Trade Competitiveness and Growth in the MENA Region

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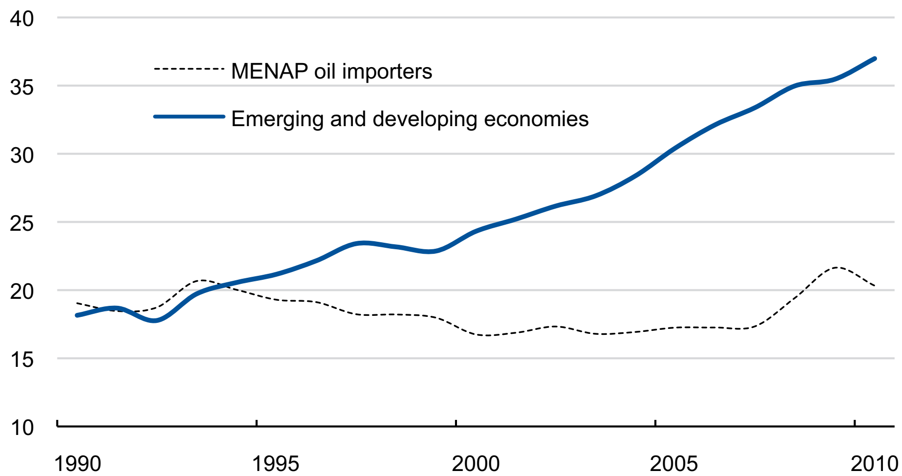
Lack of competitiveness means that the Middle East and North Africa (MENA) region is not realizing the full benefits of globalization.

Countries in the MENA[1] region on average score poorly on most indicators of competitiveness and, therefore, face difficulties competing in global export markets. This is evidenced by their relatively low export market shares: since 1990, the MENA region has only managed to maintain its share of global exports on a per capita basis, while other emerging and developing economies have succeeded in almost doubling theirs (Figure 1). A strong export performance is typically associated with high economic growth because exporters are able to not only tap domestic demand but also demand from other countries. Thus, with a stagnant export share, real per capita GDP growth in MENA has been lower than in emerging Asia for the past two decades (Figure 2). And, while there has been some pick up in growth since 2000 – prior to the 2008-2009 crisis – MENA countries were not able to create sufficient jobs for their growing populations, leaving unemployment rates among the highest in the world. In short, MENA's lack of competitiveness has prevented the region from realizing the full benefits of globalization for its population in terms of income and employment gains.

MENA has failed to increase its global market share in part because the region's exports flow mainly to Europe and are concentrated in traditional products.

Europe has been the main destination for MENA exports, reflecting proximity and long-standing linkages. Since the 1970s, the region's exports to Europe have accounted for close to 60% of total exports, while exports to Asia Pacific and Latin America, respectively, have accounted for 15% and 1% of total exports (Figure 3). Until the mid 1970s, the focus on European markets linked the region to an engine of global growth. But, more recently, this focus has implied that MENA has not been benefiting from the high growth rates achieved in emerging Asian and Latin American powerhouses, including Brazil, India and China.

Figure 1: Non-oil exports per capita (percent of world average)



MENAP Oil Importers include Djibouti, Egypt, Jordan, Lebanon, Mauritania, Morocco, Syria and Tunisia as well as Afghanistan and Pakistan

Source: IMF, World Economic Outlook; national authorities; and IMF staff calculations

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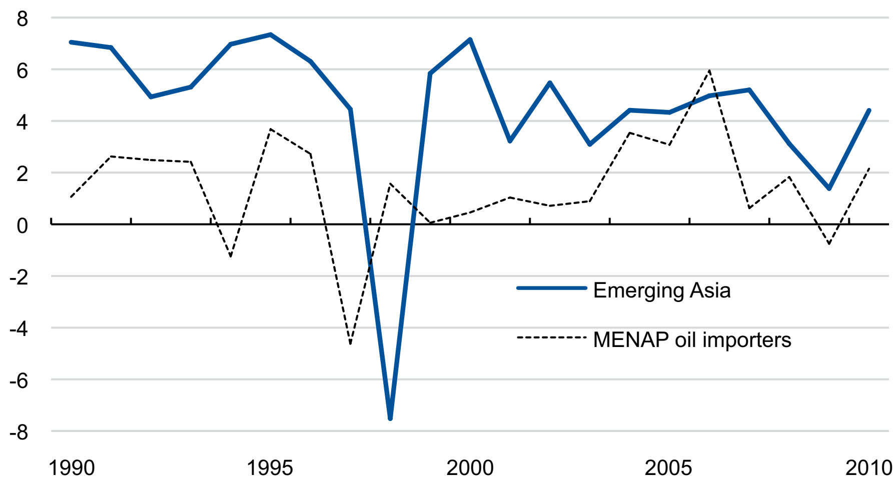
Figure 2: Real GDP per capita growth (annual percentage change)



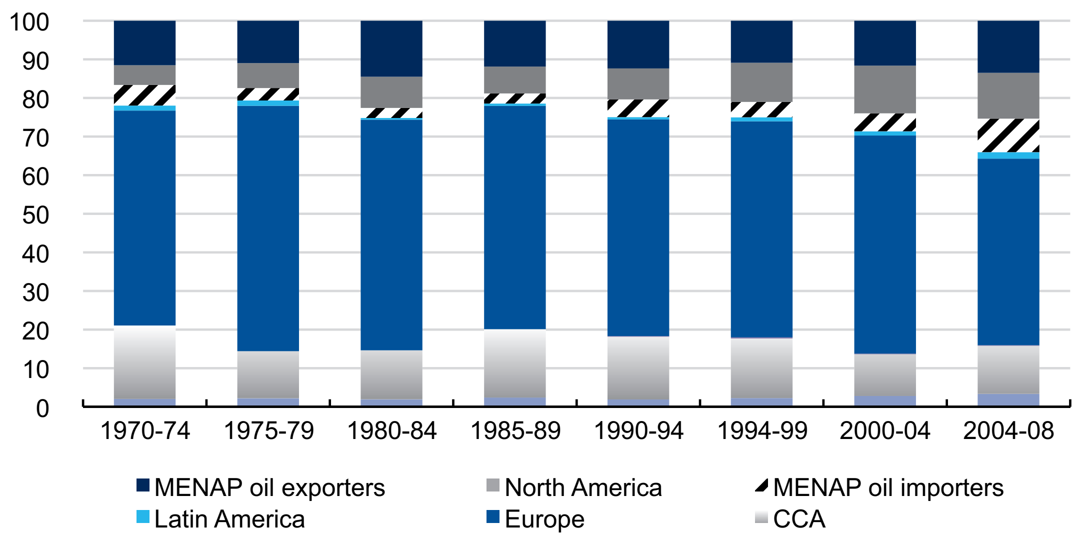
Source: IMF, World Economic Outlook; and IMF staff calculations

Looking ahead, there are some uncertainties over the speed of the recovery in Europe. Moreover, there is broad consensus that, over the medium term, growth in Europe will lag behind that of emerging Asia and Latin America. As such, it is even more important to redirect MENA's exports to these dynamic regions of the global economy to allow MENA to link more closely to the new growth engines and thus provide the basis for high and sustained growth in MENA countries as well.

MENA exports have also been mainly concentrated in primary and consumer goods, and less so in high value-added, high technology, intermediate and capital goods, which have seen the highest growth in recent years. Consumer and primary goods currently account for 64% of total exports in this region, compared to 41% for Asian countries, 57% for Latin American countries and 66% for African countries. Capital goods, on the other hand, account for only 6% of MENA exports – similar to the 7% in low-income countries – while they account for 37% of Asian exports and 11% of Latin American exports. These export patterns hold back MENA's potential for trade and, indeed, MENA countries trade less with the rest of the world than could be expected: MENA's total exports in 2009 amounted to only 28% of GDP, compared to 30% for Asia Pacific (Figure 4) – 56% when excluding the three largest economies, Japan, India and China, given that large economies typically have lower export shares.

A country's export volumes are partly driven by such characteristics as proximity to markets, tariff rates, existence of free trade agreements or cultural linkages with trading partners. However, these characteristics do not explain MENA's low export-to-GDP ratio – quite the opposite.

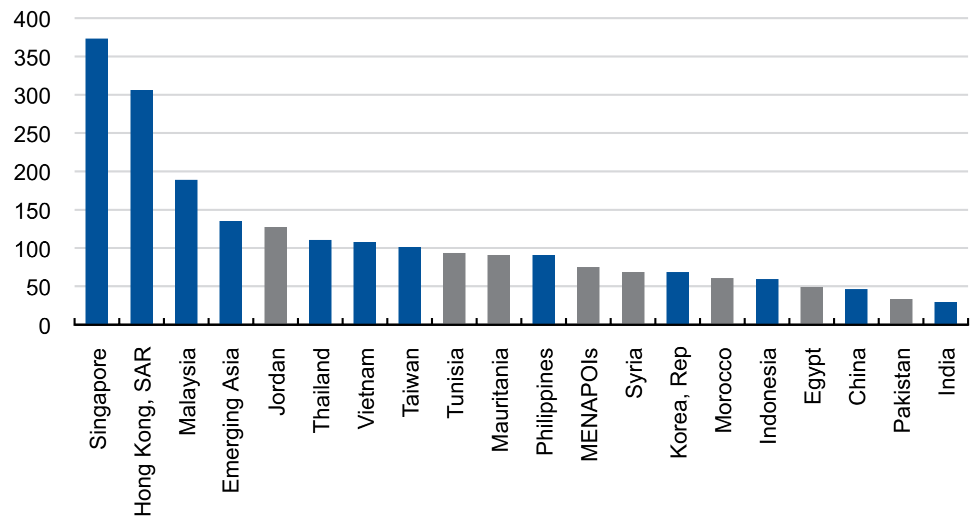
Figure 3: MENAP oil importers' export destinations 1970–2008 (percent of total exports)



MENAP oil exporters comprise Algeria, Bahrain, Iran, Iraq, Kuwait, Libya, Oman, Qatar, Saudi Arabia, Sudan, the United Arab Emirates, and Yemen. CCA countries comprise Armenia, Azerbaijan, Georgia, Kazakhstan, the Kyrgyz Republic, Tajikistan, Turkmenistan and Uzbekistan.

Source: IMF, Direction of Trade Statistics; and IMF staff calculations

Figure 4: Trade openness, 1990-2007 average (Percent of GDP)



Source: IMF, World Economic Outlook

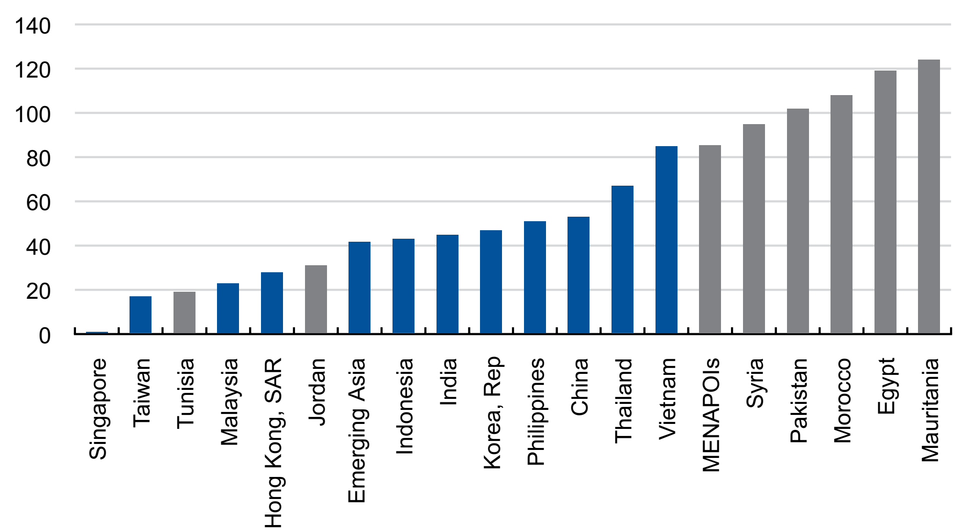
If MENA had seized the opportunities offered by these characteristics to the same degree that other middle-income countries do, its exports in 2008 would have been around 50% higher than they actually were. It is the lack of competitiveness compared to many of its peers that explains MENA's underperformance in trade.

Poor education outcomes, unfavourable business environments and overbearing governments are key reasons for MENA's lack of competitiveness.

As discussed in the previous chapter, education outcomes in MENA trail those of other countries, and workers do not have the skills that firms seek. Although enrolment rates in the region are not very different from those in other regions, the quality of education in MENA appears to be much lower than in regions with stronger export performance (Figure 5). Moreover, graduates in MENA do not have the skills that firms require to compete in today's global marketplace; unemployment is particularly high among graduates and the young, implying a mismatch between the types of skills supplied and demanded. This mismatch may, in part, be explained by the traditional role of governments as employer of first choice in the region, offering job security and good wages but not requiring qualifications sought by the private sector.

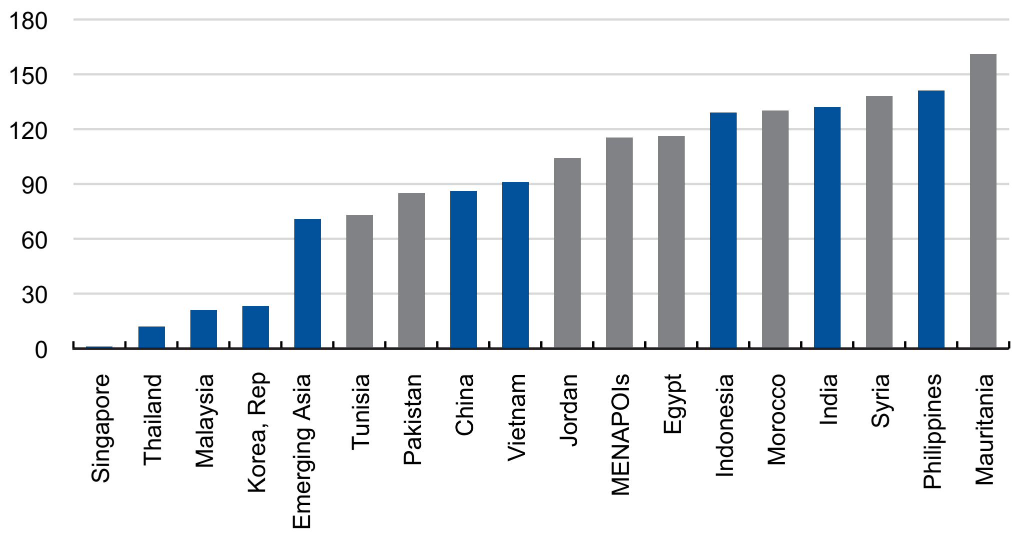
In addition, business environments are not sufficiently conducive to entrepreneurship or to fostering a dynamic private sector that can identify and exploit new business opportunities. According to the World Bank's "Ease of Doing Business" survey, MENA countries rank far below emerging Asia (Figure 6) suggesting that, in MENA, the regulatory and legal environment as well as basic

Figure 5: Education quality (latest ranking, 1 being the best)



Source: The Global Competitiveness Report 2009-2010

Figure 6: Ease of Doing Business (latest ranking, 1 being the best)



Source: World Bank, Ease of Doing Business

infrastructure, such as roads and utilities, have not kept up with developments in other countries. In addition, MENA governments spend more resources on consumption, including civil service wages and subsidies, and less on investment as a percentage of GDP than do their counterparts in emerging Asia.

Strengthening political cohesion and regional institutions would promote growth.

Advances in political cooperation and a larger role for regional institutions could impact economic activity in the region through two main channels. First, MENA countries could do more to facilitate intra-regional trade which would allow countries to specialize in their areas of strengths and yield a positive growth dividend. Second, by reducing internal trade barriers, the region would become a more integrated market and thus be more attractive to FDI which often seeks a large customer base.

But there are also success stories in the region.

To pick just two examples:

- Tunisia has become an "outsourcing hub" in the MENA region, having successfully attracted foreign direct investment in textile production, car assembly and food processing over the past several years and, more recently, in information technology (IT), customer service and aeronautics. Tunisia's car industry employs around 45,000 workers, and its aeronautical engineering industry is rapidly expanding, thanks in part to a deal with Airbus, whose first Tunisian plant becomes operational this year. To the extent that cars and airplanes, for which parts are produced in Tunisia, are exported to today's dynamic economies, this has allowed Tunisia to benefit from the growing demand of these emerging markets. Simplified regulation, modern infrastructure, government incentives and commitment to a knowledge-based economy that generates well-trained, low-cost workers, have contributed to this success. It is therefore no surprise that Tunisia scores better on competitiveness indicators - including openness, the business environment and education quality - than its MENA peers.
- Egypt has also attracted global IT investment from firms such as Microsoft, Oracle, Vodafone and IBM, and Egypt's IT exports have increased from US$ 250 million in 2005 to an anticipated US$ 1 billion by the end of 2010. Much of Egypt's IT industry is housed in the so-called "Smart Village" in Cairo, which currently employs 22,000 workers. This success has been achieved, despite Egypt's relatively low score on many competitiveness indicators, because of recent structural reforms that have led to improvements in the business environment and targeted government investments in infrastructure and language skills in the context of the "Smart Village" project.

Fostering trade competitiveness should boost growth and contribute to job creation.

The MENA region faces the sizeable challenge of having to create 18 million jobs for its growing labour force by 2020. High and sustained growth is a precondition for such large-scale job creation and for raising incomes. This, in turn, can be achieved by strengthening trade competitiveness so that the region can better benefit from globalization and the dynamics of today's high-growth regions. Improving education outcomes and ensuring that graduates acquire the skills needed by the private sector are key to attracting firms that can compete in the global marketplace. These firms also seek business friendly environments, calling for further streamlining of regulations and additional investments in infrastructure – including through public-private partnerships or by encouraging private sector investments – to increase the region's competitiveness. In this, the region can build on successes already achieved.

Endnote

[1] This note focuses on the MENA oil importers unless otherwise indicated. These include Djibouti, Egypt, Jordan, Lebanon, Mauritania, Morocco, Syria and Tunisia.