

Distr.  
GENERAL  
E/ESCWA/ED/1995/5/Add.3\*  
E/ESCWA/ID/1995/3  
31 January 1996  
ORIGINAL: ENGLISH

**ECONOMIC AND SOCIAL COMMISSION  
FOR WESTERN ASIA**

**IMPACT OF THE SINGLE EUROPEAN MARKET  
ON THE ESCWA MEMBER COUNTRIES**

**VOLUME III**

**TRADE IN MANUFACTURED PRODUCTS**



**UNITED NATIONS  
New York, 1996**

ESCWA ECONOMIC AND SOCIAL COMMISSION  
FOR WESTERN ASIA  
LIBRARY + INFORMATION

\* Reissued for technical reasons.

The designations employed and the presentation of the material in this publication do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations concerning the legal status of any country, territory, city or area or of its authorities or concerning the delimitation of its frontiers or boundaries.

The views expressed in individual contributions are those of the authors and do not necessarily reflect those of the United Nations.

Mention of firms or commercial products does not imply the endorsement of the United Nations.

The ESCWA members are Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Oman, Palestine, Qatar, Saudi Arabia, Syrian Arab Republic, United Arab Emirates and Yemen.

Bibliographical and other references have, wherever possible, been verified.

References to dollars (\$) are to United States dollars, unless otherwise stated.

96-0193

## Foreword

Geographically and culturally, Europe and Western Asia are intimately related. Over the centuries, history has shown us that major changes in Europe affect Western Asia and vice versa. The latest such change is Europe's move towards economic—and eventually political—unity. This development has far-reaching implications for the world economy in general and for the Western Asia region in particular. The establishment of the Single European Market (SEM), and subsequently the European Union (EU) in 1993, crowned a series of steps of *rapprochement* and integration, leading to the creation of a European economic bloc. The EU now forms one of the world's major economic groupings, along with the North American Free Trade Agreement (NAFTA), the Association of South-East Asian Nations (ASEAN) and the newly emerging Asia-Pacific Economic Cooperation (APEC).

Aware of the significance of these developments to Western Asia, the States members of the Economic and Social Commission for Western Asia (ESCWA) requested the ESCWA secretariat to prepare detailed studies in priority areas on the impact of the establishment of the SEM on the countries of the region (ESCWA resolution 190 XVI of 2 September 1992).

The impact of the SEM on the ESCWA region is general and pervasive, cutting across various sectors and activities. As no single scholar could be expected to cover this issue in its totality, the ESCWA secretariat commissioned a task force comprising a number of scholars from different backgrounds to study the impact of the SEM on the various aspects of the region's economic activities. Foreign trade, agriculture, manufacturing, banking, and science and technology seemed to be the obvious areas of emphasis for such a broad topic. It was thus decided that separate studies would be undertaken on each of those areas. It was agreed that, though each area would require specific expertise, they all required a unified perspective and a common outlook. In order to achieve this goal, a number of meetings and brainstorming sessions among the members of the task force took place to ensure the complementarity of the various studies. The fact remains, none the less, that differences in outlooks and perspectives of the authors of the studies cannot be totally eliminated and, in fact, they should not be. It was inevitable in such a collective work to expect some repetition, some differences in scope, measurements and data, and even a few contradictions. This should not be regarded as a source of confusion, but rather as an added advantage. With various opinions and differences in emphasis, the study is greatly enriched. Notwithstanding these few differences, the study as a whole presents a systematic, consistent and complete coverage of the impact of the SEM on the ESCWA region.

During the execution of this ambitious project, a major global event took place, ushering in a new era in international economic relations. This development, the establishment of the World Trade Organization (WTO), followed the conclusion of the Uruguay Round of multilateral trade negotiations held under the auspices of the General Agreement on Tariffs and Trade (GATT). It is bound to have profound effects on the world economy, including SEM itself. In addition, a Euro-Mediterranean initiative was also launched to pave the way for a future partnership between Europe and the south-east Mediterranean region.

Owing to the fact that the various reports comprising this study had reached different stages of progress when these developments occurred, the effects of GATT, the new WTO and the Euro-Mediterranean initiative received varying degrees of treatment in each report. In some reports, they were dealt with extensively while in others only marginally or even not at all.

In order to reconcile the need to preserve the authenticity of each author's contribution, on the one hand, and to maintain the unity and integrity of the entire work, on the other hand, we found it best to present each report in a separate volume along with an introductory summary and recommendations volume. All of the volumes have the same title: *The Impact of the Single European Market on the ESCWA Member*

*Countries*, as well as a subtitle specifying the particular sector or area of each volume. Thus the complete study comprises the following five volumes:

Volume I	Foreign Trade
Volume II	Agriculture
Volume III	Trade in Manufactured Products
Volume IV	Banking and Finance
Volume V	Science and Technology

Volumes II, III and V were prepared mainly by consultants and are, accordingly, the responsibility of those consultants. In the other volumes, the consultants' work, although separately identified, was supplemented by the ESCWA secretariat. The summary and recommendations volume, which is an overview of the whole study, was undertaken by the secretariat: in it, the main findings and recommendations of the subsequent volumes are outlined.

If one finding of the study stands out, it is perhaps the contrast between the modest performance of the ESCWA region and the impressive achievements of the European economic *rapprochement*. Although both Arab and European efforts to establish a common market started almost concurrently (in the late 1950s and early 1960s), the results achieved by the two sides were diametrically opposed. No less serious is the decline of the ESCWA region's economic clout in the international economy in general, and the European economies in particular. With the passing of the heyday of the 1970s, ESCWA economies have been left with a rather insignificant role in the European market. It is hoped, however, that with the prospects of peace closer to realization than ever before in the region, efforts and resources will be redirected towards more sustainable development.



Hazem El-Beblawi  
Executive Secretary

### **Acknowledgements**

This is volume III of the study entitled *The Impact of the Single European Market on the ESCWA Member Countries*, which was prepared by the Economic and Social Commission for Western Asia (ESCWA). On behalf of the ESCWA secretariat, I wish to express my appreciation to Atif Kubursi (McMaster University, Ottawa, Canada) for his valuable contribution to this volume.

H. B.



## CONTENTS

Page

Foreword .....	iii
Acknowledgements .....	v
Introduction .....	1
<i>Chapter</i>	
<b>I. ECONOMIC INTERACTIONS OF THE ESCWA REGION WITH THE EUROPEAN UNION .....</b>	<b>2</b>
A. The issues .....	2
B. The data .....	4
C. The future .....	10
<b>II. SECTORAL TRADE ISSUES .....</b>	<b>13</b>
A. The textile and clothing industry .....	13
B. The petrochemical industry .....	16
C. The food industry .....	18
<b>III. RECOMMENDATIONS .....</b>	<b>20</b>
A. Trade diversification and product differentiation .....	20
B. The hub-and-spoke alternative .....	20
C. Formation of a regional trade bloc .....	20
D. Investments, R and D and the training of human resources .....	20
E. Increased flexibility of production in textiles .....	21
F. Specializing in low-technology and low-polluting petrochemical products in EU-ESCWA region trade .....	21

## LIST OF FIGURES

I. Total ESCWA region exports to and imports from the EU .....	6
II. Exports of ESCWA region to the EU by country, 1980 .....	7
III. Imports of ESCWA region from the EU by country, 1980 .....	7
IV. Exports of ESCWA region to the EU by country, 1988 .....	8
V. Imports of ESCWA region from the EU by country, 1988 .....	8
VI. Exports of ESCWA region to the EU by country, 1992 .....	9
VII. Imports of ESCWA region from the EU by country, 1992 .....	9

## CONTENTS (*continued*)

*Page*

### ANNEX TABLES

1. Imports of ESCWA region from EU, selected years . . . . .	25
2. Exports of ESCWA region to EU, selected years . . . . .	26
3. Balance of trade between the ESCWA region and the EU, selected years . . . . .	27
4. ESCWA region exports to the EU by commodity, 1978 . . . . .	28
5. ESCWA region exports to the EU by commodity, 1979 . . . . .	28
6. ESCWA region exports to the EU by commodity, 1980 . . . . .	29
7. ESCWA region exports to the EU by commodity, 1987 . . . . .	29
8. ESCWA region exports to the EU by commodity, 1988 . . . . .	30
9. ESCWA region exports to the EU by commodity, 1989 . . . . .	30
10. ESCWA region exports to the EU by commodity, 1992 . . . . .	30



## INTRODUCTION

1. The prospect of a Single European Market (SEM) of over 340 million people, 12 countries and many more in line to join, a formidable purchasing power and massive and powerful industrial structures that are typically supplying a quarter or a third of world output, has already caused significant changes in business strategies and practices both inside and outside Europe. Mergers and acquisitions within the European Union (EU) have increased at a rapid pace as businesses are consolidating their positions to cater to a larger and more dynamic market. Direct foreign investment has also increased measurably as foreign firms are scrambling to gain secure access to this enlarged market. These developments are becoming increasingly complex as Eastern European countries compete with one another for speedy connections with the EU as they break with the past and find new orientations.

2. The conclusion of the Uruguay Round of multilateral trade negotiations by end-1994 is another important dimension that could eventually add to the complexity of the issue of the unification of the European market and the impact of that unification on ESCWA member countries. The net effects of the liberalization of world trade on the internal reforms of the EU and its trade and economic relations with the rest of the world is not yet clear. They will depend on the extent to which internal adjustment pressures within the EU will hamper efforts for external liberalization or the extent to which internal reforms will be applied in a discriminatory way in favour of one region against another.<sup>1</sup>

3. Developing countries cannot afford to be passive bystanders to these massive changes. The new developments pose formidable challenges and opportunities. No single group of developing countries will be more affected by these changes than the ESCWA member countries, given their geographical proximity to the region, their long history of extensive and sizeable economic interactions (trade, finance and migration) and the similarity of their structure and composition of trade to that of potential new entrants to the EU. New strategies and new modes of interaction are required to enhance the potential positive rewards of trade creation and to ward off or moderate the negative effects of trade and investment diversion.

---

<sup>1</sup> Jeffrey J. Schott, "The Single European Market and the Uruguay Round: implications for the structure of world trade", United Nations, *Journal of Development Planning*, No. 21, 1992.

# I. ECONOMIC INTERACTIONS OF THE ESCWA REGION WITH THE EUROPEAN UNION

## A. THE ISSUES

4. The EU was created in the context of overall trade liberalization. The intention was to reduce barriers on industrial goods among members progressively and cumulatively without generally raising them against the rest of the world, and new members would be added from time to time. So far, the economic growth spurred by liberalization of the internal market has made it possible to maintain the course of progressive liberalization and adding new members. However, there is no guarantee that the same policies will continue when economic growth slows or slumps. Tariffs have represented a good source of revenue for the conflict-reducing compensating mechanism in the EU. Acute policy conflicts among Community members have, from time to time, prompted the EU to impose tariffs or other protective devices in order to maximize either the size of its trade gain or its tariff revenues.

5. The goal of achieving an efficient SEM is not the sole objective of the Community; EU trade and industrial policies are also governed by another set of concerns. First among them is the promotion of cooperative research and development (R and D) initiatives within the Community. This objective has been consistently a priority concern since the signing of the Treaty of Rome in 1957. Second, there has been considerable pressure from the citizens of EU members towards more environmentally friendly production standards, and trade policies have been increasingly moderated owing to these environmental concerns. Finally, economic instability in countries bordering the EU, such as the Eastern European and the Mediterranean States, has resulted in large immigration flows. It is widely believed that these flows, if left unchecked, may threaten the security of the EU. Special economic packages and initiatives to strengthen those border regions have become an important priority for the EU.

6. With these concerns being taken into consideration, the following propositions can be derived:

(a) It is likely that some of the traditional EU-ESCWA-region trade may be diverted to countries in Southern and Eastern Europe. It is likely that the EU will introduce developmental policies favourable to Mediterranean and Eastern European States. To avoid excessive compensation to industries in Southern and Eastern Europe, the EU may impose some form of protection on goods produced in ESCWA member countries, as the factor endowments of some countries in the ESCWA region may be similar to endowments in these States;

(b) The EU is likely to bargain for favourable terms of trade and/or to restrict trade strategically with countries in the ESCWA region. There are two types of economic models (approaches) that are appropriate for dealing with this issue. There are the traditional optimal tariffs models and the more recent models based on trade negotiation and bargaining. The first type of model, developed by Johnson,<sup>2</sup> suggests that the terms of trade and gains of a country from a tariff war ultimately depend positively on the elasticity of its offer curve, relative to that of its opponent. The unification of the European economies will increase the elasticity of their offer curve. This model predicts that the terms of trade of ESCWA countries will worsen and that their market share in the EU will be curtailed. The second type of model is based on a cooperative game framework: the gains from trade negotiation for a country depend on its bargaining strength, on the trade

---

<sup>2</sup> H.G. Johnson, "Optimum tariffs and retaliation", *Review of Economic Studies* (No. 55, 1953), pp. 142-153.

options available to it when negotiation breaks down, and on the social discount rates.<sup>3</sup> Trade option, which is generally positively related to the elasticity of its offer curve, is the alternative trade arrangement that a country can have when negotiation fails. The predictions from the second, more comprehensive, approach are broadly consistent with the predictions from the first;

(c) There are sufficient grounds to suggest that the demand for exports from the ESCWA region in the EU is likely to increase as EU income rises. Market integration in the SEM will improve the efficiency of its internal market. This will substantiate the growth rate of the EU and sustain its future improvement. Owing to the proximity of ESCWA member countries to the EU, the demand for exports from the ESCWA region in the EU is expected to increase;

(d) Trade flows are not the only balance of payment component that will improve with greater internal efficiencies. Capital flows are more likely to move to the EU from the ESCWA region and from neighbouring regions. There are two reasons for the emergence of this pattern of capital flows:

- (i) The rapid growth of the EU economies must be sustained by a higher level of investment than in the past;
- (ii) The formation of the SEM introduces market security for its members. Monetary integration further reduces the exchange rate risk within the EU. As the domestic market in the EU becomes more secure than that of its trading partners, investments will move towards the more stable market. Industries with high mobility, such as those that are capital- and technology-intensive, are usually more sensitive to the security of their markets than others. This could cause an interest rate differential between the EU and the ESCWA member countries. Interest rates in the ESCWA region will have to rise (as a risk premium) to compensate for the relative insecurity brought about by the improved market security in the EU. Foreign investors will demand this risk premium before they choose the ESCWA region instead of the EU;

(e) The migration of skilled workers will continue to flow from ESCWA member countries and other developing countries to the EU. The migration pattern of skilled workers will be similar to the pattern of capital flows for similar reasons. Human capital is complementary to physical capital, particularly at the high rungs of the skill ladder;

(f) It is likely that the EU will protect its high-technology products against those which might be developed jointly by ESCWA member countries and by other developed countries; it is also likely that the EU will liberalize its trade in low-technology products. Technology is quantified according to the intensity with which it is embodied in a product, and it is viewed according to its position along a technological ladder. The ability to move up the technological ladder, according to the New Growth Theory, will depend on the industry's current position on the ladder.<sup>4</sup> Hence, the EU will strategically protect its high-income-generating and high-technology industries. It will not protect as vehemently its low- and intermediate-

---

<sup>3</sup> Kenneth S. Chan, "On trade negotiation and trade diversification: evidence from Canadian clothing import quotas", *Journal of Development Economics* (No. 40, 1993), pp. 361-370; K.S. Chan, "Trade negotiations in a Nash bargaining model", *Journal of International Economics* (No. 25, November 1988), pp. 353-363; B.R. Copeland, "Tariffs and quotas: retaliation and negotiation with two instruments of protection", *Journal of International Economics* (No. 26, 1989), pp. 179-188; and J.M. Osborne and A. Rubinstein, *Bargaining and Markets* (Academic Press, San Diego, 1990).

<sup>4</sup> G.M. Grossman and E. Helpman, *Innovation and Growth in the Global Economy* (MIT Press, Cambridge, Massachusetts, USA, 1992); and P.M. Romer, "Increasing returns and long-run growth", *Journal of Political Economy* (No. 94, 1986), pp. 1002-1037.

technology industries. Thus, it can be argued that low and intermediate technologies will complement high technology, often supplying intermediate inputs for the higher stages of production using higher levels of technology. The basic or the low-technology products from ESCWA member countries are less vulnerable to EU protectionism and exclusion. It is believed, therefore, that the elasticity of demand of ESCWA member countries for lower technology products from the EU is low. Alternatively, the elasticities of import demands for high-technology products in the EU are high owing to availability of alternative products from within the EU. The asymmetry of elasticities in high-technology and low-technology products between the EU and ESCWA member countries leads to the above proposition;

(g) It is likely that the EU will protect those manufactured products that are less harmful to the environment and liberalize its trade in goods whose production is more harmful to the environment. This pattern of trade is a result of the environmental concerns within the EU, which are greater than those observed in developing countries. Furthermore, with the bargaining strength and optimum tariffs of the EU, the compensation for environmental degradation in developing countries resulting from the production of those environmentally damaging EU

7. The above arguments will imply that the prospects for direct foreign investments in high-technology products in the ESCWA region, together with the transfer of technology that they would entail, will diminish. The lack of export demand for the ESCWA region's products in the EU will be a discouraging fact in the advancement of high technologies in these industries.

8. In some high-technology products, the possibility of free intra-industry trade exists.<sup>5</sup> Some may argue correctly that EU-ESCWA-region trade in high-technology products can be in differentiated products: free trade can only add to the product varieties, with a negligible sacrifice in demand for each product. However, in the theory of intra-industry trade, the pattern of trade is indeterminate—that is, which product a country will produce cannot be determined by economic factors, such as a country's comparative advantage. This means that the EU, with its strong bargaining power, can lay claim to those products that have a high technological advancement potential and exclude their deployment in the ESCWA region.

9. A favoured practice in the EU is the protection of high-technology products in the SEM by encouraging vertical integration through mergers and acquisitions among local firms. In this way, not only can the economies of scale be internalized, but entry barriers for foreign firms can also be created. Industries in the ESCWA region, and for that matter in most developing countries, are relatively small and are finding it increasingly difficult to compete against growing EU industrial conglomerates.

10. The above set of seven propositions defines the theoretical background against which EU-ESCWA-region trade and investment patterns before and after 1992 will be analysed. A quantitative analysis of the trade pattern between 1978 and 1992 follows.

## B. THE DATA

11. The evolving trade pattern between the EU and the ESCWA region will be analysed using International Monetary Fund (IMF) *Direction of Trade* data and the Organization for Economic Cooperation and Development (OECD) trade by commodity over three sample periods. The three periods were systematically selected in order to identify the salient features of the structural change that is likely to follow from the evolving nature of the European Union, particularly as it relates to the ESCWA region. The first period, from

---

<sup>5</sup> P. Krugman, "Increasing returns, monopolistic competition, and international trade", *Journal of International Economics* (No. 9, 1979), pp. 469-479.

1978 to 1980, covers the trade patterns that preceded the entry of Greece, Portugal and Spain into the EU. The trade patterns during this period reflect a relatively less integrated Europe with limited trade diversion to the Mediterranean countries of Europe. Most of the adjustments in trade diversion to the Mediterranean countries of Europe took place during the second period, from 1987 to 1989. Some of these adjustments may have been completed by the end of the 1980s. The recession years 1990 and 1991 were excluded from the current sample. Finally, the most recent data available for 1992 were singled out for inclusion since they may reveal the future trends in the emerging trade pattern of the EU with ESCWA member countries.

12. Figures I to VII and annex tables 1 through 10 present a number of significant features of the trade structure of the EU and the ESCWA member countries and the manner in which it evolved between 1978 and 1992:

(a) The EU as a group is by far the largest trading partner of ESCWA member countries. Proximity and a long history of trade has given Europe a decisive advantage over other trading blocs;

(b) While total annual imports to the ESCWA region from the EU remained almost stable at about \$25-30 billion during the period 1978 to 1992, the annual exports of the ESCWA region to the EU fluctuated widely, reaching a peak of \$60 billion in 1980 and a trough of \$13 billion in 1988, and were at 40 per cent of their peak level in 1992 (see annex tables 1 and 2);

(c) The ESCWA region's trade balance with the EU member countries mirrors developments in oil prices. Thus, following the dramatic adjustments in oil prices in the 1970s, ESCWA member countries maintained a balance of trade surplus with the EU member countries, with 1980 showing the largest such trade surplus. The late 1980s show a reversal of fortunes for the region, with the EU member countries maintaining a rising trade surplus with the ESCWA region (see figure I and annex table 3);

(d) Bahrain, Egypt, Jordan, Lebanon and Oman had a trade deficit with the EU throughout the period 1978 to 1992. The Syrian Arab Republic began with a large trade deficit in the late 1970s and early 1980s but managed to produce an increasing trade surplus in the late 1980s and early 1990s. Most of the oil-producing ESCWA member countries experienced a reversal of fortunes before and after 1985. Kuwait stands as an exception. It maintained a trade surplus throughout the period until the Iraqi invasion in 1990. Iraq started the period with large trade surpluses with the EU and ended the period with a trade embargo that crippled its exports and imports (see annex table 3 and figures II to VII);

(e) The commodity composition of ESCWA region exports to the EU between 1978 and 1992 did not undergo any significant change. The dominance of oil exports continued to constitute the overriding reality of the trade flows between the two groups, despite the wide fluctuations in oil prices. Only Bahrain, Jordan and Lebanon are without significant exports to the EU in oil and related products (SITC division 33). Egypt and the Syrian Arab Republic have also become exporters of oil to the EU.

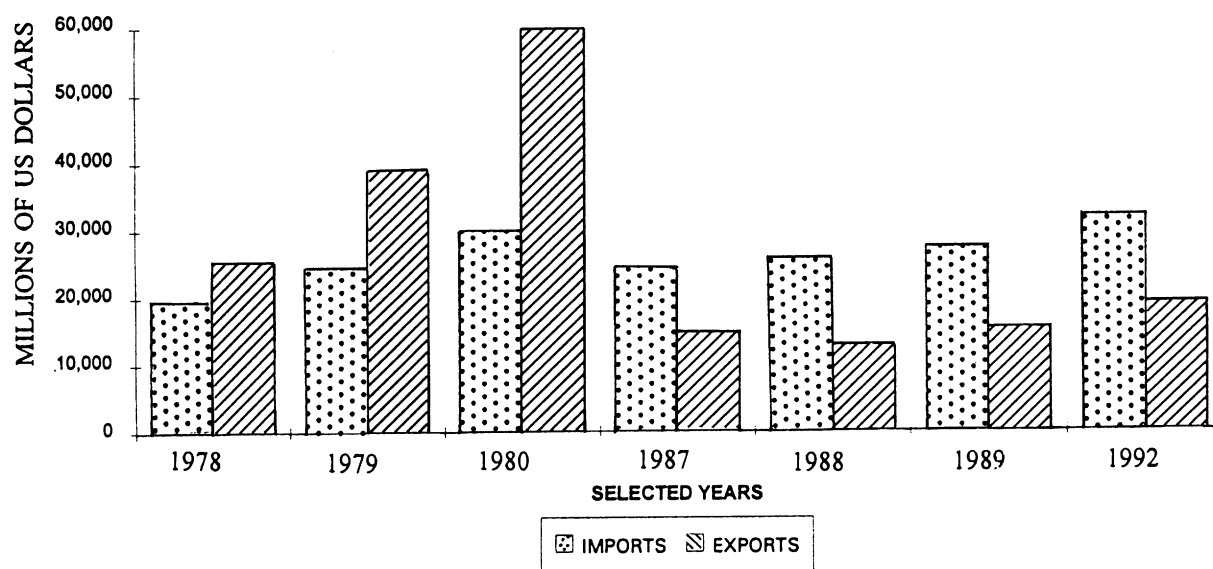
13. The large oil export levels of the late 1970s declined sharply in the late 1980s and the early 1990s. Saudi Arabia's oil exports to the EU exceeded \$33 billion in 1980 but declined to about a third of that value (\$11 billion) in 1992 (see annex tables 4 to 10).

14. Minor trade is noted under food and beverages, inorganic chemicals and chemical materials. Egypt and the Syrian Arab Republic appear to have succeeded in exporting modest amounts of textile fibres to the EU. Egypt's textile fibre export volumes declined in the 1980s, and the Syrian Arab Republic appears to have taken up the Egyptian slack. Only Egypt has any significant exports of textile yarn, fabrics and made-up articles of related products. Surprisingly, there are few ESCWA region exports of plastics and petrochemicals

to the EU. Only Saudi Arabia is credited with limited success in exporting these products, and that occurred only in 1992 (see annex tables 4 to 10).

15. The general pattern of trade displayed in the tables and figures mentioned above portrays a macro framework of the magnitudes and directions of trade between the ESCWA region and the EU over the three selected periods. They also offer the opportunity to quantify some analytical indicators that can be helpful in predicting future trends and patterns. Of particular significance and utility in this respect are two concepts—the concept of “revealed” comparative advantage (RCA)<sup>6</sup> and the concept of Trade Diversion Ratio (TDR).

FIGURE I  
TOTAL ESCWA REGION EXPORTS TO AND IMPORTS FROM THE EU



Summary statistics of EU/ESCWA region trade by year and selected commodity

Commodities	0	1	26	33	52	57	58	57/58	59	65	84
RCA2 1978	0.0229	0.0012	0.5331	7.0441	0.0232			0.0002	0.0005	0.0453	0.0030
RCA2 1979	0.0214	0.0000	0.3378	5.9812	0.0062			0.0004	0.0002	0.0809	0.0074
RCA2 1980	0.0175	0.0008	0.2709	4.9212	0.0130			0.0001	0.0015	0.0499	0.0105
RCA2 1987	0.0902	0.0033	1.2947	13.2732	0.0954	0.4995	0.0021		0.0258	0.4009	0.0591
RCA2 1988	0.1299	0.0017	1.2839	15.9650	0.1038	0.7570	0.0051		0.0064	0.3711	0.1123
RCA2 1989	0.1074	0.0020	0.8254	15.8058	0.1321	0.6499	0.0072		0.0813	0.4034	0.1805
RCA2 1992	0.0940	0.0034	0.8896	14.1952	0.0891	0.3855	0.0057		0.0433	0.4455	0.4388
Nj/Mj (1992)	0.0345	0.0090	0.0492	0.1308	0.0869	0.0766	0.1070		0.0701	0.0726	0.0250
Nj/ESCWA2j/ (1992)	28.7042	208.0257	4.4284	0.7204	58.7013	15.5427	1478.3137		125.6929	12.7403	4.4721
ESCWA2j/Mj (1992)	0.0012	0.0000	0.0111	0.1815	0.0011	0.0049	0.0001		0.0008	0.0057	0.0058
Trade Diversion Ratio (1992)	0.0357	0.0091	0.0518	0.1504	0.0717	0.0830	0.1198		0.0754	0.0783	0.0258

Source: Based on calculations using data in the annex tables.

<sup>6</sup> B. Balassa, “The changing pattern of comparative advantage in manufactured goods”, *Review of Economics and Statistics* (No. 61, 1979), pp. 259-266.

FIGURE II  
 EXPORTS OF ESCWA REGION TO THE EU BY COUNTRY, 1980

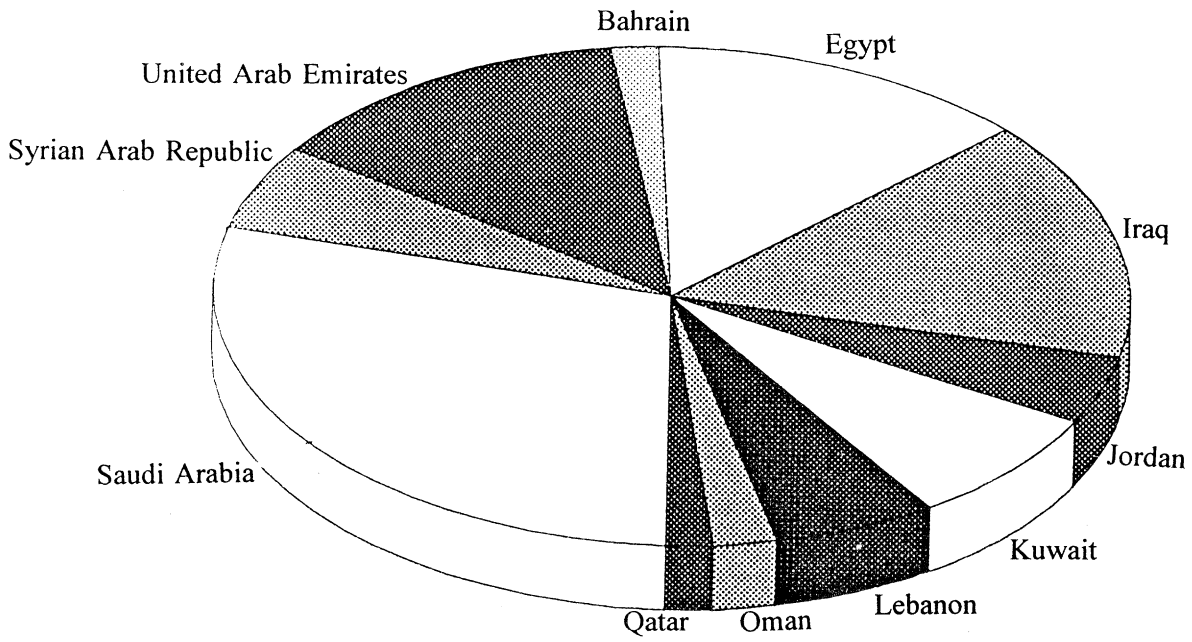


FIGURE III  
 IMPORTS OF ESCWA REGION FROM THE EU BY COUNTRY, 1980

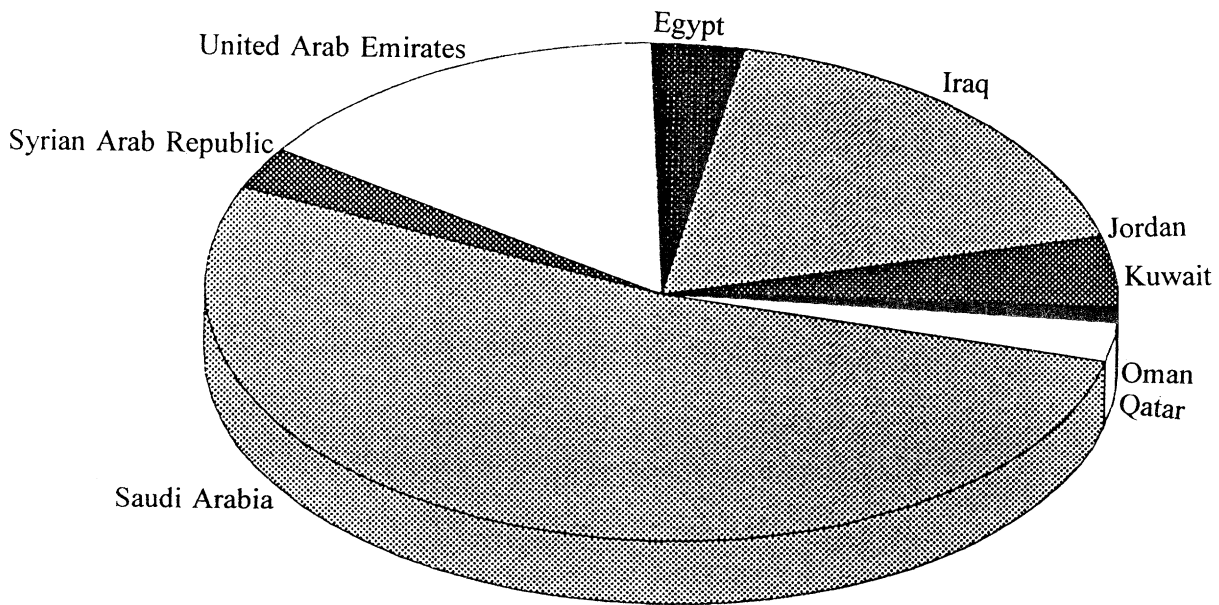


FIGURE IV  
EXPORTS OF ESCWA REGION TO THE EU BY COUNTRY, 1988

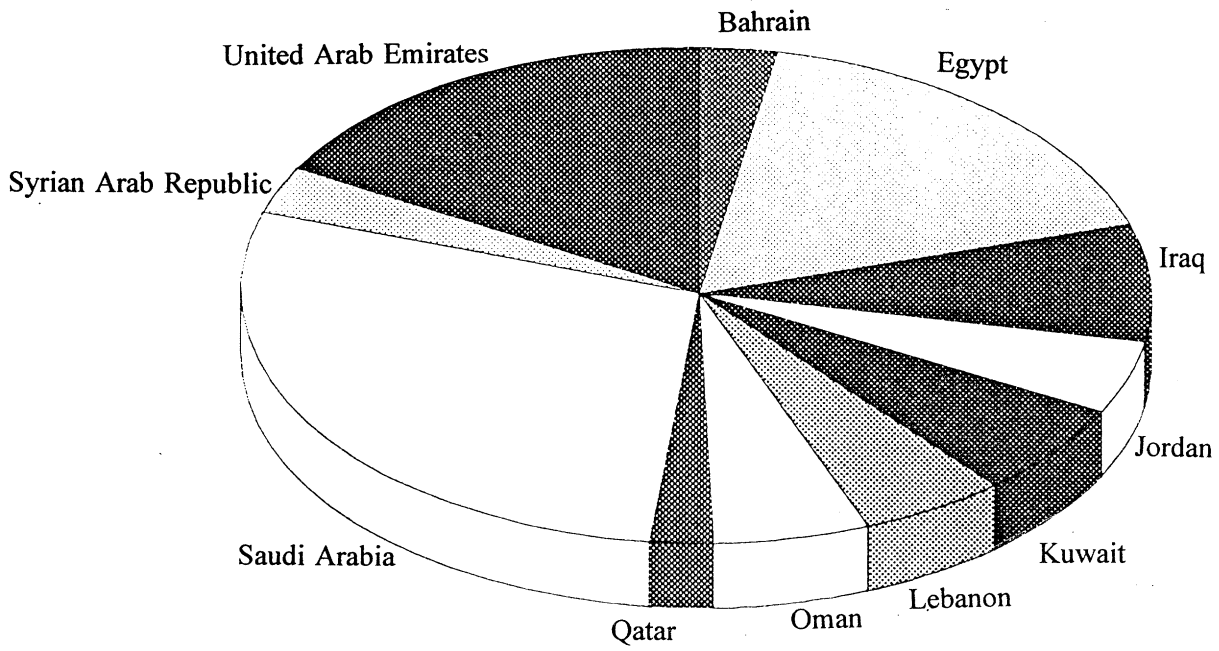


FIGURE V  
IMPORTS OF ESCWA REGION FROM THE EU BY COUNTRY, 1988

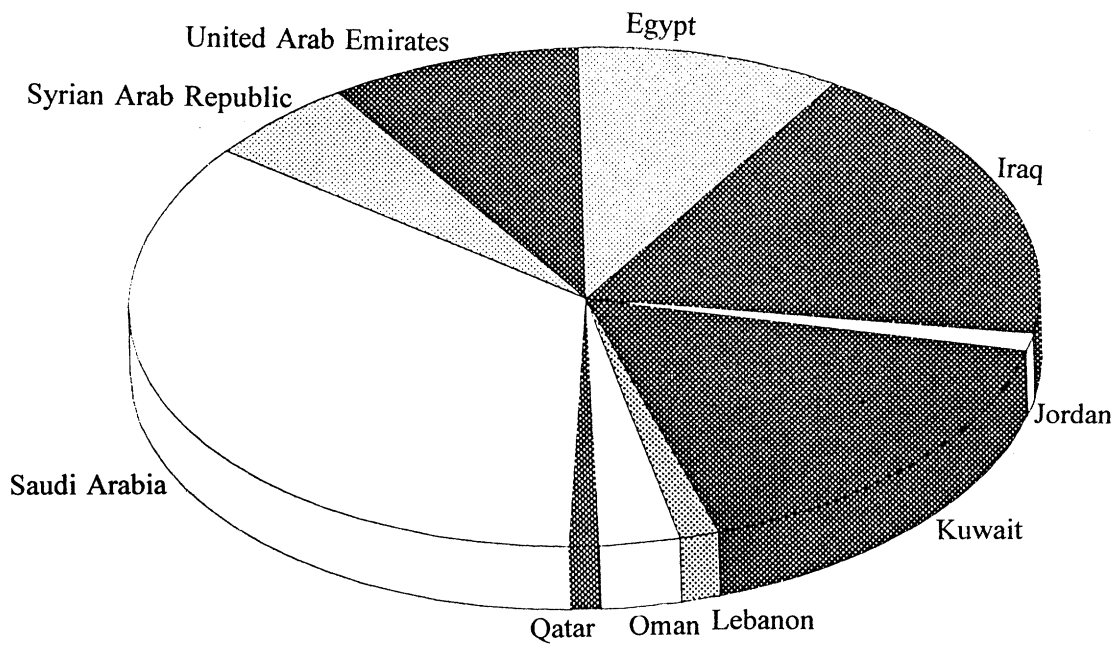




FIGURE VI  
 EXPORTS OF ESCWA REGION TO THE EU BY COUNTRY, 1992

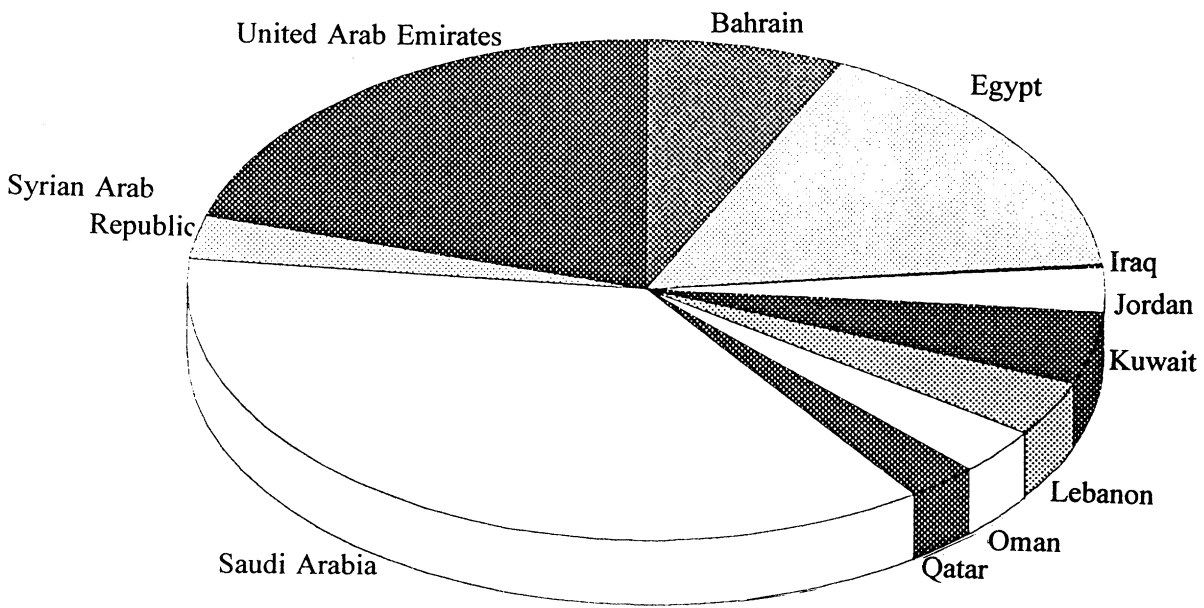
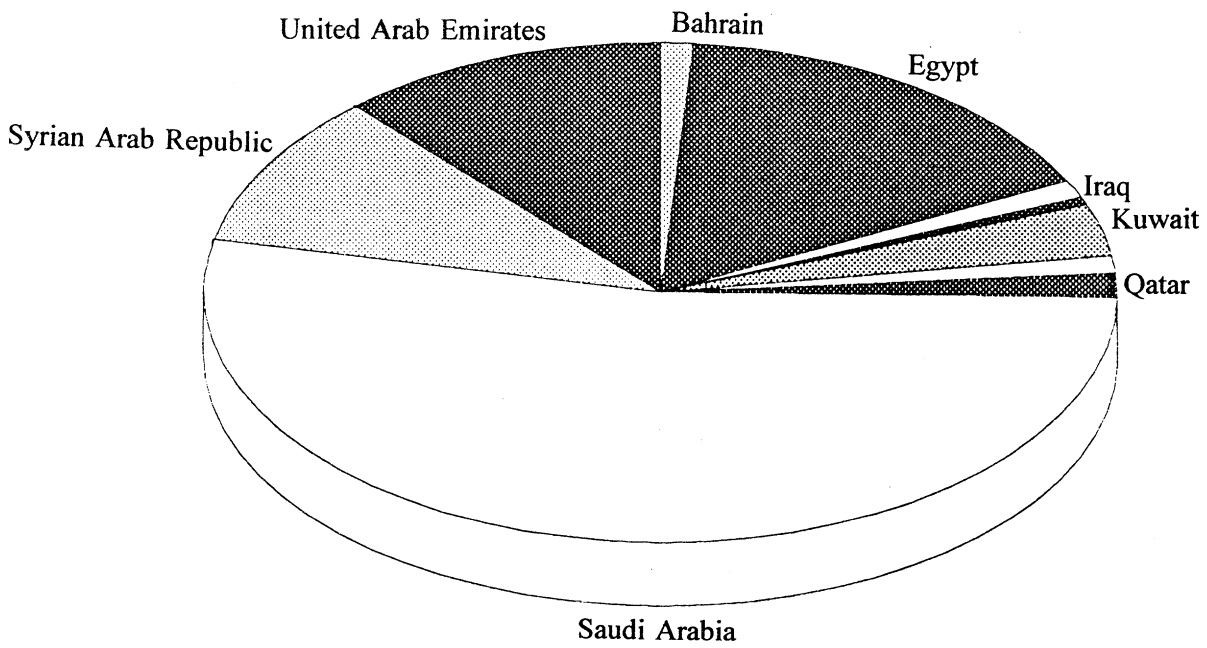


FIGURE VII  
 IMPORTS OF ESCWA REGION FROM THE EU BY COUNTRY, 1992



### C. THE FUTURE

16. The concept of RCA reflects the relative preponderance in a country's export of individual product categories, adjusted by their respective market sizes. It is defined as follows:

$$RCA_{ij} = (X_{ij}/M_j) / (X_i/M) \quad (1)$$

$X_{ij}$  = Export of commodity  $j$  from country  $i$  to the EU.

$X_i$  = Total exports of country  $i$  to the EU.

$M_j$  = Total EU imports of commodity  $j$ .

$M$  = Total imports of the EU.

17. The numerator of the RCA indicator quantifies the preponderance (share) of the exports of product  $j$  of country  $i$  in the total imports of  $j$  by its trading partner, while the denominator adjusts for differences in the relative size of the exporting to the importing country. When the RCA indicator of country  $i$  in commodity  $j$  is large, it indicates that country  $i$  has a better comparative advantage in exporting commodity  $j$  than in exporting another commodity to the same country with a smaller RCA. The RCA indicator generally reveals both the effect of various commercial policies and those factor endowments. When the RCA is larger (smaller) than one, it reveals that this country has (does not have) a comparative advantage over its average competitor in the export of the same commodity to the EU.

18. The table in figure I shows the RCAs of selected commodities. Petroleum and related products (Standard International Trade Classification [SITC] 33) show a very strong RCA (RCA index of about 15). It is also true that textile fibres (SITC 26) had an RCA index greater than 1 in 1987 and 1988. This index dropped to 0.83 in 1989 and rose slightly to 0.87 in 1992. This is indicative of a weak comparative advantage in this sector. Interestingly, ESCWA member countries have a relative strength in SITC 65 (textile yarn and fabrics), SITC 57 (primary plastics), and SITC 84 (apparel and clothing). Not surprisingly, ESCWA member countries do not appear to have a strong comparative advantage in all other commodities. It appears clearly that ESCWA member countries have relative advantages in primary production and resources, and that this strength dissipates as one moves into higher levels of processing and manufacturing. It is also clear that the ESCWA region has had some strong variations in its RCA indices over the periods under study. The following trends are, however, evident:

(a) The revealed comparative advantage of the ESCWA region in food and live animals rose slightly between 1978 and 1992;

(b) Beverages and tobacco products have weak comparative advantages in the ESCWA region, and this weakness has remained constant over the period under study;

(c) There is an obvious strengthening in the comparative advantage of the region in petroleum and petroleum products;

(d) The comparative advantages of the region in primary textiles more than doubled between 1978 and 1988. There was some weakening in the RCA of this sector between 1988 and 1992;

(e) The ESCWA region does not appear to have a significant RCA in inorganic chemicals. Over time, inorganic chemicals gained some limited strength, but on the whole they remain weak. The same is true for SITC 59 (chemical materials and products, n.e.s.);

(f) Primary plastic products (SITC 57) have a higher RCA than non-primary plastics (SITC 58). This may be a direct result of the more protective tariff structure of the EU for products at the higher end of the technological ladder. The EU imposes less protective tariffs on products at the lower end of this ladder;

(g) Textile yarn, fabrics, made-up articles n.e.s., and related products (SITC 65) have made considerable gains in relative advantage. In 1978, the RCA of this sector was as low as 0.045. By 1992 it had climbed to 0.45. The same is true for articles of apparel and clothing accessories (SITC 84), whose RCA climbed from 0.003 in 1978 to 0.44 in 1992.

19. These indices indicate clearly that ESCWA member countries will continue to export petroleum and petroleum products to the EU. They may also develop a greater capacity to export plastic products and primary textiles. If current trends continue, ESCWA member countries will face difficulties in exporting to the EU more technological products and manufactured products involving higher-end processing and technological inputs. There are, however, some looming difficulties for the ESCWA region in all products except petroleum. These difficulties have to do with the entry of Switzerland and countries in the European Free-Trade Association (EFTA) and possibly some Eastern European countries into the EU.

20. In the near future, as Switzerland and countries in the EFTA (Austria, Sweden, Finland, Norway and Iceland) and possibly some Eastern European countries join the EU, EU trade will most likely be diverted further from the ESCWA member countries to these new members. To examine this possible scenario, the following trade diversion ratio (TDR<sub>j</sub>) has been constructed:

$$D_e/E_j = TDR_j (D_n/N_j)$$

$$TDR_j = N_j / (M_j - N_j) \quad (2)$$

where:

$E_j$  = Total exports of ESCWA member countries to the EU of commodity  $j$ .

$N_j$  = Total exports of Austria, Finland, Iceland, Norway, Sweden and Switzerland to the EU of commodity  $j$ . For simplicity, this set of countries shall be known as the Nordic countries.

$M_j$  = Total EU imports of commodity  $j$ .

$D_n/N_j$  = Percentage increase of the export of commodity  $j$  to the EU as a result of trade diversion.

$D_e/E_j$  = Percentage decrease of the ESCWA region's export of commodity  $j$  to the EU as a result of trade diversion.

21. On the supposition that the new member countries of the enlarged EU will increase their export of commodity  $j$  to the EU by  $D_n/N_j$ , creating new trade diversion, the ESCWA region's exports of commodity  $j$  to the EU will diminish in proportion to the relative size of exports. TDR<sub>j</sub> is the coefficient linking the percentage increase of the new member countries' exports to the EU to the percentage decrease of the ESCWA region's exports and is related to the size of  $N_j$  and  $M_j$ . If the exports to the EU of the new member countries are large in relation to the total EU import market, the impact of trade diversion on the ESCWA region's exports to the EU will be substantial. The magnitudes of TDR<sub>j</sub> are presented in the summary statistics table (see paragraph 18).

22. The ratio of Nordic exports by commodity  $N_j$  to total EU imports in 1992 illustrates the share of these countries in the EU market. Similarly, the size of the exports to the EU of these countries relative to the ESCWA region's exports to the EU indicates the magnitude of the Nordic countries in relation to the ESCWA region's export potential. Furthermore, the ratio of the ESCWA region's exports to the corresponding EU imports defines the magnitude of the potential damage from trade diversion that the ESCWA region may suffer when the Nordic countries join the EU. Finally, the Trade Diversion Ratio as defined above is another indicator of the prospective loss to the ESCWA region from the entry of the Nordic countries into the EU. It is clear from all of the indices in the summary statistics table that only SITC 33 will be affected substantially by trade diversion from the ESCWA region to the Nordic countries.

23. Regarding future trade diversion to Eastern Europe, quantitative assessments are extremely difficult to make at present inasmuch as Eastern European countries have been undergoing some major structural adjustments. Their currently low volumes of trade with the EU hardly reflect their future potential. It is expected that security imperatives and geographical proximity would prompt greater trade between these countries and the EU than has hitherto been the case. A good part of this trade may impinge negatively and directly on EU trade with the ESCWA region.

24. Below the EU-ESCWA region trade in the textile and clothing industry, the petrochemical industry, and the food industry will be examined. The findings in these industries broadly confirm the quantitative assessment in this section and the conclusions from conventional theories that have been previously discussed.

## II. SECTORAL TRADE ISSUES

### A. THE TEXTILE AND CLOTHING INDUSTRY

25. The EU is the world's largest exporter and importer of textile and clothing products. The textile and clothing industry employs a total of 2.9 million people in the EU. The domestic market share of EU producers in the EU area is about 80 per cent. None the less, employment in the industry has declined by about 40 per cent in the past 15 years.

26. The production of textiles has fallen in Denmark, France, Germany and the United Kingdom of Great Britain and Northern Ireland, but it has risen significantly in Italy, Portugal and Spain. Still, the largest textile exporters of the EU, in absolute terms, are France, Germany and Italy. In the clothing industry, Greece, Ireland and Portugal employ the largest numbers of workers in the EU, but the largest (finished) clothing exporters in the EU are Italy and Germany.

27. The major textile and clothing exporters in the ESCWA region are Egypt, Iraq, Lebanon and the Syrian Arab Republic. Since its colonial days, Egypt has been one of the largest cotton producers among developing countries. Raw cotton constitutes the bulk of the country's exports to the EU. Similar to other textile and clothing exporting countries in the ESCWA region, the production potential in Egypt has been underutilized and undercapitalized owing to the lack of investment funds and foreign reserves as well as the highly protective stance of the EU towards its high value added textile and clothing products. The Syrian Arab Republic is the second most important textile exporting country in the region, followed by Lebanon and Iraq. The textile industry is also an important industrial activity in Jordan and the Republic of Yemen, but not to the same extent as in Egypt and the Syrian Arab Republic. With well developed petrochemical industries but high labour cost and scarce water resources, the Gulf States may develop a comparative advantage in the production of synthetic fibre.<sup>7</sup>

28. Among ESCWA member countries, only Egypt exports most of its textile and garment products to the EU, while the rest have other export markets, particularly the Syrian Arab Republic which has an export arrangement with the United States of America. Nevertheless, in most cases, ESCWA member countries never exhausted their export quotas to the EU or the United States, and thus it is believed that the MultiFiber Arrangement (MFA) was not an obstacle to the expansion of exports from these countries. Most of these countries simply were not export-oriented or dynamic enough to take advantage of this export outlet.<sup>8</sup> Although the dismantling of the MFA by the Uruguay Round agreements will eliminate the quota constraints in the future, seemingly increasing the export opportunities, other problems facing exports may be aggravated

---

<sup>7</sup> United Nations Industrial Development Organization (UNIDO), "*The Textiles and Clothing Sector*", paper submitted to the Expert Group Meeting on the Implications of the Single European Market for Industrialization in Developing Countries, Vienna, 18-20 March 1992 (UNIDO, Vienna, 9 March 1992) (ID/WG.523/3(SPEU)); and ESCWA (United Nations Economic and Social Commission for Western Asia), *Issues of Inter- and Intraregional Trade and Marketing of Manufactured Products: Sectoral Studies on Textile, Aluminium, Steel and Cement Industries in the ESCWA Region* (E/ESCWA/ID/89/9), Industrial Development Series No. 11 (United Nations, New York, 1989).

<sup>8</sup> These countries did not exhaust their quotas possibly because restriction of the quota by itself may inhibit investors from expanding production for the export market. In addition, domestic quotas on raw materials and inputs are imposed on producers of textiles and garments in Egypt and the Syrian Arab Republic. It is expected that these restrictions will diminish gradually with the current trend towards the transformation of the economies into more market-oriented economies, thus helping to encourage investors to benefit from export-oriented opportunities.

by tougher competition, particularly from India, China, the Eastern European countries and the Commonwealth of Independent States (CIS).<sup>9</sup>

29. The textile and clothing industry is a heterogeneous industry; its output ranges from low-technology and labour-intensive products to high-technology and capital-intensive products, such as synthetic fibres. Some production processes, such as dyeing, are highly polluting.

30. In the EU, there has been a considerable amount of vertical integration in the entire production process and distribution chain. In response to rapidly changing consumer tastes, the entire industry has become increasingly flexible. Subcontracting in the industry, or outsourcing, to low-wage countries is common and has been stepped up in recent years. The process of subcontracting from the EU oligopsonists (large distribution houses) to small firms in developing countries will mean that the terms-of-trade will go against the small firms in the developing countries. The ESCWA region is no exception.

31. So far, the EU has adopted a selective stance in the negotiation of MFA quotas. Countries that have large imports from the EU receive more favourable quotas. Products on the lower end of the "technological ladder", such as industrial raw materials, are granted exemption from duty or reduced tariffs. For example, in 1989, the EU tariff rates were 13 per cent for imported fabrics and 14 per cent for garments. Although these rates have been decreasing, they have remained a significant obstacle for ESCWA member countries and other developing countries. The Generalized System of Preferences (GSP) also grants tariff exemptions for very poor developing countries. However, the Republic of Yemen, the least developed ESCWA member country, together with other very poor developing countries, has not benefited much from this exemption owing to poor infrastructure, capacities and paucity of capital. Textile and clothing products from Eastern European countries are completely duty-free, a fact that is increasingly militating against the capacity of less favoured developing countries, including those in the ESCWA region.

32. With the conclusion of the Uruguay Round of multilateral trade negotiations, the textile and garment industry will be completely integrated into the international trading system. This will be done at a slow pace, however, within a period of 10 years and in three stages starting 1 January 1995. The Uruguay Round agreements, however, give countries such as Egypt,<sup>10</sup> with low levels of exports in textiles and garment products (less than 1.2 per cent of their total exports, the base year being end-1991), higher rates of quota growth averaging 25 per cent starting the date of implementation of the Uruguay Round agreements, followed by 27 per cent at the beginning of the fourth year, compared with 16 per cent and 25 per cent respectively offered to other suppliers. The Uruguay Round agreements allow exporters from such countries to enjoy preferential treatment in export markets, with the aim of developing their future export potentials and trade.<sup>11</sup> Textile and garment exporters in the ESCWA region may be able to benefit from the interim period and adjust their products partly to suit the needs and tastes of the European market. Another aspect will be the standardization and quality requirements, which suppliers will eventually have to face even in their own domestic markets in order to compete with foreign products. Complying with these standards may help exporters to improve the competitiveness of their products on the international (and domestic) market.

---

<sup>9</sup> Refik Erzam, "Liberalization of global trade in textiles and clothing", *Forum*, vol. 1, No. 4, December 1994.

<sup>10</sup> The Syrian Arab Republic is not yet a member of the World Trade Organization (WTO) agreements; thus the decision of the importers to continue imposing the quotas on non-member countries may still prevail, reducing this country's chances of benefiting from the lifting of these quotas.

<sup>11</sup> Abdulkarim Al-Mudarris, "The General Agreement on Tariffs and Trade (GATT) and its economic implications", *Sh'oun Arabiyya (Journal of Arab Affairs)*, League of Arab States, No. 80, December 1994.

33. The gradual phasing out of the MFA by the Uruguay Round will be affected by the expansion of the EU and its trading agreements with the Eastern European and CIS countries. In this respect, the EU association agreements concluded with the Central and Eastern European countries envisages the complete dismantling of the MFA in five years instead of 10 years, while tariffs on imports of most of the outward processing trade (that is, imports from Central and Eastern European countries that have inputs from the EU) in the EU are totally eliminated with immediate effect. This will give countries of Central and Eastern Europe a great advantage over other suppliers in the future, particularly potential suppliers in the ESCWA region. Nevertheless, despite the comparative advantage of the Central and Eastern European countries in skill endowment and low wage rates compared with some ESCWA member countries, their disadvantage lies in their poor endowment in most natural fibres.<sup>12</sup>
34. There is no doubt that the SEM will divert trade from the ESCWA region and other developing countries to the neighbouring Eastern European and Mediterranean countries of Europe. In a number of Eastern European countries, economic conditions are similar to those of many non-European developing countries. In addition to low wages, the proximity of Eastern European countries to the EU gives them some additional comparative advantages. The bulk of the outsourcing activities will be directed towards nearby Eastern Europe. The rapid changes in consumption patterns in the future will mean that retailers will have to reduce stocks, but an increased frequency of orders will make proximity a premium. Added to this is the increased interest of the EU in more stable and prosperous neighbouring Eastern European States. Textile and clothing deployment and outsourcing appears to be a favoured and economic vehicle for shoring up the ailing economies of Eastern Europe with minimum disruptions to the EU economies.
35. The estimated growth rate of an integrated EU amounts to a net and sustained growth from 4.5 to 7 per cent of GDP.<sup>13</sup> This robust growth in the EU creates trade. Assuming a unitary income elasticity of consumption and that the ESCWA region's export competitiveness is maintained, the export growth of textile and clothing from the ESCWA region to the EU should have a comfortable 4.5 per cent rate of growth.
36. To remain competitive in the EU textile and clothing market, ESCWA member countries and other developing countries have to increase the flexibility of production. They may gain some security of access by engaging in joint ventures with European partners that have the necessary knowledge of the market and the distribution networks. Joint ventures may also make it possible for them to learn and import new technologies from the EU.
37. In accordance with the Uruguay Round agreements, the MFA will be completely dismantled within the next 10 years. This, together with the projected robust growth of the SEM, will have a major potential positive impact on this industry for ESCWA member countries and other developing countries, albeit at a slow pace.
38. The phasing out of the MFA by the year 2005 is expected to open the door for strong competition in the EU market from exporters in other regions, particularly from the Far East. This will force countries in

---

<sup>12</sup> Refik Erzam, "Liberalization of global trade in textiles and clothing", *Forum*, vol. 1, No. 4, December 1994.

<sup>13</sup> See P. Cecchini, *The European Challenge, 1992: The Benefits of a Single Market* (Aldershot, Wildwood House, 1988); and the Commission of the European Communities, "The economies of 1992", *European Economy*, No. 35, March 1988. Also of interest is the paper by M.W.S. Davenport, entitled "The external policy of the community and its effects upon the manufactured exports of the developing countries", *Journal of Common Market Studies*, vol. 29, No. 2, December, 1990. In fact, the entire December issue of the *Journal of Common Market Studies* is devoted to the challenge of the SEM.

the ESCWA region to identify the textile industry items in which they have more comparative advantage than their counterparts from other regions so as to be able to cope with trade liberalization.

## B. THE PETROCHEMICAL INDUSTRY

39. The demand for petrochemicals in the EU is one of the highest in the world. This demand stems mainly from the plastic, fibre, fertilizer, paint, soap and detergent and other chemical industries. EU demand for ethylene in 1989 amounted to 13.1 million tons, almost a quarter of world consumption. Demand for petrochemicals is also expected to grow in line with overall economic growth.<sup>14</sup>

40. For the capital- and technology-intensive petrochemical industry, economies of scale are prevalent. This undoubtedly leads to industrial concentration in the EU in the form of plant sizes, of R and D efforts and of marketing efforts. The concentration ratio of the industry in the EU from the four leading companies was 36 per cent in 1988, calculated with regard to ethylene capacity.<sup>15</sup> The economies of scale and the technical knowledge have provided high entry barriers. Overall, the petrochemical industry in the EU is a vertically well integrated industry, and it is concentrated in high value added products.

41. Protective commercial policies are relatively few in this highly technologically intensive side of the petrochemical industry.<sup>16</sup> There is no need for protection as European companies already hold a strong position in their core markets.

42. The industrial policies of the EU have emphasized R and D and the environment among other things. Specific research programmes such as the European Strategic Research and Development Programme in Relation to Information Technologies (ESPRIT) and the Programme on Industrial and Materials Technologies (BRITE) and tax policies are set up to promote and expand this industry. These programmes have a notable effect in encouraging R and D partnerships between private firms and the EU Governments. The industry itself also undertakes a large amount of research. Therefore, investment in the petrochemical industries will likely increase in the SEM.

43. According to a 1988 EU study on the chemical industry,<sup>17</sup> the effect of an integrated European market on imports can be divided into two parts: the immediate "static" welfare effect from trade creation and trade diversion, and the long-run "dynamic" effect from the economies of scale. The former reduces the imports of the chemical industry by about 2 per cent. The latter reduces imports by about 10 per cent. In the 1980s, a massive restructuring was initiated in the chemical and the petrochemical industries. Most of the trade diversions should have been realized by now. It is doubtful that the continuation of integration in Europe in the 1990s will have any further significant impacts on the trend of evolution of this industry.

---

<sup>14</sup> UNIDO, "The Chemicals Sector", paper submitted to the *Expert Group Meeting on the Implications of the Single European Market for Industrialization in Developing Countries*, Vienna, 18-20 March 1992 (UNIDO, Vienna, 9 March 1992) (ID/WG.523/7[SPEU]).

<sup>15</sup> Ibid.

<sup>16</sup> The relatively low non-tariff barrier equivalent for the chemical industry is around 8 per cent, which is identical to those in the United States and Japan (see. J. Whalley, *Trade Liberalization Among Major World Trading Areas* [MIT Press, Cambridge, Massachusetts, U.S.A., 1985]).

<sup>17</sup> P. Cecchini, "The economics of 1992", *European Economy*, No. 35, 1988, parts of which are also reported in the UNIDO paper on the "Chemicals Sector" (see note 14).



44. Although the conclusion of the Uruguay Round agreements is expected to liberalize barriers to trade in industrial products, petrochemical products seem to have fewer chances in this process than other industrial product items. The main reason is that during the Uruguay Round negotiations, some of the main international petrochemical producing and exporting countries, such as the Arab Gulf countries, China, the Russian Federation and some Eastern European countries, were not members of the GATT at that time. Nevertheless, the trend in all these countries during 1994 and 1995 has been to join the WTO. Already Bahrain, Qatar and the United Arab Emirates, which have signed the Final Act of the Uruguay Round agreement, are applying for full membership in WTO. This could help the petrochemical industry in the ESCWA region to benefit from its competitiveness. These countries, when joining WTO, may negotiate the application of fair trade rules (national treatment, anti-dumping and subsidies by exporters and importers) on Arab petrochemical products. If successful, this may lead to the lifting of non-trade barriers, which could help ESCWA member countries to enhance their export production capacity. The unilateral actions that the EC has previously taken against imports of petrochemical products from the Gulf Cooperation Council (GCC) countries can be negotiated under the fair trade discipline of WTO.<sup>18</sup>

45. From a global perspective, the 1990s have brought overcapacity in the petrochemical industry. This glut is affecting the developing countries more than the developed countries inasmuch as the latter can move to the more protected domestic up-market, while the former must compete in the global overcapacity market in lower-end products.

46. Countries in the Gulf region have a comparative advantage in a specific constellation of petrochemicals that are feedstock-intensive since they have access to ample low-cost feedstock, an important source for these products. They have a comparative disadvantage in capital costs, mainly in relation to the high location factor cost. To the extent that low feedstock costs can mitigate against high capital costs, as the overcapacity in the industry diminishes with the global economic recovery, petrochemical exports from the ESCWA region are likely to grow faster than other developing countries' exports owing to their relative low feedstock cost advantage. Robust growth of close to 4.7 per cent could be expected in the SEM. Therefore, a 4.5 per cent growth of EU-ESCWA-region trade could be created, as the demand for petrochemicals usually moves in line with overall economic growth.

47. Currently, GCC countries' exports of petrochemicals to the EU are covered by certain arrangements under which petrochemicals are subject to tariffs ranging from 7 to 15 per cent until the EU completes the rationalization of its own petrochemical industries during the next 10 years. Beyond that, it is believed that this will improve export opportunities to regional petrochemical producers as long as they are able to maintain their international competitiveness based on low costs, and hence low prices, and updated technology.

48. Although the conclusion of the Uruguay Round agreements is, in principle, expected to liberalize trade in the ESCWA region's petrochemicals, to impose its integration into world trade requires serious negotiations and bargaining by the GCC countries to refute the arguments claiming that low-priced energy and feedstocks are forms of subsidy. Careful and in-depth comparative studies are needed to back up negotiations with the EU and other parties concerned in order to prevent measures against subsidized products and other measures provided for under international agreements from being used against the petrochemical industries of the ESCWA region.

---

<sup>18</sup> Although the GATT secretariat report on the evaluation of the UR (*The Results of the Uruguay Round*, 10 November 1994) indicated that a horizontal reduction in some petrochemical product items had been introduced, in-depth studies are needed to evaluate the impact of this reduction and its effects on items of petrochemical products in the Arab Gulf States and its impact on its comparative advantage under changing global conditions.

49. In negotiating within WTO, GCC countries should be able to base their position on a strong point, stressing the fact that gas, which is currently considered by the EU as low-priced, used to be flared up by major oil companies, a factor that leads to a reduction of the value of the gas for the producing Gulf countries as an energy source. Using it as a low-cost feedstock instead of flaring it up is reflected in the low cost of the final products. This is simply a reflection of a comparative advantage in natural endowment and cannot be interpreted as a form of subsidy.

### C. THE FOOD INDUSTRY

50. The food industry in the EU is a sizeable industry, employing 2.4 million workers. The food, drink and tobacco expenditure in the EU exceeded \$652 billion (486 billion European Currency Units [ECU]) in 1988 (in 1985 prices). The market grew by around 1.3 per cent per annum over the period 1980 to 1988. Developing countries have exported about \$24 billion (30 billion ECU) of food products to the EU in 1990, concentrated mainly in primary food commodities, such as oilseeds, fruit, coffee, cocoa, sugar and tea.<sup>19</sup>

51. The food industry in the EU is a highly State-regulated industry as it affects the public health and the environment. Import regulations range from marketing standards (packaging and labelling) to the quality of products (specific ingredients). These standards certainly make it difficult for ESCWA member countries and other developing countries to sell their high value added food products in the EU. In this way, these standards act as non-tariff barriers to exports from developing countries to the EU. In addition to these non-tariff barriers, there are import regulations that promote an overall industrial structure and protect employment in the EU. For example, the Common Agricultural Policy protects EU products from the temperate and Mediterranean zones. This deters exports from many Mediterranean ESCWA member countries. The EU Tariff Structure also discourages imports of value added processed products.<sup>20</sup>

52. The elimination of subsidies and trade barriers in agricultural products in the EU may tend to decrease levels of production of such products in the EU. This would encourage importation to the EU of agricultural products and related processed food products from non-EU countries. With respect to developing countries, including the ESCWA member countries, opportunities may arise to export agricultural products and related processed food products to the EU. Concerned countries in the ESCWA region need to identify those processed food products in which they have comparative advantage. However, competitiveness in the market will require a strict application of international standards, which requires a positive action by concerned Governments and producers in the region to ensure adherence to the required standards.

53. There is a rapid trend in the EU towards concentration, through mergers and acquisitions in production and distribution in this sector. Technological innovation has also modernized the industry. The vertical integration and the technological lead of firms in the EU have created new entry barriers for firms from ESCWA member countries and other developing countries.

54. The EU recognizes the importance of technological development in the food industry. Programmes have been set up to promote biotechnology (BRIDGE Programme) and agro-industrial (EULAIR and FLAIR programmes) and food technologies. The growth in the EPOS and EFTPS systems have provided retailers with updated retail sales information. Market demands have been changing rapidly. There are increasing trends towards health food, processed food, as well as food of higher quality and diversity, such as

---

<sup>19</sup> UNIDO, "The Food Sector", a paper submitted to the Expert Group Meeting on the Implications of the Single European Market for Industrialization in Developing Countries, Vienna, 18-20 March 1992 (UNIDO, Vienna, 9 March 1992) (ID/WG.523/2[SPEU]).

<sup>20</sup> Ibid.

delicatessen and ethnic foods. On the decline are the imports of staple commodities such as coffee, butter cereals and sugar.

55. The projected growth rate of the EU is at least 4.7 per cent.<sup>21</sup> As demand for food is income inelastic, based on an income elasticity of 0.5,<sup>22</sup> the trade creation effect of the SEM, and hence import demand for food products from the ESCWA region, should grow at no more than 2.4 per cent.

56. Trade diversion could occur as a result of changing health and environmental standards and of the harmonization of the value added tax. The effect is likely to be small<sup>23</sup> owing mainly to the fact that the bulk of developing countries' exports are of a primary commodity nature with little processing or value added.

---

<sup>21</sup> See note 17.

<sup>22</sup> M. Davenport and S. Page, *Europe: 1992 and the Developing World* (London, Overseas Development Institute, 1991).

<sup>23</sup> See estimations in UNIDO, "The Food Sector", a paper submitted to the Expert Group Meeting on the Implications of the Single European Market for Industrialization in Developing Countries, Vienna, 18 to 20 March 1992 (UNIDO, Vienna, 9 March 1992) (ID/WG.523/2[SPEU]).

### III. RECOMMENDATIONS

#### A. TRADE DIVERSIFICATION AND PRODUCT DIFFERENTIATION

57. The dependence on Europe for an export market and for the import of capital goods has increased the vulnerability of the ESCWA region's economies to changes and restrictions in the EU. There are important strategic advantages to diversifying a region's trade pattern, and to differentiating its products to the EU. An increase in trading partners other than those in the EU can increase the bargaining power as well as the elasticity of a country's offer curve with respect to the EU. In addition, an increase in the product differentiation of exports to the EU reduces direct competition with products from southern and eastern European countries. From the preceding discussion on intra-industry trade, differentiated products, particularly new specialty products, reduce trade friction inasmuch as the demand of each differentiated product after trade need not diminish. Exporters in the ESCWA region are strongly urged to diversify and differentiate their exports.

#### B. THE HUB-AND-SPOKE ALTERNATIVE

58. Even if one assumed that political factors rule out the possibility for countries in the ESCWA region to join the EU, a bilateral trade agreement between the ESCWA region and the EU is still possible in the short run. This fits into a hub-and-spoke model<sup>24</sup> where the EU is the centre (hub) with separate bilateral trade arrangements with countries outside the EU (spokes). Forming a new bilateral trade agreement with the hub will benefit the hub as well as the "new" spoke. Therefore, this is a viable alternative as long as there is no bilateral arrangement between the EU and another country with a particularly competitive trade structure. Since this will not be guaranteed, a bilateral agreement may not be feasible in the long run.

#### C. FORMATION OF A REGIONAL TRADE BLOC

59. A regional trading bloc among countries in the ESCWA region and others may be a feasible alternative. While a multilateral trade agreement under GATT or a more encompassing trade agreement with the EU is argued that either a better alternative, waiting for the slow arrival of these options may result in missed opportunities for the ESCWA region. Evidence<sup>25</sup> shows that regional bloc trade arrangements are generally quicker, more effective and more comprehensive, and they go well beyond the tariff-cutting exercise in multilateral negotiations. Formation of a regional bloc also improves the trade option and offer curve elasticity for ESCWA member countries. Upon the formation of regional blocs, bargain for more trade with the EU will be more fruitful. The GCC experience needs to be expanded to include other ESCWA members.

#### D. INVESTMENTS, R AND D AND THE TRAINING OF HUMAN RESOURCES

60. While allocation to R and D could, in certain manufacturing activities, focus on technology acquisition, adaptation and diffusion, the need in certain other manufacturing industries for innovative R and D aimed at the development of differentiated and new specialty products should be emphasized. Strategic joint ventures with European firms or direct investment in the EU (by ESCWA member countries, as Kuwait has already done) may prove fruitful inasmuch as it can consolidate their export market in the EU, avoid excessive protection, and benefit ESCWA member countries with the technology transfer. Joint ventures with

---

<sup>24</sup> Carsten Kowalczyk and Ronald Wonnacott, "Hubs and spokes, and free trade in America", Department of Economics, University of Western Ontario, Canada, Research Report 9209, September 1992.

<sup>25</sup> R. Dornbusch, "Dornbusch on Trade", *The Economist*, 4 May 1991, p. 65.

European R and D institutions should be considered an important step towards the promotion of innovative R and D. The training of human resources may risk the loss of skilled workers through emigration; it may not be cost-effective in the short run. However, it is still a worthy investment in the long run, as skilled workers may return to their home country, with their updated skills, whenever opportunities at home arise. Remittances from emigrants are also an important source of foreign earnings.

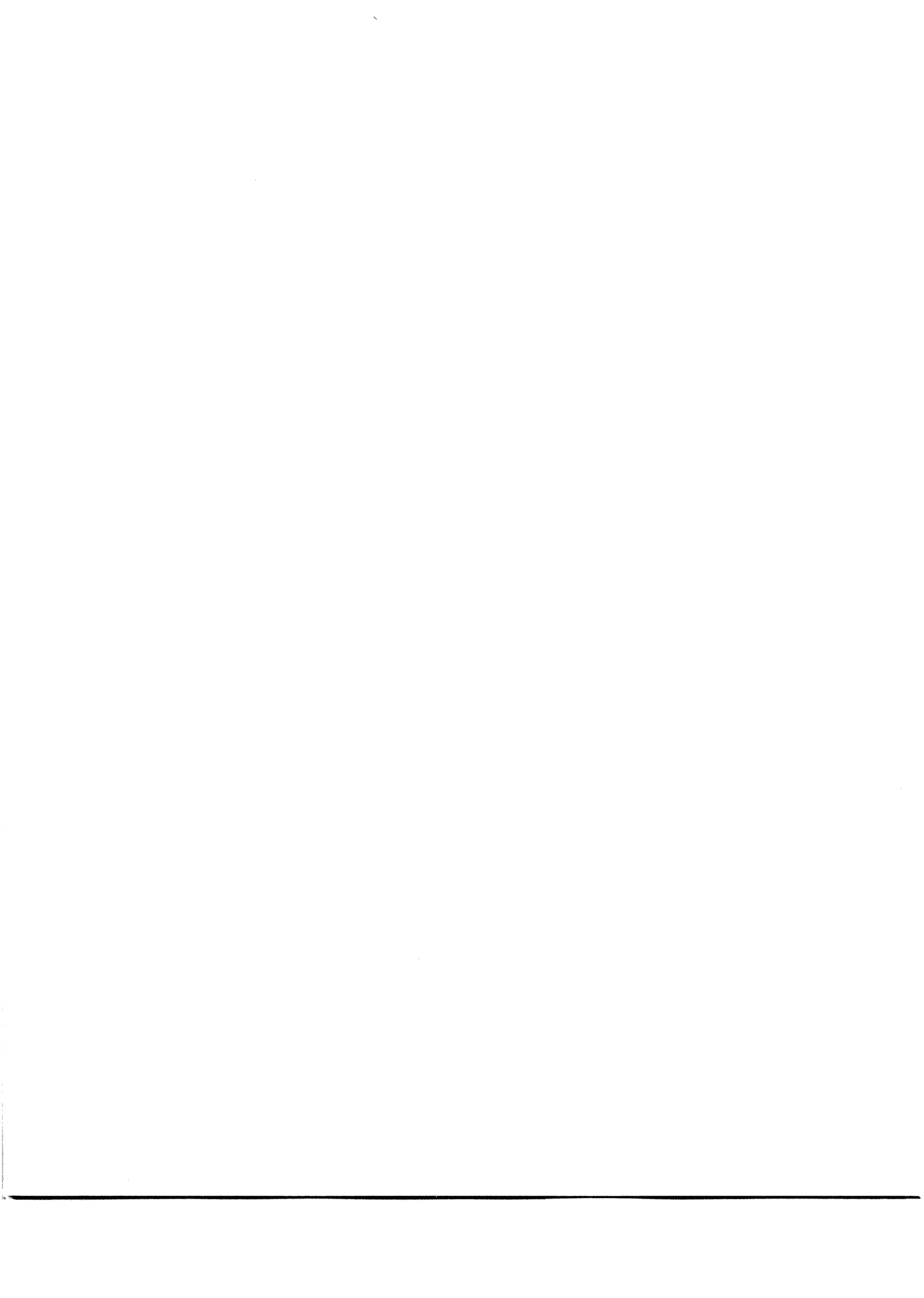
61. To offset the outflow of capital, skills and investments in the region, comprehensive and well coordinated regional industrial policies will be needed. Some of the policies used among emerging economies in South-East Asia to which it could be useful to refer are: capital subsidies, concessional loans, tax holiday, encouragement of conglomeration among important exporting industries and the creation of free-trade zones.

#### E. INCREASED FLEXIBILITY OF PRODUCTION IN TEXTILES

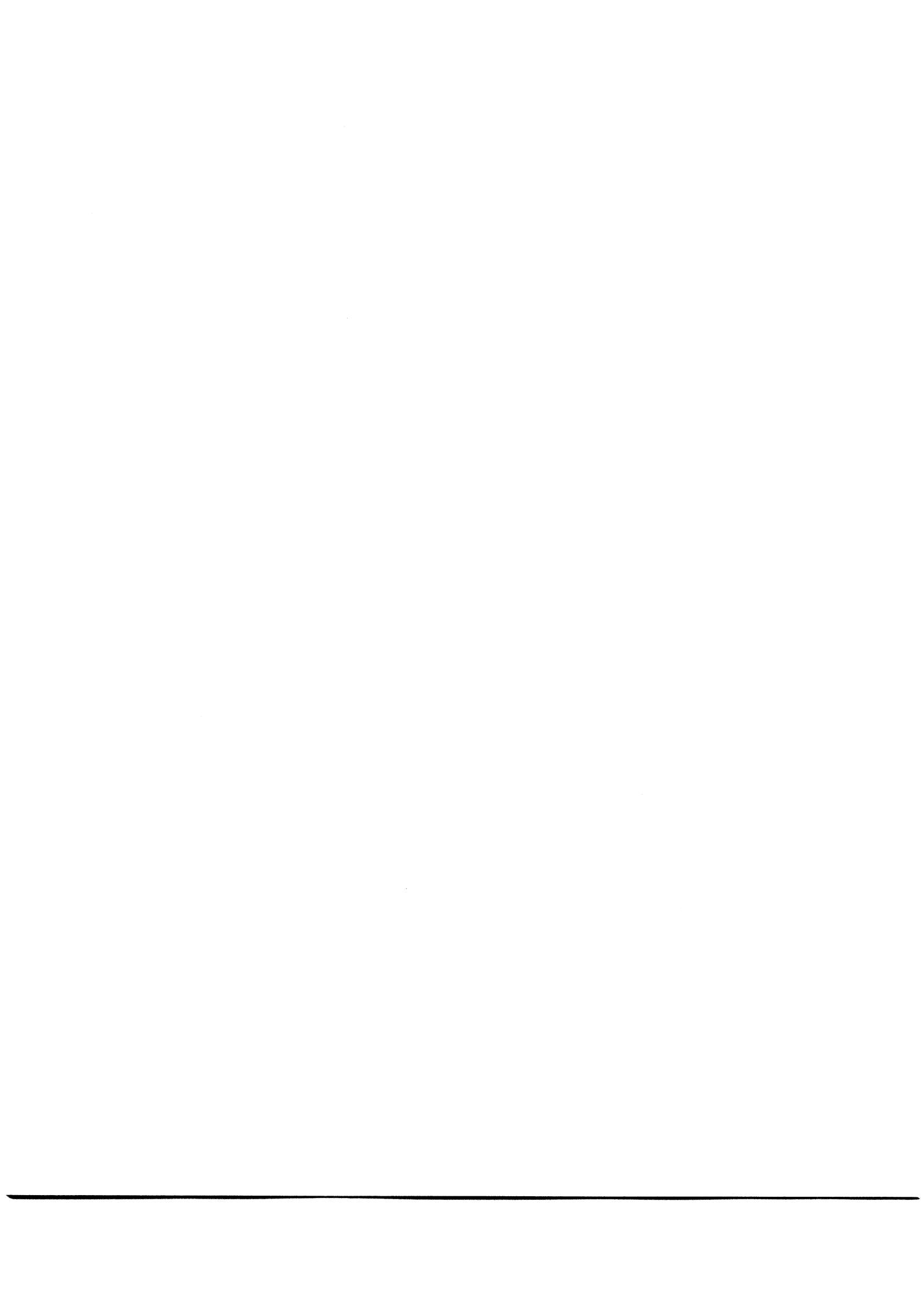
62. ESCWA member countries have to increase the flexibility of production of their textile and clothing industries to satisfy the changing tastes of the EU market, and forming joint ventures with European partners may give them secured access to that market and may make it possible for them to learn and import new technologies from the EU. With well developed petrochemical industries, though, the Gulf States may have a comparative advantage in the production of synthetic fibres, which may improve the competitiveness of the textile and garment industries in the region.

#### F. SPECIALIZING IN LOW-TECHNOLOGY AND LOW-POLLUTING PETROCHEMICAL PRODUCTS IN EU-ESCWA REGION TRADE

63. Countries of the GCC region should be able to take advantage of a comparative advantage in a specific constellation of petrochemical products that are feedstock-intensive. On the other hand, they should be able to capitalize on the advantage of their proximity to the market of the European Union, which possesses the highest demand for petrochemicals in the world. With the conclusion of the international trade agreements, new opportunities should be opened to producers in the region to expand their share of the EU market in petrochemicals. Since it is likely that the EU will protect the portion of its manufacturing production that is less harmful to the environment and it will likely liberalize its trade in goods whose production is more harmful to the environment, it may be opportune for some ESCWA member countries to specialize in low-technology petrochemical products in the EU-ESCWA region trade and to market more sophisticated products elsewhere.



## **ANNEX TABLES**





ANNEX TABLE 1. IMPORTS OF ESCWA REGION FROM EU,<sup>a/</sup> SELECTED YEARS  
(Millions of US dollars)

Country/year	1978	1979	1980	1987	1988	1989	1992
Bahrain	339	442	451	602	514	632	1,190
Egypt	2,328	3,139	4,310	4,325	4,263	4,058	4,533
Iraq	2,454	3,664	5,298	1,793	2,808	3,297	127
Jordan	498	729	957	1,223	1,176	938	1,010
Kuwait	1,660	1,841	2,052	1,629	1,648	1,818	2,106
Lebanon	771	1,126	1,430	717	1,013	929	1,668
Oman	391	634	550	815	975	816	1,142
Qatar	455	572	545	464	456	491	660
Saudi Arabia	7,224	8,595	9,888	8,912	8,909	9,525	12,683
Syrian Arab Republic	1,017	1,449	1,725	805	700	833	1,334
United Arab Emirates	2,051	2,442	2,890	2,786	3,418	4,150	5,566
Algeria	4,644	5,217	6,630	4,502	2,295	5,067	5,090
Indonesia	1,204	1,105	1,739	2,346	2,812	1,815	5,117
Venezuela	2,379	1,905	2,153	1,977	2,263	2,234	2,668
ESCWA1 <sup>b/</sup>	1,668	2,297	2,838	2,542	2,703	2,498	3,868
ESCWA2 <sup>c/</sup>	17,580	22,390	27,258	21,529	23,176	24,989	28,152
Total ESCWA	19,248	24,687	30,096	24,071	25,879	27,487	32,020

Source: IMF, *Direction of Trade Statistics*, various issues.

a/ EC statistics from 1987 to 1992 include Greece, Portugal and Spain in addition to original members.

b/ ESCWA1: Bahrain, Jordan and Lebanon.

c/ ESCWA2: includes ESCWA oil-exporting countries, namely, Egypt, the Syrian Arab Republic, Iraq, Saudi Arabia, Kuwait, the United Arab Emirates, Qatar and Oman.

ANNEX TABLE 2. EXPORTS OF ESCWA REGION TO EU,<sup>a/</sup> SELECTED YEARS  
(Millions of US dollars)

Country/year	1978	1979	1980	1987	1988	1989	1992
Bahrain	52	24	18	34	33	38	174
Egypt	536	928	1,301	771	787	1,124	2,641
Iraq	5,251	7,360	9,942	3,885	2,785	3,330	158
Jordan	4	4	7	48	69	45	58
Kuwait	3,514	5,939	5,052	2,611	2,132	2,570	795
Lebanon	41	60	68	91	125	109	101
Oman	209	306	718	271	336	153	170
Qatar	931	1,100	2,692	251	72	118	88
Saudi Arabia	11,763	18,807	32,917	4,499	5,364	5,452	11,358
Syrian Arab Republic	470	851	1,294	642	455	933	1,895
United Arab Emirates	2,824	3,653	5,937	1,439	719	1,459	1,698
Algeria	2,305	3,617	5,081	6,025	5,038	5,901	7,827
Indonesia	7,611	5,255	3,479	1,116	1,181	1,493	4,672
Venezuela	639	1,512	2,426	1,548	2,154	2,322	1,642
ESCWA1 <sup>b/</sup>	98	87	93	173	227	192	332
ESCWA2 <sup>c/</sup>	25,497	38,945	59,853	14,369	12,650	15,139	18,803
Total ESCWA	25,595	39,033	59,946	14,542	12,877	15,330	19,135

Source: IMF, *Direction of Trade Statistics*, various issues.

- a/ EC statistics from 1987 to 1992 include Greece, Portugal and Spain in addition to original members.  
b/ ESCWA1: Bahrain, Jordan and Lebanon.  
c/ ESCWA2: includes ESCWA oil-exporting countries, namely, Egypt, the Syrian Arab Republic, Iraq, Saudi Arabia, Kuwait, the United Arab Emirates, Qatar and Oman.

ANNEX TABLE 3. BALANCE OF TRADE BETWEEN THE ESCWA REGION AND THE EU,<sup>a/</sup> SELECTED YEARS  
(Millions of US dollars)

Country/year	1978	1979	1980	1987	1988	1989	1992
Bahrain	(347)	(418)	(433)	(568)	(481)	(594)	(1,016)
Egypt	(1,792)	(2,265)	(3,009)	(3,554)	(3,476)	(2,934)	(1,892)
Iraq	2,797	3,696	4,644	2,092	(23)	33	31
Jordan	(494)	(725)	(950)	(1,175)	(1,106)	(893)	(952)
Kuwait	1,854	4,098	3,000	982	484	752	(1,311)
Lebanon	(730)	(1,067)	(1,362)	(626)	(888)	(820)	(1,567)
Oman	(183)	(328)	168	(544)	(639)	(663)	(973)
Qatar	476	528	2,147	(213)	(384)	(373)	(572)
Saudi Arabia	4,539	10,212	23,029	(4,413)	(3,545)	(4,073)	(1,325)
Syrian Arab Republic	(547)	(598)	(341)	(164)	(246)	100	561
United Arab Emirates	773	1,211	3,047	(1,347)	(2,699)	(2,691)	(3,868)
Algeria	(2,339)	(1,600)	(1,459)	1,523	744	834	2,737
Indonesia	6,407	4,150	1,740	(1,230)	(1,631)	(322)	(445)
Venezuela	(1,740)	(393)	273	(429)	(109)	88	(1,026)
ESCWA1 <sup>b/</sup>	(1,570)	(2,210)	(2,745)	(2,369)	(2,476)	(2,307)	(3,536)
ESCWA2 <sup>c/</sup>	7,917	16,555	32,595	(7,161)	(10,526)	(9,850)	(9,349)
Total ESCWA	6,347	14,346	29,850	(9,529)	(13,002)	(12,157)	(12,885)

Source: IMF, *Direction of Trade Statistics*, various issues.

- a/ EC statistics from 1987 to 1992 include Greece, Portugal and Spain in addition to original members.  
b/ ESCWA1: Bahrain, Jordan and Lebanon.  
c/ ESCWA2: includes ESCWA oil-exporting countries, namely, Egypt, the Syrian Arab Republic, Iraq, Saudi Arabia, Kuwait, the United Arab Emirates, Qatar and Oman.

Standard International Trade Classification (SITC. Revised 3)		
Section 0		Food and live animals
Section 1		Beverages and tobacco
Section 2	Division 26	Textile fibres (other than wool tops and other combed wool) and their wastes (not manufactured into yarn or fabric)
Section 3	Division 33	Petroleum, petroleum products and related materials
Section 5	Division 52	Inorganic chemicals
Section 5	Division 57	Plastics in primary forms
Section 5	Division 58	Plastics in non-primary forms
Section 5	Division 59	Chemical materials and products, n.e.s.
Section 6	Division 65	Textile yarn, fabrics, made-up articles, n.e.s., and related products
Section 8	Division 84	Articles of apparel and clothing accessories

ANNEX TABLE 4. ESCWA REGION EXPORTS TO THE EU BY COMMODITY, 1978  
(Thousands of US dollars)

Country/division	0	1	26	33	52	57/58	59	65	84
Bahrain	132	9	0	43,750	0	26	0	194	221
Egypt	58,818	72	82,870	989,838	0	29	7	41,619	630
Iraq	9,030	4	1,096	5,736,954	0	0	7	228	10
Jordan	220	1	19	0	0	0	0	118	51
Kuwait	1,903	5	0	3,580,128	5,970	26	76	242	179
Lebanon	4,795	777	447	2,126	9	39	2	1,152	301
Oman	614	208	0	197,943	0	0	0	3	4
Qatar	123	2	52	950,553	838	6	0	75	32
Saudi Arabia	168	32	1,365	12,486,898	4	56	7	515	107
Syrian Arab Republic	3,846	68	60,715	553,427	15	0	25	2,116	1,316
United Arab Emirates	13	0	0	1,626,2	0	0	4	13	36

Source: OECD, *Foreign Trade by Commodities*, various issues.

ANNEX TABLE 5. ESCWA REGION EXPORTS TO THE EU BY COMMODITY, 1979  
(Thousands of US dollars)

Country/division	0	1	26	33	52	57/58	59	65	84
Bahrain	340	0	11	36,176	0	0	671	137	102
Egypt	77,010	0	85,396	1,553,668	543	66	1	84,203	5,291
Iraq	7,475	0	1,501	8,030,243	70	0	0	115	25
Jordan	382	0	31	0	0	54	16	82	119
Kuwait	543	0	0	5,884,287	0	61	19	989	55
Lebanon	2,507	0	1,091	9,872	34	39	59	1,840	493
Oman	47	0	0	163,960	0	0	0	4	21
Qatar	17	0	0	1,173,224	1,413	24	0	147	103
Saudi Arabia	495	0	227	18,693,187	665	38	42	608	650
Syrian Arab Republic	7,899	0	42,270	742,723	0	0	15	2,862	2,540
United Arab Emirates	28	0	28	2,416,253	0	116	0	67	13

Source: OECD, *Foreign Trade by Commodities*, various issues.

ANNEX TABLE 6. ESCWA REGION EXPORTS TO THE EU BY COMMODITY, 1980  
(Thousands of US dollars)

Country/division	0	1	26	33	52	57/58	59	65	84
Bahrain	57	17	0	49851	0	24	825	964	258
Egypt	91173	58	110854	2353016	0	0	13	90701	14425
Iraq	10601	0	459	10877349	181	0	105	50	10
Jordan	162	0	1033	0	29	0	0	561	129
Kuwait	257	0	0	4871328	3803	59	65	2006	360
Lebanon	4047	765	783	10	611	2	3	2057	1044
Oman	246	0	0	432903	0	0	21	4	8
Qatar	46	0	0	2006953	4491	0	292	112	81
Saudi Arabia	1327	38	84	33108287	237	10	189	1382	381
Syrian Arab Republic	3835	118	22553	1229612	23	0	60	4777	2853
United Arab Emirates	100	291	50	2915079	0	0	36	917	103

Source: OECD, *Foreign Trade by Commodities*, various issues.

ANNEX TABLE 7. ESCWA REGION EXPORTS TO THE EU BY COMMODITY, 1987  
(Thousands of US dollars)

Country/division	0	1	26	33	52	57/58	59	65	84
Egypt	84796	30	123044	1806199	53	72	2286	203487	27824
Syrian Arab Republic	1706	48	29613	551901	0	0	73	2729	954
Iraq	4754	6	5743	4010415	31	0	18	297	8
Saudi Arabia	35008	444	3271	5681745	953	109	2099	504	738
Kuwait	1359	19	3188	2861416	297	4	58	105	326
United Arab Emirates	6520	43	0	1016308	489	6	205	1006	1646
Qatar	267	0	0	218595	12916	0	3	223	188
Oman	2534	1	0	188322	0	1	58	278	180

Source: OECD, *Foreign Trade by Commodities*, various issues.

ANNEX TABLE 8. ESCWA REGION EXPORTS TO THE EU BY COMMODITY, 1988

(Thousands of US dollars)

Country/division	0	1	26	33	52	57/58	59	65	84
Egypt	92405	50	111099	1332696	75	20	7432	150990	37999
Syrian Arab Republic	1713	56	20642	370656	0	0	30	6217	1385
Iraq	4479	3	7179	2929608	223	0	244	946	72
Saudi Arabia	53865	117	2886	4912164	5682	449	1843	542	956
Kuwait	522	0	5713	2219423	50	6	37	472	261
United Arab Emirates	6223	22	161	530070	117	40	319	2623	9409
Qatar	160	0	0	44164	6768	43	222	276	157
Oman	8140	1	1	80353	4	1	36	49	348

Source: OECD, *Foreign Trade by Commodities*, various issues.

ANNEX TABLE 9. ESCWA REGION EXPORTS TO THE EU BY COMMODITY, 1989

(Thousands of US dollars)

Country/division	0	1	26	33	52	57/58	59	65	84
Egypt	75642	115	66000	2029657	108	352	9438	186189	49046
Syrian Arab Republic	5178	96	27264	741407	1	0	15	12235	4033
Iraq	3566	2	5954	3441119	3	2	5515	646	27
Saudi Arabia	48611	124	3249	6010626	4940	503	82	785	810
Kuwait	3083	0	3685	2729267	5315	22	60	353	314
United Arab Emirates	6569	6	228	1149616	1253	39	35	2190	38350
Qatar	276	0	0	97374	6075	18	0	210	230
Oman	10074	3	0	13985	6	7	24	167	488

Source: OECD, *Foreign Trade by Commodities*, various issues.

ANNEX TABLE 10. ESCWA REGION EXPORTS TO THE EU BY COMMODITY, 1992

(Thousands of US dollars)

Country/division	0	1	26	33	52	57	58	59	65	84
Egypt	126958	210	17475	1946029	5775	237	281	9288	23314	112766
Syrian Arab Republic	6624	39	68540	1737994	1	40	19	69	11593	45390
Iraq	433	0	0	45998	0	0	0	0	198	0
Saudi Arabia	6261	152	2209	10958	5798	12992	181	901	3349	1738
Kuwait	6428	0	2209	79681	487	53	5	11	374	378
United Arab Emirates	4012	376	272	94346	15	254	414	328	17323	192896
Qatar	223	40	0	40681	322	62	0	17	102	259
Oman	1431	0	0	0	3	59	53	2	2242	1774

Source: OECD, *Foreign Trade by Commodities*, various issues.