

EVENT SUMMARY

Prospects for Greater Global and Regional Integration in the Maghreb

**Peterson Institute for International Economics
Washington, DC**

May 29, 2008

The Maghreb countries—Algeria, Libya, Mauritania, Morocco, and Tunisia—could benefit greatly from enhanced integration within the region and with the global economy, notably with the European Union and the United States. Keynote speakers Deputy US Trade Representative John Veroneau and Assistant Secretary of State for Economic, Energy, and Business Affairs Daniel Sullivan both support the idea of greater regional integration as politically and economically beneficial for the development of the Maghreb region and for its ties to the global economy. John Veroneau gave an overview of the strong economic ties between the United States and the region, stating that the United States and Libya are very close to signing a Trade and Investment Framework Agreement (TIFA). Daniel Sullivan explained that a trade agreement between the United States and the Maghreb region as a whole would be a constructive step towards the Middle East Free Trade Area (MEFTA) proposed by President Bush. However, such an agreement is not currently being considered by the Administration. Ambassadors Aziz Mekouar of Morocco and Mohamed Nejib Hachana of Tunisia concluded the meeting and offered their support for greater regional and global integration.

Presenters in the first panel underlined the need for economic reforms, notably reducing tariff and nontariff barriers and creating a better investment climate through regulatory harmonization, to increase intraregional flows and raise the region's attractiveness to the global economy.

Feeble economic performance and the threat of political instability hurt the region's ability to attract trade and foreign direct investment (FDI). Political tensions between Maghreb countries are high, and countries have focused mainly on antiterrorism measures, to the detriment of economic reforms. Economic and political reforms need to go hand in hand to achieve stability in the region.

Regional initiatives have made little progress. Other regions, such as the Association of Southeast Asian Nations (ASEAN) and the Central American Common Market (CACM) are examples of successful regional integration with many of the same constraints faced by the Maghreb today, such as different economic development levels, internal resistance to liberalization, and political tensions between members.

Gravity model estimates show that EU and US bilateral free trade agreements (FTAs) with Algeria, Morocco, and Tunisia could yield trade gains of \$2 billion to \$3 billion concentrated mainly in the combined imports of the three major Maghreb countries (5 to

6 percent of Maghreb base imports). EU and US free trade areas would provide the largest trade gains. Total Maghreb trade could expand by \$4 billion to \$5 billion (3 to 5 percent) under the individual EU and US free trade areas, and by nearly \$9 billion (8 percent) if the EU and US free trade areas with the Maghreb countries were unified. These impacts could stimulate trade in ways not captured by the gravity model—for example, it could encourage greater Maghreb trade in services. The FTAs could also encourage the Maghreb countries to embrace a wider range of economic reforms.

The FDI impacts are similar in profile to the trade impacts. Inward FDI stocks would increase substantially more if closer economic ties were pursued by the Maghreb countries with either the European Union or the United States, rather than solely within the Maghreb. In the case of an EU-US-Maghreb free trade area, total Maghreb inward FDI stocks could increase by \$5.8 billion (75 percent).

A CGE model analysis finds that under an FTA between Maghreb countries, trade-creating effects are small. Bilateral agreements between Maghreb countries and the European Union have larger effects than between the Maghreb countries and the United States. An FTA between the European Union and the Maghreb region could increase Moroccan and Tunisian exports by 37 and 45 percent respectively. Results are smaller for a regional agreement with the United States. In the case of full liberalization, all gain would be from increased competitiveness and a depreciation of the real exchange rate leading to higher exports. The impacts of trade agreements on the Maghreb countries' terms of trade and national real income are negative. These findings are subject to important caveats related to the circumstances of the Maghreb countries, which have low levels of trade-related infrastructure, and the limitations of the CGE model, which does not account for the benefits of greater competition and possible increase in returns to scale under regional or wider economic integration, and does not account for FDI and trade in services. A dynamic model would likely yield greater benefits to openness. Experience shows that CGE models often significantly underestimate the true benefits of trade agreements on countries involved.

US-EU-Maghreb integration should transform the Maghreb economies to create new industries and services, more jobs, and faster growth. To that end, the United States and the European Union should work with their Maghreb partners on measures to enhance regional integration, either in the text of bilateral trade or investment agreements or in a companion agreement. Topics where the United States and the European Union should particularly encourage progress include tariff barriers, rules of origin, technical assistance and capacity building, and improving the efficiency of intraregional shipments.

The second panel presented analyses of the nontariff barriers in four of the major sectors: energy, banking and insurance, food processing, and transport.

North African countries display a wide variety of situations where their respective energy sectors are concerned, whether one considers availability, consumption levels, or the type of energy used. Energy accounts for a large share of the trade balance overall and this underlines the potential impact of excessive dependence. With the expected increase in

population and a rise in economic growth, we should expect greater energy consumption throughout the region, and thus a greater need for considerable investments. To face this challenge, the Maghreb should consider the following measures. First, it should optimize the use of existing infrastructure and reinforce it, in order to optimize investment while lowering the cost for each country and securing the energy supply for the whole region. Second, sustainable development, notably solar and wind energies, should be encouraged to limit environmental constraints and strengthen energy supply. Finally, the creation of joint ventures between the Maghreb and foreign companies, notably European ones, and Pan-North African joint ventures should be considered.

The banking sectors of the Maghreb countries also present notable differences, with Morocco leading on the path of reform. Microcredit and consumer credits have progressed, but capital risk does not play an important role. The percentage of people holding bank accounts in the region is extremely low. All banks are overliquid. There is a net outflow of capital from the region. High net worth individuals have little trust in the banking systems. The financial systems encourage the middle and lower middle classes to spend rather than save. Two-thirds of investments are self-finances and only 12 percent comes from bank credits, the lowest rate in the world. A regional financial institution with supranational powers could be set up to transform the unused liquidity into long term financial instruments of saving and investment, encourage and engineer mergers and acquisitions across the region, and ensure full convertibility of currency in order to attain complete transparency.

In the food sector, countries are close in distance and in agricultural productions, and share problems such as aridity, water scarcity, and volatility in agricultural GDP. Maghreb countries rely heavily on food imports, and intraregional trade is almost inexistent. Several measures could be implemented. Regional platform strategies, benefiting from economies of scale and similarities in consumption patterns, are already being used by companies such as Nestle or Danone and should be expanded. There are significant vertical integration opportunities based on complementarities in factor endowments and proximity. Innovation projects at the regional level would reduce the costs and risks of launching new products. Heterogeneity of rules should be reduced, as it acts as an incentive for smuggling and counterfeiting. Maghreb countries should also consider creating a common pool for regional resource conversation.

In the transport sector, much emphasis has been put on links between the Maghreb and the European Union, rather than networks within the Maghreb region. Transport infrastructure in the North African countries were largely built and operated by the state until the 1980s. Since the beginning of the 1980s, a series of reforms were implemented but failed to boost logistical efficiency. A closed border with idle infrastructure is an economic disaster. The large port infrastructure in Tangiers, which began operating in 2007, could become a regional hub facility once connected by rail to neighboring countries. An alliance grouping North African airlines could use the dense network in Casablanca to create a hub for the whole of Western and North Africa. But logistical gains will only happen if trade between the countries expands.