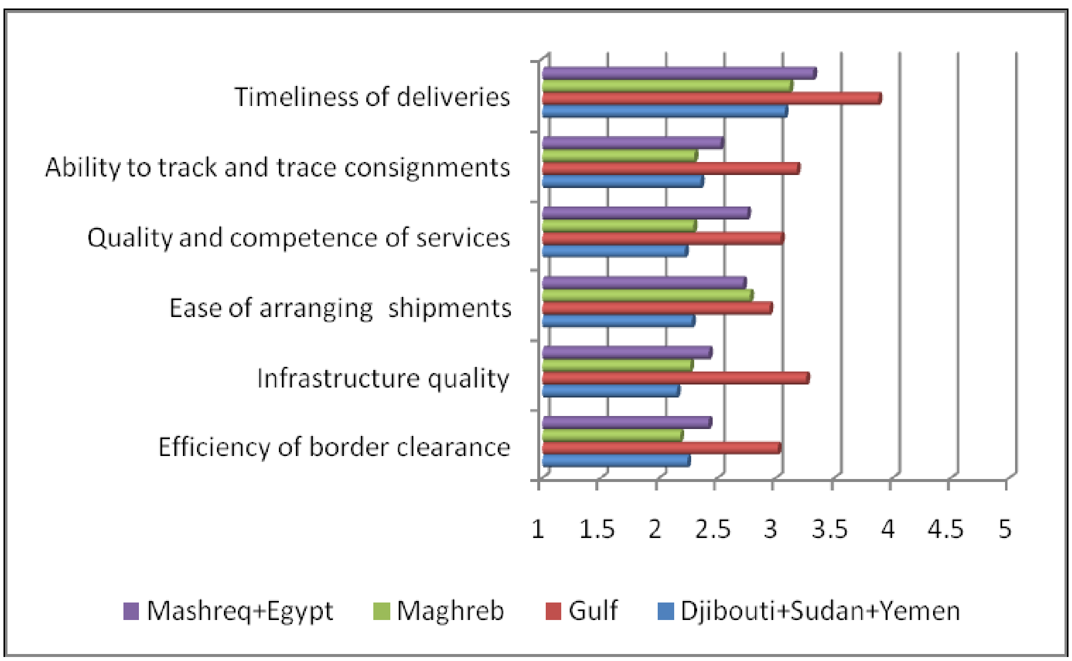
Source: World Bank and WTO QUASAR database.

In services, Arab countries have in general poor regulatory and implementation capacities, weak negotiations infrastructure, and a shortage of resources to administer trade agreements. The process may be further complicated by the fact that countries have in the past taken very different approaches to international services liberalization, as illustrated by the very diverse extent of the General Agreement on Trade in Services (GATS) liberalization commitments of the region's WTO members (Ghoneim 2011). In many instances, the extent of commitments reflects the status quo, or even less, especially for old GATT members. They have been assessed to be relatively modest and to include several restrictions on the participation of foreigners. While regional service liberalization has started in some countries (e.g., Morocco, Jordan, and to some extent new WTO acceding countries), the process is lagging behind in the region as a whole.

The Arab world has much to gain from regional services liberalization. Comprehensive services reforms that involve increased competition and regulatory streamlining would yield benefits that are two to three times the magnitude of those achieved through tariff removal alone (Konan 2003). The size of the reform benefits depends, of course, on the extent of initial openness and efficiency of the domestic services sector, the capacity of countries to cope with the adjustment needs, and the political commitment to modernization. In particular, opening services trade in the region would facilitate trade in parts and components and the emergence of regional production networks (which are expanding worldwide more rapidly than conventional trade in final goods). MENA countries have long been lagging behind in network trade and supply chains, but some Maghreb countries have been catching up in recent years (Yeats and Ng, 2000). Tunisia, in particular, has seen its share of parts and components exports almost triple over the past decade, from less than 4 percent to 10 percent of total exports. However, most of this trade is in the context of networks with Europe, rather than with partners in the MENA region.

In that context, improving the delivery of services in core logistics areas has become key to integrating global supply chains. Efficient trade logistics systems help support trade diversification and attract foreign direct investment. This is all the more important as export diversification has been difficult in the MENA region. The GCC and other resource rich countries are dependent on oil and gas for more than 80 percent of their total exports. Export growth in the Maghreb region has been at the extensive margin, with little new products being exported or new markets being conquered since 2000. With the exception of the GCC, the region's performance in the six core logistics areas tracked by the Logistics Performance Index has been weak, especially for Djibouti, Sudan, and Yemen (Figure 13).

Figure 13. Arab world sub-regions' performance in the six core logistics areas.



Source: LPI, World Bank

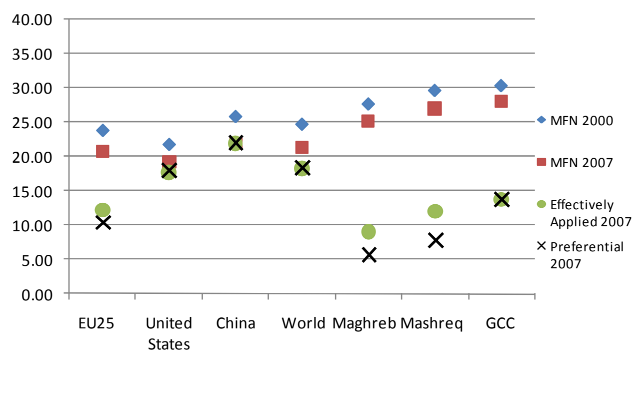
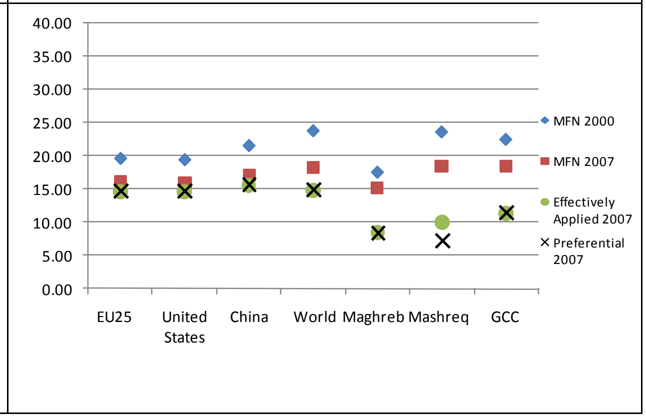
3. Proposals for a More Integrated Arab World

A more integrated Arab world does not necessarily mean a full-fledged customs union or common market; but it means a functioning free trade area for goods and services. Although Arab leaders have reiterated at their Second Arab Economic Summit in Egypt their objectives to complete an Arab Customs Union in 2015 and to launch an Arab Common Market in 2020, such grand plans may not be the most appropriate or realistic for the region. Indeed, it is not clear that the PAFTA is the most natural candidate for a customs union, especially given the preconditions to be met in terms of economic convergence and difficult decisions to be taken on the common external tariff and revenue sharing mechanism. Yet, a meaningful regional trade integration agenda would aim at (1) completing the free movement of goods within PAFTA, notably through the elimination of unnecessary non-tariff barriers; (2) launching a major regional initiative to liberalize services trade, including identifying a number of services sectors for early regional liberalization; and (3) strengthening the rules and discipline applicable to regional trade and other policies of common interest. This agenda will need to be made consistent with the PTAs that a number of Arab countries have signed with the EU, the US, and other key non-Arab trading partners.

3.1 Trade in goods

Accelerating the phasing out and convergence of the Arab world external tariffs towards those of the East Asia region would increase the region's capacity to compete. The simple average of MFN-duties in MENA countries ranges from about 5 percent in the GCC countries to more than 20 percent in a number of Maghreb and Mashreq countries (Figure 14). Virtually all countries within the region have reduced their tariffs over the past decade, and many of them to a significant extent. As a result, the MENA-wide duty average has been converging toward the world average. Yet, the spread in average tariff rates among MENA countries remains substantial, and the uneven level of import protection is an important impediment to successful intra-regional integration. Differences in tariffs imply that industries in partner countries benefit to a differing extent from policy-generated transfers, so that the costs and benefits of moving to freer trade are unevenly distributed (Fawzy 2003). Achieving agreement under these circumstances to open markets among regional partners is politically difficult. As part of the establishment of a free trade area, Arab leaders could continue to unilaterally reduce their MFN tariffs, especially tariff peaks, over 5 years. Such unilateral liberalization has proven to be a successful strategy in a number of emerging trading partners. Indeed, it is often observed that in East Asia – the region that has been most successful at harnessing trade for growth – intra-regional trade was driven not by PTAs but by unilateral trade policies and firms responding to global opportunities.

Figure 14: Tariffs of Maghreb and Mashreq for different trade partners

Maghreb	Mashreq
	

Source: TRAINS, Simple average tariff of all applied lines (MFN, preferential, and effectively applied rates).

A key policy priority to promote intra-regional trade is to reduce the incidence of NTMs in the Arab world. PAFTA-based initiatives to lower NTM-related real trade costs offer an opportunity to lower overall levels of trade restrictiveness in a way that does not generate trade diversion.[19] Regional cooperation to reduce trade costs can help stimulate both intra-regional and trade with rest of world. The policy challenge is to identify what types of policies should be given priority attention and how regional cooperation in the PAFTA context can best be used to complement national efforts to facilitate trade. In recent surveys, costs associated with administrative red tape and weaknesses in transport-related infrastructure services are ranked as the most important constraints to intra-regional trade. This suggests that from a policy perspective, efforts to reduce real trade costs deserve priority, including transportation and logistics services. Periodic monitoring and assessment of trade incentives and performance would help governments to benchmark performance and identify priority areas for action, at both the national and the sub-regional levels. These are all areas where the Secretariat, if given the mandate, can play a leading role.

Different regions of the world have taken different approaches to the streamlining of NTMs. Because countries typically have large numbers of regulations on the books, many of which with potential trade effects, streamlining them is a long and difficult undertaking. Regional trade agreements can help in several regards. Here are some examples of how other regional blocs have helped streamline NTMs. First, as in the E.U., supranational institutions—like the European Commission and the European Court of Justice—can play a leading role in fostering the elimination of NTMs, at least on intra-bloc trade, and a general streamlining and

[19] Countries with high average MFN tariffs can reduce potential trade diversion costs generated by PAFTA by reducing external levels of protection.

harmonization of regulations. Second, as in NAFTA, the agreement itself can serve as a political anchor to the reformists. That is, if the PTA enjoys strong multi-partisan backing, it can be used as a justification for domestic reforms even when they hurt particular interests (e.g. the elimination of NTMs benefitting domestic producers). Third, as in ASEAN, regional institutions can provide a useful forum to exchange experiences, to suggest directions for further moves, and to motivate reformers by overcoming their isolation at home. Finally, a guillotine approach to reviewing, streamlining, eliminating and updating regulations without the need for lengthy and costly legal action on each regulation could be adopted as in Eastern European countries during their transition.[20]

Streamlining unnecessary NTMs in PAFTA countries would aim at reducing compliance costs by avoiding unnecessary stringency; reducing red tape by streamlining procedures; and increasing predictability through better transparency. When rule-setting processes risk slipping into hidden protectionism and regulatory proliferation, governments must rely on commitment mechanisms. International or regional agreements provide that commitment. They provide a framework for distinguishing product regulations from NTMs. Several mechanisms have been put in place to limit NTM proliferation and hidden protectionism, at the multilateral level (e.g. the WTO and OECD) and at the regional level (through free-trade agreements like NAFTA or ASEAN). PAFTA could become the framework for the following concrete policy initiatives:

- **Improving transparency on the prevalence of NTMs.** NTMs are technical and diverse in nature. Because of their complexity, little is known about them, not only by private-sector operators but sometimes even within governments, as they can originate from a wide array of agencies and ministries. A number of surveys convey information on private-sector perceptions of NTMs and their effects on business, but the information is rarely reconciled with government authorities and sometimes reflects misunderstandings or inaccurate information. A first step toward streamlining NTMs is to draw up national inventories of them, based on accurate information, vetted by government authorities. Yet, because of the potential vast array of NTMs, the inventory would need to be prioritized. Given the importance given to trade facilitation in the services agenda, an initial focus could be on barriers that have broad impacts across many products such as licensing and permit requirements for importers and exporters, rules of origin and rules affecting cross-border transportation.

[20] The guillotine approach provides both a quick fix to the most critical problems of inefficient and anti-market regulations, and a permanent system for quality control of new business regulations to avoid re-occurrence of the same problems. It can be used to improve future legal security by establishing a central electronic regulatory registry with positive security.

- **Reviewing and streamlining existing NTMs.** Once inventories are available, NTMs can be reviewed and validated through workshops bringing together public and private-sector representatives. In many cases, redundant, harmful and unnecessarily complicated regulations and NTMs are easily spotted—and sometimes known by competent ministries. NTM workshops can lead naturally to the creation of permanent NTM review committees, fostering constructive dialogue between private-sector representatives and public agencies such as standard bureaus and trade, agriculture, health, and other ministries involved in the issuance of NTMs and trade-impacting regulations. On product specific barriers, to start the reform process each country could identify the most important barriers facing their exporters in regional markets with a commitment that barriers identified by partners would be removed.

- **Moving toward regional harmonization and/or mutual recognition in selected areas.** Unlike tariffs, NTMs have the potential to raise costs when they are not harmonized, because compliance with multiple standards is costly. They are thus a key area for regional cooperation. Harmonizing all product standards in PAFTA would be a difficult and perhaps unrealistic endeavor, but a sectoral approach to harmonization, targeting sectors where difficulties are moderate, has proved useful in other context (e.g., ASEAN). PAFTA meetings provide a natural forum to discuss the designation of priority sectors for harmonization.

- **Establishing good regulatory practices.** Targeting existing NTMs for streamlining is useful, but only inasmuch as they are not replaced by other harmful measures. Thus, NTM streamlining must include a dimension aimed at the flow of new regulations. In many contexts, NTM streamlining has gone in parallel with regulatory reform, including the adoption of best practices like Regulatory Impact Assessments (RIA) and the creation of regulatory oversight bodies.[21] There is substantial international evidence to draw from in order to guide national regulatory reforms aimed at improving the quality of government action in the area of regulation.

3.2 Trade in services

The potential gains from services trade in the Arab world have remained untapped. At this juncture of the PAFTA integration process, it is important for the region to reap the benefits of greater services liberalization. Services typically account for a large share of GDP and are

[21] There is no fixed scientific formula behind this acronym, but rather a list of steps—essentially asking common-sense questions—to improve the process through which NTMs are created. When fulfilled seriously, some of those requirements may involve expert studies, such as cost-benefit analysis (ensuring that the proposed measure brings more benefits than costs to society) or cost-effectiveness analysis (ensuring that the proposed measure is the least costly among feasible options).

important inputs into the production of most goods. Therefore, removing barriers to entry for both domestic and foreign firms and increasing the efficiency of services delivery promise substantial economic gains. Moreover, services liberalization in preferential arrangements, such as PAFTA, carries fewer risks of income losses than preferential merchandise trade, because lifting most common services restrictions does not cost the government revenues and thus has no trade diversion effects.

An ambitious services agenda would aim at quickly liberalizing services trade in the Arab world. The existing regional integration agreements in MENA generally do not cover services trade, or only marginally, such as through "intentions of cooperation" in certain services sectors. Intra-regional differences in regulations, restrictions on currency convertibility, and limits on the physical movement of individuals are currently creating a situation in which it is often easier for MENA countries' service providers to operate in countries outside the region (e.g., Western Europe) than within. Given the dynamic development of services exports, as well as the complementarity of net exporters of services in labor-abundant countries and net importers in resource-rich countries, significant opportunities could exist for increased regional exchange. PAFTA could become the framework for the following concrete policy initiatives:

- **Developing a regional strategy for trade in services integration.** This would include: (i) mapping a strategy for services regional integration; (ii) identifying the capacity needs required to develop a negotiating strategy and setting up the proper channels of communication with key stakeholders; and (iii) addressing regulatory capacities and weaknesses and identifying implementation bottlenecks. An initial program for 2011 could focus on training the Secretariat and member government officials in the area of trade in services.

- **Establishing "services knowledge platforms."** Many Arab countries need to strengthen regulatory institutions and identify, design and implement policies that address market failures and ensure wider access to services. The establishment of services knowledge platforms would bring together sectoral regulators, trade officials, and stakeholders to assess current policies and possible options and priorities for services policy reform and regulatory improvements (Box 2). Once beneficial reforms have been identified by governments, implementation could be assisted by the development community under an "aid for services trade" program (Hoekman and Mattoo 2011).

Box. 2 Services Knowledge Platforms

The services negotiation literature stresses that negotiators need to learn about the preferences and interests of other parties, as well as their own, and this is a process that that takes time. Negotiations invariably involve a complex process of interaction between domestic groups that result in an understanding of negotiating objectives/priorities. Learning is critical when it comes to the substance of policy rules—officials and stakeholders need to understand what the implications are of a given proposed rule and how it will impact on the economy. Matters are already complex when negotiations revolve around traditional trade policies such as tariffs and quotas. But they are an order of magnitude more complicated when it comes to services given that there is almost invariably a regulatory dimension.

There are two broad dimensions to the challenge of services reform: (i) **addressing knowledge gaps**; and (ii) **facilitating the political economy of reform**.

The establishment of a "services knowledge platform" – a forum that is aimed at fostering a substantive, evidence/analysis-based discussion of the impacts of sector-specific regulatory policies – could help build a common understanding of where there are large potential gains from opening markets to greater competition, the preconditions for realizing such gains, and options to address possible negative distributional consequences of policy reforms. Generating information on the impact and experience with reform programs that were pursued in other countries could help governments both assess prevailing policies and institutions in their own nations, and identify policy reform options.

More specifically, such a forum could fulfill a number of roles.

- First, a mechanism through which information is generated on current services activity, prices and trade flows and prevailing regulatory policies. Better information on services policies and performance would help facilitate broad based discussion on what priority sectors are and where the key regulatory problems lie.
- Second, enhance knowledge of regulatory experiences and impacts in other countries, in the process identifying alternative options/good practices through collection and sharing of information on the factors underlying successful efforts to expand trade in services and the complementary policies that can be used to address market failures and distributional concerns. Information and experiences from a range of countries can help ensure that regulations and standards that are adopted reflect local conditions and capacities for effective implementation.
- Third, by bringing together representatives of a range of countries (officials, regulators, private services suppliers) governments can discuss and learn about alternative approaches that have been pursued in practice to address the political economy constraints that may impede regulatory reform and constrain efforts to reduce barriers against foreign providers of services.

Specific modalities of operation of a knowledge platform on services policies will need to be identified. To be effective and relevant a platform must be country-focused, demand-driven, and action oriented. At the same time, the basic premise is that there is much to be learned from the experiences of countries around the world. In practice knowledge platforms may best be designed on a regional basis, linked to regional integration initiatives and regional institutions (such as the regional development banks). First steps could be to undertake a "mapping exercise" to identify existing international networks of regulators (regional or global) and related epistemic communities, and to develop pilots to test the concept, focusing either on a just a few priority sectors or clusters for a given region and on tools that can be used to assess regulatory needs and the status quo. Examples of the latter include regulatory audits and impact assessments. The various regional fora and platforms could be linked to each other – through websites; sharing of tools and databases; etc. – and be brought together annually to exchange information and results.

Source: Hoekman and Mattoo (2011)

- **Conducting a regional Regulatory Services Audit.** This would enable countries to better understand each other current regulatory regime in services and better enable them to engage in these negotiations effectively. Such an audit involves a diagnostic of what concessions (offer) could be made at low (e.g., binding status quo) or high (e.g., major reform required) costs. Frequently, lack of coordination or information-exchange within different branches or ministries of a government could serve as an impediment to realizing the constraints/concessions available in trade negotiations. A regulatory audit is an exercise that would promote better information flow between a government in identifying the status quo and strategy in services trade. This would also help assess whether negotiated agreements with third parties are less restrictive than negotiations among members within PAFTA. In the World Bank's regulatory audit for Maghreb, it was apparent that rules applicable to services trade with the EU or the US are often less restrictive than among Arab countries. This is particularly so for movements of persons and capital.

- **Negotiating a pan-Arab agreement in services.** Looking forward, the regulatory audit exercise will help to assess the areas of expeditious collaboration among PAFTA members and areas where a special work program may be required. Harnessing the knowledge of the strengths/weaknesses of their respective regulatory frameworks would also help members better design basic principles for regional liberalization. Establishing a regional database of the regulations pertaining to each services sector and country could also help regional negotiations by increasing the level of transparency and identifying the status quo and feasible results. This transparency exercise could be accompanied by training and other technical assistance to help PAFTA countries translate the collected information into negotiation positions (requests/offers).

- **Reinforcing statistical tools.** Access to reliable data on trade flows is essential to the identification of offensive/defensive trade interests and development of a broader trade strategy. In this region, it appears that some countries have not developed a data management system for trade (particularly services trade). The lack of data will impede the ability of countries to easily evaluate the current status and identify opportunities. This can be resolved by developing services trade statistical capacity. However, this process could be a more long-term approach that involves a substantial effort at data collection and data analysis. Hence, this process could take place concurrently with other activities related to services negotiations but not hinder the overall process.

To pave the way for complete services liberalization, a number of services sectors could become pilots for early regional liberalization. Key candidate sectors for such early liberalization include (1) trade facilitation & transport, given the importance of facilitating trade in key corridors and improving trade facilitation and logistics services inside the Arab region, including Customs and border agencies; (2) banking & finance, to immediately promote banking sector competition, encourage further access to credit and intra-Arab investment, and facilitate capital movement among Arab countries, including through improved information sharing and credit reporting infrastructure, and upgraded payment and securities settlement systems; and (3) information & communication, in order to enhance the competitive potentials of technology enterprises, develop legislative frameworks related to this sector, and encourage the private sector to attract investment.

- **Trade facilitation & transport**. Many opportunities for trade among Arab countries are lost because of inefficient trade facilitation processes and procedures, and to a lesser extent because of underdeveloped transport infrastructure. It has been estimated that facilitation and transport impediments impose greater losses in trade among Arab countries than formal trade tariffs and quota restrictions (Hoekman and Zarrouk 2009). In most MENA countries, trade facilitation services are under-developed. Customs brokerage and freight forwarding services are not evolving in pace with traders demands. Coordination between border agencies within countries is still in its early stages. Even the idea of "one-stop border agencies" is still largely limited to concentration of customs procedures in a single location rather than a similar concentration of all border agencies in the same location. Transit regimes are often outdated.[22] Many of the trade facilitation barriers could be reduced by technically straightforward regional solutions that are often politically and strategically difficult to implement, especially on a unilateral basis. Concluding a reciprocal or preferential regional or plurilateral agreement on trade facilitation and transport services within PAFTA could therefore help achieve a superior outcome. A comprehensive regional agreement on trade facilitation and transport services would improve the freedom of transit, streamline fees and formalities connected with importation and exportation, and strengthen the administration of trade regulations. It could in particular help (i) modernize Customs and related services; (ii) update regulation and competitiveness of logistics and transport services; (iii) upgrade transport infrastructure; and (iv) establish corridor management systems to facilitate trade in key corridors.

- **Banking & finance**. Banking sectors in the MENA region are among the biggest and deepest in the developing world. But competition among banks in the region is lower relative to other regions and has not improved in recent years (Anzoategui, Peria, and Rocha 2010). Most banking sectors in MENA operate under monopolistic competition. And GCC economies tend to be less competitive than non-oil producing countries (Murjan and Ruza 2002). The lower levels of competition are explained by the region's worse credit

[22] World Bank (2010). Regional Cross-Border Trade Facilitation and Infrastructure Study for Mashreq Countries, World Bank, mimeo. A similar study is currently being conducted for Maghreb countries.

information environment and lower market contestability. As a result, prices for banking products are relatively high, access to finance is constrained and overall bank efficiency in intermediating savings and investment is weak. Measures to promote competition in MENA should therefore focus on making banking sectors in the region more contestable and on improving information sharing and credit reporting infrastructure, increasing access to credit through reforming secured transactions, and upgrading payment and securities settlement systems. This is a reform agenda that could usefully be pursued at the regional level, where quid-pro-quo in terms of market access and national treatment could be canvassed. Also, the more competitive the MENA's banking sector become, the more stable and the less likely the landscape will be dominated by “too big to fail” financial institutions, strengthening the region’s resilience to financial shocks.

- **Information & Communication**. Information and communication technologies (ICT) is a major sector of potential economic activity, and a crucial enabler for regional competitiveness and job creation. It encompasses mobile communication services, Internet-based services, and multiple ICT development platforms, such as eGovernment services, transport management systems, or e-health services. While the MENA region has developed a well performing mobile communications sector, with some of the highest penetration rates among emerging regions, it is lagging behind in the development of the Internet market. The Arab region could greatly benefit from increased trade in software and technology services across the region and from technology-driven ICT convergence between Internet, media and communications. For instance, regional platforms for transport management systems (TMS), e-health services, geospatial referencing applications, and many other vertical software sectors are emerging as important elements in the ICT landscape of the region. In this context, ICT liberalization and harmonization on a regional scale could play a major role to boost the development of the ICT industry. This would involve (i) harmonizing regional telecommunications policy and regulation; (ii) developing ultra fast broadband; (iii) developing regional platforms for mobile apps; and (iv) supporting regional integration in the trade of IT/ITES services.

3.3 Institutional rules and discipline

There is an urgent need to reinforce regional institutions and provide the Secretariat with a stronger mandate to monitor the implementation of members’ goods liberalization commitments. Regular monitoring of implementation is important for policymakers to be able to assess the effects of the agreement. It is also a precondition for action to be taken if necessary to address specific problems concerning the operation of the agreement. Absent information of the extent of implementation it is difficult for governments to either respond to concerns on the part of consumers, workers and businesses regarding the impacts of PAFTA or to make a compelling case that PAFTA has led to greater cross-border trade among Arab states. As trade agreements are implemented and specific trade barriers are removed other constraints to trade become relatively more important. Having up-to-date information on what these constraints are is a necessary condition for policymakers to decide whether and how they might best be removed.

The Secretariat should also be given a stronger mandate to engineer and monitor the implementation of members' services liberalization commitments (Kheir-El-Din and Ghoneim 2005)**.** PAFTA could help carefully devise a services negotiations strategy that is comprehensive for the regional bloc while being specifically customized to each of the PAFTA members' needs and goals. This would require proper sequencing to manage the process of market opening and mitigate any potential downside risks. Indeed, services liberalization tends to be considerably more complicated than tariff reform. It requires coherence in services commitments, the establishment of a carefully designed regulatory system, and appropriate safeguard and enforcement mechanisms.

More broadly, the rules and discipline applicable to PAFTA to maximize the benefits of completing a free trade area should be strengthened. [23] This would involve agreeing on a new set of basic principles for the governance of PAFTA, including prohibitions of NTMs unless they fulfill a set of basics principles, such as non discrimination and necessity, effective national treatment provisions in services trade, and effective framework to guarantee the free movement of labor within the region. This would also involve creating a permanent and independent dispute settlement mechanism to oversee enforcement, including measures to ensure compliance. Such rules and discipline should be made consistent with the other treaty obligations of many Arab countries in the context of their commitments or ongoing trade negotiations with third parties, such as the Euromed agreements or prospective deep and comprehensive PTAs with the EU.

Member states and the private sector have a key complementary institutional role to play alongside the Secretariat to promote the regional agenda. Significant progress in deepening regional integration will necessarily have to be driven by the members of PAFTA. This would require establishing appropriate mechanisms to promote dialogue and information sharing both within and between members and discuss how the business community can contribute to the process of identifying and removing barriers to trade and supporting the regional integration agenda. Various options could be considered for increasing the emphasis on regional integration within government. For instances, in East Africa—an increasingly successful

[23] This would require strengthening the legal provisions of PAFTA, in particular Chapter Two on Substantive Provisions, Chapter Three on the Supervision of Agreement Implementation, and Chapter Four on Settlement of Disputes.

regional community—countries agreed to establish separate ministries of regional integration, which ensured that regional integration was given a high level of representation in the government (not just one of many sections of the Ministry of Commerce) and allowed for focused discussions and dialogue within the countries and with partners. Regional integration amongst a relatively large group of countries also raises the issue of the pace of reform and the institutional design to provide for variable geometry and allow those countries that wish to integrate faster to move at their own pace.

Finally, a key role that regional cooperation at the PAFTA level can play is to act as a focal point for policy analysis, dialogue and identification of beneficial reforms, and as a mechanism to support monitoring of progress and impacts of reforms. The services reform/integration agenda is complex, as is reform of many types of NTMs. Deciding on a common external tariff is complex as well—assuming there is a serious intent to move in that direction by a sufficiently large number of Arab countries. The next stage of a possible common market would become even more demanding in terms of institutional capacities. Adopting clear rules and discipline along the way will provide some additional insurance against the risk of reversals and setbacks.

Conclusion

Further integrating Arab countries among themselves and opening up the region to the rest of the world are two complementary avenues to improve market access, promote behind-the-border regulatory reforms, facilitate cooperation on regional public goods, foster the emergence of an "Arab factory" through regional supply chains and productions networks, and eventually create the conditions for more and better paid jobs for a growing Arab workforce. While the outcome of the current political turmoil in the Arab region remains uncertain, it could create the conditions for a big push toward greater regional and global trade integration of the Arab world. As far as regional integration is concerned, completing the PAFTA would be a good place to start. While difficult and challenging, and requiring a good dosage of flexibility and variable geometry given the parallel preferential integration of many Arab countries with the EU, the US and other important trading partners, such a regional agenda would consist in completing the free movement of goods within PAFTA, implementing a regional initiative to liberalize services trade, and strengthening the rules and discipline applicable to regional trade and other policies of common interest.

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