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FINANCIAL RESOURCES AVAILABILITY AND MANAGEMENT IN THE ESCWA REGION

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ABBREVIATIONS

GCC	Gulf Co-operation Council which includes Bahrain, Kuwait, Oman, Qatar, Saudi-Arabia and the United Arab Emirates.
Non-GCC	Other ESCWA countries which include Egypt, Iraq, Jordan, Lebanon, Syrian Arab Republic and Republic of Yemen.
IMF	International Monetary Fund.
GDP	Gross domestic product.
GNP	Gross national product.
$	United States dollar.
%	Percentage.
...	to indicate that data are not available.
--	to indicate that the figure is zero or less than half the final digit shown.
-	between years or months (i.e., 1988-1991 or March-June) to indicate the years or months covered, indicating the beginning and ending years or months.
/	between years (i.e., 1991/1992) to indicate a fiscal (financial) year.

INTRODUCTION

This study* has been prepared in implementation of activity (1.b.), titled "financial resources availability and management in the ESCWA region" of the Commission's programme of work and priorities for the biennium 1992-1993 in the area of Public Administration and Finance. The study examines and analyzes issues related to financial resources availability and management in the ESCWA region.

Following the first oil price increases in 1973/1974, ESCWA oil-exporting countries became the recipients of substantial financial resources. These resources provided the catalyst for a dramatic increase in investment and financial transfers activities by both the private and public sectors of ESCWA countries, which up til then were only peripheral participants in the flow of international financial resources.

The influx of financial resources at that scale posed many challenges to the ESCWA countries, as their still evolving financial and economic infrastructure provided only a finite degree of absorptive capacity. As a result, within a very short span of time, the ESCWA region evolved from playing only a minor role in international financial intermediation to becoming, for a brief period, the fulcrum of international financial flows.

It was in those few short years of significant current account surpluses that the initial structure of the region's investment management sector evolved. The inability of the domestic economies to absorb the financial surpluses forced investors, both public and private, to look to the international financial markets for an outlet to deploy the excess resources.

From that it was a natural step to focus on the expertise of the investment houses in the developed countries, and to entrust them with the management of the greater portion of ESCWA financial resources.

Meanwhile, a parallel development of major long-term significance was taking shape with the establishment of a domestically-owned and -controlled component of the banking system in the ESCWA surplus countries. This gave the governments (i.e., the ministries of finance and central banks), which were the recipients of the surpluses an opportunity to deploy parts of these surpluses in the banking system in the form of short-term money market deposits.

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* Parts of this study are based on a paper prepared by Dr. Osama Dabbagh who served as consultant to the Economic and Social Commission for Western Asia.

This phenomenon gave rise to a significant growth of the financial systems in individual ESCWA countries, as measured in aggregate balance sheet terms. The low absorptive capacity of ESCWA countries, and the limited stage of corporate evolution in the private sector, coupled with the inexperience of the sector in balancing the different maturities of the supply of and demand for its resources, necessitated that the major market for the redeployment of these large deposits was the interbank market in the Euromarket.

With time, and as the magnitude of the current account surpluses of the GCC-countries became more clear, and the aspirations of the governments of these countries for managing their financial resources grew, the domestic financial systems began taking steps to increase their effective involvement in the management of these surpluses.

Concomitant with this development was the rapid expansion of the GCC economies, giving rise to the boom conditions of the late 1970s and early 1980s with emphasis on developing the infrastructure. This created significant stimulation for the private sector and resulted in substantial transfers from the public to the private sector.

Starting around the mid-1980s, the ESCWA region has been experiencing a transitional period of fundamental significance with respect to the availability and management of financial resources, characterized by:

- a reduction in overall economic growth rates caused by the decline in oil revenues;
- a moderation in economic activity due to the near-completion of major infrastructural development programmes;
- a growing importance of the private sector, enabled by the significant transfers of resources from the government.

The generally low absorptive capacity of the economies of the GCC-countries, due mainly to the small size of their population and relatively limited investment outlets, enabled these countries to accumulate significant financial resources which were mostly invested in the international financial markets. However, with the increase in private sector savings, ESCWA financial markets have started as early as mid-1980s to attract part, albeit a small one, of the region's financial resources.

The hitherto shortcomings of these markets in managing ESCWA financial resources could be traced mainly to the imbalance between the supply of and demand for capital of different maturity levels. Whereas the markets are still underdeveloped and small, and the investors' liquidity preferences are high, the demand for funds is essentially of a long-term nature and therefore needs a concessional element.

Co-operation among ESCWA financial markets has been confronted, among other things, with the issue of disparities in the savings rates among member countries, and in the shortage of the types of institutions needed to transform short-term money into long-term money and effect transfer of capital between high and low savings' countries. Consequently, co-operation among ESCWA markets in this regard has not been satisfactory, especially as the way in which financial requirements are met depends to a large extent on the composition of available funds.

Despite the availability of long-term funds for aid purposes from ESCWA surplus countries to ESCWA deficit countries, most funds, including government funds, in the ESCWA region remained short-term deposits. ESCWA financial systems have not been successful in managing the process of maturity transformation of these funds. Indeed, it has been the international financial markets, partly through Arab (including ESCWA) banks and affiliated financial institutions involved in these markets, which have managed to the transformation of the region's liquidity into long-term loans in addition to having been the most important outlet for the deployment of ESCWA financial surpluses, and to their intermediation between the region's supply and demand for loanable funds. Through their strong links with ESCWA financial systems, the international financial markets have contributed to link ESCWA financial markets with each other. The strong link between ESCWA financial markets and the international financial markets is a direct reflection of the prevailing pattern of trade and economic relations among the ESCWA countries themselves, and between them and the rest of the world.

I. FINANCIAL SURPLUSES OF THE ESCWA REGION

The term ESCWA financial surpluses can be traced to the mid-1970s and early 1980s when the main ESCWA oil-exporting countries (i.e., the GCC-countries) accumulated significant funds that could not be absorbed domestically, as the level of oil production and, hence, revenues were determined by the demand on international oil markets, rather than by their own needs.

However, in addition to the diversion of resources resulting from the Iraq-Iran War and the recent Gulf crisis, the downward trend in oil revenues during the last decade led to a sharp decline in ESCWA financial resources. The existence of these resources has implied two major concerns for their holders: maintaining an adequate level for current development and ensuring for future generations needs; and, their management in the most efficient manner to secure the highest yield possible. The first concern relates to finding a balance for matching the maturities of these resources between liquidity (i.e., ready-to-use funds) and long-term investments; while the second aims at a system of portfolio management, structured to meet the objectives of the first issue.

A. Definition of ESCWA financial resources

ESCWA financial resources are viewed by some as investments, and by others as assets or holdings. The fact is that these resources differ in their structure, maturity and denomination according to the institutions and/or sectors to which they belong.

A significant portion of these resources is owned by official institutions, such as central banks and ministries of finance, which use them to support the exchange rate, or as a means to settle international obligations. Consequently, the financial resources - or more precisely holdings - of these institutions are not considered as investments per se. They are rather short- or mid-term deposits in the form of government papers, such as bonds, treasury bills and notes in the international financial markets.

Another portion of these resources represents subscriptions to international and regional financial institutions, such as the International Monetary Fund, the World Bank and the Arab Monetary Fund. Similarly, these resources can not be considered as investments.

However, during the 1970s and early 1980s, ESCWA oil-exporting countries set up special institutions for the purpose of investing their financial resources abroad. These investments were made in the form of deposits for

various terms, or in the form of public and private bonds and other financial instruments. They also took the form of direct investments in stock markets or mixed portfolios as in mutual credit funds. The investments were also made in the form of real estate and ordinary participation in industrial, commercial and services projects. The latter form is the only category which represents directly productive investments.

As concerns non-official (i.e., private sector) financial resources, these also have varied with respect to their structure, maturity and denomination. ESCWA banks and their affiliates, subsidiaries and branches abroad as well as their portfolios in foreign banks, and all types of private sector financial organizations are included in this category. The financial resources of ESCWA banks and their affiliated institutions in the international financial markets reflect normal banking business and are used either for investment or for coverage of commitments related to correspondent banking business.

The financial resources of individuals -who as independent investors are among the largest of non-official categories- constitute a significant part of investments abroad. Their investments, as the case with official investors, spans all the forms referred to above. These private resources have been transferred abroad either through proper or improper banking channels, depending on the financial and monetary legislation prevailing in the country of origin. In this context, reference is made to the significant differences in the financial and monetary systems of ESCWA countries. Countries with free systems provide lawful coverage to the transfer of funds, irrespective of the nature of the transfer. All ESCWA GCC-countries fall within this category. The other ESCWA countries, with the possible exception of Lebanon, apply financial and monetary systems with varying degrees of restrictions. Consequently, the transfer of financial resources abroad is constrained by the requlations under which the banking and financial institutions operate.

The disparity in statistical data on financial resources held by ESCWA countries abroad, be they short- or long-term, is significant. Nevertheless, this study attempts to provide a reasonable picture of these resources based on international sources in particular, but also on national ones. Considerable attention by the developed countries was given to this issue following the oil price increases in 1973/1974 and 1979/1980 and their preoccupation with recycling the surplus funds.

B. Volume of ESCWA Financial Resources

With assets of GCC-countries held in the international markets constituting the main mass of ESCWA foreign investments, it would be relatively easy to arrive at a reasonable estimate of the volume of these assets. The problem is rather associated with assets of the other ESCWA countries, as the transfer of these assets abroad has not been made through proper banking channels, owing to the restrictive banking regulations on foreign currency transfers in most of these countries.

The foreign assets of the GCC-countries could be divided into the following categories:

- official foreign exchange reserves and positions with international and regional financial institutions;

- bank deposits;

- investments in international financial markets;

- other investments, including equity participation and property.

However, information concerning these assets remains incomplete, since it is difficult to obtain reliable estimates of placements in secret banking accounts on investments in real estate and property. It is possible, nevertheless, from available information to figure out their geographic distribution and composition by major type of asset.

Table 1 shows that the volume of the region's foreign assets has not developed satisfactorily in recent years, dropping from $347.2 billion in 1987 to $231.9 billion in 1991. While the sharp drop in 1990 and 1991 could be attributed to the drawdown on these assets, mainly by the GCC-countries in the wake of the Gulf crisis, the drop in the preceding two years is attributed to the increased use of these assets to finance budget deficits.

Table 1 also shows that the annual rate of increase in foreign assets between 1983 and 1987 was about 5 percent. With interest rates in the international financial markets averaging around 8.5 percent during the same period, the recorded increase in the assets indicates an inflow rather than an outflow of capital from the region during this period.

The figures in Table 1 include official and non-official assets, i.e., reserves and non-reserves and investments. The figures also include the assets of both the private and public sectors. Consequently, by eliminating official reserves, positions with the

international financial institutions and loans to developing countries, there remains the net foreign investments of these countries, which were around $147 billion in 1991, down by $48.1 billion from their level in 1983 ($190.7 billion) and $91 billion from their peak level in 1987 ($233.6 billion).

However, it is important to bear in mind that there are differences between direct foreign investments (reflected mainly in equity shareholdings) and placements of the GCC-countries. While the former are usually long-term investments, the latter are mostly short-term. But with placements usually held abroad for extended periods, they could be regarded as long-term investments. The tendency of both types of investments to overlap makes it even more difficult to arrive at exact estimates of the total investments of GCC-countries.

Major difficulties arise concerning the estimation of the volume of foreign investments of other ESCWA countries, as most of these investments are considered to have been transferred outside the institutional system, owning to the restrictive monetary policies of most of these countries. However, a recent study dealing with this issue[1] indicates that -by considering balance of payments developments, together with figures for external debt, foreign exchange reserves and workers' remittances relating to the 15 years prior to 1988- a figure of approximately $23 billion may be considered a reasonable estimate for the volume of foreign investments of these countries at end-1988[2]. The recent Gulf crisis and the resulting financial implications for a number of these countries may have led to a decline in the volume of these investments. However, by arbitrarily assuming that the volume has not changed, foreign investments of ESCWA countries would then amount to around $165.6 billion at end-1991.

C. Portfolio Structure and Geographic Distribution of ESCWA Foreign Investments

Table 1 indicates that slightly over one-fifth of ESCWA foreign investments during the last ten years has been held in the form of direct foreign investments and real estate and property projects. The restrictions put by the developed countries on equity participation of Arab-oil

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1/ Economic and Social Commission for Western Asia, Financial Markets and Investment Promotion in the ESCWA region, E/ESCWA/DPD/1990/2.

2/ M.S. Nabulsi, Arab Foreign Investments Abroad, (Arabic), a paper presented to the conference of Union of Arab Banks, (London, 29-31 March 1988).

exporting countries during the oil-boom era partly explains the relatively low share of direct investment in total foreign investments of ESCWA countries. These countries, however, have made significant efforts to diversify the structure of their investment portfolios to minimize the risks. With no restrictions on investment in the Euromarkets, the GCC-countries have placed in these markets almost half of their foreign investments. It is worthnoting that it was these investments, most of which are short-term and ready-to-use funds, that were resorted to in 1990 and 1991 to meet the financial obligations arising from the Gulf crisis.

Most of the investments of the GCC-countries are concentrated in the developed countries. Moreover, the balance of investments outside these countries and their financial markets remains insignificant. It is worthnoting that while the share of the United States of America in total ESCWA foreign investments has been on the decline in the 1980s, namely from over 21 percent in 1983 to only 6.2 percent in 1991, the share of other developed countries, excluding the United Kingdom, increased from 30.8 percent to 39.5 percent over the same period. The deterioration in the exchange rate of the United States dollar has been a major reason for the GCC-countries to switch significant portions of their investments to other international currencies. However, the drop in the United States share of ESCWA foreign investments has not been fully compensated for by the increase in the share of other developed countries, thus indicating that ESCWA countries have switched parts of their foreign investments from developed countries to other areas, notably to the newly industrialized countries as well as to international offshore centres.

There is a marked difference between the terms "direct foreign investments" and "placements" abroad. The interpretation of the former is much more restricted and usually includes long-term investments only. It is also limited to participations or acquisitions where ownership does not exceed 10 to 15 percent of the value of the project, as regulated by most developed countries. This interpretation would significantly reduce the value of ESCWA-GCC countries' direct foreign investments. Nevertheless, there is an inclination to accept the broader interpretation of GCC investments abroad as reflected in the countries' preference for financial liquidity and short-term deposits. It follows that ESCWA short-term investments could be treated as long-term ones on account of their perpetual placement abroad. Differences in definition constitute the major reason for differences in the estimates of the value of the region's investments abroad.

Furthermore, it is necessary to differentiate between the terms "gross foreign investments" and "net foreign

investments". The first term usually refers to long-term investments, as indicated above. The second term includes the first one but deducts counter investments made by the host country in the investment-exporting country. For the GCC countries, the latter represent a small portion of the outward flow, and are mostly investments of oil companies, in addition to other investments that are generally made in banks and financial institutions.

Over 19 percent of the oil revenues of the GCC-countries between 1974 and 1990 are estimated to have been invested abroad; or the equivalent of around 17 percent of their combined gross domestic product (GDP). This compares with less than 3 percent for Japan and around 2.3 percent for the United States during the same period, where the GDP of the former was over 20 times, and that of the latter around 26 times, that of GCC-countries' GDP[3]. But whereas the accumulated foreign investments of the GCC-countries outside the ESCWA region are estimated at around $142.6 billion at end-1991, those going to other ESCWA countries are estimated to have been only around $12 billion[4]. Even with the inclusion of official financial flows[5], estimated at around $33 billion during the period from 1974 to 1991, annual financial flows[6] from the former to the latter still average less than $2.5 billion.

D. Investment Policy and Management of ESCWA Financial Resources

The gradual decline in the region's financial resources held abroad during the last few years, reconstruction requirements and the absence of plans in the GCC-countries (the main holders of these resources) for the introduction of tax systems as means of mobilization of domestic financial resources are indicators for a possible further decrease in financial resources held abroad in the coming few years, notwithstanding the fact that a number of GCC-countries are increasingly resorting to domestic as well as external borrowing instead of drawing further on their foreign investments to finance budget deficits.

3/ American Express Bank Review (AMEX REVIEW), various issues.

4/ These investments were mostly in real estate and property in Egypt and Lebanon (the latter prior to the start of civil war in 1976), and in banking and finance in Bahrain.

5/ Include Government aid, grants and loans as well as loans of national development finance institutions.

6/ Excluding workers' remittances.

The preference for liquidity and short-term deposits is not an investment policy limited to the official sector of ESCWA countries. It is also the attitutde of the private sector, especially as concerns banks and financial institutions. The foreign investments of both sectors have been denominated mostly in United States dollars, whether through investing directly in the United States or through placing funds in Euromarkets and other international financial centres[7]. However, this investment policy has undergone a major change during the last few years, prompted by the desire to diversify by transferring into other major currencies and markets, which in turn could be related to:

- the increases in risks associated with the future of the United States economy in light of the large and persistent twin deficits in the budget and trade;

- the declining significance of the Eurodollar, as reflected in the relative retreat in the market for syndicated loans and securities, as well as in the drop in the nominal interest rates of dollar-denominated financial investments;

- the increasing activities of the Far Eastern financial markets.

ESCWA investors, have generally been hesitant during most of the last two decades to acquire equity participation in the industrial, agricultural and services sectors in the developed countries, with the notable exception of investment in down-stream oil industries during the second half of the 1980s. Moreover, most of the direct foreign investments of the GCC-countries have been made either by proxy or through affiliates of institutions incorporated in the host countries. The GCC-investors had to be careful in feeling their way and to avoid the spotlights given the policy of the host countries to restrict investments purely within the limits of their interests.

An evaluation of the management of ESCWA foreign investments from the point of view of their yield is difficult, not only because information on maturities of investments is inadequate, but also because of movements in exchange rates and inflation. Hence, such an evaluation remains necessarily a matter of estimation, especially as the issue of yield may not conform with that of liquidity preference. This consideration has been of utmost

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7/ The denomination of most of the investments of the GCC-countries in United States dollar is attributed -among other things- to the fact that their oil revenues, which are the main source of their investments, and oil prices are denominated in United States dollars.

importance to the GCC-countries which were forced to draw down on their foreign investments during 1990 and 1991 to meet the financial obligations resulting from the Gulf crisis.

During the period between 1974 and 1981, when the bulk of the region's foreign investments was made, placements in the Eurodollar market appear to have delivered the highest return. The diversification of investments is seen as having resulted in significant rates of return, due mainly to the speculative nature of the market at that time. Investments have also been negatively affected by the then lower yield on bills and deposits in the money market. However, the exchange rates were favourable to the dollar-investments and the high interest rates could compensate for the effects of inflation.

The decade of the 1980s could be considered a major turning point for the region's investments in the international financial markets, regardless of the worldwide stock market crash in 1987 and the drastic fluctuations in the exchange rates of the major international currencies. Indeed, the short-term maturity of most ESCWA foreign investments has made it easy for ESCWA investors to switch swiftly form high bank liquidity risks to financial instruments of lower risks, such as bills and market equities. This policy of conversion has benefitted ESCWA investors in many ways, most important of which are the following:

- The profit from the decline of bank rates to the extent of reverting to public and private bills;

- The profit from shifting to the stock markets whenever these markets experienced a real boom. It is noteworthy that losses incurred by ESCWA investors in the 1987 stock market crash were relative as investors who entered the markets two or three years prior to the crash were still winners, considering that stock prices after the crash were still higher than what they were a year before.

- The profit from the policy of diversification at the right time, not only with respect to markets, but also currencies.

The conservative policy of managing ESCWA foreign investments was successful as long as investments had short-term maturity. The aforementioned average growth of only 5 percent annually of these investments during almost a decade, while the interest rate in the international financial markets was averaging around 8.5 percent, indicates that the management of ESCWA financial resources was less successful in the long-term.

Saudi-Arabia, has been the major investor among GCC-

countries. Its conservative investment approach with respect to maturity has established the basis for a relative stability in the country's foreign investment policies, as reflected in the Kingdom's objectives to put security and liquidity of investments ahead of yield. Saudi-Arabia has tended to profit from the depth of the United States markets, while at the same time meeting its obligations for development and foreign assistance.

Kuwait has followed an investment strategy based on giving priority to yield and diversification. Kuwait's investments were made mostly on long-term basis by holding portfolios of medium and long-term maturity bonds and stocks. In this regard, Kuwait has made investments in the equities and real estate markets to the extent allowed by restrictions imposed by developed host countries. Kuwait has also aimed at entering the oil investment markets to secure outlets for its own oil and promote down-stream diversification. To this end, Kuwait has made significant investments in international oil companies and in oil distribution and marketing.

As concerns the United Arab Emirates, its investment strategy has been a mix of that of Saudi-Arabia and Kuwait, though closer to the Saudi approach.

Table 1

Foreign Assets of GCC Countries, 1983-1991
($billion; percent)

	1983	1984	1985	1986	1987	1988	1989	1990	1991 1/
A. Geographical distribution									
United Kingdom (total)	42.8	39.8	44.2	43.2	46.4	47.3	44.2	35.3	33.2
Sterling bank deposits	3.6	3.5	4.4	4.6	5.2	4.1	3.5	2.5	32.2
Eurocurrency bank deposits	32.4	30.9	32.8	29.9	28.7	31.3	30.0	24.9	27.9
Government papers	2.5	1.7	2.1	3.0	4.1	3.8	2.8	2.6	1.6
Other assets 2/	4.1	3.8	4.9	5.5	8.4	8.1	7.9	6.0	2.3
% of total assets	14.2	13.3	13.7	12.7	13.4	14.4	13.9	13.3	14.1
United States (total)	63.7	62.6	60.3	57.6	50.2	34.5	30.6	22.5	14.6
Bank deposits	13.1	15.9	16.4	16.9	15.7	11.2	11.1	5.3	2.4
Government papers	25.7	23.4	22.3	20.8	16.2	18.1	16.2	14.1	9.3
Other assets 2/	24.9	23.3	21.6	19.9	18.1	5.2	3.3	3.1	2.9
% of total assets	21.1	21.0	18.7	16.9	14.4	10.5	9.6	8.5	6.2
Other industrial countries (total)	93.1	92.2	107.7	124.3	133.0	129.0	124.2	103.0	92.7
Domestic currency bank deposits	5.6	5.2	6.0	8.4	8.8	9.2	10.3	7.3	3.2
Eurocurrency bank deposits	35.2	35.8	38.8	34.4	35.0	36.8	31.3	24.2	19.2
Government papers	31.4	22.6	27.0	28.8	29.3	28.3	27.8	22.3	22.2
Other assets 2/	20.9	28.7	35.8	52.9	59.3	54.7	54.5	49.2	48.1
% of total assets	30.8	30.7	33.4	36.6	38.3	39.3	39.1	38.9	39.5
IMF and World Bank	26.7	23.9	26.1	29.6	30.1	32.2	33.7	33.5	30.8
Credit to non-banks	5.7	6.3	8.4	9.1	9.4	10.2	2.2	5.1	2.2
Placement with Developing countries	42.9	43.8	45.2	45.2	45.2	45.0	45.7	46.0	46.3
Banks deposits in offshore centres	27.0	31.4	29.9	31.0	32.9	30.0	27.3	19.2	12.1
Total identified assets	301.9	300.0	321.8	340.0	347.2	328.3	317.9	264.6	231.9

Table 1 (cont'd)

	1983		1984		1985		1986		1987		1988		1989		1990		1991 1/	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
B. Type of assets																		
Bank deposits	22.3	7.4	24.6	8.2	26.8	8.3	29.9	8.8	29.7	8.6	24.5	7.5	24.9	7.8	15.1	5.7	7.0	3.0
Eurocurrency deposits	67.6	22.4	66.7	22.2	71.6	22.2	64.3	18.9	63.7	18.3	68.1	20.7	61.3	19.3	48.4	18.2	47.1	20.1
Government papers	59.6	19.7	47.7	15.9	51.4	16.0	52.6	15.4	50.1	14.4	50.2	15.3	46.8	14.7	39.0	14.7	33.1	14.1
Placements with developing countries	42.9	14.2	43.8	14.6	45.2	14.0	45.2	13.3	45.2	13.0	45.0	13.7	45.7	14.4	46.0	17.4	46.3	19.7
Other assets 2/	49.4	16.5	55.8	18.6	62.3	19.4	78.3	23.0	85.8	24.7	68.0	20.8	66.0	20.8	58.3	22.0	53.3	22.7
Credit to non-banks	5.7	1.9	6.3	2.1	8.4	2.6	9.1	2.7	10.2	3.1	12.2	3.1	12.2	3.8	5.1	1.9	2.2	14.4
IMF and World Bank	26.7	8.8	23.9	8.0	26.1	8.1	29.6	8.7	30.1	8.7	32.3	9.8	33.7	10.6	33.5	12.7	33.8	5.2
Banks deposits in offshore centres	27.0	8.9	31.4	10.4	29.9	9.3	31.0	9.1	32.9	9.4	30.0	9.1	27.7	8.6	19.2	7.2	12.1	5.2
Total	301.9	100.0	300.0	100.0	321.8	100.0	340.0	100.0	347.2	100.0	328.3	100.0	317.9	100.0	264.6	100.0	234.9	100.0
Minus																		
Official foreign reserves	41.6		36.5		41.1		34.7		38.3		35.2		30.3		16.1		12.2	
IMF Bank World Bank	26.7		23.9		26.1		29.6		30.1		32.3		33.7		33.5		33.8	
Placement with LDCs	42.9		23.9		45.2		45.2		45.2		45.0		45.7		46.0		46.3	
Total foreign investment	190.7		195.8		209.4		230.5		233.6		215.8		208.2		169.0		142.6	

Source: ESCWA calculations based on: Bank of England, Quarterly Reports; various publications of the Bank for International Settlements; OECD; Morgan Guaranty Trust Company; and others

1/ Estimates.
2/ Including equities, properties and other assets.

II. OBSTACLES FACING RECYCLING ESCWA FINANCIAL RESOURCES ABROAD TO THE REGION

The first thing that comes to mind when referring to ESCWA financial resources abroad, is that the presence of these resources there has assumed a semblance of permanency. This calls for analyzing the reasons behind the "expatriation" of these resources.

The reasons behind the expatriation of ESCWA financial resources are manifold. As concerns the GCC-countries, the lack in investment outlets, reflecting the smallness of their domestic markets, and inadequate domestic financial markets, have not been helpful. With regard to other ESCWA countries, domestic economic policies and conditions have not generally been helpful in retaining private capital. Similarly, the overall situation in the region has not been conducive to the flow of investment funds between countries, especially between the surplus and deficit countries. This trend has been reinforced by interest rate differentials between ESCWA domestic markets and the international financial markets, the volatility of the exchange rates, and last but not least, the presumed risks associated with investment in the deficit member countries.

The absence of satisfactorily developed financial markets in the region is considered a major obstacle facing recycling of ESCWA financial resources held abroad to the region. Indeed, ESCWA financial markets have not been able to play any significant intermediary role between GCC-countries and other countries in the region. The generally inadequate investment environment in ESCWA non-GCC-countries, compared with that in international financial markets, the relatively underdeveloped banking and financial systems in the region and absence of innovative banking and financial techniques, have been additional obstacles facing recycling.

Furthermore, the state of ESCWA financial markets is closely linked to the state of the region's economies, and to the political and public administration systems in place. In the non-GCC countries, the effectiveness of investment promotion laws has often been obstructed by administrative regulations and legal procedures. In GCC countries, restrictions to the entry of persons and corporations of other ESCWA countries into their financial markets remain a major obstacle to the establishment of strong linkages between the financial markets of both groups of ESCWA countries, and consequently for a smooth flow of financial resources between them.

Another obstacles resides in the unfavourable investment environment in ESCWA deficit countries. A trust-inspiring political and economic environment is perhaps more important for the promotion of intraregional financial flows than the level of development of the financial markets of these countries.

It is worthnoting that "excessive" financial resources during the oil-boom era, and the assumption that this could have generated that the availability of these resources can be taken for granted, have not encouraged member countries to consider long-term financial planning to be an urgent task, neither at the national nor at the regional level.

Financial flows within the region have been further obstructed by administrative obstacles to private investments, especially in industrial projects, where bureaucratic regulations and procedures have often prevented the establishment of a competitive investment environment. Frequent changes in investment laws and amendments have confused investors and made investment costs difficult to calculate. The arbitrary application of unfavourable exchange rates to the transfer of profits and dividends, the fixing of uncompetitive prices in the domestic market for investment project outputs, and restrictions imposed on the import of necessary inputs have adversely affected the flow of financial resources within the ESCWA region.

These obstacles at the regional level, notwithstanding, ESCWA's investments abroad have not been completely risk-free. The freezing and confiscation of assets (e.g., Iraq), indicate that the regions investments abroad are not immune to this kind of political risk . These investments are also susceptible to financial risks, reflected, on the one hand, in the depreciation of the United States dollar, which is the major currency of denomination of most of these investments, and, on the other, in the fluctuation of the prices of stocks, which constitute a significant portion of the investment portfolio.

III. SPECIFICATIONS OF DEFICITS IN ESCWA NON-GCC-COUNTRIES

The economies of ESCWA non-GCC-countries are generally characterized by persistent balance of payments and budget deficits. To a considerable extent, this reflects the poor state of regional coopertation which has mitigated against taking advantage of existing and potential complementarities among member countries.

The overall balance of payments deficits of these countries have been smaller than the trade deficits, due mainly to capital inflows and transfers in the form of loans, grants, and workers' remittances. In spite of these substantial inflows, the overall balance of payments position of ESCWA non-GCC-countries remained generally weak.

The drop in official financial flows from GCC-countries and other sources after 1982 resulted in widening the budget deficits of the recipient non-GCC member countries. Both, the rise in current expenditures, and the implementation of development projects committed in previous years, have contributed to worsen the budget situation, especially as the governments of these countries were unable to improve significantly the process of domestic resources mobilization, nor could they continue to borrow externally, with the deterioration in their credit-worthiness resulting, to a considerable degree, from the budget deficits.

The difficult financial position of ESCWA-non-GCC-countries has led some of them (Egypt and Jordan) to enter into agreements with the IMF to implement economic stabilization and adjustment programmes, securing in the process direct or fund-induced financial assistance in the form of external debt-rescheduling or through direct financial assistance, especially on a bilateral basis. The external and internal imbalances from which the ESCWA non-GCC-countries suffer are likely to persist as long as the process of mobilization and allocation of domestic financial resources remains incompatible with development finance requirements, and the inflow of external financial resources, remains inadequate to fill the resource gap. It should be pointed out, that these imbalances could, to a significant extent, be related to external factors beyond the control of the countries concerned, although these factors could be compounded by domestic failures to accommodate economic development to changing exogenous influences. In this context, the ESCWA deficit countries appear to have failed to establish a proper balance between financing their deficits and adjustment of their economies, especially as the imbalances cannot be considered as self-correcting and, consequently, external financing alone is not a long-term solution. Therefore, a policy of reliance on external financing, or to that effect, propositions for recycling

foreign financial resources of GCC-countries, without viable economic adjustment programmes, could lead to a further rise in the external debt of these countries and the erosion of their credit-worthiness. The economic adjustment programmes recommended by the IMF involve a reduction in the propensity to consume by restructuring the relationship between domestic demand and supply, so as to promote exports and foreign exchange earnings and consequently the flow of foreign financial resources. The IMF approach, involving as it does a long-term perspective, implies that the ESCWA-non-GCC-countries which have entered into agreements with it should incorporate structural adjustment programmes into their long-term development process. Considerable external resources are needed in the process to supplement own efforts, including the recycling of funds.

A number of issues comes to mind in considering these policies. In particular, it is questionable whether the objectives of the countries of the region are consistent with achieving a blend of financial recycling and economic restructuring. The overriding objectives of ESCWA surplus countries is to invest their financial resources in a minimum risk portofolio of assets yielding a positive real rate of return and preserving the real value of the assets. To achieve this objective, ESCWA surplus countries have invested most of their financial resources in the international financial markets and the developed countries. Any large-scale recycling of these resources in support of economic development in ESCWA deficit countries has to surmount two main obstacles. Firstly, most of the ESCWA deficit countries do not offer investment opportunities that could satisfy the risk and return objectives of the surplus countries; and, secondly, it is difficult to reconcile the long-term nature of investments in economic development in the deficit countries with the liquidity preference of the surplus countries. What may be considered by the deficit countries as a recycling problem, is seen by the surplus countries as an investment decision. These perceptions have different implications for the mobilization, management and allocation of financial resources.

As concerns the objectives of ESCWA deficit countries, the main issue is achieving a balance between available financial resources and development requirements. The response of these countries to the drop in financial flows from GCC-countries after 1982 has been to resort to external borrowing to maintain expenditure, thus, delaying needed adjustment.

The pattern of expenditures during the oil-boom era indicates that member countries appeared at times to overlook considerations of efficiency. In both, the surplus and deficit countries, governments seem to have been quick in spending the additional direct or indirect gains from the oil revenues, sometimes on hastily conceived projects that have little relationship to real development. Consequently, there was a rapid growth in money supply and imports, whereby the former led

to high rates of inflation and the latter to some economies becoming import-distribution ones. Furthermore, following the drop in spillovers from GCC-countries, the ESCWA non-GCC-countries leaned increasingly towards external borrowing to maintain spending levels; the end effect has been that the oil-boom era left some of them in a weaker financial position than they were in at the beginning.

IV. FINANCIAL RESOURCES NEEDS OF THE ESCWA REGION

Economic development in the ESCWA region during the last decade was confronted with various challenges, most important among which was the availability of development finance, especially in non-GCC- countries, structural imbalances and vulnerability to external developments. The ESCWA countries suffer from the lack of adequate and efficient channels through which savings could be mobilized and allocated for productive investments. Although the GCC-countries have accumulated significant financial resources abroad to which they could resort to finance development, as well as budget deficits, their aggregate domestic savings/GDP ratios have declined sharply over the 1980s, (Table 2). This unfavourable tend reflects the trend in overall income, including the return on investments abroad.

Table 2 shows that the resource balance of the ESCWA region as a whole was unfavourable during most of the last decade, especially in post-1982, following the start of the recession in the region, with investments exceeding savings by a peak of 9.3 percent in 1986, when oil prices and consequently oil revenues-the major source of savings in the GCC-countries -were lowest. Several factors have led to this development, including excessive reliance on the oil sector, the inability of the financial systems to generate savings, and maintenance of high levels of government expenditures resulting from previous commitments.

The savings-investment relationship in the GCC-countries deteriorated sharply as a result of the Gulf crisis . The significantly reduced savings efforts in these countries in 1990 resulted in an unprecedented negative resource balance ratio of 16.3 percent.

The unfavourable trend in the resource balance of the ESCWA region during the 1980s is projected to continue into the 1990s (Table 3). This will be the result of increased reconstruction and development expenditures, coupled with relatively lower oil revenues and return on foreign investments.

Table 3 shows a widening of the savings/investment gap during the next four years up to 1995 which is projected to rise from $1.9 billion in 1992 to $2.4 billion in 1995 for ESCWA GCC-countries, and from $13.4 billion to $16.5 billion for other ESCWA countries. The figures in the Table 2 imply that by 1995 total ESCWA savings would amount to 17.5 percent of GDP, compared with an investment/GDP ratio of 22.9 percent. For the ESCWA region as a whole, the gap will rise from $15.3 billion in 1992 to $18.7 billion in 1995. With savings insufficient to finance investments, the ESCWA countries, especially non-GCC-countries, would have to look for financial resources to fill the gap, most probably through external borrowing. For the GCC-countries, there would be pressure to draw on their financial resources abroad to fill the gap.

Table 2

Ratios of Savings, Investment and Resource Balance, 1980-1990
(percentage of GDP)

Country group	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
GCC-countries											
- savings ratio	57.1	53.8	41.1	32.4	30.6	24.3	17.1	20.8	18.4	28.2	2.3
- investment ratio	21.2	25.2	24.0	29.6	28.9	26.3	23.0	20.2	20.7	24.2	18.6
- resource balance ratio	35.9	28.8	17.1	2.8	1.7	(2.0)	(5.9)	0.6	(2.3)	4.0	(16.3)
Diversified economies1/											
- savings ratio	16.1	8.2	10.7	10.1	11.2	9.9	10.2	15.9	18.2	21.0	11.5
- investment ratio	29.2	25.6	23.1	23.9	23.6	24.4	23.7	23.1	24.3	24.6	16.2
- resource balance ratio	(13.1)	(17.4)	(12.4)	(13.8)	(12.4)	(14.5)	(13.5)	(7.2)	(6.1)	(3.6)	(4.7)
Least developed countries2/											
- savings ratio	(19.9)	(23.8)	(23.2)	(23.7)	(16.3)	(15.5)	(11.5)	(20.2)	(10.4)	(5.9)	(2.6)
- investment ratio	29.2	25.6	23.1	23.9	23.6	24.4	23.7	16.8	16.7	16.7	16.4
- resource balance ratio	(59.8)	(59.7)	(55.5)	(48.7)	(40.4)	(36.8)	(29.0)	(37.01)	(27.1)	(22.7)	(19.0)
Total ESCWA countries1/											
- savings ratio	48.5	43.8	33.6	25.8	24.7	19.4	14.3	17.7	17.5	24.3	18.6
- investment ratio	22.9	25.3	24.3	28.1	27.5	25.7	23.6	21.4	22.1	24.1	21.3
- resource balance ratio	25.6	18.5	9.3	(2.3)	(2.8)	(6.3)	(9.3)	(3.7)	(4.6)	0.2	(2.7)

Source: ESCWA, Survey of Economic and Social Developments in the ESCWA Region (various issues).

1/ Excluding Iraq and Lebanon, owing to lack of data.
2/ Up to 1988, including the former two regions of the Republic of Yemen, namely Democratic Yemen and Yemen. 1989 and 1990, for the Republic of Yemen.

Table 3

Projections of GDP, Investments, Savings and Savings Gaps in the ESCWA Region*/, 1992-1995, at constant 1980 price
($billion)

	1992	1993	1994	1995
GCC-Countries				
- GDP	196.7	210.4	225.2	240.9
- Investments	45.0	48.2	51.6	55.2
- Savings	43.1	46.1	49.3	52.8
- Savings/investment gap	(1.9)	(2.1)	(2.3)	(2.4)
Other ESCWA Countries				
- GDP	88.6	94.8	101.5	108.6
- Investments	20.3	21.7	23.3	24.9
- Savings	6.9	7.4	7.7	8.4
- Savings/investment gap	(1.4)	(14.3)	(15.6)	(16.5)
Total ESCWA				
- GDP	285.3	305.3	326.7	349.5
- Investments	65.3	69.9	74.9	80.1
- Savings	50.0	53.5	57.0	61.2
- Savings/investment gap	(15.3)	(16.4)	(17.9)	(18.7)

Source: Calculation based on national and international sources.

* Excluding Iraq and Lebanon, owing to lack of data.

Note: The projections are based on the capital /output ratio which is the lower, the higher the level of the development stage, and vice-versa, and is an integral part of the acceleration model (the Harrod- Domar growth model) for the estimation of the equilibrium levels of capital (investment) required at different levels of changing output). According to the model, the required financial resources for investment for a given capital/output ratio can be specified as follows.

$$I_t = \Delta K = B\ (Y_t - Y_{t-I}),$$

where I_t is the net required investments in period t, Δ K is the change in equilibrium capital stock, Y_t is he gross domestic product in period t, and B is the capital output/ratio.

The resutls in this Table are based on the 7 percent growth rate target of the International Development Strategy for the developing countries, and the assumption of a capital/output ratio of 3.5 percent.

V. FINANCIAL FLOWS BETWEEN ESCWA SURPLUS AND ESCWA DEFICIT COUNTRIES

The oil-boom era extended from 1973 to 1981. Its effects on the ESCWA region were manifold. Most notable among these was the flow of financial resources from the GCC-countries (surplus countries) to non-GCC-countries (deficit countries), on a scale unprecedented before. These transfers assumed two distinct forms:

- Workers' remittances

- Official financial assistance through national and regional development finance institutions, but essentially bilateral.

Economic activity in the non-GCC-countries became increasingly dependent on workers' remittances since the mid-1970s. These remittances, together with other forms of transfers, from the GCC-countries rendered fiscal and monetary management in non-GCC-countries less pressing, in the expectation of the continuation of these transfers from the GCC-countries, and thus adversely affecting the process of domestic financial resources mobilization and allocation. Although workers' remittances reflected a positive interaction between the two groups of countries, they remained essentially the outcome of a spontaneous or voluntary process.

Workers' remittances to ESCWA non-GCC-countries increased from just $238 million in 1973 to over $5.5 billion in 1989, totalling $69 billion for the whole period (Table 4). Remittances of Egyptian workers constituted around 55 percent of the total. The remittances accruing to the remaining countries increased from $115 million in 1973 to an average of $2.8 billion during the 1980s. Excluding Egypt, Jordan and Yemen received each around one-third. The ousting of Jordanians and Yemenies from the GCC-countries in the wake of the Gulf crisis affected considerably the level of remittances to both countries. Recent official Jordanian estimates indicate that remittances of Jordanians working in the GCC-countries have dropped in early 1992 to less than a third of their level in 1989[8].

In terms of GDP (Table 5), workers' remittances were highest for the former Democratic Yemen with a cumulative ratio of 34.9 percent between 1973 and 1989, followed by Jordan (20.3 percent), former Yemen (18.0 percent), Egypt (10.8 percent) and the Syrian Arab Republic (2.2 percent).

8/ Central Bank of Jordan, Monthly Statistical Bulletin, July 1992.

Table 4

Workers' Remittances to ESCWA Non-GCC-Countries*, 1973-1989
($ million)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	Total
Democratic Yemen	33	43	59	119	181	255	312	347	405	470	486	499	426	293	303	253	172	4656
Egypt	123	310	455	755	928	1773	2213	2696	2181	2439	3666	3963	3212	2506	3604	3770	4254	38848
Jordan	45	75	467	390	424	455	512	640	875	905	909	983	786	937	754	740	536	10142
Syrian Arab Republic	37	45	52	53	92	94	112	773	436	411	387	321	350	323	334	360	355	4535
Yemen	--	136	272	677	950	877	893	1024	741	866	1030	946	725	501	672	298	230	10838

Source: IMF, Financial Assistance from Arab Countries an Arab Regional Institutions, occasional paper 87, (September 1991), p. 81.

* Excluding Lebanon, owing to lack of data.

Table 5

Ratio of Workers' Remittances in GDP of ESCWA Non-GCC-countries*, 1973-1989
(Percent)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	Cumulative
Democratic Yemen	11.9	12.9	19.0	28.9	33.4	41.0	42.2	42.8	44.5	47.0	45.9	44.4	40.5	32.2	32.2	23.3	13.9	34.9
Egypt	1.3	3.5	4.1	5.8	6.5	12.5	13.0	12.6	10.0	10.2	14.0	13.9	10.2	7.9	11.0	14.0	15.1	10.8
Jordan	6.6	9.5	16.3	29.5	26.8	21.9	20.6	19.5	24.6	24.0	23.4	26.5	20.4	21.2	16.2	16.8	12.4	20.3
Syrian Arab Republic	1.0	0.9	0.8	0.7	1.2	1.0	1.0	5.9	3.1	2.7	2.7	2.0	2.1	1.7	1.4	1.8	--	2.2
Yemen	--	18.0	28.9	54.6	58.1	35.7	29.0	28.9	18.9	17.1	19.5	16.4	14.3	10.6	13.8	5.6	3.8	18.0

Source: IMF, Financial Assistance from Arab Countries an Arab Regional Institutions, occasional paper 87, (September 1991), p. 84.

* Excluding Lebanon, owing to lack of data.

In the aggregate, workers' remittances were equivalent to around 33 percent of imports of ESCWA non-GCC-countries between 1973 and 1989 (Table 6), with the highest ratio (54.6 percent) being in former Yemen, followed by former Democratic Yemen (38.2 percent), Jordan (29.2 percent), Egypt (32.5 percent), and the Syrian Arab Republic (9.1 percent).

Workers' remittances have also played a significant role in financing investments in non-GCC countries. For example, in the former Yemen, workers' remittances exceeded investments in many years. In Jordan, workers' remittances amounted to over 60 percent of investments between 1973 and 1989. The cumulative ratio for Egypt was over 43 percent during the same period (Table 7).

Official financial assistance from the GCC-countries and affiliated development finance institutions to other ESCWA countries amounted to about $36.3 billion between 1973 and 1989 (Table 8). The cumulative share of the Syrian Arab Republic in these flows was around one-third of the total ($12.3 billion), followed by Egypt ($9.4 billion), Jordan ($8.9 billion) and the former two Yemens with a combined share of around $4 billion.

The end of the oil-boom era in 1982 marked the start of declining official financial assistance of the GCC-countries to other ESCWA countries. Official financial assistance reached a low $360 million in 1989, compared to a peak of around $3.5 billion in 1979. The low level of official assistance in 1988 and 1989 reflected essentially the cessation of the general financial support programme to Jordan and the Syrian Arab Republic pledged by the Arab Summit in Baghdad in 1978 and repayments of earlier loans.

Official financial assistance extended by the GCC-countries constituted around 5.9 percent of the cumulative GNP of ESCWA recipient countries between 1973 and 1989 (Table 9). The ratio was highest in Jordan (17.8 percent), followed by fromer Democratic Yemen (7.2 percent), and the Syrian Arab Republic (6 percent).

In terms of imports, total official assistance represented on average 12 percent between 1973-1989 (Table 10). The highest level of import cover was for Jordan fluctuating between a high of 61.2 percent in 1979 and a low of 6 percent in 1989, and attaining a cumulative ratio of 25.5 percent followed by the Syrian Arab Republic with a cumulative ratio of 24.8 percent and the former Yemen (14.8 percent).

Official financial assistance originating in the GCC-countries played also a significant role in financing investments in ESCWA non-GCC-countries. Table 11 indicates that the highest cumulative assistance/investment ratio was for Jordan (53.1 percent), followed by the former Yemen (27.0 percent) and the Syrian Arab Republic (23.6 percent). Egypt enjoyed relatively high ratios between 1973 and 1978, dropping to low or even negative ratios in the following years, as a result of Egypt signing the Camp David accords with Israel and the cessation of official assistance from the GCC-countries.

Table 6

Ratio of Workers' Remittances to Imports in ESCWA Non-GCC-Countries*, 1973-1989
(Percent)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	Cumulative
Democratic Yemen	19.2	10.6	18.8	35.6	33.2	44.3	33.7	22.8	28.5	54.6	57.8	56.2	57.6	60.5	45.4	34.4	22.4	37.4
Egypt	13.6	13.2	12.1	19.8	19.3	26.4	57.7	55.5	24.7	26.9	35.7	36.8	32.2	21.8	30.2	43.5	57.2	31.0
Jordan	13.6	15.4	22.8	38.8	30.7	30.2	26.5	26.6	27.6	27.9	29.9	35.3	28.8	38.5	27.8	27.1	25.2	27.8
Syrian Arab Republic	6.0	3.6	3.1	2.2	3.4	3.8	3.4	18.8	8.7	10.2	8.5	7.8	8.8	11.8	13.4	16.1	16.9	8.6
Yemen	--	71.3	92.1	163.8	91.4	68.3	59.9	55.3	42.1	59.9	64.7	60.7	55.8	43.3	51.3	20.0	15.8	59.6
Cumulative (1973-1989)																		32.9

Source: IMF, Financial Assistance from Arab Countries an Arab Regional Institutions, occasional paper 87, (September 1991), p. 85.

* Excluding Lebanon, owing to lack of data.

Table 7

Ratio of Workers' Remittances to Investments of ESCWA Non-GCC-Countries*, 1973-1989
(Percent)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	Cumulative
Egypt	10.7	18.9	13.3	20.2	19.8	26.3	41.8	46.5	35.4	37.0	47.6	49.1	57.5	43.7	68.0	64.3	71.2	43.4
Jordan	31.2	38.3	60.4	93.9	69.5	60.6	53.1	48.0	51.1	53.4	60.2	71.2	68.0	77.4	62.0	66.3	54.1	60.7
Syrian Arab Republic	8.7	5.3	3.7	2.6	3.8	4.1	4.3	21.5	11.2	9.9	8.8	7.1	6.9	5.4	5.6	13.9	--	8.0
Yemen	--	105.5	160.3	206.3	137.2	90.0	83.5	85.5	57.2	69.3	107.3	115.0	117.4	97.8	112.2	--	--	96.4

Source: IMF, Financial Assistance from Arab Countries an Arab Regional Institutions, occasional paper 87, (September 1991), p. 86.

* Excluding Democratic Yemen and Lebanon, owing to lack of data.

Table 8

Net Disbursements of Total Official Financial Assistance from ESCWA GCC Countries to ESCWA Non-GCC-Countries*, 1973-1989
($ million)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	Total
Democratic Yemen	12	31	47	147	120	59	34	74	35	141	37	60	52	1	44	28	35	955
Egypt	700	1292	2526	1549	1636	1404	211	2	-23	-20	-68	-27	-27	54	56	8	83	9364
Iraq	4	-2	28	-1	-2	16	-2	-2	0	298	201	44	60	37	0	16	35	730
Jordan	94	212	297	427	274	344	1201	1165	1042	759	713	639	468	465	381	264	129	8870
Syrian Arab Republic	290	573	657	482	755	753	1768	1579	1376	835	733	611	599	667	601	17	20	12317
Yemen	19	96	149	212	210	259	189	369	346	259	236	204	160	110	173	16	20	2927
Total	1121	2338	3717	2824	3050	2990	3466	3386	3152	2355	1866	1530	1323	1335	1173	360	360	36316

Source: IMF, Financial Assistance from Arab Countries an Arab Regional Institutions, occasional paper 87, (September 1991), p. 72.

* Excluding Lebanon, owing to lack of data.

Table 9

Ratio of Total Official Financial Assistance from GCC-Countries, in the GNP of ESCWA non-GCC-Countries, 1973-1989
(Percent)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	Cumulative
Democaratic Yemen	4.3	9.2	15.2	35.6	22.2	6.5	4.6	9.1	3.9	14.1	3.5	5.3	4.9	0.1	4.7	2.6	2.8	7.2
Egypt	7.4	14.5	22.6	11.9	11.5	9.9	1.2	0.0	-0.1	-0.1	-0.3	-0.1	0.1	0.2	0.2	0.0	0.3	2.6
Iraq	0.1	0.0	0.2	0.0	0.0	0.1	0.1	0.0	0.0	0.0	0.7	0.5	0.1	0.1	0.1	0.0	0.1	0.1
Jordan	13.8	26.8	28.9	32.2	17.3	16.6	47.5	35.5	29.3	20.1	18.4	17.2	12.1	10.5	8.2	6.0	3.0	17.8
Lebanon	0.1	3.9	0.3	0.5	2.1	5.2	1.9	4.9	9.6	3.1	0.3	0.0	0.6	0.1	0.8	--	--	2.5
Syrian Arab Republic	8.9	11.0	9.6	6.3	9.8	8.1	16.1	12.1	9.7	5.6	4.6	3.8	3.6	3.5	2.5	0.1	--	6.0
Yemen	3.2	12.8	15.9	17.1	12.8	10.6	6.1	10.4	8.8	5.3	4.5	3.5	3.2	2.3	1.5	0.3	0.3	4.9
Cumulative (1973-1989)																		5.9

Source: IMF, Financial Assistance from Arab Countries an Arab Regional Institutions, occasional paper 87, (September 1991), p. 81.

Table 10

Ratio of Total Official Financial Assistance from GCC-Countries in Imports of ESCWA non-GCC-Countries, 1973-1989
(Percent)

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	Cumulative
Democaratic Yemen	6.9	7.5	15.1	43.9	22.0	10.2	3.7	4.8	2.5	16.4	4.4	6.7	7.0	0.3	6.6	3.8	4.5	7.8
Egypt	77.3	55.0	67.3	40.7	34.0	20.9	5.5	0.0	-0.3	-0.2	-0.7	-0.3	-0.3	0.5	0.5	0.1	1.0	7.8
Iraq	0.5	0.1	0.7	0.0	0.0	0.4	0.0	0.0	0.0	1.4	1.7	0.4	0.6	0.4	0.0	0.2	0.3	0.5
Jordan	28.3	43.4	40.5	42.5	19.8	22.9	61.2	48.5	32.9	23.4	23.5	22.9	17.1	19.1	14.0	9.6	6.1	25.5
Lebanon	0.1	5.8	0.6	1.3	3.7	8.1	2.4	5.4	10.8	2.5	0.4	0.0	0.5	0.1	1.0	0.5	0.2	2.8
Syrian Arab Republic	47.4	46.8	39.0	20.2	28.2	30.6	53.1	38.3	27.3	20.8	16.1	14.8	15.1	24.4	24.2	0.8	0.9	24.8
Yemen	15.4	50.7	50.8	51.3	20.1	20.2	12.7	19.9	19.7	17.1	14.8	13.1	12.3	9.5	5.5	1.1	1.4	14.8

Source: IMF, Financial Assistance from Arab Countries an Arab Regional Institutions, occasional paper 87, (September 1991), p. 87.

Table 11

Ratio of Total Official Financial Assistance from GCC-Countries in Investment of ESCWA Non-GCC-Countries*, 1973-1989

	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	Cumulative
Egypt	60.2	78.6	74.0	41.5	34.8	20.8	4.0	0.0	-0.4	-0.3	-0.9	-0.3	-0.5	0.9	1.2	0.1	1.4	10.5
Iraq	0.4	0.1	0.8	0.0	0.0	0.2	0.0	0.0	0.0	1.6	1.3	0.3	0.5	0.4	0.0	0.2	--	0.5
Jordan	65.0	107.7	107.6	102.6	44.8	45.9	122.4	87.3	60.9	44.8	47.2	46.2	40.4	38.4	31.3	23.6	13.0	53.1
Lebanon	0.4	--	--	2.7	10.1	28.0	10.5	31.0	46.7	33.3	22.1	--	--	--	--	--	--	--
Syrian Arab Republic	68.0	69.7	47.2	23.9	30.9	33.3	68.1	43.9	35.4	20.2	16.6	13.4	11.9	11.2	10.1	0.7	--	23.6
Yemen	22.7	75.1	88.2	64.6	30.2	26.6	17.6	30.8	26.7	20.8	24.6	24.8	25.9	21.5	12.1	-	--	27.0

Source: IMF, Financial Assistance from Arab Countries an Arab Regional Institutions, occasional paper 87, (September 1991), p. 83.

* Excluding Democratic Yemen, owing to lack of data.

VI. ROLE OF FINANCIAL MARKETS IN MANAGING FINANCIAL RESOURCES[9]

Financial markets play a major role in mobilizing and allocating financial resources. In order to play this role effectively, several preconditions should be met, most important among which are free entry into the markets and rates of return that reflect the real cost of capital. Furthermore, the level of development of financial markets as reflected in the extent of their width and depth is another precondition that determines the ability of the markets to perform assigned functions in the process of mobilization and allocation of financial resources. The existence of monopoly positions and/or inappropriate official measures and policies would result in fragmented and inefficient financial markets, and hence, disorderly organized mobilization and allocation of financial resources.

In brief, efficient financial markets could benefit the economy by:

- raising the volume of savings;
- improving the process of allocation of financial resources; and
- increasing the volume of investment.

An efficient financial market could stimulate a higher propensity to save in so far as it can, firstly, improve the opportunities for gaining access to credit and, consequently, for investments by productive units, and secondly, increase the rates of return on financial assets.

Furthermore, a diversified structure of financial assets must be created that caters to the various needs of the potential investors and financial investments outlets must absorb an increasing volume of real productive resources if they are to have a positive effect on growth and development. In addition, these investments are expected to respond positively to the following propositions: Whether the combination of their features make them as attractive as or more attractive than any "new" financial assets; whether there was a propensity for savers to invest in financial investments with these features, and if this were the case, whether such investments would induce savers to reduce their spending on consumption in order to invest more of their income therein.

In view of the above, it can be said that the development of a financial market will lead to an increase in aggregate savings at the same time that it improves the opportunities for productive investments and, hence, absorptive capacity.

9/ Based in part on an earlier ESCWA study: Financial Markets and Investment Promotion in the ESCWA region, E/ESCWA/DPD/1990/2.

In a number of ESCWA countries, where financial markets are still at an embryonic stage, and where other financial intermediaries do not exist, commercial banks are generally the only medium for mobilizing private savings. In some ESCWA countries, the problem is not one of shortage of savings, but of converting such savings into productive investment.

There are four principal ways in which a financial market could evolve:

1. The financial market may remain self-sufficient, serving domestic savers and borrowers.

2. The financial market may continue to be self-sufficient with regard to the supply of funds, but seeks outward growth beyond national boundaries in so far as the use of funds is concerned.

3. The financial market may encounter heavy demand for funds without being able to satisfy this demand from internally generated funds,in which case the market is characterized by an inflow of funds from abroad.

4. The financial market may grow drawing on external funds and meeting external demands.

The Syrian Arab Republic, Iraq and the Republic of Yemen can be cited as countries where financial markets can be developed on the basis of self-sufficiency, although the centrally-planned nature of the economy of the first two countries is not conducive to the development of such a market.

Kuwait's financial market is an example of the second type, with similar potential in the case of Saudi-Arabia and the United Arab Emirates.

The financial markets of Egypt, Jordan and Oman are examples of the third type, while Bahrain's financial market represents the fourth.

However, the nature of the portfolio structure of domestic financial institutions and individuals in GCC-countries has provided for limited use of investment capital available. From the standpoint of financial intermediation, the paucity of financial instruments for investment purposes and the limited participation in capital accumulation have resulted in reduced efficiency of capital available in the market, and, hence reduced capital mobility and flexibility.

Moreover, the ESCWA financial markets have not expanded beyond national boundaries, being constrained by legal, administrative and monetary frameworks and policies.

The financial markets of GCC-countries have been restrictive with regard to access of non-nationals and to registration of non-domestically incorporated companies, as well as public

placing of foreign financial investments, but have been generally liberal as concerns the outflow of capital. In contrast, the financial markets of ESCWA non-GCC-countries have been restrictive with regard to the outflow of capital, but liberal as concerns capital inflow. While the restrictions in GCC-countries have been attributed to government policy in reserving the limited domestic investment outlets to its own citizens, those in ESCWA non-GCC-countries have been justified on the ground that these countries are net capital importers.

In addition, the flow of financial resources between ESCWA financial markets and, hence, their integration, continues to face other obstacles, including:

1. The underdeveloped legal, organizational and institutional infrastructure of the financial markets. In contrast to the organizational aspects of the primary markets, which have developed relatively satisfactorily over the past years, the legal framework has not. Evidence of this is seen in the frequent changes in the legal provisions. With regard to the secondary markets, these are either partially or barely organized. Administrative rather than legal regulations and procedures determine the business being processed in these markets, thus leaving those dealing in them legally unprotected. The small investor, in particular, is at the mercy of arbitrary price fluctuations caused mainly by speculation.

2. The narrowness and lack of depth of the financial markets. The number of financial instruments traded in most ESCWA financial markets is very limited. In some of these markets, these instruments are limited to the shares of public shareholding companies. An indication of the lack of depth of the markets is that any change in the volume of business, regardless of size, can cause a fluctuation in market prices.

3. The lack of developed market intermediaries and techniques. In the majority of ESCWA financial markets, financial institutions do not meet expectations as to their role as intermediaries between investors and borrowers. Aside from issues intermediated and managed during the late 1970s and early 1980s, mainly as a result of the liquidity available at that time, most of the new issues made since then could not be satisfactorily placed in the market, mainly owing to inefficient methods of offering subscriptions and marketing issues. In addition, the unattractiveness of new issues failed to attract ESCWA financial surpluses abroad to the region, nor have they succeeded in reducing the outflow of private capital from the region. Furthermore, the low capital base of most financial intermediaries fails to reassure investors of their ability to guarantee the new issue in full.

VII. MOBILIZATION, MANAGEMENT AND ALLOCATION OF FINANCIAL RESOURCES

A. The Role of Fiscal Policy

A formulation of fiscal policy to achieve a proper management of financial resources in the ESCWA region ought to start with a clear identification and recognition of the institutional aspects of government finance, such as the prevailing tax system and incidence, budget formulation and execution, and national financial management objectives. The focus on fiscal budgeting, as a tool of financial management, is on the attainment of efficiency in the mobilization, management and allocation of financial resources and is influenced, at any stage of development, by the national objectives of economic development.

In the ESCWA region, the role of the public sector in the implementation of major development projects and in influencing the flow of financial resources is essential. The availability of financial resources in GCC-countries has made planning and management of fiscal policy a less pressing issue. Consequently, the usually urgent issue of mobilization, management and allocation of financial resources among the different sectors of the economy through adequate fiscal (and monetary) policies has not been given priority. In addition, abundant financial resources in these countries made it unnecessary for them to make use of the tax system as a vehicle for mobilizing domestic financial resources.

In the ESCWA non-GCC-countries, fiscal (and monetary) policies were formulated in the expectation of continuing high levels of spillovers from GCC-countries, to the effect that these policies were rarely formulated to cope with national economic objectives under various financial scenarios. Only after the recent Gulf crisis and the subsequent decline of the spillovers to a number of these countries, that they have started reformulating fiscal policies in light of the new conditions.

Fiscal policy, in general, has acquired a wide range of functions over the years. But the actual fiscal policy at any given stage of development involves the transmutation of attitudes and approaches into specific responses to challenges that are recognized in the functioning of the economy. In particular, one major task of fiscal policy relates to the determination of the resources to be acquired by government from the private sector, and to the maintenance of balance between the private sector and the public sector. The need for financial resources by the governments of ESCWA countries is determined partly by their expenditures plans and partly

by the size of budget deficits considered to be sustainable. Sustainability in this context relates to the delicate demarcation line between the public and the private sectors' demand for financial resources (the internal resources balance) and to the balance between total foreign exchange receipts and payments (the external resources balance). The balance between the public and private sectors is primarily a political choice and is influenced by several considerations. The process of making the choice is complex and controversial at the same time. But a practical approach to making the choice is seen in determining the relative boundaries and the duration for which the demarcation line would remain in force, taking into account that the role of the modern state in determining fiscal policies has become dominant.

Tax systems and tax incidence are considered as important policy tools in the process of domestic resources mobilization and their allocation between the private and the public sectors. The problems of taxation in connection with their effects on the economic absorptive capacity are seen from two different points of view, namely, that concerning the tax incentives and that related to the financial resources. Both involve distinct and conflicting considerations. As concerns incentives, they are seen as a major factor that leads to improvement in the existing tax systems through granting additional concessions with less regard to the unfavourable effects on the mobilization, management and allocation of financial resources. As concerns resources, their inadequacy is considered as the major reason behind the insufficient investment and growth in the ESCWA region, thus the need to increase financial resources through additional taxation, even at the cost of increasing disincentives.

However, past experience of ESCWA non-GCC-countries suggests that a great deal of the prevailing concern with tax incentives is misplaced. It is the shortage of financial resources rather than the lack of tax incentives that has affected the level of investment and, hence, the level of development. An effective tax system and other compulsory levies could provide an appropriate instrument for increasing financial resources for capital formation.

It is difficult to define the appropriate taxes that can be relied on for maximum mobilization of financial resources in the ESCWA region. In fact, this issue does not admit to any general answer in the widely varying economic conditions and structures of ESCWA countries. A common feature of ESCWA non-GCC-countries is that these countries suffer from a shortage of tax revenues. This is partly because of their low taxation potential. But more important is that taxation potential of these countries has not been fully exploited. Added to this are inefficient tax systems, tax laws and tax administration. Many factors interact to determine the tax potential in these countries.

Most important among them are the real per capita income, the degree of inequality in the distribution of income, the relative importance of the various economic sectors in GDP, and last but not least, the administrative competence of the tax-collection instances in government. Usually, it is the highest income groups that offer the highest potential tax revenues, i.e., the taxation potential is strongly dependent on the prevailing distribution of income. This in turn is closely linked to the relative importance of income derived from property and other assets as against income resulting from work (i.e., wages and salaries). In the GCC-countries, progressive taxes on income and wealth are potentially important for the mobilization of domestic financial resources.

However, it is noteworthy that the efficiency of a tax system is not just a matter of appropriate tax laws. It is also a matter of the integrity of the tax administration, in order that tax provisions be enforced and a collusion between tax administration and tax payers be avoided.

B. The Role of Monetary Policy

Monetary policy has gained considerable attention during the last few years in the process of mobilization and allocation of financial resources. The observed paucity of savings in ESCWA-non-GCC-countries has led monetary authorities in these countries to raise interest rates to elicit larger amounts of savings, in the belief that savings and not investments are the limiting factor in the development process. However, the issue at the centre of monetary policy in individual ESCWA countries is the existence of proper channels through which financial resources of some economic agents can be diverted to those which are in need for them.

Consequently, the main issue confronting monetary policy in the ESCWA region is finding appropriate procedures to induce the flow of savings to deficit sectors in order to ensure higher investment and growth, to provide financial assets for surplus agents to hold their savings, (i.e., to change liquid assets for financial assets), and to increase the amount of aggregate savings. This process of skimming-off available excess savings for use by investment agents through the medium of financial assets is supposed to be accompanied by policy measures aimed at enlarging the amount of transferable savings in the ESCWA region. Achieving this objective would be through altering the structure of savings, a large proportion of which is generally invested in physical assets (such as precious metals, properties and real estate). Therefore, the policy needs to be so designed as to make it attractive for surplus agents to hold their savings in financial assets. This is to say, that for the development process to proceed

smoothly, the ratio of financial assets to total savings must grow. Concomitantly, the return on financial assets must be raised in "appropriate proportions" in order that the volume of excess savings itself be enlarged in the expectation of high yields.

The interest rate policy remains effective as a monetary policy instrument in most ESCWA countries, not as a stimulant to save, but, rather as indication of the opportunity cost of holding different kinds of financial and real assets, which is determined by what the asset holder would receive on alternative uses of savings. Monetary equilibrium will be attained when rates of return on various assets, financial or real, converge among ESCWA financial markets.

From the standpoint of investment in the region, a "high" interest rate policy would yield some beneficial results, although there might appear some contradiction in such interest rates being conducive simultaneously to accumulation of financial assets and to investment. Firstly, it is important to consider the term "high" in a relative sense, and as long as the interest rate is not higher than the return on real productive investment, investment demand would not be discouraged. Secondly, with a growing institutionalization of savings and investments, the weighted average cost of loanable funds would decline. This is so because with a rapid accumulation of financial savings, a larger size of investments would be financed by various institutional sources, where the interest rates charged, although higher than before, would still be lower than in the unorganized and narrow financial markets. Apart from this, financial savings would be used by "real enterprises" rather than by agents whose sole claim to enterprise comes from their "ownership" of savings. To the extent that efficiency in the economic structure of ESCWA countries is thus enhanced, the rate of profit could be higher even with higher interest rates.

C. The Role of Financial Markets

In the ESCWA region, where financial markets are rudimentary, and where rates of return are either artificially fixed or do not conform to the real (social) costs of investment, private investments tend to be self-financed. When investments are undertaken in this direct way, savers may not make the most efficient use of available resources and would not have a wide range of alternative projects from which to select. In this case, only by chance is the individual saver/investor satisfied in terms of risk preferences and project yield due to the limited choices available.

In the developed countries, development and management of financial markets coincided with the thrust to industrialization and was motivated by demands for financial resources from growing industrial ventures. This process of financial markets development and management sprang from the demand provoked by economic development and rising absorptive capacity and became known among economists as "demand-following" financial markets.

If such markets are effectively stimulated, the process generates what is called "supply-leading" financial markets, where the supply of financial instruments would activate economic development. Once established, the "demand-following" and the "supply-leading" features of the market would interact and promote economic development and economic capacity. In this sense, promotion and management of financial markets along these lines are viewed as means of encouraging savings and mobilizing financial resources, and further as a channel for efficient allocation of resources in the process of optimal sustainable growth.

However, where the active emergence and management of financial markets is made through "official policy" and not through free market stimulation, the markets may not be in a proper position as to stimulate investment or assist in financial resources mobilization and allocation. In fact, the argument that financial resources will be mobilized and made available to the most efficient investment projects may not be valid whenever monopoly power and government protection determines the course of business. In this case, the lack of information would provoke a lack of confidence in the market, and hence, inhibits its efficiency and even ability to operate without official support.

Compared with other developing regions with respect to the availability of financial resources for development, the issue confronting the ESCWA region has not been one of shortage of resources, but rather of management of surpluses. In this context, an effective and efficient organization and management of ESCWA financial markets becomes an imperative necessity. However, in order for this to materialize, the following issues should be addressed[10]:

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[10]/ ESCWA. Financial Markets and Investment Promotion in the ESCWA Region (February 1990). pp. 36-40.

(1) Establishing an adequate investment environment. Political, financial and developmental risks in some ESCWA financial markets are not conducive to the stimulation of investment in the region. The promotion of competitive conditions among ESCWA financial markets would minimize these risks and, thereupon, facilitate a smooth flow of resources between surplus and deficit ESCWA countries.

(2) Creating effective institutional and legal structures for ESCWA financial markets. The present state of ESCWA primary and secondary financial markets points to the urgent need for harmonizing the institutional and legal frameworks of these markets together with the respective procedures, policies and norms of business.

(3) Promoting investment in public shareholding companies. This would require:

(a) Reducing tax rates on profits and dividends to levels lower than those levied on returns from commercial bank deposits.

(b) Fixing nominal stock prices at levels affordable by small investors, together with elimination of the minimum number of stocks an individual investor can subscribe to.

(c) Transforming public sector enterprises into public shareholding companies.

(d) Deregulating and liberalizing procedures related to the transfer of profits and dividends among ESCWA countries.

(e) Removing restrictions applied by ESCWA surplus countries on the registration, listing and placing of companies and financial institutions from other ESCWA countries.

(f) tightening supervision of the business conduct and activities of public shareholding companies.

(4) With respect to ESCWA primary financial markets, there is need to boost their capital base and improve the efficiency of the management of the underwriting business of investment banks and security houses. This procedure would increase the placing power of these institutions and help mobilize and recycle financial surpluses held abroad. With regard to ESCWA secondary financial markets, there is a felt shortage of qualified market dealers and makers as well as traders, capable of buying and selling financial instruments in such volumes as to secure market and price stability. In fact, the lack of this

precondition has induced speculative tendencies and, consequently, scared off small savers/investors. Such conditions have long-term effects of preventing the establishment of a trust-building environment, and would not help mobilize untapped financial resources and savings.

(5) Financial instruments in the ESCWA region must be diversified to suit the incomes and preferences of a wide variety of savers and investors.

CONCLUSIONS

While ESCWA non-GCC-countries continue to experience payment difficulties, the GCC-countries still enjoy significant financial resources, notwithstanding the pressure on these resources which the Gulf crisis generated. To some extent, the financial imbalances in the ESCWA region are due to exogenous factors beyond the control of both groups of countries as well as domestic failures to accommodate their economies to changing exogenous influences.

In their attempt to promote economic growth and development, the ESCWA non-GCC countries have been generally constrained by low propensities to save. Concurrently, efficient and adequate mechanisms through which savings could be promoted and financial surpluses mobilized, managed and allocated for investment purposes in the region, have equally been lacking.

The state of affairs with respect to economic conditions as well as financial markets in the ESCWA region has not been successful in attracting financial surpluses for investment in the region. The paucity of viable investment ventures has contributed to this.

The establishment of efficient financial markets on a national and regional basis remains a necessary but insufficient condition for recycling ESCWA's financial surpluses held abroad. The development of free market economic systems and the creation of a trust-building investment environment and expanding absorptive capacity of ESCWA economies are additional prerequisites.

The recycling of ESCWA financial surpluses within the region has been essentially in the form of government-to-government transactions (grants and concessional credit) and expatriate workers' remittances. However, the 1980s saw a weakening of this trend with the sharp drop in oil revenues. Although the absolute level of financial flows from GCC-countries to ESCWA non-GCC-countries has declined in recent years, it undoubtedly has accelerated ESCWA recipient countries' economic development far beyond what would have otherwise been possible.

This flow also brought some negative side-effects. It created entrenched consumption habits, a high dependency on imports, often unrealistically overvalued national currencies and a higher degree of vulnerability to external shocks. These weaknesses brought the economies of recipient ESCWA countries under strain when the flow fell markedly in the late 1980s. Many of them had to adopt stringent adjustment programmes to redress their economic situation.

The development of domestic financial markets in the ESCWA region during the last decade indicates that these markets have not been successful beyond national boundaries and thus unable

to stimulate inter-regional resource flows. Development finance institutions and financial markets could play an important role in the mobilization of domestic savings and financial surpluses of the ESCWA region. An efficient structure of financial institutions could stimulate a higher propensity to save, in so far as they could increase opportunities for gaining access to credit and, consequently, for investment by productive units, and, raise the rate of return on financial assets.

It should be realized that promoting and developing financial markets is a gradual and time-consuming process. If the operations of these markets is not up to the standards prevailing in developed countries , this does not mean that these markets have completely failed, but rather that the level of efficiency of the institutions operating in them should be improved through the creation of a diversified structure of financial assets that caters to the various needs of potential investors in the ESCWA region, and which is capable of absorbing an increasing volume of real productive resources.

In addition, any further development of financial markets in the ESCWA countries would depend on the governments' approach to financial regulations and on the availability of institutional expertise. Market-making financial institutions should be created for regional risk-taking. And as such market-makers require substantial capital commitments, the capitalization should be made possible through an association of the existing financial structures and banking systems in the ESCWA region.

Government-held financial resources in the ESCWA region are significant in relation to the total available. The amounts involved are of such magnitude that a re-formulation of economic policy is required to achieve an optimal allocation of financial resources between the public and private sectors.

During the oil-boom era, the flow of financial resources to ESCWA non-GCC-countries made government budget planning and management less of a pressing issue than it should have been. With the end of that era, in the early 1980s these countries started facing difficulties. Only in the late 1980s and early 1990s have they begun introducing drastic fiscal and monetary policies to cope with the new situation. Some have committed themselves to implement structural adjustment programmes aimed at reducing the ratio of the budget deficit to GDP through restraining government expenditures and raising domestic revenues; increasing investments and savings efforts; removing domestic and external price distortions and rigidities that interfere with the allocation of financial resources; and reducing the burden of the external debt.

In the ESCWA region, the concern with respect to economic policy should relate to defining a proper demarcation line between the public and the private sectors' claim on financial resources. On their part, financial resources needed by ESCWA governments should be determined by their expenditures plans and by the size of budget deficit sustainable by their economies.

However, financing the budget deficit by borrowing from the public, which is supposed to create income and thereby encourage private investments could contribute to financial "crowding out" of the private sector. Therefore, the long-term implications of these policies should be taken into consideration when earmarking financial resources for different uses in the public sectors of ESCWA countries.

Tax systems could be invaluable policy instruments in the process of financial resources allocation between the public and the private sectors. However, the ESCWA countries not only suffer from a shortage of tax revenues, but more important is that their taxation potential has not been fully exploited. Inefficient tax systems, tax laws and tax administrations are responsible for this state of affairs. But the observed low tax potential could also be attributed to powerful pressure groups who block the way to effective tax reform. Therefore, an efficient tax administration is an important prerequisite for mobilizing domestic financial resources and exploiting fully the taxation potential of ESCWA countries. This conclusion is given more credibility in as much as more reliance is placed on the tools of fiscal policy because of the features associated with the working of monetary policy in the ESCWA region.