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The Challenge of Implementing the Overlapping Regional Trade Agreements in Egypt

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The Challenge of Implementing the Overlapping Regional Trade Agreements in Egypt

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بسم الله الرحمن الرحيم

Dedication:

To my parents

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List of Abbreviations

AD: Anti-Dumping

AL: Arab League

BTA: Bilateral Trade Agreement

CAPMAS: Central Agency for Public Mobilization and Statistics

CCC: Customs Cooperation Council

CIF: Cost, Insurance and Freight

CM: Common Market

CoO: Certificate of Origin

COMESA: Common Market for Eastern and Southern Africa

CU: Customs Union

CUSFTA: Canada-USA Free Trade Agreement

EC: European Community

EFTA: European Free Trade Association

EOQS: Egyptian Organization for Quality and Standardization

ESC: Economic and Social Council

EU: European Union

Euro-Med: European-Mediterranean Partnership Agreements

FDI: Foreign Direct Investment

FOB: Free On Board

FTA: Free Trade Area

FTAA: FTA of the Americas

GAFTA: Greater Arab Free Trade Area

GATS: General Agreement on Trade in Services

GATT: General Agreement on Tariffs and Trade

GCA: General Cooperation Agreement

GCC: Gulf Cooperation Council

GDP: Gross Domestic Production

GOEIC: General Organization of Export and Import Control

IPR: Intellectual Property Rights

MAFTA: Med-Arab Free Trade Area

MEDA: MESURES D'ACCOMPAGNEMENT

MENA: Middle East and North African

MERCOSUR: Mercado Común del Sur

MFN: Most Favored Nations

MU: Monetary Union

NAFTA: North American Free Trade Agreement

NTB: Non-Tariff Barrier

OECD: Organization for Economic Co-operation and Development

PTA: Preferential Trade Arrangement

RCA: Revealed Comparative Advantage

RoO: Rules of Origin

RTA: Regional Trade Agreement

SACU: South African Customs Union

SADC: Southern African Development Community

SPS measures: Sanitary and Phytosanitary measures

SRCA: Symmetric RCA

TBT: Technical Barriers to Trade

TRIPS: Trade-Related Aspects of Intellectual Property Rights

UAE: United Arab Emirates

USA: United States of America

WCO: World Customs Organization

WTO: World Trade Organization

German Summary

Deutsche Zusammenfassung

Die Herausforderung der Implementierung sich überlappender Regionaler Handelsabkommen in Ägypten

Über die seit 1995 bestehende Mitgliedschaft bei der Welthandelsorganisation (WHO) hinaus, ist Ägypten an mehreren Regionalen Handelsabkommen (RHA) beteiligt. So schloss sich Ägypten 1997 der Größeren Arabischen Freihandelszone (engl. *Greater Arab Free Trade Area* = GAFTA) und 1998 dem Gemeinsamen Markt für das Südliche und Östliche Afrika (engl. *Common Market for Eastern and Southern Africa* = COMESA) an; 2001 folgte der Beitritt zum Europäisch-Mediterranen Partnerschaftsabkommen (Euro-Med) und 2004 zum Aghadir-Abkommen. Von den 22 arabischen Ländern beteiligten sich 17 an der GAFTA, wobei eine Mitgliedschaft bei der GAFTA den fünf übrigen arabischen Ländern ebenfalls offen steht. Der COMESA besteht bisher aus 19 Mitgliedsländern, wohingegen der Euro-Med aus 10 mediterranen Ländern (einschließlich Ägyptens) und den 25 Ländern der Europäischen Union (EU) besteht. Ein entscheidender Schritt hin zur Einführung dieser Euro-Mediterranen Freihandelszone ist das Aghadir-Abkommen, ein Freihandelsabkommen zwischen Jordanien, Ägypten, Tunesien und Marokko, bei denen es sich gleichzeitig um Mitgliedsländer des Euro-Med handelt.

Ziel der Studie ist es,

1. die Kluft zwischen den Implementierungsplänen und der tatsächlichen Implementierung der ägyptischen RHA festzustellen, und zwar durch eine umfassende Analyse der vorhandenen Dokumente, die sich mit den vier verschiedenen RHA beschäftigen, sowie durch einen Vergleich zwischen diesen RHA;
2. das wirtschaftliche Potential der ägyptischen RHA auszumachen, und zwar mit Hilfe einer Revealed Comparative Advantage (RCA) - Analyse;
3. den Einfluss der institutionellen Faktoren auf die potentielle Implementierung der RHA zu berechnen, und zwar durch ein Gravitations-Regressionsmodell;
4. die wichtigsten institutionellen Faktoren, die die unzureichende und verzögerte Implementierung verursachen, auszumachen, und zwar anhand einer Analyse der

Ergebnisse verschiedener Interviews mit betroffenen ägyptischen Regierungsvertretern, Produzenten, Importeuren und Exporteuren; und

5. die Durchführbarkeit der sich überlappenden Ursprungsregeln (UR) der besagten RHA zu beurteilen, und zwar durch das Aufspüren und Analysieren der detaillierten Produktionsprozesse der wichtigsten ägyptischen Produkte, die für den Export in die Länder der verschiedenen RHA geeignet sind.

Die wichtigsten Schlussfolgerungen der Studie sind u.a. die folgenden:

1. Die unzureichende und verzögerte Implementierung der ägyptischen RHA sind nicht direkt auf organisierte Lobbys oder Ministerien zurückzuführen, die der Implementierung im Wege stehen, sondern eher auf das fehlende Bewusstsein für die potentiellen Vorteile der RHA, auf mangelhafte Institutionen, auf fehlende Anreize, und - in geringerem Maße - auf die sich überlappenden UR. Zum Beispiel ist das Aghadir-Abkommen bisher nicht in Kraft getreten, obwohl es einen erheblichen, positiven Einfluss auf die wirtschaftlichen Beziehungen der vier beteiligten Länder zur EU haben könnte.
2. In Bezug auf die möglichen statischen Gewinne der RHA belegt die GAFTA den ersten Rang, gefolgt von dem COMESA. Dasselbe gilt für die dynamischen Gewinne, da im Vergleich zum Euro-Med innerhalb dieser beiden RHA noch ein enormer, bisher ungenutzter Raum für Investition, steigende Konkurrenz sowie Größenvorteile gegeben ist. Dennoch trägt das Fehlen von geeigneten Institutionen in den an diesen beiden Abkommen beteiligten Ländern zur Verhinderung der angemessenen Implementierung bei.
3. Die institutionelle Qualität hat eine positive Auswirkung auf den Handelsverkehr, und hierdurch auf die eventuelle Implementierung der ägyptischen RHA.
4. Obwohl Ägypten als Mitglied mehrerer RHA grundsätzlich die UR als ein nicht-tarifliches Handelshemmnis in Betracht ziehen sollte, sind die meisten Rohmaterialien und Zwischenprodukte, die im Produktionsprozess der ägyptischen Produkte verwendet werden, ägyptischen Ursprungs. In den restlichen Fällen stammen diese aus der EU oder aber aus Ländern, die nicht Mitglied der ägyptischen RHA sind. Daher sind in diesem Zusammenhang die eventuellen Exportprobleme Ägyptens im Handel mit der EU geringer als im Rahmen von GAFTA und COMESA. Ferner könnte das Problem der UR in gewissem Maße in jedem RHA als eine separate Angelegenheit betrachtet werden, da in vielen Fällen die Rohmaterialien und Zwischenprodukte aus Asien stammen und

deswegen das diesbezügliche Überlappungsproblem zwischen den RHA, die diese Studie abdeckt, nicht zur Sprache kommt. Andererseits ist das vor Kurzem vorgeschlagene UR-Protokoll in der GAFTA nahezu identisch mit dem des Euro-Med. Nichtsdestotrotz haben die Mitgliedsländer der GAFTA diesem Protokoll bisher nicht zugestimmt, was ein wesentliches Hindernis auf dem Wege der vollständigen Implementierung des Abkommens darstellt.

Die Studie empfiehlt u.a. folgendes:

1. Die Verbesserung der Infrastruktur der in der ägyptischen Wirtschaft tief verwurzelten Institutionen, jedoch auch der Institutionen der Wirtschaften der übrigen an der GAFTA und dem COMESA beteiligten Länder, auch wenn dies eine langfristige Strategie erfordern würde. Zum Beispiel ist die ägyptische Wirtschaft darauf angewiesen, dass Bürokratieprobleme gelöst und flexible Marktsysteme geschaffen werden. Die Anreize und Motivationen der Handelsvertreter sollten verstärkt und gewisse Rigiditäten im Hinblick auf das Steuern- und Subventionssystem beseitigt werden. Zudem sollten die Garantiesysteme weiterentwickelt werden, um die Sicherheit der Importeure und Exporteure zu gewährleisten, was automatisch einen positiven Einfluss auf den Handelsverkehr haben würde.
2. Die Verstärkung der Verbindungen zwischen den Ländern der betroffenen RHA durch mehr Informationen, Netzwerke und moderne Transportsysteme.
3. Die Harmonisierung zwischen den wirtschaftlichen Binnenpolitiken der Mitgliedsländer der verschiedenen RHA.
4. Die Mobilisierung der ägyptischen Investitionen in Frachtfirmen, um die Transportprobleme zu lösen.
5. Die volle Nutzung der finanziellen und technischen Hilfsprogramme, die seitens der EU angeboten werden. Dies würde den Handel nicht nur mit den EU-Ländern, sondern auch mit den restlichen Handelspartnern intensivieren.
6. Die Nutzung der ähnlichen Produktionsstrukturen zwischen Ägypten und den restlichen GAFTA- und COMESA-Ländern durch die Diversifizierung und Spezialisierung der Produkte, um niedrigere Kosten und weltweite Wettbewerbsfähigkeit zu erreichen.
7. Den Beitritt der restlichen GAFTA- und COMESA-Länder zu gemeinsamen Freihandelszonen mit der EU und die Befolgung der UR der letzteren, zumal diese im Vergleich zu den anderen deutlicher, detaillierter und umfassender formuliert sind.

Abstract

Beside its membership (1995) in the World Trade Organization (WTO), Egypt joined Regional Trade Agreements (RTAs) such as the Greater Arab Free Trade Area (GAFTA) in 1997, the Common Market for Eastern and Southern Africa (COMESA) in 1998, the European-Mediterranean Partnership Agreement (Euro-Med) in 2001 and the Aghadir Agreement in 2004. The study attempts to recognize the gap between the implementation plans and the real implementation of the Egyptian RTAs; to identify the economic potential of these RTAs; to find out the impact of institutional factors on the potential implementation of the RTAs; to identify the institutional factors behind the weak/delayed implementation; and to assess the applicability of the complex Rules of Origin (RoO) of the overlapping RTAs.

The main results that the study demonstrates are the fact that the delayed implementation of the Egyptian RTAs cannot really be referred to organized lobbies or to certain ministries who would officially object the RTAs but rather to the missing awareness of the potential benefits of the RTAs, the weak institutions, the low incentives and - to a lesser extent - the overlapping RoO. GAFTA and COMESA can have a very high potential concerning the static as well as the dynamic effects, since there is still a huge unutilized space for investment stimulation, increased competition and economies of scale within both RTAs as compared to the Agreement with the European Union (EU) countries. The institutional quality has a positive impact on trade flows, and hence, on the potential implementation of the Egyptian RTAs. Although the RoO can indeed be regarded as a Non-Tariff Barrier (NTB) for Egypt as a common country in Euro-Med, COMESA and GAFTA, most of the inputs that are used in the Egyptian products originate in Egypt, in the EU or in countries other than GAFTA or COMESA. Therefore, the RoO problems that Egypt faces when exporting to countries of Euro-Med are far less than exporting to countries of the two other RTAs.

The study suggests improving the institutions deeply rooted in the economies of Egypt and the GAFTA and COMESA countries in general; strengthening the linkages between the countries of the different RTAs through better networking systems; fulfilling deep integration by harmonizing the domestic policies of the different RTA member countries; mobilizing the Egyptian investors for investing in freight companies in order to contribute in solving the transportation problems;

radically solving the enormous bureaucracy and red tap obstacles; making use of the financial and technical assistance program offered by the EU in the frame of Euro-Med; overcoming the rigidities in the Egyptian economic system by introducing more transparent exchange rates, export subsidies towards higher quality products, and a tax system that encourages the production and exportation; diversifying and specializing within the Arab and African products; and unifying the GAFTA and COMESA RoO such that they comply with the Euro-Med RoO which are based on more detailed, concrete and clear tariff line definitions.

Introduction

1. Egypt as a member of different RTAs

The Arab Republic of Egypt is a country located at the crossroads between Europe, the Middle East and Africa. It has always acted as a major link between these regional markets and their access to Asia, especially since the construction of the Suez Canal in 1869, which connects the Red Sea with the Mediterranean.

Egypt is therefore considered an Arab, Middle Eastern, African and Mediterranean country. As an Arab country, Egypt has played a leading political, economic and cultural role in the region. The Arab League (AL) that brings the 22 Arab countries together was established 1945 in Cairo. As a Middle Eastern country, Egypt has played a leading role in the peace process in the Israeli-Palestinian conflict and has signed 1978 the Camp David Peace Treaty with Israel. As an African country, it has also been influential, since over the years it has participated in dispute resolutions between different African countries. As a Mediterranean country, it has played an important role for European countries who were seeking market access to Africa and Asia. Egypt also makes a link between Mashrek (Eastern) and Maghreb (Western) countries of the Arab region (Egypt, Country Profile, 2005).

These different regional classifications were an important reason why Egypt has been involved in several Regional Trade Agreements (RTAs) besides its membership (1995) in the World Trade Organization (WTO). For example, Egypt joined the Common Market for Eastern and Southern Africa (COMESA) in 1998, being hereby the 19th member of the Agreement. An initiative that took place 1995 during the Barcelona Conference lead to the establishment of European-Mediterranean Partnership Agreements - also called Euro-Med - between European countries on one hand and Mediterranean countries on the other. This Agreement aims at a Free Trade Area[1] (FTA) between all the signatory countries of both sides in 2010. Egypt signed in 2001. In order to facilitate the Partnership Agreements between the European Union (EU) and four Arab countries including Egypt, the Aghadir Agreement was signed in 2004 and was supposed to lead to an FTA in 2005. Last but not least, 17 Arab countries including Egypt are part of the Greater Arab Free Trade Area (GAFTA) which aimed in the year 1997 at establishing an FTA by the year 2007 that

[1] The exact meaning of the Free Trade Area is to be elaborated in section 1.1.

was later accelerated to the year 2005. As will be elaborated in detail, RTAs have different degrees of economic integration, where the Monetary or Currency Union - like the case of COMESA - is the most sophisticated one, whereas in the case of FTAs - like the three other Agreements - , movement of goods within member countries is - under certain conditions - exempted from tariff barriers and every country keeps its right to impose its own tariffs on the rest of the world.

2. A brief historical background of RTAs

In an opening sentence of a Working Paper by *Crawford and Fiorentino* (2005) they state that "RTAs are a major and perhaps irreversible feature of the multilateral trading system"[2]. Till June 2005, 312 RTAs had been notified to the General Agreement on Tariffs and Trade (GATT)/WTO, and 196 of these were in the decade after the establishment of the WTO in January 1995. Between January 2004 and February 2005 alone, 43 RTAs have been notified to the WTO, which made this period the most abundant one in the history of RTAs (Pomfret, 2006). These numbers are even underestimated, since some RTAs under negotiation have not yet been notified to the WTO and others are among non-WTO members[3]. Therefore, it has become a stylized fact of the world trading system that regionalism is growing at an accelerating rate.

Except for Mongolia, all the WTO member countries are part of RTAs. According to *Crawford and Fiorentino* (2005), for some of these members preferential trade represents over 90 percent of their total trade. *Schiff and Winters* (1998) state that "some 55 to 60 percent of world trade now occurs within such trading blocs"[4]. These percentages hint to the fact that the Most Favored Nations[5] (MFN) treatment required by the WTO's is in reality applied only on 10-50 percent of the world trade (Pomfret, 2006).

[2] Crawford, Jo-Ann, and R. Fiorentino (2005) 'The Changing Landscape of Regional Trade Agreements', WTO Discussion Paper No.8, World Trade Organization, Geneva, p. 1

[3] At the same time, the cumulative WTO counts overestimate the number of RTAs, since they do not consider the RTAs that have been ceased.

[4] Schiff, Maurice and L.A. Winters (1998) 'Dynamics and Politics in Regional Integration Arrangements: An Introduction', *World Bank Economic Review 12(2)*, p. 178.

[5] An agreement according to which the signatories agree to accord each other the same favourable terms that are offered in agreements with any other nation.

3. Research problem

When studying the membership of one country in different RTAs, one should consider the political motivations and pressures that the country is subject to. In many cases, there is no other choice for the country than getting integrated in such RTAs. This has been the general trend for the past decades. In such case, the country should attempt to make the best out of these RTAs in accordance with its own interests. For example, Egypt needs the financial and technical assistance of the developed countries, such as the EU. Being part of a Partnership with these countries is supposed to facilitate the access to their markets as well as their technology and know-how.

In general, the economic benefits of Bilateral Trade Agreements can be well determined and the implementation is a simple task compared to RTAs that include several countries. It is argued that the RTAs that Egypt is part of were signed due to political rather than economic reasons. Hence, no real assessment of expected trade creation/diversion was run before signing the Agreements. Moreover, many of the RTAs have only been weakly implemented, if at all.

In addition to the difference between the announced tariff reductions and the implemented ones, there are still significant Non-Tariff Barriers (NTBs) across member countries in all the RTAs.

Each of the RTAs includes a different set of Rules of Origin (RoO). The co-existence of multiple RoO is inconvenient for both exporters and producers who may be unable to achieve any benefits from the preferential treatment granted by all these RTAs.

The reasons behind not implementing the Agreements properly might be lobbies/interest groups protecting local producers and hindering proper implementation; resistance of the government, due to a loss of revenue (tariff collection); the lack of common policies and standards among countries that have signed these RTAs; conflicting interests between different ministries, stakeholders, etc. within one member country (in this case, Egypt); the RoO overlap and/or the high transaction and administrative costs incorporated with the RTAs; and/or the economic worthlessness of the RTAs, leading in turn to the lack of incentive for implementing them.

4. Research objectives

1. To recognize the gap between the implementation plans and the real implementation of the Egyptian RTAs.
2. To identify the economic potential of the Egyptian RTAs.
3. To find out the impact of institutional factors on the potential implementation of the RTAs and the institutional factors behind the weakness/delay of implementation.
4. To assess the applicability of the complex RoO of the overlapping RTAs.

5. Research questions

1. What is the status/degree of implementation of the four RTAs that Egypt is member of?
2. What is the impact of the RTAs on trade creation/ trade diversion and what are their expected static, dynamic and institutional effects on Egypt?
3. To what extent do the institutional factors affect the implementation of the RTAs?
4. Do the RoO of the signed RTAs conflict and how would this affect/constrain the implementation process?

6. Research hypotheses

1. There is a gap between what the signed RTAs entail and what is implemented in reality.
2. COMESA, GAFTA and Aghadir are not less trade creating than Euro-Med, thus, there must be other problems making Euro-Med apparently more advantageous so far.
3. Institutional factors have a significant effect on implementing the RTAs, and therefore, GAFTA, COMESA and Aghadir which lack the good institutions seem to be less advantageous than Euro-Med.
4. The complex RoO are an obstacle on the way of implementing the overlapping RTAs that Egypt has signed, due to:
   -Contradicting and hence, inapplicable rules.
   -Institutional problems associated with RoO.

7. Research methodology

1. In order to recognize the gap between the implementation plans and the real implementation of the Egyptian RTAs, a comprehensive analysis of the available documents of the RTAs and a comparison between them is run.
2. In order to identify the economic potential of the Egyptian RTAs the study relies on the trade creation/diversion criteria and uses hereby a Revealed Comparative Advantage analysis.
3. In order to find out the impact of institutional factors on the eventual implementation of the RTAs a gravity regression model is used, where the key variables are the institutional factors existing in the different countries of the RTAs of study. In addition, a descriptive analysis, based on interviews with Egyptian government officials, producers, importers and exporters is run, in order to find out the institutional factors behind the weakness/delay of implementation.
4. In order to assess the applicability of the complex RoO of the overlapping RTAs the detailed production processes of the important Egyptian products that are exported to the countries of the different RTAs are traced, taking into account the necessary inputs and raw materials used in the production.

8. Time, geographic and product coverage of the research

Although the RTAs that Egypt has signed include other countries, in general, the main focus of the study is on Egypt and its implementation of these RTAs as a case study. The starting year for the study period is 1994, where the first RTA that Egypt joined (COMESA) was signed.

In order to have a sufficient number of observations, the gravity regressions include all the countries of the RTAs that Egypt is part of in addition to the member countries of the WTO. The year of estimation is the year 2002, where there is a database available for the most important institutional factors existing in the countries of the RTAs and that might have an influence on the trade among them.

The Revealed Comparative Advantage analysis comprehends 240 commodities produced and traded in the countries of the RTAs, based on the Standard International Trade Classification.

The RoO analysis concentrates on the twenty most important products that Egypt exports to the members of each RTA.

9. Research limitations

Due to time and financial constraints, it was not possible to run the interviews with government officials, local producers, importers and exporters in countries of the RTAs other than Egypt.

Originally, it was planned for the dependent variable of the gravity regressions to be the exact degree of implementation of the RTAs, in order to find out to which extent this variable would be influenced by the institutional factors. However, running the regressions with a discrete dependent variable based on the subjective and diverse opinions of the government officials could end up with misleading results, especially that the problem of lack of information and transparency is widespread in Egypt and within many of the member countries of the RTAs. Therefore, the trade flows between the member countries is taken as a proxy for the potential implementation of the RTAs. Nevertheless, the evaluation of the government officials is still considered as a supporting outcome of the study.

The institutions included in the gravity model are based on a certain index. However, there are other institutions that are hard to measure but which might play a more significant role. In an attempt to lessen this limitation, these institutions are dealt with in a descriptive approach in a chapter of the study specified for this aim.

Chapter 1 gives a theoretical background about some important concepts related to RTAs, such as trade diversion, trade creation, RoO, and institutional aspects associated with international trade. *Chapter 2* attempts to identify the differences between the four RTAs that Egypt is member of and the status of their implementation. *Chapter 3* deals with the static, dynamic and institutional effects that might have an influence on Egypt as a consequence of its membership in the different RTAs. *Chapter 4* demonstrates the important institutional obstacles hindering the full implementation of the signed RTAs. *Chapter 5* measures the impact of the institutional quality on the trade flows between the different countries of the RTAs. *Chapter 6* assesses the applicability of the complex RoO of the RTAs and the extent to which their overlapping could constrain the implementation. Finally, *Chapter 7* presents the concluding remarks of the study.

CHAPTER 1

Theoretical Background

It would be necessary to shed some light on a number of concepts and definitions that will be used in this study, such as the different degrees of economic integration, especially that the four RTAs that this study is concerned with do not have the same degree of integration as a target. The problems associated with signing a network of different RTAs is also an important point that should be raised, since the study is concerned with the overlapping RTAs and their institutional problems. And since the study focuses on the RoO as an important non-tariff barrier of trade, a section is devoted to this concept. Another important concept that is introduced and which is highly associated with RTAs and RoO is trade creation/ trade diversion. In addition, this chapter gives a theoretical background about the potential institutional problems associated with signing and implementing RTAs.

1.1. Degrees of Economic Integration

The theory of economic integration refers to the commercial policy of discriminatively reducing or eliminating trade barriers only among the nations joining together (Salvatore, 1998). The degree of economic integration takes different forms that could range from Preferential Trade Arrangements to Free Trade Areas, Customs Unions, Common Markets, and Economic Unions.

In the *Preferential Trade Arrangements (PTAs)* there are usually lower tariff barriers on trade among participating nations than on trade with non-member nations. This arrangement, which usually refers to only one or a few products, could be considered as the most flexible form of economic integration. The British Common Wealth Preference Scheme, established in 1932, is the best example of a PTA.

In a *Free Trade Area (FTA)* all tariff barriers among members are removed from all goods. However, each nation keeps its own tariff barriers to trade with non-members. A good example is the European Free Trade Association (EFTA), formed in 1960 by the United Kingdom, Austria, Denmark, Norway, Portugal, Sweden, and Switzerland (Finland joined later in 1961). One other

good example is the North American Free Trade Agreement (NAFTA) formed by the United States of America (USA), Canada, and Mexico in 1993.

A *Customs Union (CU)* is an association of nations to promote free trade within the union and set common tariffs for nations that are not members. The most famous example is the European Community (EC), formed in 1957 by West Germany, France, Italy, Belgium, the Netherlands, and Luxembourg.

A *Common Market (CM)* further allows free movement of labor and capital among member nations. At the beginning of 1993, the EU achieved the status of a CM.

The most advanced type of economic integration is the *Economic Union*, where the monetary and fiscal policies of member states are harmonized and sometimes even completely unified. An example is Benelux, which was the Economic Union of Belgium, the Netherlands, and Luxembourg, formed after the Second World War. The extreme case of an Economic Union could be a *Monetary Union (MU)*. A good example for the former is the countries of the EU who use a single currency, the Euro.

An important factor is the extent to which the RTA enhances the credibility of the government's commitment to liberalize the economy and maintain an outward-oriented and investment-friendly policy stance.

1.2. The static effects of implementing the RTAs

The *static effects* of forming an FTA are measured in terms of trade creation and trade diversion. *Trade creation* takes place when part of the domestic production in a country which is a member of the FTA is replaced by lower-cost imports from a member country in the same FTA. This is supposed to increase the welfare of member countries, since it leads to greater specialization in production based on comparative advantage. A trade-creating FTA can also increase the welfare of non-member countries, as some of the increase in the real income of the FTA (as a result of greater specialization in production) can spill over into an increased volume of overall imports from the rest of the world.

Trade diversion takes place when lower-cost imports from outside the FTA get replaced by higher cost imports from an FTA member. This may result due to the preferential trade treatment given to member nations of the agreement. In that case, welfare is reduced, since trade diversion shifts production from more efficient producers outside the FTA to relatively less efficient producers inside it. Hence, trade diversion negatively affects the international allocation of resources and accordingly shifts production away from comparative advantage.

This could be regarded as a good example of the theory of the *second best* (Lipsey and Lancaster, 1956), which states that 'if all the conditions required to maximize welfare cannot be satisfied, trying to satisfy as many of these conditions as possible does not necessarily (rather usually) lead to the second-best position'. Hence, forming an FTA and removing trade barriers only among the members might not always lead to the second-best situation, due to the fact that welfare could rise or fall.

According to *Salvatore* (1998)[6], an FTA is more likely to lead to trade creation and increased welfare under the following conditions:

1. The more competitive - rather than complementary - the economies of the member countries, the greater are the opportunities for specialization in production and trade creation with the formation of the FTA. Thus, the latter is more likely to increase welfare if formed by countries with similar production and export structures.
2. The greater the pre-FTA trade and economic relationship among potential members of the agreement, the greater would be the opportunities for welfare gains after forming the FTA.
3. The shorter the geographic distance between the member countries of one FTA, the less of an obstacle to trade creation among members would the transportation costs represent.
4. The greater the size of the FTA, i.e. the number of countries forming it, the greater would be the probability that low-cost producers are part of the agreement, leading in turn to more trade creation.
5. The higher the pre-FTA trade barriers between member countries, the greater is the probability that its formation will pay off and be rather trade-creating for the members.

[6] Salvatore's work was to a certain extent based on Viner's (1950) arguments that were also reviewed extensively by Bahadir (1984).

6. The lower the FTA's barriers on trade with the rest of the world, the less likely will the formation of the FTA lead to trade diversion.

For example, the reasons why the success in the case of the EU was greater than in the case of EFTA could be referred to the fact that the countries forming the EU were much more competitive than complementary.

1.3. The dynamic effects of implementing the RTAs

The modern international trade literature suggests that *dynamic effects* of an economic integration depend primarily on increased competition, economies of scale and stimulus to investment. The former takes place through two effects associated with the establishment of FTAs (Baldwin et al., 1995). The first effect, known as investment creation, results from the increase in domestic and foreign direct investment to benefit from expanded markets generated by regional integration. The second effect, known as investment diversion, results from redirecting investments from non-member to member states.

1.4. The overlapping RTAs

The configuration of RTAs is diverse and becoming increasingly more complex with overlapping RTAs spanning within and across continents at the regional and sub-regional levels. More complex are those agreements in which one of the partners is involved in another or other several RTAs.

1.4.1. Problems associated with overlapping RTAs

1. Countries with membership in several RTAs might be interesting for foreign investors, but the latter are often also deterred by the complexity of trade regulations that arises due to different RTAs, especially when these include too many NTBs. While RTAs are supposed to reduce or eliminate tariff barriers, they could create a range of these NTBs, such as duty drawback provisions, Anti-Dumping (AD) provisions, countervailing duties, quantitative restrictions, import prohibitions and trade embargoes. Each of these trade regulations involve discriminating between domestic and foreign goods, or discriminating among foreign goods, which could lead to trade diversion (Ghoneim, 2003).

2. Some countries involved in different RTAs will have to face conflicting obligations and inconsistencies. For instance, some members of a new RTA, such as COMESA, may be confused about offering preferences to non-members with whom they are already partners in the frame of another RTA called the Southern African Development Community (SADC).

3. The overlapping of regional integration zones could have counter-productive effects on the process of regionalization, such as difficulties in recruiting officials for different institutions, lack of transparency towards private agents, political tension and duplication of regional institutions. This is especially the case for low-income countries with limited administrative manpower and know-how. Thus, the complexity due to various RTAs could reduce the commitment and pace by which the government agencies implement the trade arrangements.

4. When there are too many RTAs that a country is involved in, then the country commits itself to a complex network of trade policies. When these policies contradict with the domestic policies applied in the country, this could lead to complications in applying the RTAs.

1.4.2. Rules of Origin

One important NTB aspect closely related to the overlapping problem of the RTAs is the RoO. Therefore, we devote a complete section in this chapter and later a complete chapter for this issue.

The origin is the place from which something is attained, or the starting point of something. When origin refers to people, it means descent or ancestry. In mathematics, the origin is the point of intersection of coordinate axes, where the values of the coordinates are all zero. Nevertheless, when it comes to defining the origin of goods, things get more complicated. The origin of different products is not always the point at which they come into existence. Given the globalization and increasing multi-country production of goods, it is hard to reach consensus as where they originate. This makes specifying a set of principles according to which the origin of a product is determined, or RoO, pretty important.

The RoO determine the nationality or regionality of a product subject to preferential tariff rates within an RTA. However, they can serve as a protectionist device, mainly by excluding products

originated in non-members, even if they are transformed in a member country. The problem can be enhanced, if a country is subject to many RTAs[7].

1.4.2.1. The Functions of RoO

The RoO have been set to mainly fulfill the following functions:

1. To prevent the trans-shipment of goods imported into the area via member states with low external tariffs into member states with higher ones (Concept of trade deflection).
2. To prevent the superficial transformation of non-originating goods in one member state for re-export into others.

However, such rules can entail large compliance costs for intra-bloc exporters forced to source intermediate inputs in the area when outside suppliers would be cheaper (Concept of trade diversion).

According to *Krueger* (1993), the existence of preferential RoO represents a protection to industries in the member countries of an RTA. Hence, the firms could insist on maintaining protection, in order to fulfill their vested interest. This could on turn reduce the willingness of the RTA to engage in external liberalization. Therefore, RoO can be regarded as a major weapon for protectionists who wish to discriminate against the outside world. They may be used to change what might otherwise be a trade-creating FTA into a trade-diverting one (Ghoneim, 2003).

1.4.2.2. The Role of RoO in Free Trade Areas (FTA) and Customs Unions (CU)

A major worry associated with FTAs is trade deflection, i.e. the redirection of imports from third countries through the FTA member with the lowest external tariff. The usual solution for that is RoO, which require that goods qualifying for tariff-free trade within the FTA should be produced in a member country rather than just pass through other member countries with lower tariffs. However, CUs have common external tariffs and therefore do not formally need RoO.

[7] As will be shown, RoO are mainly associated with FTAs, but in certain cases of CUs, such as the initial stage of COMESA, there are RoO set.

Harmonizing NTBs is not a simple task. This requires in many cases of CUs the existence of border formalities such as RoO, in order to define partner goods. This makes *Schiff and Winters* (2003) argue that a CU needs not only to have a Common External Tariff (CET) but also a common trade policy, in order to be able to forego a system of RoO.

1.4.2.3. Bilateral versus Diagonal Cumulation of RoO

Augier (2003) uses the following example, in order to distinguish between *bilateral* and *diagonal cumulation* of RoO; country A and country B have each signed an agreement with country C, according to which each of them can have tariff free access to C, provided that the good confers origin in their respective countries. Although goods of country B have tariff free access to country C, if country A exports a good to the country C consisting of intermediates from country B, those intermediates of the product cannot be treated similarly to intermediates of country A used in determining originating status. Nonetheless, if the intermediates used came from country C, their value could then be cumulated. This means that the agreement is based on *bilateral cumulation*. But if countries were linked by a series of identical agreements, *diagonal cumulation* would allow for intermediates originating in country A, B or C to be included in determining originating status.

1.4.2.4. Problems associated with RoO

FTAs require controls on products crossing internal frontiers to ensure compliance with RoO and the payment of customs duties for non-complying imports, and this can pose significant administrative costs. For instance, using firm-level data, administrative compliance costs under the FTA between EFTA and EC were estimated between 1.4 and 5.7 percent of the value of export transactions and the average export transaction from EFTA to the EC required 35 documents and 360 copies for RoO (Ibarra-Yunez, 2001). Alone the EU's Agreement with Poland has 81 pages of small print for the RoO section, while NAFTA has about 200. Documentation and verification - and their associated costs - must be a continuing part of FTA arrangements in order for importing countries to avoid tariff revenue losses and keep the protection system effective. Moreover, RoO allow customs authorities - and individual customs officers - a good deal of discretion. The administrative cost of ensuring that this discretion is not abused is considerable, and the cost of failing to do so is even higher (Schiff and Winter, 2003). The combination of bookkeeping costs with RoO-induced constraints on international sourcing

can be particularly penalizing for companies operating globally integrated supply chains, which is now the norm in many manufacturing sectors. Since the RoO are often quite expensive to document, as a result, even if a product satisfies origin, an importer may prefer to pay the tariff rather than bother with the documentation needed (Krishna, 2004). Thus, the traders either have to cope with the mass of complex rules or seek to avoid them. The problem can be seen more obviously in the case of small scale enterprises when they seek certificates proving origin, since their budget is usually small and their sources of finance limited.

In addition, determining a certain percentage of the product value that proves origin is quite subjective. It can also differ from one agreement to the other, based on non-economic factors. For example, in the basic RoO determining textiles, which mainly follow value added criteria, the latter are set in some cases to reach 60 - 75 percent. Such different rates of value added criteria might not be justified by any clear reasoning (Ghoneim, 2003).

A very important term used when talking about RoO, especially in the case of overlapping RTAs, is the so called 'Spaghetti bowl' of *Bhagwati* (1996). His argument posits that the differing and overlapping RoO resulting from RTAs can be so complex as to be trade inhibiting, contributing hereby to higher costs and trade diversion pressures. As a consequence, the involvement in too many RTAs could be a burden on human and technical capacity of the economy and could generate diseconomies in the administration of multiple RTAs. It would be useful for each country, before signing an RTA, to consider the latter's RoO, in order to know whether this RTA fits into its network of already signed RTAs.

Bhagwati (2002) argues that such situation was not foreseen by the designers of GATT Article 24 who would be stunned today at the developments that occurred after a huge and increasing number of RTAs of all kinds have been formed. He goes: "…..if this epidemic had been foreseen at the end of the Second World War, the architects of the GATT would have had serious reservations about inserting Article 24 into the agreement."[8] When he tries to answer the question why the RTAs have multiplied, he finds many reasons, several of them political, among which are the following:

[8] Bhagwati, Jagdish (2002) 'Free Trade Today', Princeton University Press, p. 112.

- Bureaucrats make use of the RTAs. They even often take the rank of ambassadors in the frame of these agreements.
- At multilateral negotiations, the media often concentrate on such big players as the EU's trade commissioner or the USA trade representative. But at RTAs level, the media give attention to the local politicians and bureaucrats, who therefore have a personal stake in proliferating their RTAs.
- Bureaucrats and politicians, however, have a short tenure predisposing them towards immediate results; and Bilateral Trade Agreements are easier to sign. So they opt for more of such agreements.

1.5. Institutional Framework

Forming and sustaining an RTA is a hard work, and success is by no means guaranteed. While the economic outcomes of an RTA will be the most important factors in determining its long-run viability, aspects of its institutional design can be a facilitating factor. This becomes more complicated if the discussion is about a complex system of RTAs. According to *Schiff and Winters* (2003), it is hard to manage multiple RTAs. Nevertheless, the high credibility and administrative skills could facilitate implementing theses complex RTAs.

In general terms, policy is made by bureaucrats and ministers representing their own governments, and this in itself can lead to protectionist bias. The incentives for bureaucrats who can reap no direct reward from the profits RTAs can create tend toward the protectionist actions (Messerlin, 1983). According to *Wheeler* (1996), political competition, power relationships, and the dynamics of leadership and elite interaction all affect the institutional flexibility, especially in the absence of a careful economic assessment of the costs and benefits - and hence, the overall net economic impact - of offering such flexibility.

In the new institutional economics literature the major stumbling block to realizing potential gains from trade is political. There should be a particular political mechanism of credible commitment. This mechanism essentially involves self-binding by the rulers. In most RTAs between developing countries the ‘commitment institutions’ which underpin the sustainability of these arrangements are likely to be weak (Matthews, 2003).

An institutional weakness highly related to commitment in RTAs is the lack of enforcement mechanisms which ensure that states abide by the common rules or what is called rule of law. In much of the literature on the new institutional economics the importance of the state is recognized but mostly in the narrow context of how to use its 'monopoly of violence' in the enforcement of contracts. This dilemma is implicit in the standard recommendation in this literature for a "strong but limited" government. To counter this, agreements should increasingly include some form of dispute settlement procedure to resolve difficulties which may arise (Matthews, 2003). The institutional economics literature suggests that the traditional institutions of exchange in developing countries often did not evolve into more complex (impersonal, open, legal-rational) rules or institutions of enforcement and emphasizes the need for such an evolution (Bardhan, 1999).

There are usually lobbies and interest groups who do not want to see the RTAs implemented. The theory of regulation tackled by *Harmathy* (1988) has the merit of directing attention to the costs and benefits of the regulatory process and also to the question of whose interest regulation serves. It has also been observed that the selection of instruments of state intervention in the economy does not take place simply according to a judgment of their effectiveness but under the influence of institutional and political constraints.

The theoretical pressure group model of *Rogowski* (1992) illustrates in a simplified principal-agent framework how domestic interest groups influence the government on policy issues, such as trade integration.[9] It identifies four domestic interest groups that form the government's policy choice in the case of RTAs. For example, while local producers typically lobby for enhanced protection in order to skim the benefits of remaining high tariffs, consumers prefer reduced protection, since lower tariffs and prices improve the available variety of products and the value of their utility function (Fratzscher, 1996).

The Rogowski-model distinguishes between the four following domestic interest groups:

1. A producer typically supporting liberalization in trade among member countries of economic integration. This producer is the *exporter* who usually gains through reduced tariffs, increasing returns to scale, and improved market access.

[9] According to Rogowski, the governments acts as the agent and the interest groups as principles.

2. A *local producer* typically loosing from liberalization, such as import-substitution industries, especially if the initial protection had been high and producer prices drop significantly due to tariff reductions.
3. A *consumer* usually gaining through a larger variety of products, lower prices and higher quality.
4. A final interest group typically guided more by ideological rather than economic views on trade policy. This group sometimes shows resistance that arises through current political or structural changes. For instance, trade can create political dependencies, trade can reduce the self-sufficiency of countries, and trade can induce structural changes with substantial adjustment costs. Most likely, these non-economic interests are stronger in countries which have experienced high protection, which have employed a large proportion of their labor force in less competitive industries, and which experienced some failure of regional integration in the past (Jansen and Nordas, 2004).

A key institutional issue in RTAs is ensuring the transparency of decision-making and the accountability of domestic institutions. In their absence, the political influence of groups able to organize effectively may be strengthened, hindering the implementation of the RTAs. The "old" institutional economists - including Marxists - used to point out how a given institutional arrangement serving the interests of some powerful groups or class acts as a long-lasting barrier to economic progress. As has been suggested in *Bardhan* (1999), the new institutional economists, however, sometimes understate the tenacity of vested interests, the enormity of the collective action problem in bringing about institutional change, and the differential capacity of different social groups in mobilization and coordination. According to the new theory of public choice, some self-interested and rent-seeking pressure groups can distort economic activity in directions of inefficient and inequitable allocation of resources (Streeten, 1989).

Lobbying is very crucial for trade policymakers, and building an RTA makes interest groups face new threats and gives them new opportunities to influence the policy. For instance, when industrial associations were asked for their views on the FTA of the Americas (FTAA), the Florida Citrus Mutual said that the proposed RTA would mean the end of the U.S. industry' and that citrus products must be exempted from further tariff cuts (Schiff and Winters, 2003). Governments respond to pressures from domestic interest groups to increase support. *Hillman* (1989) and *Baldwin* (1985) observed that in many cases, decision makers are not fully informed of the economic interests of their electorate. Therefore, they suggested that voters, either

producers or consumers, may have to engage in costly lobbying activities to bring their interests to the attention of these decision makers.

For many governments trying to implement the regulations of RTAs one finds usually a declining incentive for trade liberalization on a multilateral basis, especially, when the fiscal implications of opening the domestic market (loss of tariff revenue) are severe. This problem can also be associated with rent seeking and corruption in many countries, where again, the beneficiaries of protection would fight against implementing RTAs.

Thus, the RTAs are more probable to be properly implemented, if certain domestic institutional factors create an environment that is favorable for implementation. Institutions set the rules for the interaction between public and private actors (North, 1990). Well functioning institutions therefore reduce the level of uncertainty inherent to this interaction and as a result reduce transaction costs. High quality institutions are expected to have a positive effect on economic activity in general and on international trade in particular. Inefficient institutions, in contrast, can lead to serious obstacles for trade.

Domestic institutions, both in the home and the foreign country, can thus be expected to affect a country's choice of trading partners, and as a consequence, the overall pattern of bilateral trade. *Galal* (1996) draws the example of two countries A and B. The two countries are identical in all respects (market size, prices, products, external tariffs, etc.), but differ in the institutional environments. He assumes that, unlike country A, the behavior of the government in country B is unpredictable; disputes are not settled fairly, the costs of satisfying or avoiding certain regulations are high, there is no sound legislation system and no strict enforcement of laws. Other things being equal, country C will rather be willing to create trade relations with country A.

Last but not least, we would expect that institutions affect the effectiveness of trade policy. Even if a country lowers its trade barriers, outsiders may be reluctant to trade with that country if, for instance, they do not believe contracts can be enforced or are not sure whether payments will be made (Jansen and Nordas, 2004).

The following chapters are essentially concerned with the degree of implementation of the main Egyptian RTAs, their potential for Egypt, the institutional factors affecting their implementation and the overlapping problem in the light of their RoO.

CHAPTER 2

Overview of the Egyptian Regional Trade Agreements and their Status of Implementation

2.1. Introduction

This chapter deals with the main RTAs that Egypt is member of, the trade flows between Egypt and the countries of the RTAs, the current state of implementation of these RTAs, as well as a comparison between their legislative, regulatory and administrative commitments.

2.2. The Greater Arab Free Trade Area (GAFTA)

2.2.1. Overview

The GAFTA refers to the declaration made by the Heads of Arab States in the Cairo 1996 Arab Summit to revive the executive program of the 1981 Agreement on the Facilitation and Development of Trade and to establish an FTA with zero-percent tariff rates in the year 2007. To complete the process, the Economic and Social Council (ESC) of the AL approved the program in 1997 and the Agreement was signed in the same year. Initially, it was planned to reduce the tariffs by 10 percent on yearly basis to reach an FTA with a zero tariff within 10 years (ending in 01/01/2007). However, in 2001, a decision by the ESC (based on the recommendation of the Arab Summit in Amman 2001) accelerated the implementation period to 8 years (to reach the zero tariff by 01/01/2005).

Egypt was among the 14 countries (Bahrain, Egypt, Iraq, Kuwait, Lebanon, Libya, Morocco, Oman, Qatar, Saudi Arabia, Sudan, Syria, Tunisia, and the United Arab Emirates (UAE)) out of the 22 Arab states that joined GAFTA. Later, Jordan, the Palestinian Autonomy and Yemen joined the Agreement as well, which is also open for the five remaining countries of the AL (Algeria, Comoros Islands, Djibouti, Mauritania and Somalia).

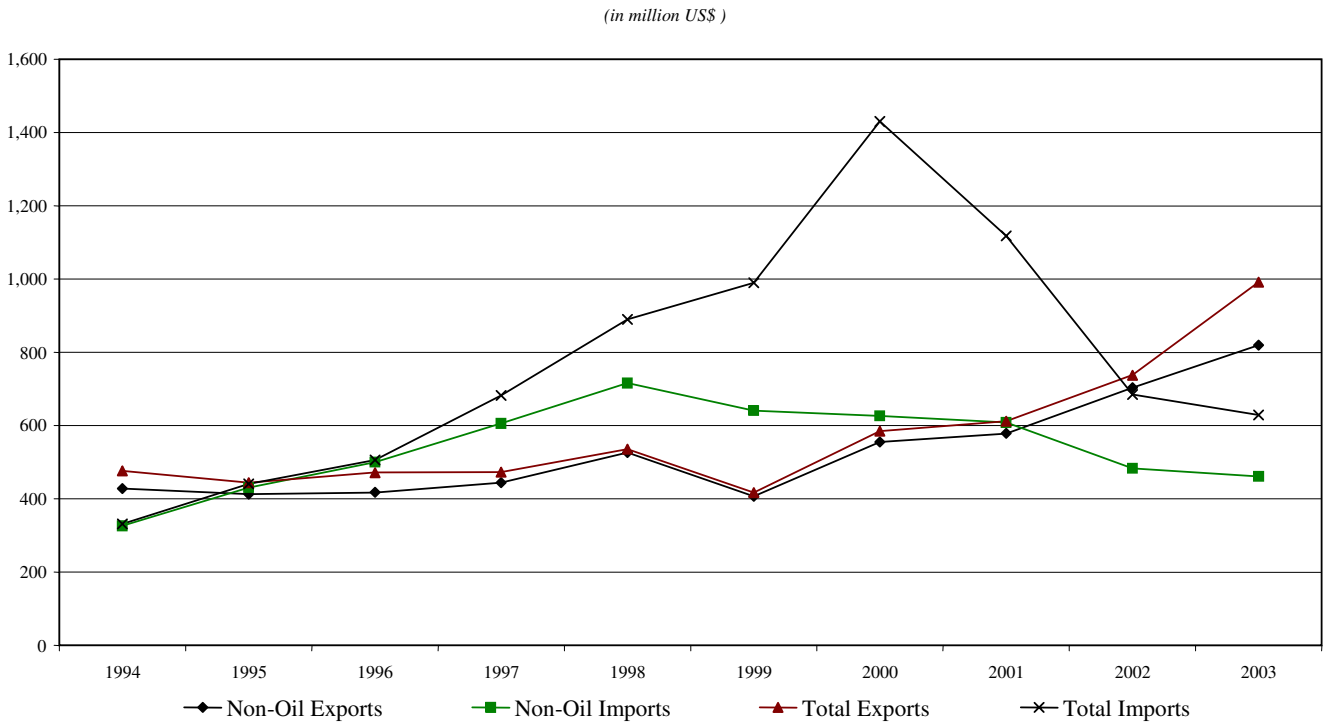
2.2.2. The trade flows between Egypt and the GAFTA countries

The trade between Egypt and the GAFTA countries increased from US$ 808 million in 1994 to US$ 1.6 billion in 2003. As a percentage of Egypt's total trade (exports + imports), the share of trade with the GAFTA countries was 6.2 percent in 1994, and it reached its peak in 2000 (10.8 percent) before it fell to 9.5 percent in 2003. The trade between Egypt and the GAFTA countries witnessed a surplus of US$ 145 million in 1994 which was reversed till the trade deficit sore to US$ 800 million in 2000 but was again reversed in 2003, when Egypt's trade ended with a surplus of US$ 363 million.

Thus, it is hard to draw a clear trend for Egypt's trade with the GAFTA countries. If we correlate the beginning of the transitional period of GAFTA with the trade balance, we observe that starting from 1998 (the starting date for tariff reductions in the context of GAFTA), Egypt has experienced a trade deficit that widened significantly till 2000 (when 30 percent of the tariffs were cut down). Then the deficit started to narrow down till it ended up in a surplus in the year 2002 (when 50 percent of the tariffs were cut down) and continued to increase in 2003. The main reasons behind such fluctuations were both a high growth rate for imports till 2000 (reaching an average of more than 25 percent on annual basis) accompanied by a modest increase of exports (around an average of 6 percent on annual basis). Starting from 2001, the average annual growth of exports excelled to reach more than 20 percent, whereas the imports decreased by more than 20 percent on average annual basis.

Egypt increased its exports (including oil) from US$ 476 million in 1994 to US$ 1 billion in 2003 with an average rate of growth of 10 percent, whereas it increased its imports (including oil) from US$ 331 million to US$ 628 million with an average yearly growth rate of 11 percent. The picture does not change significantly when excluding oil, where exports increased from US$ 428 million to US$ 819 million and imports from US$ 326 million to US$ 461 million through the period 1994-2003. *Figure 1* shows the development of trade between Egypt and the GAFTA countries through the same period.

Figure 1: Egypt's Trade with GAFTA



Source: World Integrated Trade Solution (WITS) Database, World Bank, 2004.

2.2.3. The GAFTA state of implementation

2.2.3.1. Tariff reductions

The implementation of the tariff reductions has been the most successful element in GAFTA's overall implementation process so far. However, some Egyptian exporters complain that some Arab countries did not eliminate tariffs by 2005 as scheduled. For example, the food products still face tariffs in Morocco (ranging from 5 to 10 percent), whereas in the case of Libya, a new surcharge has been imposed on imported products. This surcharge - so called consumption tax - does not apply to domestically produced products. Although Yemen is allowed to enjoy preferential treatment, it discriminates against Egyptian products when compared to imports from other GAFTA members; it imposes on average a 25 percent tariff rate on Egyptian products and allows other Arab products to enter its market duty free[10]. Furthermore, where some of the

[10] See Al Ahram Newspaper (06/03/2005).

member countries are completely running deficits in their trade balances, there are six months exemptions - subject to renewal - from the complete dismantling of tariffs.

2.2.3.2. Exception lists for industrial products (negative lists) and agricultural products (Roznama)

Apart from the examples of violation cases listed in the previous section, GAFTA covers all industrial products. Nonetheless, the members were allowed to draw up official lists of exceptions (negative lists) for a specified period of a maximum of 3 years, following Article 15 of the Agreement[11]. In the year 1998, the total number of products asked to be exempted by the GAFTA countries reached 832 products out of a total of 6000 traded products (representing 14 percent out of the total)[12]. Six Arab countries (Egypt, Jordan, Lebanon, Morocco, Syria and Tunisia) submitted lists of exempted products. In the year 2000, a decision was taken by the ESC to eliminate those exceptions by September 2002. In 2003, five member countries submitted notifications of the elimination of those negative lists. Egypt submitted its notification in October 2003. However, it tied its elimination of its negative list to the condition of finalizing a Protocol on Detailed RoO for GAFTA. The argument provided by the Egyptian Government was its need of ensuring protection for its strategic industries (e.g., textiles and automobiles) against non-Arab production, which cannot be properly implemented without a detailed system of RoO. Since the agreement on detailed RoO is still lagging behind, such condition implies de facto that Egypt still did not remove its negative list, and thus can still keep its tariff rates on the imports of those goods. It is worth mentioning that several members (e.g., Jordan and some Gulf states) have threatened to reciprocate against the treatment of selected Egyptian exports, due to this unilateral Egyptian action, especially since the ESC decision on the elimination of exemptions did not relate its implementation to reaching a conclusion on detailed RoO.

As for the agricultural products, they were in principle subject to progressive tariff reductions to reach full liberalization within 10 years. Nonetheless, the practical experience proved the

[11] These exceptions follow certain conditions including the following: 1) The commodity should be produced by the country asking for exception and should have a similar product produced in one of the other member countries; 2) The exception is granted for a specific period not exceeding 4 years; 3) The total percentage of the exempted products should not exceed 15 percent of the total exports of the concerned country to other members and 4) A member country is entitled to ask for a counter exemption if it is negatively affected by the exemption asked by one of the other member countries.

[12] This number can be overestimated, since there might be common goods in the lists of the different countries.

difficulty of immediate full liberalization of the Arab agricultural trade, as agricultural production constitutes a great share of the total production in all the Arab countries. Thus, the member countries were not able to implement full liberalization of agricultural trade. To overcome such obstacles, the executive program of GAFTA applied two major principles concerning liberalization of trade in agricultural products:

- The gradual reduction of customs duties and other duties of similar effect to be fully liberalized within ten years.
- The implementation of the production season (Agricultural Products Group or the so called Farmer's Roznama), in which a number of agricultural products shall not be subject to tariff reductions till the beginning of 2007, which was brought forward later to the beginning of 2005 in order to be in line with the full entry into force of the Agreement. Egypt was among the countries that had a number of agricultural products exempted, but it officially notified the cancellation of this list in due time.

The de facto removal of product exceptions is impossible to trace or report upon, since the notifications that countries submit to the AL secretariat may not necessarily be implemented in practice by their customs. Hence, relying on these notifications may well be misleading. In addition, the assessment is difficult, due to the absence of a clear definition for NTBs and a determination of duties of similar effect. There are current negotiations on the duties that are paid for certain services related to the trade deals among GAFTA countries. These duties need to be estimated thoroughly without exaggerations. The Egyptian Ministry of Industry and Foreign Trade requested indeed from the Ministry of Foreign Affaires, Ministry of Agriculture and the Customs Authority clarifications and detailed reports on these services and their associated duties. However, no concrete results came out of this action.

Up to present, GAFTA is not acknowledged by the WTO, since in order for this acknowledgement to occur, such that the GAFTA countries get exempted from the MFN rule towards non-member countries of the Agreement, they have to fulfill two conditions; forming and enforcing an FTA among them. The first condition has already been fulfilled by signing the GAFTA Agreement and declaring the FTA in 2005. However, what is still missing is the proper enforcement; the latter means liberalizing 'almost' all of the trade, i.e., reaching the zero-tariffs when the FTA comes into effect. When some officials of the Egyptian Ministry of Foreign Affaires inquired in the year 1996 after the indication of 'almost', they were informed that it was

75 percent of the total trade. In December 2002, this percentage increased already to 90 percent. According to the Egyptian officials, the main reason why GAFTA has not been acknowledged yet by the WTO is the fact that there are still many products exempted from the Agreement (negative lists). Other officials claim that this reason is just a cover for some other political reasons.

The problem associated with the WTO not acknowledging GAFTA is the following: Third countries (Non-GAFTA-members) who are members of the WTO[13] can require from Egypt the treatment of the MFN. In this case, Egypt does not have the right to discriminate against their cheap imports in favor of the imports of the GAFTA members, as long as the FTA is not fully applied and the Agreement is not acknowledged by the WTO. The result could be bankruptcies within many Egyptian and Arab industries.

2.2.3.3. Coherence with international rules

Article 8 of the executive program of GAFTA states that the parties concerned shall hold negotiations with the aim of imposing uniform and appropriate restrictions of similar effect on goods imported from non-Arab states, which are competitive or alternative to Arab goods.

The same Article calls for the application of international rules regarding subsidies, countervailing measures and safeguards. Moreover, the ESC may adopt any other measures with a view to dealing with cases of dumping and discriminatory policies that Arab and non-Arab states may adopt. However, the program does not explicitly refer to the WTO Agreements, such as GATT.

2.2.3.4. Rules of Origin

To enjoy the preferential treatment provided by GAFTA, a product should meet the RoO determined in the Agreement on the Facilitation and Development of Trade. The general RoO indicate that the value added within the boundaries of one or more member countries should be no less than 40 percent of the final ex-factory price of the products[14], and this percentage is

[13] A very clear example is China, whose competition is feared by the Egyptian local producers at most.

[14] An example for that is Egypt contributing with 10 percent of the final ex-factory price of the product separately from Jordan which contributes with 30 percent. In this case, both of them together contribute with 40 percent.

lowered to 20 percent in the case of joint Arab production, such as a joint enterprise officially carrying the name of two or more Arab countries. These rules are general and temporary. The executive program explicitly instructed the member countries to design and agree on a more detailed protocol for RoO. The member countries are still in the process of designing such a protocol that is supposed to be quite similar to the Euro-Med Protocol for RoO.

One of the most important problems of GAFTA is the fact that there is confusion about the concept of 'value added' with regard to the RoO; the 40 percent 'local component' is a more relaxed concept than the 'value added'. If the value added concept is adopted, then this would be stricter, since one would have to exclude those inputs that are imported from abroad and included in the product when running the calculations. The Arab countries apply the less strict 'local component' concept among themselves, which further proves that the inputs imported from non-member countries are in fact underestimated in the RoO calculations of GAFTA.

In general terms, Egypt, Morocco, Tunisia, and - to a lesser extent - Syria are the GAFTA countries that consider the issue of the RoO at most. This can be referred to the fact that these are the Arab countries with the strongest industrial bases.

The second major problem related to RoO - after the lack of a detailed protocol - is the manipulation of origin within GAFTA. With the absence of a capable mechanism ensuring the adherence to RoO (even the general basic rule), manipulation has been increasing, leading in turn to several trade frictions. For example, some lobbies that dominate the decision making in Egypt and are in favor of importing from non-member countries of the Egyptian RTAs do not take the RoO seriously. Furthermore, when the Egyptian importers deal with the Jordanian side, they are often shocked when the products are almost completely imported from a third country, and due to some slight transformations taking place in Jordan are considered conferring origin. For example, using Jordanian labor alone counts for 30 percent. This means that importing a refrigerator from China, using Jordanian labor (which alone counts for 30 percent local component) in installing the compressors fulfils the 40 percent local component condition. In this case, Egypt imports the product from Jordan, while in fact it was produced in a third country outside GAFTA.

In even worse cases, Jordan and the UAE often import finished goods from non-member countries, label the national tickets on them and export them tariff free to Egypt and other Arab countries. For example, Jordan is notorious for buying products - specifically ovens - from

Europe, removing the tickets and exporting them to other Arab countries, including Egypt, after giving them the Jordanian stamps and trade marks, which could be considered ‘smuggling’ rather than ‘free trade’. A RoO case was reported in the year 2005 between Egypt and Jordan, when the former had doubts about imported televisions from the latter. An Egyptian delegation of the Ministry of Industry and Foreign Trade, the Egyptian Federation of Industries, the customs and Egyptian television producers visited the factory in Jordan to check the origin. The delegation could not prove any violations. This is called the 'mechanism of visiting factories' and it is based on an Egyptian law. However, the Jordanian side could have refused this visit, since such a law is missing in GAFTA and is only declared as a national law in Egypt.

In general, the very low local component percentage does not give enough incentives for the member countries to rely on their local inputs, and hence, does not help the national industries to flourish.

2.2.3.5. Customs

According to GAFTA, the member countries shall hold negotiations with the aim of imposing uniform and appropriate minimum customs duties, taxes and restrictions of a similar effect on products imported from non-Arab countries, which compete with the Arab products. Nevertheless, the meetings of the CU Committee are largely perceived as quite ineffective and rhetoric, since the gap in the tariff structures of Arab countries is almost impossible to bridge in the near future. For example, in addition to the Gulf Cooperation Council (GCC) CU, there is another Draft Treaty on a Unified Customs Law under the Council of Arab Economic Union which comprises 9 Arab countries. This draft has never been adopted.

2.2.3.6. Trade-related domestic regulations

GAFTA does not include any specific rules on the application of measures related to Sanitary and Phytosanitary (SPS) measures, Technical Barriers to Trade (TBT), NTBs, Labor Standards or Environmental Standards. While there is a working party that was established to prepare studies and reports on NTBs, the work of the former is largely limited to the inspection of NTBs related to border measures, such as the fees of documentation and inspection.

Several trade frictions and disputes have occurred among the member countries, and most of them have been related to SPS and/or TBT measures. The lack of the appropriate rules within GAFTA proved to be a major loophole for proper implementation, and it seems that member countries prefer to resolve those disputes through bilateral consultations or unilateral retaliations, due to the lack of a proper and comprehensive dispute settlement mechanism[15].

2.2.3.7. Trade in services

Regarding services liberalization, a Framework Agreement on the Liberalization of Trade in Services was concluded in 2003. The Agreement was designed to be similar to the WTO General Agreement on Trade in Services (GATS), adopting the same progressive liberalization concept. The first round of negotiations on the specific commitments was held in September 2004 in Beirut, where 9 Arab countries (Bahrain, Egypt, Lebanon, Morocco, Oman, Qatar, Saudi Arabia, Tunisia and the UAE) presented their initial offers. The negotiations took place on bilateral basis between each two countries. It was agreed that the initial offers should not go below the level of commitments provided in the WTO (for the Arab countries that are already members of the WTO or negotiating their accession). To meet the WTO rules on RTAs (GATS Article V), the Arab Agreement is expected to provide larger sectoral coverage and/or deeper liberalization in the specific commitments already submitted under the GATS framework. It might be early to provide any expectations about the final outcome of these negotiations, but the active participation of most Arab countries indicates that it could be promising.

Egypt has submitted commitments as initial offers in the sectors where it has already undertaken commitments in the GATS. The offers it submitted under this Agreement were GATS +, i.e., beyond the GATS Agreement; these sectors are construction, tourism, financial, maritime and telecommunications. However, the exact type of offers submitted and negotiated are confidential and cannot be released at this stage.

2.2.3.8. Country specific problems and NTBs within GAFTA

There are several problems within GAFTA, among which is the problem of customs valuation with Jordan, extra unjustified surcharges in some Saudi ports and the tendency to stop importation of onions out of the allowed season, and the reluctance of the Libyan customs

[15] See subsection 2.6.5.

authorities to import Egyptian products based on the argument that they do not meet the required standards.

There is a need of an agency in Yemen that facilitates the movement and entry of Egyptian exports. In the case of the UAE, the problem of authenticating the RoO certificates exists. Moreover, there are problems associated with free zones in Dubai as well as problems of identifying which imports are imported from free zones and which are not. The UAE importers also need to obtain import permissions from their Ministry of Industry and Foreign Trade in the case of importing manufactured products from Egypt, and from their Ministry of Agriculture in the case of agricultural imports.

In the case of Algeria, there are problems associated with customs procedures, non-transparency in banking regulations concerning trade activities, RoO certificates and registration of Egyptian pharmaceuticals. Last but not least, the trade with Saudi Arabia faces the following obstacles: embargo on potatoes; embargo on fresh frozen meet; manipulation of SPS measures regarding agricultural products and pesticides; dumping of steel; imposing extra surcharges not in line with GAFTA on some products; and not keeping in line with tariff reductions according to GAFTA. On the other hand, there are indeed problems between Egypt and Syria, where the latter supports its exporters and where the Syrian products are sold cheaper in Egypt markets than in the Syrian ones, creating hereby dumping problems.

The import permissions make up a big problem among the GAFTA countries, since they can be considered a strong NTB. For example, it is very hard for Tunisian importers to import Egyptian products. There are so many burdens facing the Egyptian exports in Arab countries, including import permissions. The cases differ from one importer to the other and one period to the other. Although GAFTA officially cancelled this sort of burden, Morocco and Tunisia still impose this condition. In February 2005 there was a meeting for the ESC in Yemen, and there was a complaint against Morocco and Tunisia in this regard. And Tunisia by that time did not have yet reduced its tariffs by the last 20 percent. After this meeting and being penalized by the AL, Tunisia eliminated its tariffs to zero, but to date, it imposes the condition of import permission, under the excuse that these permissions are necessary for the statistical calculations on the Tunisian imports. However, the Egyptian exporters and government officials observe it as a clear NTB.

2.2.4. GAFTA and the Arab Bilateral Trade Agreements with Egypt

2.2.4.1. Overview

Egypt has concluded a number of Bilateral Trade Agreements (BTAs) with a number of Arab countries. Each agreement has its own products coverage and list of exemptions.

The relationship between the GAFTA and such bilateral agreements is not clear and causes a number of disputes. For instance, the agricultural products group (Roznama) that was agreed upon under the auspices of the GAFTA was not completely in line with the negative list adopted in some Arab BTAs. This is a major issue that the ESC of GAFTA has been trying to handle.

In many cases, Egypt applies the rules of the GAFTA or the Arab BTAs according to its own discretion that hides behind its protectionist attitude and non-transparency. In other cases, the Egyptian authorities undertake such actions to retaliate against problems facing the Egyptian exporters in some other Arab countries. Interviews with Egyptian government officials in the Egyptian Customs Authority emphasized that they face no problems in applying GAFTA in parallel with the Arab BTAs, where exporters from Arab countries have the right to choose among the different Agreements. In fact, some officials pinpointed that it is better to apply the bilateral rules rather than the GAFTA ones as there is some sort of dispute settlement mechanism under such BTAs, which is missing in GAFTA.

The BTAs concluded between Egypt and a number of Arab countries include: Libya (1990), Syria (1990), Tunisia (1998), Morocco (1998), Lebanon 1998), Jordan (1998), and Iraq (2001). Appendix I provides further details on the transitional periods and dates of implementation of these BTAs.

It is worth noting that such BTAs were preferential and never reached the status of being fully implemneted. Services were completely excluded and several negative lists were included in these Agreements.

2.2.4.2. Country specific problems and NTBs within the Arab Bilateral Trade Agreements with Egypt

In view of the separate Arab BTAs, the following problems facing the Egyptian exporters are worth mentioning:

Libya:

- No application of international standards and quality control
- Import licensing requirements
- Authentication requirements of certificates of origin
- Doubting about the Egyptian origin
- Inspection procedures
- Customs procedures

Syria:

- Restriction of some imports to the public sector
- Need of different approvals for the Syrian importers
- Multiplicity of exchange rates
- Extra surcharges and tariffs on the products that should have been liberalized
- Dumping in Egyptian markets

Tunisia:

- Import licensing requirements
- Extra surcharges
- RoO authentication requirements
- Registration requirements of pharmaceutical products

Morocco:

Import licensing requirements

Lebanon:

- Abuse of standards
- Refusal of some agricultural products (because of Daraq fly)

Jordan:

- Abuse of SPS measures affecting some agricultural products (Daraq fly), solved partially
- Refusal of dried onions without providing reasons
- Imposing additional surcharges on all Egyptian exports of macaroni and some home appliances

Sudan:

- Banking procedures
- Customs valuation and customs procedures
- Transport

2.3. The Common Market for Eastern and Southern Africa (COMESA)

2.3.1. Overview

By definition, COMESA is not merely an FTA. It was established in 1994 as a strengthened successor to the Preferential Trade Area for Eastern and Southern Africa founded in 1981 and envisaged the establishment of a CM and a MU in the future (2025). Presently, COMESA includes the 19 following members: Angola, Burundi, Comoros, Democratic R. Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia and Zimbabwe. Egypt joined in the year 1998. Countries that used to be members of COMESA and withdrew are Lesotho (1997), Mozambique (1997), Tanzania (2000) and Namibia (2004)[16].

A PTA was initially established with low tariffs applied to trade among member countries relative to trade with non-member countries. The granting of preferential treatment in the form of reduced tariffs to intra-regional trade commenced on the 1st of July 1984 under the original PTA framework. Initially, the reduced tariffs to products originating in the region applied to a group of selected commodities contained in a common list. The common list was expanded every two years by the inclusion of additional commodities. Within various commodities in the common list, different levels of tariff reductions were applied according to the commodity groups into which they were classified. The PTA categorized the common list products into the following six groups: Food (excluding luxury items), Raw Materials, Intermediate Goods, Manufactured

[16] Libya joined the Agreement on the 3rd of June 2005, after the model of this study and the RCA calculations had been run.

Consumer Goods (excluding luxury items), Capital Goods (including transport equipment), and Luxury Goods. *Table 2.1.* shows the reductions agreed upon.

Table 2.1.: Tariff reductions on commodity groups under the PTA

Commodity Group	Product Description	Initial Tariff Reduction
Group I	**Food (excluding luxury items)**	**30 percent**
Group II	**Raw Materials:** **Agricultural** **Non-Agricultural**	 **50 percent** **60 percent**
Group III	**Intermediate Goods**	**65 percent**
Group IV	**Manufactured Consumer Goods (excluding luxury items):** **Durable Consumer Goods** **Non-durable Consumer Goods** **Highly Competing Consumer Goods** **Consumer Goods of Particular Economic Importance to Economic Development**	 **40 percent** **35 percent** **30 percent** **70 percent**
Group V	**Capital Goods (including transport equipment)**	**70 percent**
Group VI	**Luxury Goods**	**10 percent**

Source: COMESA website, www.comesa.int

2.3.2. The trade flows between Egypt and the COMESA countries

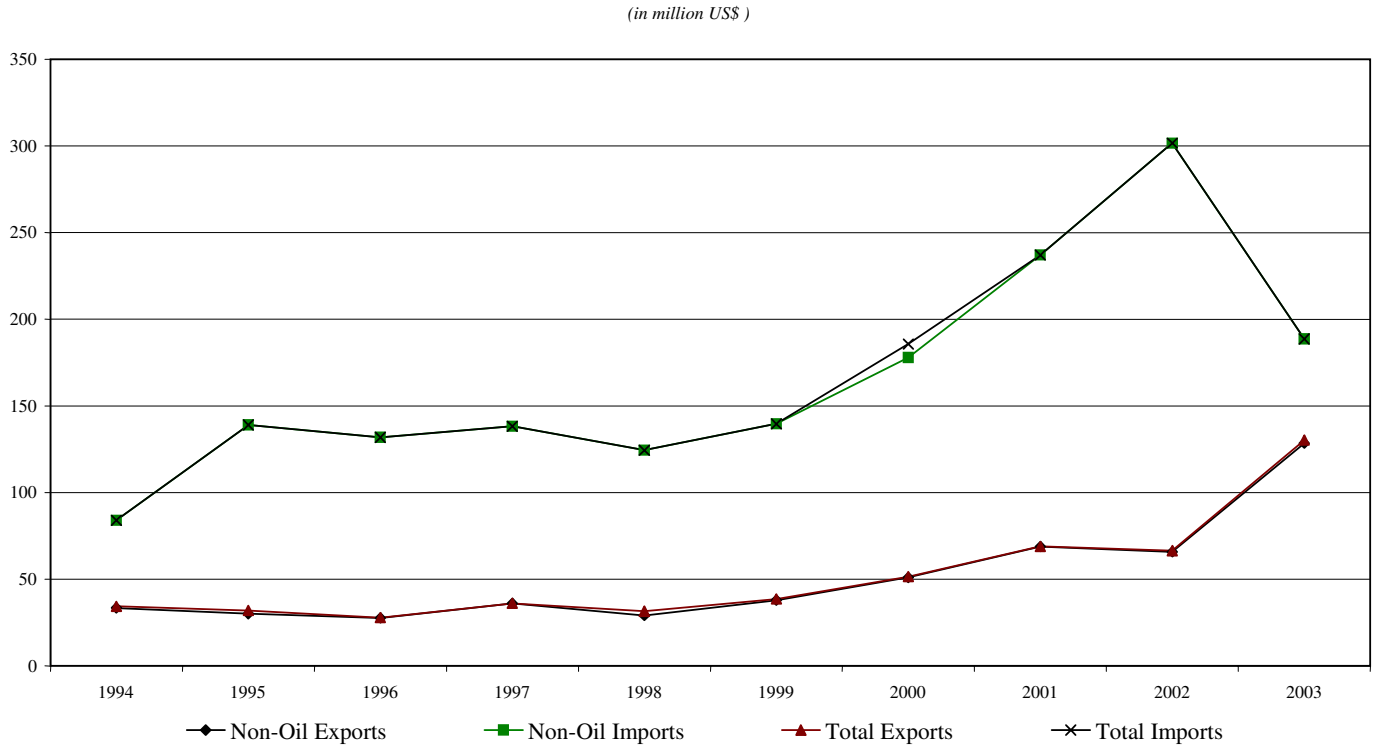
The trade between Egypt and the COMESA countries increased from US$ 118 million in 1994 to US$ 319 million in 2003. As a percentage of Egypt's total trade, the share of trade with the COMESA countries barely increased from 1 percent in 1994 to 2 percent in 2003. The trade deficit between Egypt and these countries has widened from US$ 50 million in 1994 to US$ 235 million in 2000. Then it fell to US$ 59 million in 2003. On the exports side (including oil), Egypt increased its exports to the COMESA countries from US$ 34 million in 1994 to US$ 130 million in 2003 with a yearly average growth rate of 20 percent. On the imports side, Egypt increased its imports (including oil) from US$ 84 million to US$ 189 million with a yearly average growth rate

of 13 percent. The picture remains quite similar when excluding oil, since the exports increased from US$ 33 million to US$ 129 million and the import remained with no change. *Figure 2* shows the development of trade between Egypt and the COMESA countries through the period 1994-2003.

The reason behind this chronic but varying deficit was mainly the huge increase in imports in 1994 (mainly arising from tea imports from Kenya). Through the period 1994-2000, the growth rates of exports and imports varied between being positive and being negative. Starting from 2000, there was a huge increase in the growth rates of both the exports and imports, but since imports were starting from a higher level, the deficit remained. In addition, the exports growth rate in 2002 declined significantly and even turned negative, which explains the peak of the deficit in that year. In the year 2003, the exports growth rate reached an unprecedented rate of 96 percent, whereas the imports growth rate remained stable, which explains why the deficit was heavily curtailed in 2003.

It should be noted that the deficit could be considered 'healthy', since Egypt mainly imports raw materials from the COMESA countries and exports manufactured products to them. Therefore, the trade structure is generally in favor of Egypt, even if it sometimes comes to a deficit in favor of its COMESA partner countries.

Figure 2: Egypt's Trade with COMESA



Source: World Integrated Trade Solution (WITS) Database, World Bank, 2004.

2.3.3. The COMESA state of implementation

In the context of the multilateral trading system, COMESA was notified to the WTO under the *Enabling Clause* in May 1995. As such, it did not have to undergo an examination under Article XXIV, GATT 1994. This implies that issues, such as the lack of full coverage of trade and the transitional periods exceeding 10 years, do not apply to the case of COMESA.

In general, COMESA has managed to reach some remarkable and visible achievements. The areas where COMESA has - to a certain extent - made good progress include the following:

- Removal of tariff barriers.
- Elimination of NTBs, particularly the classic ones (quantitative restrictions, licensing, import permits and restrictive foreign exchange controls).
- Simplification of RoO, with the rules undergoing further changes to take into account developments at the WTO and World Customs Organization (WCO).

On the other hand, COMESA suffers from a high degree of non-transparency, where the Treaty identifies several provisions that are not implemented in reality. Among the most important of which, is the absence of any negative lists in the Treaty and their presence in reality. For the Egyptian authorities there have been two main problems; the first problem is related to the absence of a clear mechanism required to tackle the problems related to trade remedy measures, and the second problem is related to the manipulation of origin of goods imported from COMESA members.

Moreover, the dual membership of COMESA and other overlapping blocks may bring about complications in managing the regional trade policies and the overlapping of some activities could bring about some duplication or even inconsistencies (e.g., the case of Sudan and Egypt, both being members of GAFTA and COMESA). An exporter from Sudan might prefer to use the GAFTA rules rather than the COMESA ones and the same applies for Egyptian exporters exporting to Sudan. Agreeing between governments on a negative list under GAFTA would imply that it supercedes COMESA, which is not the case, since it has never been mentioned in any of the agreements that countries have the right to draw their own bilateral arrangements. Moreover, such duplication of rules and regulations create an atmosphere of non transparency and vagueness among the different members, which is the case in the trade relationship between Sudan and Egypt.

The lack of provisions on Intellectual Property Rights, as well, is one of the problems facing COMESA. In the following, a number of important issues concerning the COMESA status of implementation are covered in detail.

2.3.3.1. Tariff reductions

Once the initial tariff reductions came into effect in the frame of the 1981 PTA for Eastern and Southern Africa, a progressive reduction schedule of tariffs was applied with a view to eliminate the tariffs by the 30th of September 1992. Due to the concern about the loss of government revenues, the target date for the FTA was postponed to the 31st of October 2000 by the Heads of States at their Summit held in 1992, where they adopted a new program for the progressive reduction of tariffs applied to all products. This new tariff reduction program provided the attainment of an FTA on the 31st of October, 2000. The new tariff reductions that were adopted

were scheduled at an annual 10 percent reduction, such that the tariffs would reach the zero-level by the beginning of 2000.

Egypt signed the COMESA Treaty in 1998. The Agreement entered into force in 1999 (with an initial tariff rate reduction of 80 percent). The 100 percent tariff reduction was achieved on the 31st of October 2000 after two 10 percent tariff cuts per annum.

Twelve other countries achieved a 100 percent reduction of tariffs on imports. Theses countries are Burundi, Comoros, Djibouti, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Sudan, Zambia and Zimbabwe. Burundi was the last country to reach the zero tariff rates; it first achieved an 80 percent reduction on tariffs on January 1st, 2003, and then 100 percent reduction on January 1st, 2004. This thirteen-countries FTA has not only cancelled customs tariffs amongst its members, but has also involved the relaxation of several quantitative restrictions and other NTBs.

Other COMESA members apply different levels of reductions on reciprocal basis; the Comoros Islands and Eritrea have achieved an 80 percent reduction on tariffs with expected further reductions to reach the 100 percent level. The Democratic Republic of Congo approved in its 12th cabinet meeting (2000) a tariff reduction of 70 percent, but it requested to conduct a research to assess the impact of losing customs income on the national budget. Thus, it has not yet implemented the 70 percent reduction. Ethiopia currently applies a 10 percent reduction and is assessing the possible effect of further reductions on the national economy. Swaziland is currently consulting the South African Customs Union (SACU) to comply with their obligations of tariff reductions. Rwanda applies 80 percent tariff reductions since 2001 and was assumed to achieve the reductions agreed upon in 2004. However, this reduction has not yet taken place. Seychelles undertook a decision to apply a 100 percent tariff reduction as of the 1st of June, 2001, but has not implemented this reduction up to date of this research. Uganda also requested the finalization of a compensatory mechanism for reduction of tariff revenues and the softening of the safeguard measures.

In general terms, the COMESA countries that are in the thirteen-countries FTA trade on a duty-free basis among themselves; members not in the FTA are granted trade preferences by the FTA member countries on the basis of the tariff reduction they have attained; and members that have

not applied the minimum tariff reduction of 60 percent are neither granted any preferential rate by the FTA members nor by those that have reduced tariffs by more than 60 percent.

2.3.3.2. Product coverage and exemptions

COMESA is supposed to cover all agricultural and animal products; mineral and non-mineral ores; and manufactured products. The Treaty does not refer to any possible prior exemptions or the rights of members to include negative lists. However, some members apply exemptions to some tariff lines with prior notifications. Textiles and yarns are a typical example in the Egyptian case. Gradual removal of the exempted tariff lines is constantly taking place where members are annually submitting notifications of the removal of exemptions. Several documents and proceedings of ministerial meetings include indications of the suspension/extension of exemptions in place (e.g., by Sudan, Egypt, and Kenya) of several tariff lines. In general, all the Egyptian exports enjoy duty free access in the countries of the FTA. There are few exceptions with Sudan, Mauritius, and Kenya. Since May 2001, Sudan has a negative list of 58 items that are not allowed to be imported from Egypt, unless the full amount of tariff duties is paid. On Egyptian demands, Sudan reconsidered the negative list in July 2003 and reduced 30 percent of the tariffs for 12 out of the 58 items. Kenya has lately undertaken safeguard measures on its imports of Egyptian sugar for 4 years (the duty free quota allowed is 111 thousand tons for treated sugar and 89 thousand tons for raw sugar), which should end by the end of 2007.

2.3.3.3. Customs

Negotiations on the modalities and the framework for application of a CU with a CET for all the member countries of COMESA are still in their early stages; it was initially planned for the CU to take place in 2004 (4 years after the FTA entry into force). Nonetheless, such a timetable has proven to be quite unrealistic, especially because not all the member countries are included in the FTA. Another date was determined in the meeting of the African Trade Ministers (2005) for reaching the CU in 2008. There was a suggestion by the Secretary to create a CU among the 10 countries who already established an FTA among each other, but this suggestion was dampened, since it could have lead to widening the gap between these ten countries and the rest of the COMESA countries who did not yet reach the zero-tariff level, especially that one of the most important aims of COMESA is to homogenize between all its 19 member countries.

The road to the CU does not only imply a much higher sense of discipline, but its establishment raises several important challenges for the member countries. The most important of these challenges is to reach a compromise concerning CET. This makes the implementation of a MU by the year 2025 quite doubtful.

2.3.3.4. Rules of Origin

The general RoO applied in COMESA is the following: In order for the product to confer origin, the value added resulting from the process of production must account for at least 40 percent[17] of the final product.

Despite the occurrence of a Protocol on RoO in COMESA, there have been many claims of incidents of fraud in origin certificates (particularly on the part of Egypt). The issue remains to be a constant item on the agenda of ministerial meetings.

It is also worth mentioning that there is a long list of exemptions from those RoO, where members are allowed to apply different RoO to some goods of economic importance (around 145 goods). On casual basis, these procedures are usually undertaken and reviewed under the ministerial meetings.

The RoO written in the COMESA protocol cannot be regarded as serious, since the 35-40 percent value added is in fact insufficient. For instance, Egypt exports flour to Kenya, although the latter originally produces local wheat and the former is originally one of the biggest importers of wheat in the world. While Kenya imposes tariffs ranging from 30 to 35 percent in order to protect its local production of wheat, Egypt imposes only one percent tariffs. But following the rules of COMESA, the Kenyans import Egyptian flour tariff-free, as long as the product confers Egyptian origin (35 percent value added). This means that Egypt only needs to grind the wheat imported from non-COMESA countries, such as the USA, and pack it in order to reach these 35 percent. As a result, several Kenyan wheat mills with big investments were crowded out and shut down and the local flour industry died. In such cases, COMESA cannot be considered an FTA but rather an agreement on making use of the tariff differences (trade deflection, *see Chapter 1*). In

[17] The ratio was initially 35 percent until the members agreed on an Egyptian request to raise it to 40 percent in 2002. Beforehand, Egypt initially applied a unilateral and reciprocal rule of 40 percent, while the rest applied the 35 percent ratio.

other words, Kenya imports the flour from the USA through Egypt, since it cannot do that tariff free.

Another important example for the Egyptian abuse of the RoO concept is the exportation of photocopying and toilet paper to Kenya. Many Egyptian producers import paper from Israel, cut it, make slight transformations and directly export it to Kenya, which in turn causes the shutting down of many Kenyan paper factories. Once the Kenyan side refuses to import from Egypt or puts some constraints for such reasons, Egypt complains about the Kenyan violation of the Agreement. The same applies to the cement, an industry that has flourished in Egypt in the recent years and at the same time threatens the local factories in other COMESA countries.

The key RoO for the agricultural products in almost all of the RTAs and based on Article 24 of GATT is the condition for the product to be 'wholly obtained'. And if COMESA were to follow this RoO, Egypt would not have been allowed to export flour to Kenya, unless the wheat is locally planted in Egypt. But when COMESA was signed, these RoO were not well studied; the member countries were enthusiastic about the Agreement to the extent that they overlooked important details. Every negotiation was postponed till the signing takes place. Hence, after that, when the concerned countries attempted to negotiate over the RoO, Egypt kept postponing, since - to a great extent - it is benefiting from the 35-40 percent value added concept.

On the other hand, falsifying the certificates of origin is a common problem in Egypt and other member countries of COMESA as well. A clear example is the following: The Egypt National Company for Plastics imports yearly huge amounts of Urea from Kenya for extracting the Melamine from it. In one incidence, there were doubts about the Certificate of Origin (CoO), the certificate for customs clearance and the freight police. Later it was discovered that, although the insurance policy is Kenyan, the ship transporting the Urea carries the Israeli nationality and passes by Israel before arriving to the Egyptian harbor. The Egyptian government requested from the Kenyan Ministry of Trade to run its investigations. Moreover, Egypt sent some specialists to check whether a Kenyan factory for Urea exists. The team of specialists discovered that the factory did exist but does not produce all the Urea that Egypt imports and, for that reason, the ship was used to pass by Israel to collect the rest of the Urea to be exported to Egypt. Both the Kenyan exporters and Egyptian importers knew about the details of these deals. We should stress on the fact that this case was easily discovered and came to public due its political dimensions, as any issue where Israel is mentioned carries political sensitivities, and this case in particular was

apparently monitored by the Egyptian secret service. However, there might be numerous similar cases that have not been discovered or disclosed, due to the political irrelevance.

2.3.3.5. Non-Tariff Barriers and Trade Remedies

Despite the fact that there are a number of articles that deal with such issues (Articles 51, 52, 53 and 54 of Chapter Six of the Agreement), until the end of 2001 COMESA did not have proper trade remedy provisions, AD, countervailing, injury to industry, etc.), and the member countries devised their own measures to counter what they considered to be major market disruptions. Thus, for example, when faced with the surge of imports from Egypt in a number of products, Mauritius and Kenya had bilateral talks with the Egyptian authorities to re-introduce duties on these products. Sudan also applies unilateral exemptions of some Egyptian exports. Egypt had bilateral talks with Kenya to stop the surge of Kenyan tea imports. Such unilateral measures can be double-edged swords and their abuse can frustrate trade. Egypt has been a victim to some of these unilateral measures. But many analysts believe that such safeguards, even on ad hoc basis, helped to have greater participation of "smaller" countries in the FTA.

In order for Kenya to protect its local production of flour in the year 2005, it was willing to set quotas on its imports of this Egyptian product. Nevertheless, Egypt protested against these quotas, since the latter were not based on a certain benchmark. Therefore, in the Kigali meeting of March 2005, the two partners agreed on the following: The quota would be determined according to the highest value of the Egyptian exports of flour to Kenya in the past three years. And this quota would be applied for further three years, i.e. till the year 2008, before any further negotiations take place.

In the case of Kenya imposing a safeguard measure against Egyptian flour by a quantitative restriction, some issues need to be highlighted; the restrictions were imposed without any investigation having been made to determine the extent of the local industry's injury and the causal link between imports and the affected industry. To date, the margin of dumping has not been established. The cause of the Egyptian flour exports to Kenya can be linked to cases of under valuation, under invoicing or lack of proper controls at the Egyptian borders. Many reports stress that the export prices compared with the contracted or the normal value have been

determined or established to enable one conclude a case of dumping of flour exported to the Kenyan markets[18].

The Twelfth Meeting of the Council of Ministers in Lusaka, Zambia, on the 30th of November, 2001, adopted Trade Remedy Regulations for invocation of safeguards, AD, subsidies and countervailing measures. Work is on-going through a Working Group of Experts to elaborate the regional safeguards and trade remedies, as is the case at the WTO, especially with regard to the investigation and verification procedures.

2.3.3.6. Trade-related domestic regulations

Concerning the SPS measures, the members of COMESA agreed on detailed provisions set in the Treaty. However, none of the measures can be recognized as implemented. There is almost no information on the progress of implementing these far reaching commitments and their relevant domestic adjustments. And to date, there is no information that any of the member countries has undertaken major changes or modifications to its domestic regulations in these areas.

2.3.3.7. Trade Facilitation

In order to reduce the cumbersome, time-consuming and costly procedures that are faced by the business community in the conduct of international trade, COMESA has adopted and is implementing a number of measures on the simplification and harmonization of trade documents and customs procedures. In this regard, the member countries acceded to the International Convention on the Simplification and Harmonization of Customs Procedures. The Convention provides a modern basis for customs administration. But these procedures have not yet been fully implemented by the members.

2.3.3.8. Trade in services

COMESA does not cover liberalization of trade in services. However, based on Article 164 of the Treaty, the members agreed to adopt, individually, at bilateral or regional levels, the necessary measures in order to progressively achieve the free movement of persons, labor and services, and to ensure the enjoyment of the right of establishment and residence by their citizens within the

[18] No data on the actual legal investigations is currently accessible.

CM. They agreed that the Protocol on the Gradual Relaxation and Eventual Elimination of Visa Requirements within the PTA adopted under the PTA Treaty shall remain in force until such time that a Protocol on the Free Movement of Persons, Labor, Service, Right of Establishment and Residence enters into force. But in reality, no negotiations on any modalities or legal frameworks for the liberalization of trade in services took place to date.

There are current talks on cooperation in the field of investments and services. But this has not resulted in any agreement yet. The Secretary of COMESA sent to the Egyptian Agreements Office of the Ministry of Industry and Foreign Trade a request to come together with the representatives of the different sectors in Egypt and to choose the first four sectors that would be worth considering at the beginning.

2.4. The Euro-Mediterranean Partnership Agreement (Euro-Med)

2.4.1. Overview

In January 1977, the General Cooperation Agreement (GCA) was signed between Egypt and the EC. Its main objective was to develop the economic, technical and financial cooperation between Egypt and the EC. This was to be achieved through the provision of an improved access for the Egyptian exports in the EC market accompanied by financial and technical assistance within the context of financial protocols. The Egyptian industrial exports (excluding sensitive commodities as textiles and fabrics as well as some processed agricultural products) entered duty-free to the EC markets, and preferential access for some agricultural commodities was provided[19]. The Agreement was not reciprocal, and Egypt continued to apply the MFN tariffs to goods of EC origin. A number of additional protocols were signed afterwards in order to organize the trade relations in certain sectors such as coal and steel (which are also considered sensitive products) or to reduce the negative effects of the accession of Spain and Portugal to the EC on the access of the Egyptian products, especially agricultural products.

After 18 years of increasingly intensive bilateral trade and development cooperation between the 15 member states of the EU and their 12 Mediterranean Partners, the 27 countries held the Conference of EU and Mediterranean Foreign Ministers in Barcelona (27-28 November 1995). In

[19] An elaborated review of cooperation and association agreements between the EC and the Mediterranean countries is available in Bahadir (1997).

this conference a new framework for the relationship between the EU and the South Mediterranean countries was set up. This new setup was announced under the so-called Barcelona Declaration which marked the start of a new 'Partnership' phase of the relationship including bilateral and multilateral or regional cooperation to reach the largest FTA in the world by 2010. The original EU countries (EU15) are Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden and the United Kingdom. The new EU countries after the recent enlargement (2004) are Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia. The Mediterranean countries of Euro-Med are Algeria, Egypt, Israel, Jordan, Lebanon, Morocco, Palestine, Syria, Tunisia and Turkey[20].

Concerning the Egyptian case, Article 6 of the additional Protocol that supplemented GCA in 1987 had determined that by the year 1994 the EU and Egypt should evaluate the past cooperation between them within the context of the Agreement and its additional protocols. After two rounds of exploratory talks in July and September 1994, formal negotiations on the details of the Egyptian-European Partnership started in January 1995. Since then, a series of negotiation rounds have been held in Brussels and Cairo to draft an Egyptian-European Partnership Agreement that is meant to change the philosophy of the relationship from a donor-recipient basis to a more reciprocal basis, to deepen the existing level of economic relations and, to widen the scope of the relations beyond the conventional economic field. This aimed at encompassing all the areas that the parties find necessary, useful and possible. The negotiations with Egypt were concluded in June 1999, and the Egyptian-European Partnership Agreement was signed in June 2001.

On the EU side, starting from 01.01.2004, a complete dismantling of customs duties and other charges having equivalent effects on the Egyptian industrial products was supposed to occur without any quantitative restrictions, with the exception of textiles and ready-made garments. These two products were subject to quotas.

On the Egyptian side, a 25 percent customs duties reduction a year for European raw materials and industrial equipment was planned for the period from 01.01.2004 to 01.01.2007. From 01.01.2007 to 01.01.2013, a 10 percent customs duties reduction in the first year and 15 percent

[20] Before the EU enlargement, Cyprus and Malta were also in the Partnership Agreement, but they were in the Mediterranean part of the Agreement.

in each successive year for European industrial supplies, semi-manufactured goods and construction materials are supposed to take place. From 01.01.2009 to 01.01.2016, a 5 percent customs duties reduction in the first and second year and 15 percent customs duties reduction in the following years for European clothes, electrical domestic appliances, cosmetics, furniture and motor vehicles for the transport of goods) are expected to take place according to the time plan. Finally, from 01.01.2010 to 01.01.2019, European motor vehicles designed for the transport of persons are supposed to be subject to a 10 percent customs duties reduction each year, as can be seen in *Table 2.2*.

Table 2.2.: The most important dates in the Egyptian-European Partnership Agreement

Date	**Event**
January 1995	Start of formal negotiations with Egypt
27th to 28th of November 1995	Barcelona Process, marking the start into a new 'Partnership' phase of the relationship between the EU and the Mediterranean countries, including bilateral and multilateral regional cooperation.
June 1999	Negotiations with Egypt concluded.
2010	Planned year for FTA
Starting from 01.01.2004	-A complete dismantling of customs duties and other charges having equivalent effect for Egyptian industrial products. -No quantitative restrictions.
From 01.01.2004 to 01.01.2007	25 percent customs duties reduction each year (European raw materials and industrial equipment).
From 01.01.2007 to 01.01.2013	10 percent customs duties reduction first year and 15 percent customs duties reduction each successive year (European industrial supplies, semi-manufactured goods and construction materials).
From 01.01.2009 to 01.01.2016	5 percent customs duties reduction first and second year and 15 percent customs duties reduction each successive year (European clothes, electrical domestic appliances, cosmetics, furniture and motor vehicles for the transport of goods).
From 01.01.2010 to 01.01.2019	10 percent customs duties reduction each year (European motor vehicles designed for the transport of persons).

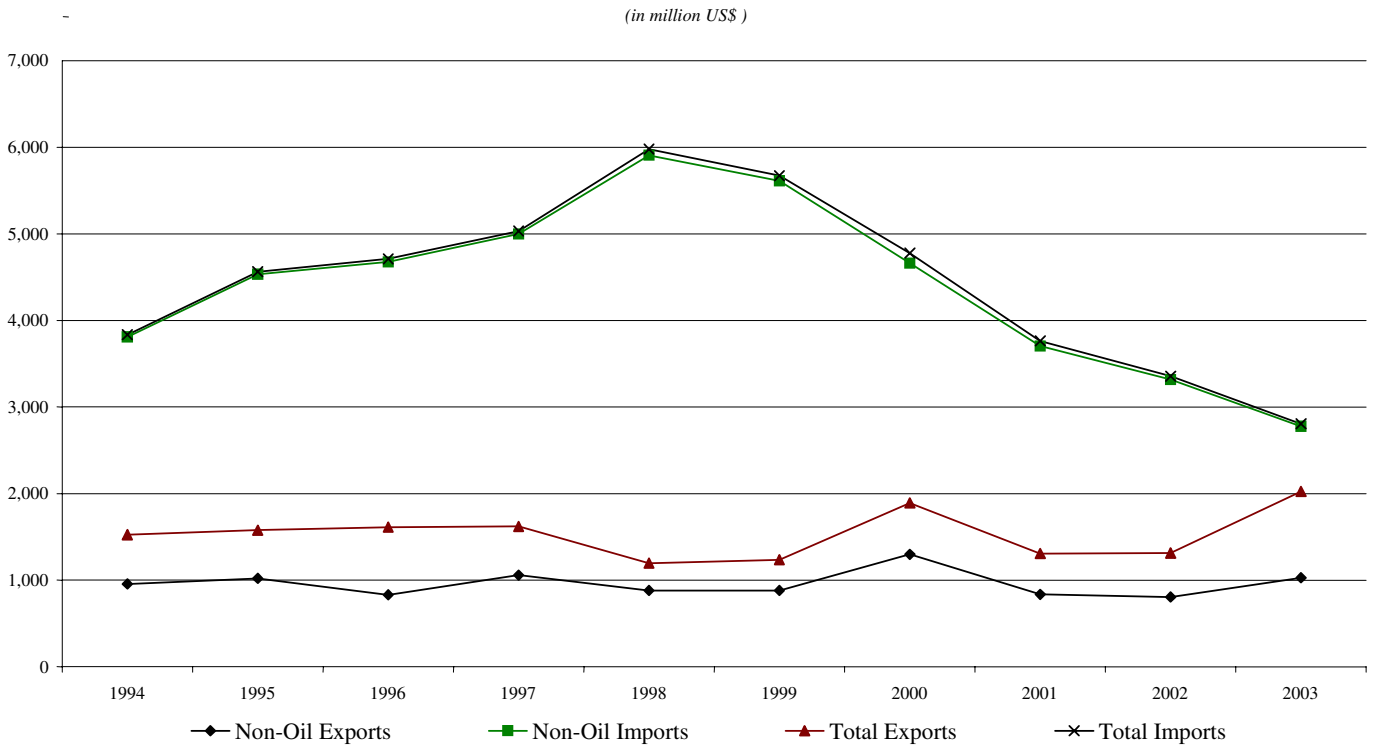
Source: Ministry of Industry and Foreign Trade (2003)

2.4.2. The trade flows between Egypt and the EU countries

The trade between Egypt and the EU15 increased from US$ 5.4 billion in 1994 to reach a maximum of US$ 7.2 billion in 1998. Then it dropped to US$ 4.8 billion by 2003. As a percentage of Egypt's total trade, the share of trade with the EU15 was 42 percent in 1994 and decreased to 28 percent in 2003. The trade deficit between Egypt and the EU15 has widened from US$ 2.3 billion in 1994 to reach US$ 4.8 billion in 1998. Then it fell to US$ 782 million in 2003. On the exports side (including oil), Egypt increased its exports from US$ 1.5 billion in 1994 to US$ 2 billion in 2003 with a 7 percent average rate of growth, whereas on the imports side, Egypt decreased its imports (including oil) from US$ 3.8 billion in 1994 to US$ 2.8 billion in 2003 with a -2 percent average annual rate of growth. The picture changes significantly if oil is excluded, where exports increased from US$ 954 million in 1994 to US$ 1 billion in 2003, while for the imports there is no significant change. *Figure 3* shows the development of the trade between Egypt and the EU15 during the period from 1994 to 2003. The non-oil exports experienced a very modest increase of around US$ 46 million, where it started from a base of US$ 954 million in 1994 and ended up with US$ 1 billion in 2003.

The Egyptian trade deficit with the EU15 has been chronic. It increased from 1994 onwards and reached its peak in 1998, where it started to decline afterwards. The overall picture reveals a reduced deficit, mainly due to the higher average annual growth rate of exports (7 percent) than the modest increase of imports which averaged -4 percent on annual basis during the period 1994-2003.

Figure 3: Egypt's Trade with the EU



Source: World Integrated Trade Solution (WITS) Database, World Bank, 2004.

2.4.3. The Egyptian-European Partnership Agreement state of implementation

The Agreement started to be implemented in 2004. There is no enough time that has elapsed to identify any problems in implementation, but at the same time, there are no recorded incidents of any worrisome problems that faced the implementation of the Agreement, and so far, the tariff reductions have taken place according to schedule.

2.4.3.1. Product coverage

The Egyptian-European Partnership Agreement includes a number of fisheries and processed agricultural products that are either subject to tariff quotas (in the case of agricultural goods and fisheries) or other terms of restricted or delayed liberalization of processed agricultural goods. Such terms differ from one product to another and the Association Council has the right to change the terms when deemed necessary.

Although the officials believe that the Egyptian-European Partnership Agreement has a high potential for Egypt, they argue that many of the products that are covered in the Agreement are not traded, so far, between the two sides.

A problem in dealing with the countries of the EU is the fact that they strongly protect their agricultural products. Therefore, they introduced the Common Agricultural Policy that applies to any country signing an agreement with them. This policy is the reference for any deal concerned with agricultural products. The policy includes the quotas system, although the GATT itself calls for calling off the quotas. Egypt could have negotiated this problem and asked for a full cancellation of the quotas, but it did not for two reasons; firstly, Egypt would have had to accept all the imported agricultural products quota-free, which would enormously harm the local farmers. Secondly, the EU quota for the Egyptian agricultural products is generous: It is six times what the EU really imports from Egypt, while the Egyptian quota for the EU agricultural products is only 14 percent of what the EU really exports to Egypt.

2.4.3.2. Rules of Origin

The RoOs under the Egyptian-European Partnership Agreement are relatively complicated and follow a mixture of value added, change of tariff headings, and specific production processes that indicate the sufficient transformation of the traded products. Bilateral cumulation is allowed as well as diagonal cumulation with the South Mediterranean countries, as long as the latter follow the same system of RoO and conclude an FTA between them. Since not all of these countries have done that, the diagonal cumulation is not always valid.

The officials in the Egyptian Ministry of Foreign Affaires believe that the most 'dangerous' column in the Protocol for RoO is the one concerning the sufficient transformation. For example, the EU does not plant the coffee but imports it raw from African non-members of the Agreement. And in order to give this coffee a sufficient European origin, the EU countries smash and heat it. On that occasion, the same officials claim that the RoO of the European Partnership Agreements have been set to serve for the interests of the EU industries rather than their Mediterranean partners; for example, when the Egyptian officials asked to be informed in detail about the RoO of the Agreement, the European personnel providing them with the information were not government officials like it is in the case of Egypt, but people really involved in the industrial

sector. Furthermore, the Egyptian officials discovered that the European factories comprise departments specialized in the issues of origin, which is completely missing in Egypt and the countries of the Arab world, and hence, reduces their bargaining power.

2.4.3.3. Trade in services

The Egyptian-European Partnership Agreement does not cover the liberalization of trade in services. However, the parties will consider extending the scope of the Agreement to include the right of companies' establishments of one party in the territory of another party as well as the liberalization of the services supply by companies of one party to serve the consumers in another party.

2.5. The Aghadir Agreement

2.5.1. Overview

The Barcelona process that started in 1995 had the objective of strengthening relations between the then 15 EU members and the 12 South Mediterranean countries. To make the aims of the Barcelona Process attainable, a need was seen to intensify "South-South" co-operation among the Mediterranean partners, starting - where appropriate - on a sub-regional basis. Each partner's willingness to build good relationships with its neighbors should be an important determinant of its readiness to move closer to the goal of close cooperation and integration with the EU countries.

In the 4th Euro-Med Conference of Foreign Ministers (Marseilles, 15-16 November 2000), the Ministers welcomed the desire expressed by four Arab Mediterranean countries that are part of Euro-Med (Egypt, Jordan, Morocco and Tunisia) to establish an FTA amongst themselves. This initiative ended by the decision for the Agreement on the 8th of May 2001 in Aghadir, Morocco. Negotiations of the Aghadir Agreement - also called Med-Arab Free Trade Area (MAFTA) - were concluded in January 2003, and the Agreement was signed on the 25th of February 2004 in accordance with the provisions of GATT for the year 1994 and the other agreements attached to the WTO. The initiative is open for other Arab countries wishing to join in. For example, Algeria, Lebanon and Syria are expected to join the Aghadir Agreement after meeting all the necessary conditions and requirements.

The RoO in the Aghadir Agreement follow the so-called Pan-European RoO, where the main intention behind it is to allow for bilateral and diagonal cumulation among Aghadir members, in order for them to enter the EU markets duty free. The importance of the Aghadir Agreement for the signatory countries would be that the common RoO they will adopt in their trade with the EU is expected to enable these countries to manufacture jointly in diagonal cumulation and then export the end product to the EU. In this case, a manufacturer can use any raw material or component from the area in the manufacture of finished products, without running the risk of losing free trade status if it is exported within the area (GACICI).

2.5.2. The trade flows between Egypt and the Aghadir countries

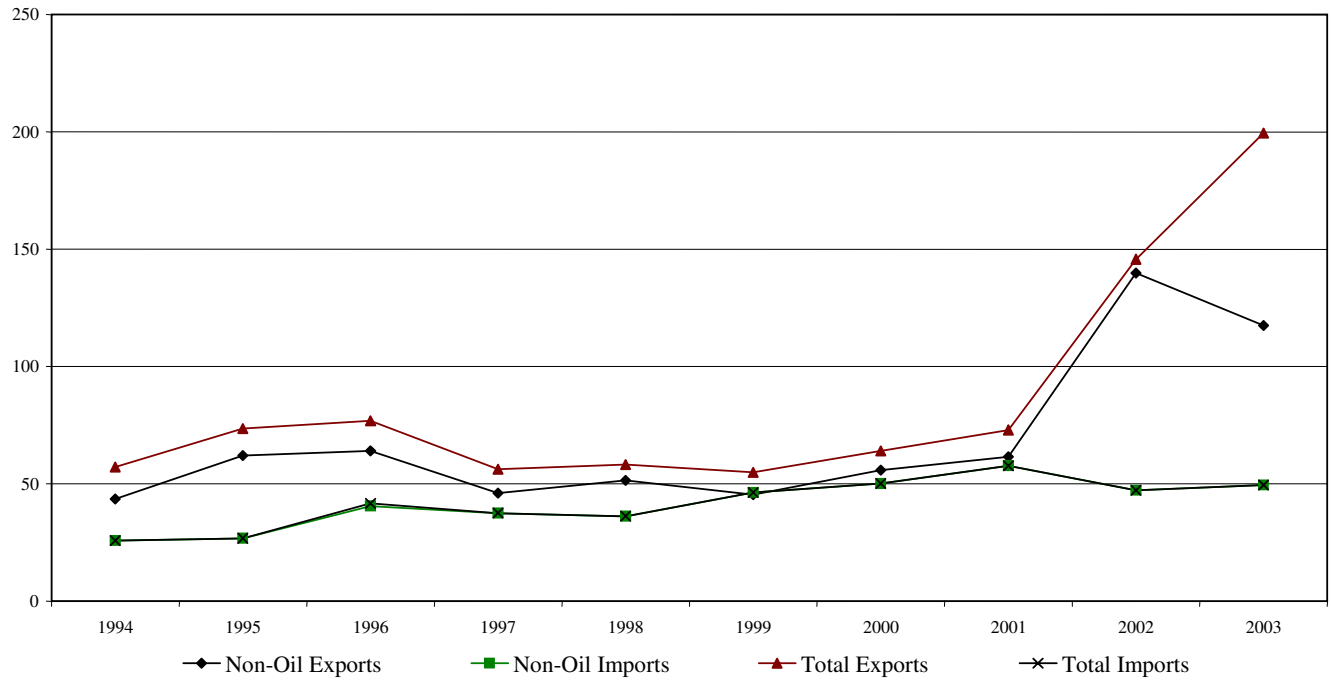
The trade between Egypt and the Aghadir countries increased from US$ 83 million in 1994 to US$ 249 million in 2003. As a percentage of Egypt's total trade, the share of trade with the Aghadir countries was 0.6 percent in 1994 and barely increased to 1.5 percent in 2003. The trade between Egypt and the Aghadir countries witnessed a surplus throughout the period 1994 till 2003, with the exception of 1999. The surplus widened from US$ 18 million in 1994 to reach US$ 98 million in 2003. On the exports side (including oil), Egypt increased its exports from US$ 57 million in 1994 to US$ 200 million in 2003 with an average annual rate of growth of 19 percent, whereas on the imports side, Egypt increased its imports (including oil) from US$ 26 million to US$ 50 million with an average annual rate of growth of 9 percent. Non-oil exports increased from US$ 44 million to US$ 117 million while for imports there is no change. *Figure 4* shows the development of trade between Egypt and the Aghadir countries over the period 1994 to 2003.

The case of Aghadir is the only case where Egypt has enjoyed a chronic trade surplus. However, this surplus has varied widely over the period investigated. Oil represents a major component in the Egyptian exports to the Aghadir countries (around 20 percent in 1994), and increased slightly as a percentage of total exports in 2003. The growth rates of both exports (oil and non-oil) and imports have been stable.

Figure 4:

Egypt's Trade with Aghadir Countries

(in million US$)



Source: World Integrated Trade Solution (WITS) Database, World Bank, 2004.

2.5.3. The Aghadir state of implementation

Aghadir follows GAFTA in terms of the agricultural liberalization; agricultural and processed agricultural products shall be liberalized in accordance with the Executive Program of the Agreement on Facilitation and Promotion of Trade Exchange among the Arab countries.

The Agreement does not liberalize trade in services beyond GATS commitments. Members shall implement their obligations as stated in the WTO's specific schedules of GATS and shall endeavor to expand the scope of this trade, in accordance with the rules and regulations in force. The Ministerial Committee shall periodically examine any developments in the services trade among members after the entry into force of this Agreement.

The Agreement was supposed to enter into force by the year 2003, where tariffs would be decreased by 65 percent, followed by a decrease by 80 percent on 01/01/2004, by 90 percent on

01/01/2005, and finally by 100 percent on 01/01/2006. Nevertheless, since Jordan has not yet ratified the Agreement, the latter is still frozen and has not entered into force. Egypt and Tunisia ratified in 2004 and Morocco in 2005. This implies that the schedule of tariffs reduction mentioned above is meaningless, especially that GAFTA has surpassed Aghadir, and hence, the zero tariff target among Aghadir members was achieved under the GAFTA before Aghadir.

2.6. A comparison between the legislative, regulatory and administrative commitments of the Egyptian RTAs

In this section, we focus on the difference between the four RTAs. We use a sectoral approach, where we discuss various issues and assess how they are managed in different RTAs. We complement our analysis by referring to the Egyptian laws, regulations, and organizations that have been established to handle such RTAs.

2.6.1. Product coverage of merchandise trade

The COMESA has the widest coverage, followed by GAFTA which had negative lists that are still questionable, followed by Aghadir. In the case of the Egyptian-European Partnership, agricultural products and fisheries follow certain procedures that in some cases are clearly determined and in others left for the future negotiations. Problems and areas of conflict can arise in the case of processed agricultural goods covered by Aghadir but follow other norms in the Egyptian-European Partnership Agreement.

2.6.1.1. Industrial products

The four RTAs differ significantly in terms of their transitional periods. The longest is the Egyptian-European Partnership Agreement, where the transitional period is 12 years, with the exception of cars with 16 years. The GAFTA follows with an initial 10 years transitional period which was later shortened to 8 years. COMESA has a shorter period for Egypt which was fully implemented in 2 years. Aghadir is supposed to have a short transitional period of 2 years. It should be noted that the approach for tariff reductions differs significantly between the Egyptian-European Partnership Agreement on one hand, and the three other Agreements on the other. In

the case of the Egyptian-European Partnership Agreement, tariffs on industrial goods are classified under three main categories, each lasting for four years. The three other RTAs adopt a simpler approach of 'across the boarder' equal tariff reductions without differentiating between the types of goods.

2.6.1.2. Agricultural products

In the Egyptian-European Partnership Agreement, duty-free quotas are allowed for some commodities, but are not expanded over time. The GAFTA entailed in the transitional period a negative list 'Farmer's Roznama". However, it had a time limit, and was officially abolished by 2005. Aghadir does not allow for any negative lists. Theoretically, and according to the Treaty, COMESA is free of negative lists. But in practice, it is difficult to detect this issue, since the trade within COMESA contains goods that can be subject to quotas or extra surcharges or tariffs, such as the case of sugar between Egypt and Kenya.

2.6.2. Services

The Egyptian-European Partnership Agreement confined its obligations to GATS. However, it extended it in a vague flexible form for starting negotiations after five years from entry into force of the Agreement, hereby allowing for further potential liberalization. GAFTA did not include services but follows the Framework Agreement on the Liberalization of Trade in Services concluded in 2003. The latter obliges its signatories to go beyond GATS, whether in terms of extra sectors or deepening the existing ones. COMESA includes a clause for progressive liberalization of trade in services. It is as vague as the case of the Egyptian-European Partnership Agreement but is better in the sense that it allows flexibility in terms of either adopting the liberalization on bilateral or collective basis[21]. The Aghadir Agreement is the vaguest RTA as compared to the three others, since it is the least Agreement that emphasizes on the issue of services liberalization, although its members are also members of GAFTA. Moreover, problems can rise in case of countries that are members of both COMESA and GAFTA.

[21] Based on Article 164, the member countries agreed to adopt, individually, at bilateral or regional levels the necessary measures, in order to achieve progressively the free movement of persons, labor and services and to ensure the enjoyment of the right of establishment and residence by their citizens within the CM.

2.6.3. Intellectual Property Rights (IPR)

None of the RTAs went further beyond the Trade-Related Aspects of Intellectual Property Rights (TRIPS) of the WTO. Aghadir is the only Agreement that refers explicitly to TRIPS, whereas GAFTA mentions that the consultation over IPR shall take place in the future, without identifying a specific date. COMESA does not include any article related to IPR, whereas the Egyptian-European Partnership Agreement asks for adopting the highest prevailing international standards regarding IPR without mentioning explicitly what these highest prevailing international standards are.

It is worth mentioning that Egypt has released a comprehensive IPR law that is in line with the TRIPS requirements. The problem with IPR is the high cost of enforcement and the lack of human capacity able to implement the law efficiently. Egypt has received substantial amount of aid, especially from the USA to upgrade its IPR system.

2.6.4. Standards

None of the RTAs went beyond the WTO requirements concerning the standards. In fact, all the Agreements call for cooperation in the field of harmonization of standards in the future. The Egyptian-European Partnership Agreement and Aghadir even call for mutual recognition. However, in practice all the Agreements were extremely flexible in their wording without identifying concrete steps to be undertaken or specific dates to be followed.

The Egyptian Organization for Quality and Standardization (EOQS), which is in charge of setting Egyptian standards, is working on harmonizing the Egyptian standards with the European ones. The problem is the lack of enforcement and mixing safety with health measures. This was evident in several incidents between EOQS and the Egyptian Ministry of Health, where the interpretation of many provisions was absent. Furthermore, Egypt lacks an internationally recognized body that is able to accredit standards. There is a number of internationally accredited labs, but they are few and do not cover all the fields.

2.6.5. Dispute settlement systems

GAFTA still does not include a dispute settlement system, but in 2004 the ESC approved the executive decree of a dispute settlement mechanism, which is still not functioning, as this system is still not adopted and even the list of judges is still incomplete. For example, in the year 2005, Saudi Arabia refused to import Egyptian potatoes. The argument was as follows: Saudi Arabia 'was informed' that the Egyptian potatoes are infected with the brown rot disease, without showing clear evidence or examining the Egyptian potatoes beforehand. However, Egypt could not strike back, since there is no such system in GAFTA that protects harmed countries, in this case Egypt.

The executive decree for dispute settlement within GAFTA includes the following steps: 1) Bilateral consultations between the two countries in dispute; 2) Arbitration and 3) Referring to the Investment Court.

COMESA calls for the establishment of a Court of Justice (Chapter Five of the Treaty) to solve related problems. To date, most disputes have been handled through bilateral consultations and discussions of ministerial meetings. No details are available on these disputes, which implies non-transparency.

The Egyptian-European Partnership Agreement has a clear dispute settlement mechanism, mainly handled by the Association Council, while Aghadir has a clear dispute settlement mechanism, mainly handled by the Ministerial Committee.

2.6.6. Competition policies

This is one of the main areas where incompatibility among the different RTAs is present and can create certain difficulties in their implementation, since each is expected to follow different norms.

GAFTA has no specific provision on competition, but it calls for the harmonization of the Common Competition Policy, although only four GAFTA members have a competition law (Egypt, Jordan, Morocco, and Tunisia, also Aghadir members). Beyond GAFTA, the ESC has recently adopted a set of guidelines in the form of non-binding rules that the member countries

should follow while designing and introducing their competition laws. The working party on competition policy remains operative and is supposed to hold annual meetings to consult on the developments in the introduction and implementation of competition laws.

COMESA is among the very active RTAs in terms of having a regional competition policy. Despite the fact that this competition policy is still not enacted, several serious steps have been undertaken by the Secretariat. An expert group has already concluded a draft for the competition law of COMESA. This draft is quite comprehensive with a clear view of the implementation methodology and the establishment of a Common Competition Authority. Nonetheless, the divergence in legal, political, and economic systems prevailing in the member countries makes the actual feasibility of implementation highly questionable. It is worth mentioning that this draft sets a precedent, in the sense that it explicitly states that it will supersede the national legislations of the member countries in the case of contradictions.

The Egyptian-European Partnership Agreement has a specific provision on competition; all agreements between undertakings, decisions by associations of undertakings, concerted practices between undertakings and any public aids which have as their object or effect the prevention, restriction or distortion of competition, are incompatible with the proper functioning of the Agreement. Abuses are handled by the Association Committee. At the time of signing the Agreement, Egypt did not have a competition law. Therefore, the wording of the Agreement was as follows: “The parties recognize that Egypt is currently in the process of drafting its own competition law. While drafting its law, Egypt will take into account the competition rules developed within the EU. If serious problems arise, the parties may raise the matter for consideration in the Association Council.” There is no mention in the Aghadir Agreement on competition issues.

It is worth mentioning that Egypt has released its competition law in 2004, which is still not enforced, since the executive regulations are still not issued and the Competition Authority is not established. The issuing of the competition law came after a long period (since 1995) of drafting different versions that reached 18 drafts. Part of the pressure on issuing the law came from the EU.

2.6.7. Customs coordination

GAFTA calls for the harmonization of the external tariffs in the context of a CU. However, the committee responsible for this CU has never met.

COMESA did not include any article on customs coordination, although it should have reached a CU by 2004. The procedures and mechanisms for establishing a CU were not included in the Agreement, although the title of the latter indicates that it even aims at achieving a further target, which is the creation of a CM.

A vital problem among GAFTA and COMESA is the fact that the countries of each Agreement of them does not have a unified tariff towards the rest of the world as it is the case among the EU countries[22]; although the tariffs among the Arab countries have been completely eliminated after January 2005, towards third parties, the tariffs of the Arab countries are highly diverse. For example, the external tariffs in Syria are on average 62.5 percent, in Egypt 40 percent and in Saudi Arabia 5 percent. Egypt produces refrigerators for a relatively cheap price and low quality. According to the GAFTA rules, after January 2005, it exports the refrigerators to Saudi Arabia tariff free. However, Saudi Arabia imports from the EU refrigerators that are a bit more expensive, but enter Saudi Arabia with a 5 percent tariff level and with higher quality. The logic result is that the Saudi Arabians prefer the EU refrigerators, even if they are a bit more expensive. This means that the Egyptian products cannot be competitive in some other Arab markets, if the countries of the latter have very low tariffs towards the rest of the world. Even the Egyptians would prefer to buy the more expensive high quality refrigerators, but what hinders them is the fact that the tariff rates on imported refrigerators from non-members of Egyptian RTAs exceed 200 percent. But if the Egyptians export their refrigerators to Syria, there would be a difference from the case of Saudi Arabia, because the difference in the price between Egyptian refrigerators and European refrigerators in Syria would be quite high, and the Syrians might prefer - or rather can afford - to buy the Egyptian ones.

[22] In COMESA, there was supposed to be a CU by the beginning of 2004, but it was not applied, since not even an FTA among all its member countries was established. As for GAFTA, an FTA apparently took place by the beginning of 2005, but a CU is not foreseen.

The Egyptian-European Partnership Agreement calls for cooperation in the field of customs procedures without identifying any clear steps in this regard. The Aghadir Agreement does not contain any provisions regarding customs coordination.

2.6.8. Trade remedies (including safeguards, countervailing measures, and AD)

AD rules and countervailing measures differ substantially among the RTAs, where the Egyptian-European Partnership and Aghadir Agreements are the most transparent. In case of COMESA and GAFTA, the rules refer to international standards, without defining these international standards. In the case of COMESA, there are some rules that govern AD, but the mechanism of applying such rules remains absent. In the case of GAFTA, the AD disputes can be solved via the dispute settlement mechanism initiated by the ESC.

In the area of safeguards, the Egyptian-European Partnership and Aghadir Agreements follow the same norms of WTO, while GAFTA and COMESA follow the decisions of the ESC and the confined council, respectively. The application of different safeguard mechanisms is not likely to create serious problems when the RTAs are implemented.

Regarding the Arab BTAs, we observe that the AD measures are absent in the case of the Agreement with Libya and to be solved by the Joint Committee in the case of Syria. As for Tunisia and Morocco, the AD measures are supposed to follow the WTO rules. In the Agreement with Lebanon, the AD measures do not yet exist, and in the Agreement with Jordan a special Article following WTO rules and regulations is to be followed. In the Agreement with Iraq, a special Article is devoted for that purpose, and the Agreement with Sudan follows the COMESA rules.

2.6.9. Government procurements

GAFTA has an Article that calls for preferential treatment of the countries of the Agreement in the government procurement projects (Article 8 of GAFTA). However, in reality, no consultation took place. The Egyptian-European Partnership Agreement does not include government procurements but refers to progressive future liberalization in vague terms. COMESA did not include any preferential treatment but makes sure that no discrimination with third countries takes

place. Aghadir did not include any provisions on preferential liberalization of government procurements.

2.6.10. Duty drawback

Concerning duty drawbacks, there are large differences among the RTAs. The former is granted in the transitional period of GAFTA (ten years that were reduced to eight), only for six years in the Egyptian-European Partnership Agreement, eligible for certain products within limits in the case of Aghadir (also for six years from entry into force), and it is not clear in the case of COMESA. This could result in problems in application, even in the most two harmonized Agreements (Egyptian-European Partnership and Aghadir Agreements), where the Aghadir Agreement has not yet entered into force, and therefore, the cancellation of the duty drawback cannot take place in the year 2009.

2.6.11. Standardization and conformity assessment

The Standardization and conformity assessment is one of the main areas that can create several problems in coordination and implementation. All the RTAs call for harmonization and mutual recognition. Nevertheless, the terms of implementation and schedules for harmonization and mutual recognition schemes are not clear.

2.7. Summary and main findings

This chapter identifies the differences between the four RTAs under study. In some cases, there is a wide gap between the provisions of the RTAs and what is implemented in reality. GAFTA and COMESA are clear examples of non-transparency in this regard. Many provisions of these two RTAs need more development, elaboration and editing, and many of the clear provisions have not been implemented to date.

The time that passed since the implementation was too short to allow for testing for this gap in the case of the Egyptian-European Partnership Agreement, although the latter seems to be promising, and the provisions have been implemented so far. The Aghadir Agreement has not entered into force yet, since the member countries are waiting for Jordan to ratify it.

In general terms, the overlapping of the RTAs does not seem to entail a lot of costs, since they are shallow, and hence, the deep aspects (as harmonization of rules and regulations) are still not in effect, which creates less friction and problems arising from the overlapping. An example for the violation of this rule is the case of Sudan, where it is not known whether the commercial deals between Egypt and Sudan should follow the rules of GAFTA or COMESA, as the two countries are members of both Agreements. Another example is the clashing between GAFTA and the Arab BTAs. Nevertheless, the authorities give the importers and exporters the space for choosing among the Agreements to be applied in their special cases. Although the EU is regarded as one trading bloc, Egypt still needs to consider the differences between the specific standards of each separate EU member, in addition to the common standards written in the Egyptian-European Partnership Agreement. Unfortunately, many Egyptian exporters are still not aware of these conditions and standards. As for the overlapping of the RoO in specific, it will be discussed in more detail in *Chapter 6*.

CHAPTER 3

Egypt's Expected Gains from Implementing its Regional Trade Agreements

3.1. Introduction

This chapter sheds a light on the expected gains from implementing GAFTA, COMESA, Euro-Med and Aghadir. It focuses on the concept of FTAs, since the four RTAs are based on this form of integration. Then the expected static, dynamic and institutional effects of the four RTAs are assessed.

3.2. Free Trade Areas

As mentioned before, in an FTA all tariff barriers among members are removed from all goods. However, each nation keeps its own tariff barriers to trade with non-members. In the following, the static, dynamic and institutional effects of forming an FTA will be discussed, taking Egypt and the RTAs it is involved in as a case study.

3.2.1. The expected static effects of implementing the RTAs

As already indicated in *Chapter 1*, an FTA is more likely to lead to trade creation if the economies of the member countries are competitive rather than complementary[23], the pre-FTA trade and economic relationship among potential members of the agreement is rather great, the geographic distance between the member countries of one FTA is rather short, the FTA-size is rather large, the pre-FTA trade barriers between the member countries are rather high and the FTA's barriers on trade with the rest of the world are rather low.

In this study, the sixth criterion concerning the barriers on trade with the rest of the world is hard to assess, since not all of the Agreements have been implemented yet and it is not possible to

[23] This is highly based on the intra-industry trade model mentioned before.

predict the barriers that will exist in case they would be fully implemented. In the following, the five other criteria will be covered.

3.2.1.1. The production and export structures of the member countries

In order to assess whether the production and export structures of the countries included in each Agreement are similar (rather competitive economies) to the production and export structure of Egypt, the Revealed Comparative Advantage (RCA) measure is used. This measure was first used by *Balassa* (1965). Since then the measure has been applied in numerous studies and papers, such as *Laursen* (1998), *TIPS*[24] (2000) and *Bender and K. Li* (2002). The RCA approach assumes that the true pattern of comparative advantage can be observed from post-trade data. The availability of data at different levels of aggregation and the data bias that might be caused by some government policy distortions (e.g. non-trade barriers and export subsidies) caused some damage to the "true" pattern of comparative advantage. However, Balassa's "stages of comparative advantages" thesis advocated a "catch up" process that shifts economies from one area of comparative advantage to another. Typically, when developing countries take over the labor-intensive product lines from industrialized countries, the production shift provides room for the developed countries to concentrate on the export of technology-intensive products (Bender and Li, 2002).

The typical RCA[25] - which is also used in this study - takes the following fraction:

$$\mathbf{RCA} = \frac{\mathbf{(Xij/Xwj)}}{\mathbf{(\Sigma Xi/\Sigma Xw)}}$$

where Xij/Xwj = the ratio of country i's exports of commodity j to the world's exports of the same commodity,
and ΣXi/ΣXw = the ratio of country i's total exports to the world's total exports.

The data used are the current dollar value of imports in the year 2000, per commodity and country of origin as reported by each importing country, for 240 commodities in the Standard International Trade Classification revision 2 (SITC rev 2).

[24] Trade and Industrial Policy Secretariat.

[25] The typical RCA measure was also used by El-Khawaga et al. (1999)

Imports are expressed in most cases using the Cost, Insurance and Freight (CIF) value. These import values may differ from those concerning the same trade flow (same year, product, country of origin and country of destination) as registered by the exporting country, which are often measured using the Free On Board (FOB) definition (World Bank *Trade CAN* 2002)[26].

The RCA is calculated for a list of goods in Egypt and in each separate country and a comparison is run. If RCA is greater than 1 then this means that a country has an RCA in producing/exporting this good (specialization). If RCA is less than 1 the country does not have an RCA in producing/exporting this good (revealed comparative disadvantage or under-specialization) (Richardson 1999).

Using this criterion, the goods where Egypt and all other countries of the RTAs have a comparative advantage are obtained and compared, in order to detect the number of common goods where both Egypt and each separate country have a comparative advantage (*Table A* of Appendix II). Then the mean and median[27] of these numbers are calculated and compared with the number of common goods where each separate country and Egypt have comparative advantage. The countries where this number is greater than the mean (median) are considered relatively trade-creating with Egypt as compared to countries where this number is lower than the mean (median). As a next step, for each RTA the percentage of potentially trade-creating countries with Egypt to the total number of countries of the RTA is calculated. By comparing the latter percentage between the different RTAs it can be indicated which one of the latter can be considered trade creating relative to the other(s).

The mean and the median calculated are both around 12 goods, as can be seen from the same table and the results for each separate RTA are shown in *Table 3.1*. For GAFTA, in 5 out of 15 countries (around 33.3 percent of the countries), the number of goods where both Egypt and each concerned country have comparative advantage exceeds 12. For COMESA, this occurs in 5 out of 17 countries (around 29.4 percent of the countries). In Aghadir, the three countries (100 percent of the countries) fulfill this condition and finally 23 out of the 32 Euro-Med partner countries

[26] Due to the lack of detailed data and information about Palestine's and Swaziland's disaggregated exports, the latter are excluded here. Furthermore, in the Trade CAN data of 2002, Belgium and Luxembourg are merged as one country. This makes Egypt's available partner countries in GAFTA 15, in COMESA 17 and in Euro-Med 32 for this part of analysis.

[27] The median as a benchmark is more accurate in this case, since it divides the number of countries into two equal numbers and would not be biased to higher values as the mean could be.

(around 71.9 percent of the countries) exceed this benchmark. Hence, Aghadir takes the first rank in relative potential trade creation with Egypt, Euro-Med the second, GAFTA the third followed by COMESA at the end.

Table 3.1.: Countries having RCA in more than 12 common goods with Egypt

	GAFTA	**COMESA**	**EURO-MED**	**AGHADIR**
Countries having RCA in more than 12 common goods with Egypt (number of goods in brackets)	Jordan (14)	Djibouti (14)	Austria (13)	Jordan (14)
	Lebanon (22)	Eritrea (15)	Belgium & Luxembourg (20)	Morocco (21)
	Morocco (21)	Kenya (15)	Cyprus (15)	Tunisia (15)
	Syria (15)	Madagascar (18)	Czech Republic (17)	
	Tunisia (15)	Zimbabwe (22)	Estonia (14)	
			France (18)	
			Greece (26)	
			Israel (14)	
			Italy (20)	
			Jordan (14)	
			Latvia (19)	
			Lebanon (22)	
			Lithuania (24)	
			Morocco (21)	
			Netherlands (19)	
			Poland (24)	
			Portugal (21)	
			Slovakia (21)	
			Slovenia (15)	
			Spain (23)	
			Syria (15)	
			Tunisia (15)	
			Turkey (26)	
Percentage of these countries to the total number of countries in the Agreement	***33 percent***	***29.4 percent***	***71.9 percent***	***100 percent***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

To broaden the analysis, the correlation coefficient between the RCA index (including the 240 goods) of Egypt and each separate country is obtained and compared among the four Agreements. But first the RCA has to be adjusted (Symmetric RCA). Otherwise there exists no normality around the unity, since the values greater than one range between 1 and infinity while the values smaller than one range between 0 and 1. As *Vollrath* (1991) suggests, the possibility of taking the

logarithm of the RCAs exists, but in the case of zero exports the results would not be identified. Therefore the formula introduced by *Laursen* (1998) is used. It is formulated as follows:

Adjusted (Symmetric) RCA:

$$\textbf{SRCA} = \frac{\textbf{RCA} - 1}{\textbf{RCA} + 1}$$

The SRCA takes the values between -1 and +1, which means that it is normally distributed around the zero and does not give much weight to - and is not biased towards - values above unity. The values below zero indicate that there is weak competitiveness (weak RCA), whereas the values above zero indicate rather strong competitiveness (strong RCA) in a certain commodity.

Tables 3.2., 3.3., 3.4. and 3.*5.* show for each separate Agreement the correlation coefficients between the adjusted RCA index of Egypt and that of each country of the Agreement. They also demonstrate the average correlation coefficient for each Agreement. The results show Aghadir taking the first rank, GAFTA the second, COMESA the third and Euro-Med the fourth.

Table 3.2.: Correlation coefficients between the adjusted RCA index of Egypt and that of each country in GAFTA

Country	**Correlation Coefficient**
Bahrain	0.34337711
Iraq	0.154114233
Jordan	0.364551016
Kuwait	0.2105459
Lebanon	0.416329921
Libya	0.27800894
Morocco	0.432848354
Oman	0.244151777
Qatar	0.156843151
Saudi Arabia	0.194414953
Sudan	0.310145491
Syria	0.572121952
Tunisia	0.406096085
United Arab Emirates	0.37818085
Yemen	0.2128603
Average correlation coefficient	***0.311639336***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table 3.3.: Correlation coefficients between the adjusted RCA index of Egypt and that of each country in COMESA

Country	**Correlation Coefficient**
Angola	0.103257182
Burundi	0.060106733
Comoros	0.052986295
Congo (DR)	-0.047581659
Djibouti	0.183636653
Eritrea	0.196278347
Ethiopia	0.248892297
Kenya	0.34848119
Madagascar	0.442442577
Malawi	0.381783395
Mauritius	0.273978033
Rwanda	0.070549843
Seychelles	0.091783655
Sudan	0.310145491
Uganda	0.145594652
Zambia	0.246734443
Zimbabwe	0.430870653
Average correlation coefficient	**0.208231752**

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table 3.4.: Correlation coefficients between the adjusted RCA index of Egypt and that of each country in Aghadir

Country	**Correlation Coefficient**
Jordan	0.364551016
Morocco	0.432848354
Tunisia	0.406096085
Average correlation coefficient	***0.401165152***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table 3.5.: Correlation coefficients between the adjusted RCA index of Egypt and that of each country in Euro-Med

Country	Correlation Coefficient
Algeria	0.206499991
Austria	-0.045814554
Belgium and Luxembourg	0.084058114
Cyprus	0.337428781
Czech Republic	0.082952444
Denmark	-0.009798905
Estonia	0.219323677
Finland	-0.159833578
France	-0.005649992
Germany	-0.184305521
Greece	0.468853585
Hungary	0.103619586
Ireland	-0.089240997
Israel	0.202351539
Italy	0.090069157
Jordan	0.364551016
Latvia	0.3327036
Lebanon	0.416329921
Lithuania	0.333974352
Malta	0.129329002
Morocco	0.432848354
Netherlands	0.097530226
Poland	0.22957658
Portugal	0.233538462
Slovakia	0.157544588
Slovenia	0.056521068
Spain	0.116491233
Sweden	-0.192495138
Syria	0.572121952
Tunisia	0.406096085
Turkey	0.42939411
United Kingdom	-0.111810139
Average correlation coefficient	***0.165773706***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Again, the mean and median of the adjusted correlation coefficients of all countries in the four Agreements are taken as a benchmark for potential trade creation (*Table B* of Appendix II). For each separate Agreement, we take the number of countries where the correlation coefficient of their adjusted RCA with Egypt exceeds the median[28] as a percentage of the total number of countries of the same Agreement. This percentage is compared among the Agreements. As can be

[28] These countries are considered rather trade-creating to Egypt.

seen in *Table 3.6.*, Aghadir takes the first rank for potential trade creation with Egypt. Then come GAFTA, COMESA and Euro-Med in order. We obtain the similar results when taking the mean as a bench mark.

Table 3.6.: Countries that have an adjusted RCA correlation coefficient with Egypt exceeding the median

GAFTA		**COMESA**		**EURO-MED**		**AGHADIR**	
Bahrain	0.343377	Ethiopia	0.248892	Algeria	0.2065	Jordan	0.364551
Jordan	0.364551	Kenya	0.348481	Cyprus	0.337429	Morocco	0.432848
Kuwait	0.210546	Madagascar	0.442443	Estonia	0.219324	Tunisia	0.406096
Lebanon	0.41633	Malawi	0.381783	Greece	0.468854		
Libya	0.278009	Mauritius	0.273978	Israel	0.202352		
Morocco	0.432848	Sudan	0.310145	Jordan	0.364551		
Oman	0.244152	Zambia	0.246734	Latvia	0.332704		
Sudan	0.310145	Zimbabwe	0.430871	Lebanon	0.41633		
Syria	0.572122			Lithuania	0.333974		
Tunisia	0.406096			Morocco	0.432848		
UAE	0.378181			Poland	0.229577		
Yemen	0.21286			Portugal	0.233538		
				Syria	0.572122		
				Tunisia	0.406096		
				Turkey	0.429394		
Percentage of these countries to the total number of countries in the Agreement							
80 percent		***47 percent***		***46 percent***		***100 percent***	

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Using the same analysis after transforming the raw RCA results into dummy variables that take the value 1 if RCA is greater than unity and the value zero if RCA is less than unity, we obtain the results shown in *Tables 3.7., 3.8., 3.9.* and 3.*10.*; they indicate that the average correlation coefficient between the dummy RCA index of Egypt and that of other Aghadir countries is the greatest and the one of Euro-Med the least. GAFTA and COMESA take the second and third rank respectively. Once again we run the median (mean) analysis, but this time with the dummy variables (*Table C* of Appendix II). From the results shown in *Table 3.11.* we find out that the same ranks apply when using the median as a benchmark. And using the mean as a benchmark would also give us the same results.

Table 3.7.: Correlation coefficients between the dummy RCA index of Egypt and that of each country in GAFTA

Country	Correlation coefficient
Bahrain	0.237766253
Iraq	0.129302698
Jordan	0.189664392
Kuwait	0.13896574
Lebanon	0.278573691
Libya	0.197030096
Morocco	0.344794454
Oman	0.09874035
Qatar	0.139099243
Saudi Arabia	0.103884776
Sudan	0.263379506
Syria	0.470743905
Tunisia	0.262932635
United Arab Emirates	0.125300422
Yemen	0.123865339
Average correlation coefficient	***0.206936233***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table 3.8.: Correlation coefficients between the dummy RCA index of Egypt and that of each country in COMESA

Country	Correlation coefficient
Angola	0.097423741
Burundi	0.042521156
Comoros	0.097321571
Congo (DR)	-0.028131291
Djibouti	0.126138421
Eritrea	0.226869092
Ethiopia	0.227353287
Kenya	0.251392214
Madagascar	0.354939809
Malawi	0.277360654
Mauritius	0.237766253
Rwanda	0.039414928
Seychelles	0.171690567
Sudan	0.263379506
Uganda	0.122930377
Zambia	0.19381166
Zimbabwe	0.381359063
Average correlation coefficient	***0.181384765***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table 3.9.: Correlation coefficients between the dummy RCA index of Egypt and that of each country in Euro-Med

Country	Correlation coefficient
Algeria	0.175146742
Austria	-0.113481804
Belgium and Luxembourg	0.006752331
Cyprus	0.12731077
Czech Republic	-0.005918084
Denmark	-0.170114637
Estonia	0.139134302
Finland	-0.129372114
France	-0.056651271
Germany	-0.246459502
Greece	0.257108547
Hungary	0.013535164
Ireland	-0.109822472
Israel	0.139134302
Italy	0.006752331
Jordan	0.189664392
Latvia	0.324685212
Lebanon	0.278573691
Lithuania	0.294304601
Malta	-0.031499899
Morocco	0.344794454
Netherlands	0.006901373
Poland	0.127706076
Portugal	0.19786956
Slovakia	0.192140819
Slovenia	-0.010379652
Spain	0.070455239
Sweden	-0.169479343
Syria	0.470743905
Tunisia	0.262932635
Turkey	0.297712848
United Kingdom	-0.160358307
Average correlation coefficient	***0.084994444***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table 3.10.: Correlation coefficients between the dummy RCA index of Egypt and that of each country in Aghadir

Country	Correlation coefficient
Jordan	0.189664392
Morocco	0.344794454
Tunisia	0.262932635
Average correlation coefficient	***0.26579716***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table 3.11.: Countries that have a dummy RCA correlation coefficient with Egypt exceeding the median

GAFTA		COMESA		EURO-MED		AGHADIR	
Bahrain	0.237766	Eritrea	0.226869	Algeria	0.175147	Jordan	0.189664
Iraq	0.129303	Ethiopia	0.227353	Estonia	0.139134	Morocco	0.344794
Jordan	0.189664	Kenya	0.251392	Greece	0.257109	Tunisia	0.262933
Kuwait	0.138966	Madagascar	0.35494	Israel	0.139134		
Lebanon	0.278574	Malawi	0.277361	Jordan	0.189664		
Libya	0.19703	Mauritius	0.237766	Latvia	0.324685		
Morocco	0.344794	Seychelles	0.171691	Lebanon	0.278574		
Qatar	0.139099	Sudan	0.26338	Lithuania	0.294305		
Sudan	0.26338	Zambia	0.193812	Morocco	0.344794		
Syria	0.470744	Zimbabwe	0.381359	Portugal	0.19787		
Tunisia	0.262933			Slovakia	0.192141		
				Syria	0.470744		
				Tunisia	0.262933		
				Turkey	0.297713		
Percentage of these countries to the total number of countries in the Agreement							
73 percent		***59 percent***		***44 percent***		***100 percent***	

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Now it is clear that all the methods of analysis give us the same ranks for the four Agreements, except for *Table 3.1.* which is the only table giving Euro-Med the second rank in relative trade creation with Egypt. However, this high rank could be referred to the fact that many non-original EU countries and many Mediterranean countries (which are also part of GAFTA and Aghadir) are included in the Euro-Med classification; as can be seen in *Table 3.12.*, although 69.5 percent of the potential Euro-Med trade-creating countries are EU countries, only 34.8 percent of them are original EU-countries before enlargement. More than half (56.2 percent) of the EU potential

trade-creating countries are non-original EU countries. In general, non-original EU countries and Mediterranean countries represent the lion share (65.2 percent) of the potential trade-creating Euro-Med countries to Egypt. Moreover, the number of goods where the original EU countries have a high comparative advantage in general is high. Hence, the probability of having common competitive goods with Egypt is greater than this occurring between Egypt and African or Arab countries. But the correlation coefficient gives a more accurate picture about the real competitiveness among countries, since it includes the entire 240 commodities subject to the analysis. In any case, GAFTA comes always before COMESA in the ranks.

Table 3.12.: Regional distribution of the Euro-Med potential trade-creating countries for Egypt

Percentage of EU countries to the potential trade-creating Euro-Med countries to Egypt.	69.5 percent
Percentage of original-EU countries to the potential trade-creating Euro-Med countries to Egypt.	34.78 percent
Percentage of new-EU countries to the total EU trade-creating countries to Egypt.	56.25 percent
Percentage of non-original EU countries and Mediterranean countries to the potential trade creating Euro-Med countries to Egypt.	65.2 percent

Source: Researcher's calculations from World Bank *Trade CAN* 2002

3.2.1.2. The pre-FTA trade and economic relationship among member countries

The trade flows between the countries of an agreement are an important indicator for trade relations and can give a picture on how successful the FTA can be after it is formed and implemented. We take the total trade flows[29] between Egypt and the countries of each Agreement in the year 2003 as a measure for the economic relations and compare the results among the four Agreements. We also take the average exchange in each Agreement as a further indicator.

It can be seen from *Table 3.13.* that the Euro-Med countries are the greatest trade partners of Egypt compared to the countries of all other Agreements in total terms and on average. The second rank is occupied by the GAFTA countries. On average, Egypt's trade with the Aghadir countries is greater than with countries of COMESA. But since Aghadir includes only three

[29] With the trade flows we mean the sum of exports and imports with the partner countries of each Agreement.

countries, the trade with the 18 COMESA countries is much greater in total terms. However, the latter's trade with Egypt is still less than GAFTA and far less than Euro-Med countries.

Table 3.13.: Total and average trade flows between Egypt and the countries of the four RTAs

(Trade flows are in USD and for the year 2003)

	Total trade flows with Egypt	Average trade flows with Egypt
GAFTA	1,621,203,395.22	101,325,212.20
COMESA	318,799,953.12	17,711,108.51
EURO-MED	6,365,789,288.64	187,229,096.72
AGHADIR	249,121,226.83	83,040,408.94

Source: Researcher's calculations from CAPMAS 2004

3.2.1.3. The geographic distance between the member countries

Since the countries of each Agreement are more or less located in one region, it is not hard to predict the results in advance.

There are two kinds of distance measures: simple distances, for which only one city is necessary to calculate international distances; and weighted distances, for which we need data on the principal cities in each country. The simple distances are calculated following the great circle formula, which uses latitudes and longitudes of the most important city (in terms of population) or of the official capital. These two variables incorporate internal distances based on areas provided in the *CEPII* (2005)[30]. The two weighted distance measures use city-level data to assess the geographic distribution of population inside each nation. The idea is to calculate distance between two countries based on bilateral distances between the largest cities of those two countries, those inter-city distances being weighted by the share of the city in the overall country's population. This procedure can be used in a totally consistent way for both internal and international distances[31].

[30] Centre D'Etudes Prospectives Et D'Informations Internationales.

[31] The latitudes, longitudes and population data of main agglomerations of all the countries included in the analysis and calculations of CEPII are available in the World Gazetteer Website.

Table 3.14. shows that whether we use the simple or weighted distances, the average distance between countries of GAFTA and Egypt is the least, followed by Aghadir, Euro-Med and COMESA in order. This means that - based on this criterion - GAFTA would be the most trade creating and COMESA the least.

Table 3.14.: Distance between Egypt and the countries of the four RTAs

(Distance in kilometers)

	Average distance (significant cities)	**Average distance (capitals)**	**Weighted average distance (significant cities)**	**Weighted average distance (capitals)**
GAFTA	1684.427494	1684.427494	1694.028619	1668.399056
COMESA	4131.784	4131.784	4149.804167	4135.768778
EURO-MED	2404.545703	2394.33835	2404.376076	2388.624638
AGHADIR	2061.332067	2061.332067	2055.722833	2045.363233

Source: Researcher's calculations from CEPII 2005

3.2.1.4. The size of the FTAs

This criterion can be considered a complementary one, since if all other criteria are fulfilled, then the size of the FTA should not be a factor of great significance. From the number of countries included in each Agreement we can easily predict Euro-Med to be the most potentially trade-creating Agreement. Then comes COMESA followed with a slight difference by GAFTA, and Aghadir comes at last.

3.2.1.5. The pre-FTA trade barriers between member countries

The main tangible barrier of trade between countries is the tariffs applied among them. Hence, the higher the tariffs applied between the different countries of one FTA before forming the latter, the greater the potential gains and the more trade creation should be expected. The analysis here is based on firstly taking the simple average of the weighted average tariffs of the different countries of each RTA and comparing the results among the Agreements; the higher this simple average, the more likely trade creation should be expected for Egypt after applying a given RTA, since this would mean that Egypt would benefit from a relatively greater access of its goods into the markets of this RTA than in the case of another RTA where the average tariffs of the

countries would be low from the beginning. As a second step, this average is weighted by the volume of Egyptian exports to each separate country, since the former reflects the importance of trade relations between Egypt and other countries, particularly, the initial access of Egyptian goods to their markets. Again, the results can be compared among the four Agreements.

In the results shown in *Table 3.15.*, the Aghadir Agreement comes in the first rank, followed by COMESA, GAFTA, and Euro-Med when taking the simple average of the weighted average tariffs in each separate RTA. This could be an indicator for Aghadir being the relatively most trade creating Agreement and Euro-Med the least, regarding this criterion.

When weighing the average tariffs of the countries by their respective imports from Egypt and taking the average, the results do not change for the first and fourth rank (Aghadir and Euro-Med respectively). However, COMESA and GAFTA change their ranks. This can be explained by the fact that the trade volume between Egypt and GAFTA is greater than the trade volume between Egypt and COMESA (see *Table 3.13.*).

Table 3.15.: Average tariffs of the four Agreements

(Figures are in percent and in the year 2002)

	GAFTA	COMESA	EURO-MED	AGHADIR
Simple average of weighted average tariffs of the Agreement	12.0625	12.64375	6.12479	22.3
Weighted average of weighted average tariffs of the Agreement	12.1731	8.7717	5.27545	16.84683

Source: Researcher's calculations based on data from the Index of Economic Freedom 2005.

Furthermore, the median of the weighted average tariffs of all the countries included in the four Agreements in total is calculated (*Table D* of Appendix II), in order to take it as a benchmark for trade creation. In case the weighted average tariff of one separate country is higher than the median, then it can be considered trade-creating to Egypt, relative to other countries whose weighted average tariff falls below the median. The same analysis is applied once again but by using the mean.

Table 3.16. shows the countries of the four RTAs that can be considered trade-creating (taking the median as a benchmark) and demonstrates the percentage of these countries to the total number of countries in each separate RTA, based on that criterion.

Again, Aghadir takes the first rank in potential trade creation, since the percentage of rather trade creating countries to the total number of countries of the Agreement is the highest. Also, Euro-Med takes the last rank as the case before. With a very tiny difference, COMESA and GAFTA take the second and third ranks, respectively. We get similar ranks when applying the same analysis using the mean.

Table 3.16.: Countries with a weighted average tariff exceeding the median

(Figures are in percent and in the year 2002)

GAFTA		COMESA		EURO-MED		AGHADIR	
Bahrain	7.7	Angola	10	Algeria	15.3	Jordan	11.3
Iraq	5	Burundi	23.5	Hungary	7.5	Morocco	28.2
Jordan	11.3	Comoros	38.9	Jordan	11.3	Tunisia	27.4
Lebanon	8	Congo	15.6	Lebanon	8		
Libya	15.9	Djibouti	21	Morocco	28.2		
Morocco	28.2	Ethiopia	16.5	Palestine	8.5		
Oman	6.7	Kenya	14.4	Slovakia	6.1		
Palestine	8.5	Malawi	12.5	Syria	35		
Saudi Arabia	10.5	Mauritius	15.8	Tunisia	27.4		
Syria	35	Rwanda	6.6				
Tunisia	27.4	Seychelles	28.3				
Yemen	12.6	Uganda	6.8				
		Zambia	8.4				
		Zimbabwe	12				
Percentage of these countries to the total number of countries in the Agreement							
75 percent		***82 percent***		***26 percent***		***100 percent***	

Source: Researcher's calculations based on data from the Index of Economic Freedom 2005.

3.2.1.6. Other historical and cultural factors

Common historical and cultural factors could increase the potential for trade creation among countries. Accordingly, in this section we grasp some of these factors, such as common borders, common languages, common religions, colonial relationships, etc., in order to find out the countries that have the strongest links with Egypt and to which Agreements these countries belong. The detailed figures for the four Agreements are presented in *Tables E, F, G* and *H* of the Appendix II and the results are summarized in *Table 3.17.*; GAFTA occupies the first rank in all

these factors. All other Agreements vary from one factor to the other. And in all cases, COMESA comes after GAFTA.

Table 3.17.: Historical and cultural factors

(Figures are in percent)

	GAFTA	COMESA	EURO-MED	AGHADIR
Percentage of countries having a common border with Egypt	19	6	6	0
Percentage of countries having (a) common official language(s) with Egypt	100	17	18	100
Percentage of countries having (a) common ethnical/spoken language(s) with Egypt	100	61	30	100
Percentage of countries having (a) colonial relationship(s) with Egypt	6	6	6	0
Percentage of countries having (a) common colonizer(s) with Egypt	75	56	24	67
Percentage of countries having a common dominant religion with Egypt	100	28	24	100

Source: Researcher's calculations from CEPII 2005

From the analysis above, it can be noted that - from a pure theoretical economic and even cultural point of view - , Euro-Med does not necessarily have the best potential for trade creation - at least for Egypt - , compared to COMESA and GAFTA. The only criterion where the EU proves that it is the most trade creating is the fact that the trade flows between Egypt and the EU are the greatest in total and on average. But even this fact could be explained in terms of sound institutions in the EU countries; the high volume of trade flows can be a result of good institutions rather than a reason for potential trade creation in the future. In other words, the strong institutions existing in the EU countries and missing in the two other RTAs, automatically facilitate the trade between the EU countries and Egypt, and therefore, their trade volume increases. If these strong institutions exist in the two other RTAs, there is not reason why the trade flows between their countries and Egypt should not increase as well.

Regarding the rest of the criteria, Aghadir and GAFTA take the first ranks. Nevertheless, the implementation process of Euro-Med is working more smoothly and - most importantly - without considerable complaints from either side as will later be shown in detail. And whereas Aghadir takes in most cases the first rank as a trade-creating Agreement for Egypt, it has not even entered into force, although the number of countries included in it are few, a factor that should help avoid any discrepancies in points of view or complications in implementation. Furthermore, Aghadir is supposed to be an extension of Euro-Med. However, while the same four countries are working quite successfully as members of Euro-Med, they cannot agree on a date for the enforcement of their joint Agreement.

The fact that GAFTA, COMESA and Aghadir are not implemented properly as compared to Euro-Med, although the latter does not have a better economic potential, raises the question whether there are some other institutional factors that are missing in the three former RTAs and what these factors are. For that purpose, interviews were run with Egyptian government officials in the Customs Authority, Ministry of Industry and Foreign Trade, and the federation of Egyptian Industries on one hand and Egyptian market representatives (producers, importers and exporters) on the other, which will be discussed in detail in *Chapter 4*.

3.2.2. The expected dynamic effects of implementing the RTAs

Alongside the static welfare effects, countries forming an FTA can also gain several important dynamic benefits (*see Chapter 1*). These are mainly the effects accompanied by stimulus to investment, increased competition and economies of scale, as will be discussed in the following.

3.2.2.1. Stimulus to investment

Forming an FTA is a good opportunity for member countries to take advantage of the enlarged market and to meet the increased competition by stimulating their investments. In addition, non-member countries might also set up production facilities within the FTA to avoid the discriminatory trade barriers imposed on their goods. These are the so-called tariff factories[32]. An example for that are the huge investments that USA firms started in Europe after 1955 and once again after 1986, fearing to be excluded from the rapidly growing EU market. As a result of globalization, Foreign Direct Investment (FDI) became recently more interested in export oriented activities. Accordingly, more liberal and open developing countries attracted more FDI accompanied by its industrial activities.

As for Egypt, there are three important sources of foreign investment. These are Europe, the USA and the Arab world, particularly the Gulf states. According to Egyptian statistics, the USA holds the largest FDI stock in Egypt. Foreign investments in Lebanon, Morocco, Syria and Tunisia are dominated by European firms (over 70 per cent). Concerning the energy-related investments, The USA is a very important investor in Algeria and Egypt. A striking difference between the Middle East and North African (MENA) region and other developing regions is the relatively low level

[32] Direct investment made in a nation or other economic unit (such as an RTA) to avoid import tariffs.

of regional investment in the former. However, in Egypt, Arab investors participate in a quarter of all approved projects. But these tend to be more in construction and less in manufacturing or in industries with the potential to transfer technology and managerial experience (Investment Policy Review 1999).

In general, FDI in Egypt fell to the lowest level for 25 years in 2003, just USD 240 Millions (El-Feki, 2003). But this would bring us to the institutional problems; most of the foreign investors do not find the encouraging environment for investment in Egypt. Beside the political instability in the region, the foreign investors fear risk, uncertainty, unstable investment laws, high costs of services[33], red tape, bureaucracy, capital repatriation problems and further institutional distortions (*see Chapter 4*).

The membership of Egypt in Euro-Med can enhance the FDI inflows from EU countries, if the former manages to activate its liberal and open trade policies, which would in turn reduce uncertainty associated with unstable macroeconomic environment that FDI usually faces. For example, the adoption of the competition policy rules of the EU could contribute in reducing the uncertainty correlated with unstable competition environment in Egypt, leading in turn to more FDI inflows.

If the institutional problems are solved, not only EU investments would increase, but also Arab and African investors would be motivated to invest in Egypt and the Arab and African region as a whole instead of concentrating on the European and USA markets. And in this case, the 'investment creation' by Arab and African countries would be relatively more significant, since although more European investment is needed in Egypt, its share of total foreign investments in Egypt is quite high as compared to the modest Arab and African investments.

In principal, no 'investment diversion' should be expected from Egypt's membership in GAFTA, COMESA, and Euro-Med, since most of the biggest foreign investing countries in Egypt are part of these RTAs. Thus, theoretically, there should be no bias against any foreign investor. However, when regarding the EU countries as non-members in GAFTA or COMESA, there is the possibility of what is called the 'hub and spoke' effect. The latter states the following: Because the tariff rates differ between the member countries of one FTA towards the rest of the world, foreign investments are more likely to be allocated in the FTA countries whose tariff rates are

[33] Also see: Abdel-Salam (2002).

relatively low, in order for the foreign investors to benefit from the importation of raw materials and exportation of capital goods on low tariff measures. At the same time, these investors would enjoy the advantage of serving a large market and exploiting economies of scale, due to the zero tariffs among the FTA member countries. The cases of GAFTA and COMESA are very clear examples for that; the tariff rates vary among countries of GAFTA and COMESA and the likelihood of asymmetric tariff structures is high, due to the low or zero tariff rates of the EU countries and the high and variant tariff rates of the member countries of the two other RTAs. Thus, the hub and spoke effect can occur, especially in the phase where Egypt has not yet completely reduced all the tariffs towards EU products and the latter could use other countries of GAFTA or COMESA as channels to export its goods to Egypt. The same would apply to FDI, leading to the possibility of capital outflows rather than inflows. This could be an important sign for Egypt to further liberalize towards the EU, in order for the former to directly harvest the fruits of FDI and not to rely on indirect channels for achieving this. Sooner or later, Egypt will have to cope with this issue, since by the end of the transitional period with the EU, Egypt will have to reach the zero tariffs in all goods.

3.2.2.2. Increased competition

In the absence of an FTA, monopolistic and oligopolistic producers have a greater chance to be protected by trade barriers and grow sluggish. But after forming an FTA and trade barriers among member countries are eliminated, producers in every member country are forced to be more efficient, facing competition of other producers within the FTA. Other options for them are to merge or give up the business. The higher the level of competition the more likely would the development and utilization of new technology be stimulated. All of these factors would help reduce the costs of production, leading in turn to the welfare increase for the consumers. It is however important to note that after the formation of an FTA, it is still possible for some firms to undertake some oligopolistic practices, such as collusion and market-sharing agreements,.etc. But undoubtedly, the probability decreases, since the market widens and the competition in general increases after forming the FTA.

In the case of Egypt, the potential for increased competition would be expected to be higher when dealing with GAFTA and COMESA countries as compared to EU countries, since as seen in section 2.1., the RCA of the Egyptian goods is highly correlated with the RCA of the goods in

GAFTA and COMESA countries relative to EU countries. This implies that the production and export structure of Egypt is rather similar to the one in the countries of GAFTA and COMESA.

This dynamic benefit is also highly related to the concept that is discussed above, namely the differentiation and specialization within one product and hence, the enhancement of intra-industry trade between the countries of one region. Since the most similar production and export structures exist between Egypt and the Arab countries, it is worth focusing on the potential for intra-industry trade in this region; most countries in the Arab region have historically relied on their natural resources and raw materials. Consequently, they lacked the pressure and incentive to diversify and specialize their industrial base. Some Arab countries are more able to adapt to new trade opportunities whereas others have less flexibility to adjust to new market opportunities and increased competition[34]. In the trade literature, the amount of intra-industry trade, or trade in similar goods, is often taken as a measure of the diversity, degree of specialization, and degree of technical sophistication of its industrial sector. This can be used to infer the country's ability to compete in a changing environment.

Although there is a relatively high potential for intra-industry trade among Arab countries, the former proved to be quite modest compared to other RTAs all over the world, such as NAFTA and Mercado Común del Sur (MERCOSUR) in Latin America. Within the Arab region, the highest level of intra-industry trade is registered in Oman and Tunisia, followed by Jordan, Morocco and Egypt (Havrylyshyn and Kunzel, 1997). Low levels are registered in Kuwait and Syria, whereas the rest of the Arab countries have even lower levels of intra-industry trade within the region. Improvements are registered in Oman and to a lesser extent for Egypt, Jordan, Morocco, Saudi Arabia and Tunisia. Djibouti, Syria and Kuwait have even registered a decline in their intra-industry trade levels.

For proximity reasons, one should expect that intra-industry trade is more likely to occur among countries that are geographically close to each other; the cost of information for trade in differentiated products is higher than for standardized products and increases with distance[35]. But as will be seen in *Chapter 4*, there are other institutional and political obstacles that override this

[34] See Nsouli et al. (1996).

[35] For more elaboration see Balassa and Bauwens (1987).

advantage in Arab countries and therefore dampen the intra-industry trade, the differentiation through product groups and the competition.

An important factor that reduces the possibility of intra-industry trade is the fact that many Arab countries are mainly oil exporting economies. Although these countries have done lots of efforts to diversify their economies since the 1970s, they still rely largely on their oil-generating revenues. A few cases of oil exporting countries managed to generate derivative products and industries that reflect some specialization, such as chemical products. The best two examples are Oman and Saudi Arabia. And since Egypt relies less on oil-exports, its intra-industry trade in that field is relatively modest.

It is clear that the Arab region as a whole does not have a highly advanced industrial base that would allow for differentiation and specialization within product groups, especially when compared to industrial countries or even other RTAs between developing countries. But although the intra-industry trade among Arab countries is much less than it should be (based on the argument of the relatively high correlation coefficients, at least between Egypt and other Arab countries) it is still more significant than between Arab and EU countries. This proves again that Arab countries have more similar levels of industry specialization, and that they compete more effectively in the intra-regional or multilateral setting than specifically with the EU. Egypt in particular is not included in the Arab countries that have a higher ability to compete effectively with the EU[36]. After all, an essential factor for enhancing competition between Egypt and the countries of any of the RTAs it is part of is the need of market oriented and open economy policy combined with efficient and reliable institutions, which will be discussed in detail in *Chapter 4*.

3.2.2.3. Economies of scale

Originally, the importance of economies of scale for developing countries within the context of RTAs was focused upon by *Cooper and Massell* (1965) and further stressed by *Bhagwati* (1990). They argued that the costs of import-substitution used to reach a certain level of local production could be reduced through forming RTAs among different countries. This would allow for internal specialization in more efficient industrial areas and realization of economies of scale.

[36] These countries are mainly Oman, Saudi Arabia, Tunisia and the UAE.

But it should also be noted that even a small country which is not a member of any FTA can overcome its small domestic market and achieve substantial economies of scale in production by exporting to the rest of the world. Nonetheless, the probability increases by being member of an FTA. For instance, the size of some plants in small European countries, such as Belgium and the Netherlands before joining the EU were already big enough as compared to the size of USA plants, since the former produced for the local and foreign markets and achieved hereby good economies of scale. However, more significant economies of scale were reached after the formation of the EU.

Egypt as a common member country in GAFTA, COMESA and Euro-Med would be expected to gain more economies of scale from GAFTA and COMESA, firstly, because the structures of production are rather similar, which would in turn allow for specialization within certain product groups and benefiting from economies of scale within joint industries, and secondly, because the European markets, which represent a great part of Euro-Med, are already fairly open to the Egyptian products, relative to the two other Agreements..

Nonetheless, a quite important factor for reaping economies of scale when joining an RTA is the extent of the comprehensiveness and the deepness of the agreement itself. By considering this criterion, Euro-Med would be given a greater weight, since it is deeper, more comprehensive and properly implemented relative to the other Agreements. Unless GAFTA and COMESA overcome their institutional and implementation problems, not much would be added to the ability of their member countries to derive additional scale economies.

3.2.3. The expected institutional effects after implementing the RTAs

Institutional effects of forming an RTA are usually harvested in a special case of integration called “deep” rather than “shallow” integration (Lawrence, 1997). In the latter case, the main focus is on tariff reduction or abolition among member countries while in the former case other domestic trade-related policies are included as well. Therefore, the question is not whether Euro-Med, GAFTA or COMESA would attain the institutional gains but rather which Agreement(s) of them cover the necessary requirements for a deep integration, leading in turn to positive institutional effects. In what follows, the most important features of institutional effects accompanied by forming an RTA, such as competition policy and the harmonization of non-border measures will be examined.

3.2.3.1. Competition policy rules

The existence of competition policy rules forces the member countries of an rta to be more market-oriented. It also stimulates microeconomic competition; this can be achieved through weakening the domestic monopolies and rent seeking activities, and setting constraints on export subsidies granted by governments. This sort of business environment stability by the use of credible competition policies and regulations could be highly beneficial to the economic development of the member countries[37].

Starting with Euro-Med, all agreements between undertakings, decisions by associations of undertakings, concerted practices between undertakings and any public aids which have as their object or effect the prevention, restriction or distortion of competition are incompatible with the proper functioning of the Agreement. Abuses are supposed to be handled by the Association Committee. Egypt is currently in the process of drafting its own competition law. While drafting its law, Egypt will take into account the competition rules developed within the EU. If serious problems arise, the Parties may raise the matter for consideration in the Association Council. To date, no problems have been reported and it seems that the process is on track.

As for GAFTA, although there is no specific article on competition law, the former calls for the harmonization of common competition policy. Only four GAFTA members have or are in the process of drafting a competition law (Egypt, Jordan, Morocco and Tunisia). But in order to benefit from that law, all or at least the majority of the 17 GAFTA countries should attain it. Further more, GAFTA calls for consultations among members over harmonization of trade systems, legislations and policies. However, there was no identified period for such consultations.

Moving on to COMESA, a quite comprehensive and clear draft for a Competition Law that establishes a common competition policy has been worked on. However, the possibility of implementing this draft is questionable, due to the discrepancy in the legal, political and economic systems existing in the member countries.

[37] For the relation between RTAs and competition policy see: Plummer (1997).

3.2.3.2. Harmonization of non-border measures

The harmonization of non-border measures has positive effects on the countries of one RTA. Although such measures are hard to achieve on the global level, achieving them on the regional level represents at least a confirmation of some measures to the global standards. In fact, such cooperative efforts can even be pursued unilaterally, but formal agreements would be more efficient in inducing the administrative bodies involved to cooperate.

A problem that might rise is the ambiguity related to the non-transparency of such measures[38]. It might also lead to another form of trade restriction even among members of an rta. Thus, transparency is a vital aspect when dealing with such measures which, if absent, can trigger their role as restrictions to trade rather than trade facilitators.

The most comprehensive Agreement is the Egyptian-European Partnership Agreement, where all the non-border measures are covered. And so far, no problems have occurred among the member countries. But since GAFTA and COMESA are more of shallow integration Agreements, they are missing a number of non-border measures.

For example, GAFTA does not include any specific rules on the application of measures related to SPS measures, TBT, NTBs, Labor Standards, or Environmental Standards. While there is a working party that has been established to prepare studies and reports on NTBs, the work of the former has been largely limited to the inspection of NTBs related to border measures, such as the fees of documentation and inspection.

Several trade frictions and disputes have occurred among member countries and most of them have been related to SPS and/or TBT measures. The lack of such rules within GAFTA has proved to be a major loophole for proper implementation and it seems that member countries prefer to resolve those disputes through bilateral consultations or unilateral retaliations due to the lack of a proper and comprehensive dispute settlement mechanism.

The GAFTA Agreement states that member countries shall consult over protection of IPR. It also calls the members for determining a preferential treatment for Arab goods vis-à-vis competitive or alternative non-Arab goods. One other important consultation shall be devoted to the

[38] Hoekman and Djankov (1997).

government procurements. In practice, none of such consultations have started yet. In addition, the executive program of GAFTA states that member countries shall consult over harmonization of trade systems, legislations and policies. Furthermore, the Arab Agency for the Harmonization of Standards[39] has prepared several drafts on the unification of standards and codes, but the draft has never been considered for adoption due to the objections of several members.

Concerning COMESA, its member countries agreed on detailed provisions set in the Treaty about SPS measures. However, none of the measures can be recognized as implemented. There is almost no information on the progress of implementing these far reaching commitments and their relevant domestic adjustments. And to date, there is no information that any of the member countries has undertaken major changes or modifications to its domestic regulations in these areas to adjust to COMESA obligations. There is also no article or provision in COMESA that deals with IPR and no cooperation or harmonization has occurred to date. As for the public procurement reform initiative in COMESA, its main goal is promoting good governance through transparency and accountability in public procurement. The only considerable effort in this respect - even though still in an early stage - is the initiation of an intra-COMESA online database for procurement and the establishment of a review mechanism for transparency in practices and undertakings. The implementation of both is still in early stages.

3.3. Summary and main findings

This chapter dealt with the static, dynamic and institutional effects that might influence Egypt as a consequence of its membership in the different RTAs.

Taking into account that Aghadir is a complementary Agreement of Euro-Med, GAFTA takes the first ranks in most of the criteria concerned with the static gains, as can be seen in *Table 3.18*. Hence, on a theoretical basis, GAFTA would be the most promising Agreement followed by COMESA. The reasons therefore are - among others - the shorter geographic distance, the relative similarities in production structures, the relative high tariff barriers among the member countries and the common historical and cultural factors.

[39] An agency operating under the supervision of the Council of the Ministers of Industry.

Table 3.18.: Summary: Expected static gains of the main RTAs in ranks

	GAFTA	COMESA	EURO-MED
Production and export structures	1	2	3
Pre-FTA trade and economic relationships	2	3	1
Geographic distance between member countries	1	3	2
Pre-FTA trade barriers	1	2	3
Historical and cultural factors	1	2	3

As for the dynamic effects, again, and as can be seen in *Table 3.19.*, GAFTA and COMESA can have a very high potential, since there is still a huge space for investment stimulation, increased competition and economies of scale to be utilized as compared to the Agreement with the EU countries. But what makes the latter more advantageous so far, is the lack of sound institutions in the two other RTAs, which brings us to the third effect, which is the institutional effect.

Table 3.19.: Summary: Expected dynamic gains of the main RTAs in ranks[40]

	GAFTA	COMESA	EURO-MED
Investment stimulation	1	1	2
Increased competition	1	1	2
Economies of scale	1	1	2

GAFTA and COMESA are less comprehensive concerning the type of integration. They are rather shallow integration Agreements as compared to Euro-Med, which covers many details, giving it the privilege being a deep integration Agreement. Harmonizing the domestic policies of the members of any of the two former RTAs should have enormous institutional effects, not only on the Egyptian economy, but on all the member countries of these RTAs. Therefore, *Chapter 4* in this study will be devoted to the institutions which exist in the different RTAs that Egypt is member of. Moreover, the results of the interviews run with Egyptian government officials, market representatives (local producers, exporters and importers) will be demonstrated, in order to link them with the economic theory.

[40] GAFTA and COMESA are given the same ranks, since -as compared to Euro-Med- the statuses of the countries included in both RTAs are quite similar; there is still much space for the opportunities of investment, competition and economies of scales among these countries to be utilized -assuming that the institutional problems in these countries can be overcome-, as has been shown in the analysis above.

CHAPTER 4

The Institutional Problems associated with Egypt and its RTAs

4.1. Introduction

The costs associated with international trade incorporate transaction costs resulting from inefficiencies in customs clearance procedures, bad transport and transport regulations, and requirements that prevent competition from foreign suppliers. Transaction costs are also associated with the red tape generated in the administration of complex documentary requirements such as RoO, packing and labeling (Zarrouk, 2003). These types of trading costs often have a major negative effect on free trade. The absence of good information on these costs impedes the ability of policymakers to assign priority to needed reforms.

Several studies tackled the problem of institutions; for example, *Fawzy* (2003) refers the failure of Arab countries in reaching a sound economic integration to - among other factors - the lack of political incentives, the lack of political will, the lack of political commitment and disputes over regional leadership. In his survey on barriers to trade and investment in Arab countries, *Zarrouk* (2003) attempts to quantify the administrative costs accompanying trade in eight Arab countries. He concludes that although tariffs and other taxes on imports have been declining in most Arab countries in recent years, Arab companies still perceive non-tariff trading costs - including red tape and other bureaucratic barriers - to be relatively high. Furthermore, customs duties tend to be compounded by the costs of complying with regulations and administrative constraints, which have been estimated by 230 randomly selected companies in the same eight Arab countries to range between 8 and 10 percent of the value of trade. His survey also shows that a typical sea freight import transaction in Arab countries takes two to ten days to clear, whereas the norm[41] is less than twenty-four hours. A truck delivering goods to markets across any two Arab countries may take one to three days to clear, whereas the norm is four hours. In addition, an average Arab company spends ninety-five workdays per year - more than one week a month - in resolving problems with customs and other trade officials. In fact, in most of these companies there are

[41] Zarrouk refers to the norms set in Hoekman and Messerlin (2002).

employees hired just for undertaking these duties, which in itself is a waste of human resources, and such daily contact with government officials represents an additional trading cost and an inducement to corruption in the form of customs officials' demands for informal payments. Arab companies estimate these additional payments to represent one percent of the costs of delivered goods.

This chapter attempts to analyze the weak and/or delayed implementation of the Egyptian RTAs according to the view points of the different groupings of the Egyptian economy. The analysis is more of a descriptive nature, based on the theoretical pressure group model of *Rogowski* (1992) elaborated in *Chapter 1* and which distinguishes between the *exporter* usually gaining through reduced tariffs and improved market access, the *local producer* typically loosing from liberalization, the *consumer* usually gaining through a larger variety of products, lower prices and higher quality, and a final *interest group* sometimes showing resistance arising through current political or structural changes.

In most of the developing countries, such as Egypt, it is quite difficult for the third group (*consumers*) to participate in the decision making concerning trade integration issues, since the link between this group and the decision makers is usually missing, mainly due to the lack of information and full democracy. Thus, the study takes *the importers* as a proxy for the consumers, since ultimately the interests of both groups considerably cross together. Concerning the fourth group, the government representatives of different involved Egyptian ministries mentioned in detail in the next paragraph are considered the most appropriate group.

The four groups were interviewed in Cairo[42] and the outcomes of the interviews are demonstrated in this chapter. The interviews were run with representatives of 70 Egyptian importing, exporting and local production companies[43], who were randomly selected from a database provided by the Egyptian Federation for Industries and including 420 firms in Cairo. There was no focus on a certain sector or product, since the main concern is the institutional problems that generally face

[42] Due to the time and financial constraints, the focus was only on the Capital of Egypt, which is the case study and the only common country in all the RTAs tackled in the study. There were two phases of the interviews, the first took place from August 2004-February2005 and, in order to refine and follow up, the second took place from July 2005-September 2005. Noteworthy is the fact that Cairo is the pole of big importers and exporters and it also contains most of the important authorities and ministries.

[43] Out of the 70 companies, there are 18 local producers, 23 exporters, 21 importers and 8 companies that have both importing and exporting activities.

the market representatives and dampens their trade activities in practice. In addition, 18 government officials in the Egyptian Customs Authority, the Ministry of Industry and Foreign Trade, the Ministry of Agriculture and the Ministry of Foreign Affaires were interviewed.

Within each section of this chapter, the four RTAs are discussed from the different groups' points of view. The sections are not sorted according to the RTAs but rather according to the four groups, since the RTAs overlap and it is useful to link all of them within each separate group, especially that many importers, exporters and local producers face similar problems when dealing with countries of different RTAs.

4.2. The Egyptian exporters

In this section the Egyptian exporters mainly express their opinion about the EU versus COMESA and GAFTA, the competition they are facing from other countries abroad, the competition among them, the new standards and terms of trade of the Gulf countries, the customs problems in other GAFTA countries, the missing information and guarantees systems, freight and transportation problems, the competition among GAFTA members, the obstacles of the Egyptian government and the problems in the Egyptian customs outlets.

4.2.1. Egypt as a temporal channel between EU and COMESA

Many of the interviewed Egyptian exporters believe that - so far - the main way how they are benefiting from COMESA and the Egyptian-European Partnership Agreement is as follows: Egypt imports the raw materials (roughly for only 5 percent tariffs) and machines (roughly for only 2 percent tariffs) from the EU[44], according to the Partnership Agreement. Most of the COMESA countries did not sign similar agreements with the EU countries. Therefore, the Egyptian exporters have the privilege of exporting the products that are manufactured using EU machines and raw materials to the African countries or even directly re-exporting the European machines to them, without being subject to tariffs, according to the COMESA Agreement. Nevertheless, once the European products will have duty free access to the COMESA markets, the Egyptian exporters will lose this privilege, since the latter is not always really based on a value added of real production as much as a process of re-exportation and benefiting from the tariff differences of the RTAs.

[44] Starting from 2005, these tariffs were even cancelled, and the products enter tariff free.

4.2.2. EU as a provider for machines, capital goods and investments for Egypt and the rest of the GAFTA countries

Most of the exporters stress on the fact that Euro-Med is only useful for them as importers of machines and capital goods. However, opening markets there for their exports has much lower chances, since reaching the quality that the EU countries require is very costly. Therefore, in that concern, they would prefer to export to GAFTA and COMESA countries, where the latter have even a greater potential as compared to the former, since the production structures of the COMESA countries - as compared to the GAFTA countries - are more different from the Egyptian one.

Egypt has already several BTAs with Arab countries that are concurrently members of GAFTA. But the Egyptian exporters always have problems accessing their markets on a wide basis, since all the Arab countries prefer to receive their imports from EU countries, firstly, due to the guaranteed higher quality, secondly due to the different production structures between the Arab countries and the EU countries as compared to the production structures among the Arab countries, and thirdly due to the better commitment institutions existing in the EU countries.

4.2.3. Egypt's competitors abroad

When comparing Egypt as an exporting country with other countries that are not members of any of the Egyptian RTAs, most of the exporters point at China and the East Asian Countries, which are regarded as significant competitors for them in the international markets. In contrast to Egypt, China is more attractive for European investors due to the following:

(i) The Chinese produce at a high level of productivity; the workers and the land might be more expensive than in the Egyptian case, but the mass production, and thus the cheaper average prices override this problem and give them a comparative advantage.

(ii) The Chinese exporters are more skilled in promoting for their products abroad.

(iii) The Chinese know how to adapt their production according to the requirements of the international markets. Where high quality is required - such as the case of EU markets - they produce at higher quality, threatening hereby their Egyptian competitors in the European markets. Where the quantity plays a greater role - such

as the case of Egypt and further developing countries - they consider mass production at the expense of quality, threatening hereby the local Egyptian producers of shutting down.

4.2.4. New standards and terms of trade of the Gulf countries

Another important problem for the Egyptian exporters is the fact that some GAFTA countries, such as Saudi Arabia, no longer rely heavily on the Egyptian products as compared to the 1980s and early 1990s, although the GAFTA Agreement was signed in the late 1990s and should therefore have increased the trade volume with these countries. The Egyptian products do not comply with their new standards, which are to a great extent similar to the EU ones. At the same time, the quality of the Egyptian products has decreased, due to the higher costs of production caused partially by the deterioration of the exchange rate of the local currency. It is also worth mentioning that the packing and labeling of the Egyptian products are far below the level required for entering the markets of these countries. The Egyptian exporters rely on low quality packing, in order to be able to cover their high costs. Therefore, they currently export only a few crops to the Gulf countries, such as tomatoes and potatoes, thus creating vulnerability in trade and hindering risk diversification.

Since the Egyptian exporters largely compete with each other on their market shares in the Gulf countries instead of lobbying together for the benefit of all of them as one group, the importing countries determine the prices, as the terms of trade are against the Egyptian exporters. For example, a fruit like guava is only imported from Egypt, and there are almost no international competitors, but since the Egyptian exporters compete among each other, and they have excess production, there is no chance for them to determine the price in the Gulf markets.

An important problem related to this is the fact that some Gulf countries, such as Saudi Arabia, determine the prices of the products according to a list of fixed prices. These prices do not consider the production and local transportation costs of the Egyptian producers. On the other hand, a so called 'Egyptian Committee for Agricultural Goods' releases an export price list every month, where the prices differ depending on the exporting region (Arab, European and African countries, etc.). The Egyptian exporters are squeezed between the two price lists; when they exchange the hard currency that they receive from an export deal, the Egyptian banks assume that they exported their products at this ‘Egyptian’ high price, overestimating hereby the total amount

that they received in hard currency, and requesting them in turn to exchange this amount for Egyptian Pounds. The same applies to the calculations of the Egyptian tax authorities which assume that the Egyptian exporters received these overestimated amounts in foreign currency and request from them exaggerated tax amounts.

Basically, the intention of this 'Egyptian' price list was privileging the Egyptian agricultural producers and exporters by setting minimum prices for their products that had decreased in the international markets and led to big losses, due to the deteriorating terms of trade. Nevertheless, if the bargaining power of these exporters is low, then this artificial price list has no real significance in the export markets, and at the end, the Egyptian exporters are the ones who pay the price.

4.2.5. Customs problems in other GAFTA countries

Since now the terms of trade of the Egyptian exporters towards the importing Gulf countries are in favor of the latter, the tariffs are paid by the Egyptian exporters, in order for their products to have market access there. Also, these countries - and not Egypt - determine the tariff rates. The 'additional amounts' that the customs employees receive as rent seeking in these countries are also paid by the Egyptian exporters. The fact that GAFTA was signed and apparently implemented did not change the situation.

The Egyptian exporters also complain about the rigidities when dealing with the customs officials of these countries, since the latter insist on certain details related to the labeling, and which do not have directly to do with the products.

The date on the insurance policy has to comply with the date on the CoO. But in many cases, the employees in the Egyptian customs stamp the CoO some hours later, writing hereby the date of the next day. In this case, the products might be stuck in the customs of the other Arab country or the Arab importers have to pay a penalty[45]. Again, at the end, the Egyptian exporters are the ones who bear these penalties. Otherwise, the products might be kept in the customs till they get spoiled. Moreover, if the stamps are not obvious enough, the customs of the importing Arab countries cause similar problems. Most of the exporters interviewed believe that the customs of

[45] For example, this penalty exceeds 500 Saudi Real in Saudi Arabia.

the Arab countries ask for these penalties in order to cover deficits in their own budgets, and not for justified or acceptable reasons.

Quotas as NTBs do not exist in the Gulf countries towards Egyptian exports. However, this should not be taken as a privilege, since opening the market for unlimited quantities decreases the prices of the Egyptian products and helps deteriorate the terms of trade.

As compared to GAFTA, surprisingly, the Egyptian exporters state that the EU customs control on the RoO is not as strict as it was expected. An important exporter of ready made garments claims that the EU customs officials purposely keep their eyes closed - at least for the time being. Hence, although the GAFTA RoO are very superficial as compared to those of the Egyptian-European Partnership Agreement, the latter is much more simple in application, since it is not linked with corruption and rent seeking as in the case in some GAFTA countries.

4.2.6. Information systems

A very important problem for the Egyptian exporters is the lack of information and data about potential markets, especially in Africa. Many of the interviewed exporters did not know about COMESA or only heard about it from the media - if at all - , and were hoping that they could increase their exports to the African countries. They mainly obtain their information through individual efforts.

Exporting the products is getting very expensive; every procedure for exporting a product means more expenditure on raw materials, air tickets for representatives who market the product, freight, etc. Hence, starting a new market in COMESA countries based on individual expectations and efforts is risky and costly. This applies particularly to Egyptian exporters of agricultural products, such as vegetables and fruits; the containers they need for sending samples to other African countries are usually very expensive. Therefore, most of the exporters prefer to keep dealing with the importers that they already have contact to, in order to avoid any risk.

The exporters would also need to obtain information about the demand seasons of the COMESA countries, i.e., when they are in need of certain products that are produced in Egypt. For example, the excess guava produced in Egypt for the purpose of exporting to the Gulf countries could be exported to the COMESA countries. Nevertheless, there is no enough information about their

markets and their importers, although this information should be covered by the Egyptian commercial delegations abroad.

4.2.7. Guarantees system

It is not only the lack of information that hinders the exporters from exploring and opening new markets, but also the lack of guarantees and protection. They call for clear commitments and rights within the RTAs and on the part of the Egyptian government. A number of the exporters give examples about their bad experience when exporting to Arab and African countries. They exported their products years ago and have not received the payments till the dates of the interviews. Therefore, they directly called off all the deals with these countries, since there was no authority that could protect their rights. They also argue that the importers in other Arab/African countries would not give them any payments before they themselves receive the products, since they most probably suffer from bad experiences as well where they did not receive the products timely and/or according to the quantities and/or qualities agreed upon. Thus, this is the problem of mutual mistrust between the Arab and African countries.

There is a good example given by some exporters who produce a special sort of Egyptian grapes called 'Janaklese'; these grapes are not feasible to sell in the local market, since the costs of production are very high as compared to the low market price caused by the low local demand. As a result, many of the Egyptian producers burnt their crops in order to avoid enormous losses in the local market. However, in Sudan, a GAFTA and COMESA member, the demand for these grapes is very high. Therefore, there is a big potential for the local producers to benefit from this demand. And indeed, there are many offers from Sudanese importers to import this crop. However, in order to protect their rights, the Egyptian producers set a condition for the Sudanese importers to pay in advance. The latter refused, since - according to them - they do not have enough liquidity for that; they first need to distribute the product locally in order to be able to collect the money they would pay to the Egyptian exporters. And in neither of the countries the banking system is advanced enough to rely on letters of guarantee. In addition, the latter procedure is costly for many small exporters.

4.2.8. Freight and transportation problems

In general, the airline companies set certain conditions to cooperate with the Egyptian exporters; the more an exporter exports in one season, the higher the quota s/he is allowed to have on board of the plane for the rest of the seasons. Hence, if an exporter is specialized in producing and exporting a certain crop that is harvested in winter, s/he has to make sure to fill her/his space in the other seasons. This is very costly, especially for the small exporters. For example, Egyptian producers of guava have to use their full capacity on board of the airplanes in the summer in order to have a chance to export other crops in the winter. Therefore, the supply of guava in the Gulf markets increases as compared to the demand, and thus, the price decreases.

In addition, the national airlines have infrequent flights to the extent that some interviewed exporters claimed that they are allowed to export a maximum of one ton of their crops every 10-15 days at most. In the case where the production is mainly for exportation, the producers have to get rid of the product remainders, and hence, bear great losses. An apparently easy solution could be relying on shipping where the capacity on board of the ships would be much bigger. However, the exporters see it differently, since - according to them - in order for shipping to pay off, they need to export much huger quantities of the products. This is in many cases not possible, since not all of the producers work on a large scale, and even in the cases where it is possible, this could be at the expenses of the quality. Assuming that the latter would not be affected, exaggerating in the supply of the products would lead to an enormous decrease in their prices abroad.

Another difficulty facing the Egyptian exporters of agricultural goods is the fact that the Arab airlines do not allow them to load the equipment that are necessary for preserving the fresh vegetables and fruits on board of the airplanes, which in turn harms the products.

The Egyptian exporters also face freight problems when exporting to the EU countries. In the relatively cheap Egyptian airlines big exporters monopolize the spaces in the cargos (four times a week), even if their export activities are just for the sake of ‘money laundering’, since they have been cooperating with these airlines for a long time. When a small exporter attempts to penetrate this 'market' the chances are quite low, since the strong contacts are missing. When officials in some foreign airlines were interviewed and asked about the reason for the high prices as compared to the national airlines they argued that many of the Egyptian exporters surprise the

airlines with their deals in the middle of the seasons, and therefore they have to pay more. The small exporters in turn claim that they are faced by uncertainties in the local market and that it is hard for them to determine the exact time when they would be able to export their products. Hence, they are not always capable of signing the contracts with the airline companies at the beginning of the season. As a general rule, the exporters are seeking profit, and paying a lot of money in foreign airlines reduces this profit. Hence, they take the cheaper Egyptian airlines which are infrequent as a resort, creating hereby a vicious circle of a decreasing volume of exports.

According to the interviewed exporters, the payments for the freight and insurance should be covered by the importers before the products are transported. However, the Arab importers prefer to do these payments after receiving the products and reimburse them later to the Egyptian exporters. But in many cases these importers do the payments delayed, incomplete, and in the extreme cases they refuse to pay. The Egyptian exporters believe that GAFTA has not protected their rights in that regard, which would be more important than reducing or abolishing the tariffs.

4.2.9. Competition among GAFTA members

The Egyptian exporters face strong competition from other Arab non-Gulf countries in the Gulf markets. A good example for that is Syria, where the quality is not necessarily better but the quantities and the packing. This can be referred to the export support that the Syrian exporters receive from their government and which is missing in the Egyptian case. Although the Egyptian exporters admit that the Egyptian government has been supporting them to a certain extent starting from the late 1990s, they believe that this step should have been taken long time ago, since their Arab non-Gulf competitors have already established their markets in the Gulf countries.

4.2.10. Obstacles within the Egyptian borders

Since the bargaining power of the exporters is low, they usually first send their products abroad and wait for receiving the payments. When the artificial overvaluation of the Egyptian Pound occurs in the time lag between sending the products abroad and receiving the hard currency, the exporters are faced by receiving a payment that is worth less than what they had expected. Since hereby their profits decrease, they are forced to decrease the production in the next year, dismiss

some employees, and - in extreme cases - exit the market. This has a negative impact on the total production.

Till the end of 2004, the Egyptian exporters - according to their words - were not supposed to keep the hard currency they receive when exporting their products. The government used to exchange the hard currency they obtained for Egyptian Pounds, in order to guarantee that they would not sell it in the black market, which would in turn lead to a decrease in the value of the local currency. But since the beginning of 2005, a new rule gives the exporters the right to keep the hard currency. Nonetheless, they would only be provided with the export subsidies if they would show a proof from the bank that they have exchanged the hard currency for Egyptian Pounds. This means that, in practice, the Egyptian exporters do not have another choice than giving up the hard currency that they obtain from exporting their products. A problem that arises consequently is the shortage of imported raw materials. Moreover, contacts through banks, letter of guarantee, letters of credit, insurance and freight require the availability of hard currency. The exporters claim that this is a common problem facing most of the other Arab countries they deal with, which in turn reduces the trade volume among all these countries. In many cases, the Arab countries are forced to run barter deals, due to the shortage of hard currency.

Trying to overcome the problem of hard currency shortage, a number of the interviewed exporters admit that they first use high quality imported inputs in their production, in order to pursue the confidence of the foreign importers and establish strong markets abroad, especially in the EU. But over time, they replace these inputs by the low quality local inputs, for which they do not need hard currency. Naturally, this might negatively affect their trade relations with their foreign partners.

Several exporters do not own factories but rent production lines. When they apply for building their own factories in order to increase their export volume and get independent, they are not provided with enough financial and legal support; they might be able to obtain a very cheap piece of land in one of the industrial cities for building a factory after preparing a very costly feasibility study. But then they would be shocked by the bureaucratic and corruption problems facing them, besides the fact that the infrastructure for building factories in such cities is very weak, since these cities are located in the desert. And it is very costly for an investor or producer to arrange for her/his own infrastructure.

Accessing new markets needs promoting and marketing for the new products. This means that samples of the products have to be sent and personnel have to travel to do the marketing. Some Arab importers who principally agree on importing from the Egyptian exporters request huge amounts of money in order to be able to test for the quality of the products (special machines, etc.). The exporters should be able to pay them these amounts, since the former are seeking new markets. All these procedures need money that many small exporters cannot afford. These exporters criticize the government for not providing them with this kind of financial support.

By the end of the year, the exporters have to show all their documents to the tax authorities. In these documents, the 'extra amounts' paid to different employees are included. However, the tax officials do not take them into account, since they are not proven by any sort of official documents. In fact, the reports of the tax officials are mainly based on overestimated calculations, and the exporters are required to prove the opposite. Therefore, the exporters have to go along with the tax officials and 'cooperate' with them as well. Otherwise, the cases can go to court, which is time and money consuming.

4.2.11. Problems in the customs outlets

A crucial problem facing the Egyptian exporters is the draw-back system. When they import the inputs, they have to pay the tariffs for that. But when they re-export these inputs in the form of the final product, they have the right to have the money that they had paid reimbursed only if they show a proof for that. This proof is usually a customs certificate that is obtained from the customs officials. Many exporters complain about corruption cases. They argue that they can only get this certificate after facing difficulties and having to pay 'extra amounts'. These amounts are fixed and do not represent a percentage of the deal. Thus, for small exporters these payments are very costly.

Another aspect of corruption can be observed in the Egyptian airport. According to some interviewed exporters, many employees receive 'extra amounts' in order for the deals to work successfully, and the Egyptian exporters are apparently used to bargain with them. Till the end of 2003, this applied more to the employees at the customs outlets related to Egyptian airlines. When the rumors about these employees were spread through the airport, the directors decided to make a positive change by re-allocating and re-distributing the employees who work at the outlets related to the Egyptian airlines all over the airport, in order to separate them from each other and

hinder their lobbying. They thought that they could hereby solve the problem, since these corrupt employees would not be concentrated in one spot of the airport. Nonetheless, these employees tried to spread their corruption to the rest of the outlets. For example, these employees know the exporters personally and know that they used to pay the 'extra amounts' when they were at other outlets, so therefore they request them to pay the same even if it is in new outlets related to other airlines than the Egyptian ones. In fact, these officials receive very high salaries, but they are still used to a certain 'rent seeking' culture.

The bureaucratic problems that the Egyptian exporters have to deal with in the customs of the Arab countries are considerable; most of the customs authorities in the Arab countries accept the Egyptian products based on the availability of the following documents:

1. A valid CoO that is approved by the Egyptian Ministries of Agriculture or Industry (depending on the product), the Egyptian Ministry of Foreign Affaires and the Embassy or Consulate of the importing Arab country in Cairo.
2. The invoice of the deal.
3. A certificate from the Ministries of Agriculture or Industry (depending on the product) that approves the deal.
4. A copy of the insurance policy.
5. A filled application for examining the products approved by the Egyptian Ministry of Foreign Affaires.
6. A filled exportation application.

In fact, the CoO does not really tell any details about the products; within the GAFTA member countries, this certificate is unified and it only needs to be stamped by the customs officials in the exporting country and approved by the concerned ministries. According to some exporters, many of the customs employees do not even understand the rationale of these certificates and stamp them automatically.

In each exporting enterprise there is one employee specialized in 'facilitating' the procedures in the customs authorities. The small exporters complain at most about the extra payments and transaction costs that they have to bear when exporting abroad. These costs might be high to the extent that they do not attain profits and are forced to cancel the deals. What was noticed in the

interviews is the fact that the big exporters did not really complain about such costs. This indicates that these costs are fixed apart from the size of the exporting enterprises.

The Egyptian exporters used to deal with many Arab countries according to the BTAs. And just before January 2005, time for applying the zero-tariffs among GAFTA countries, the customs officials assured that the deals would be based on the rules of this agreement, replacing hereby the bilateral ones, and that the tariffs would be cancelled. But according to many exporters, the tariffs remained between the Arab countries.

4.3. The importers

4.3.1. Internal impediments

In general, the Egyptian importers complain about many administrative and bureaucratic problems facing them when attempting to start a new import activity. According to them, there are too many documents that have to be filled and signed before even getting the permission for being registered as importers. It can take one to three years till such permission is issued. And after the potential importer obtains it, s/he is faced by the fact that s/he directly has to renew it, since it is usually expired after three years. In order for the permission to be renewed, it has to be reviewed by many committees and high duties have to be paid for that purpose. Even the exporters of the products have to be in contact with these committees and send them detailed information about the products, in order for the committees to compare this information with the imported products. The renewal takes on average nine months. The importers do not believe that any of the signed RTAs would make any change in that, since it is a matter of mind set and a deeply rooted institution.

A number of importers claim that they are not given the import licenses unless they choose the Egyptian airlines. However, the latter does not offer frequent flights and does not give enough space on board for new importers.

Even if the tariffs have been cancelled, many of the importers argue that some other constraints have been set, such as new prohibition of the entry of certain products or the requirement of extra payments for the entry of other products that are believed to harm the environment, such as acetone. The latter had been easily imported before the beginning of 2005. Many other products

are allowed to enter in limited quantities or with special permissions[46], which the importers believe to be time and money consuming procedures.

Recently, some other chemical products, such as cyanide, potassium permanganate and chloroform, are no longer supposed to enter the Egyptian market commercially; the entry requires issuing a letter of credit in the name of the forensic specialist and a specific end user certificate. There is also a follow up, where authorized persons of the Ministry of Health have to be informed exactly where these products are used and in which quantities. In other cases there have to be official import licenses from the concerned authorities. As a result, these drugs have got very expensive in the local market. For example, after obtaining one liter of chloroform for 112 Egyptian Pounds by the end of 2004, starting from the beginning of 2005 it can only be obtained - if at all - for 440 Egyptian Pounds. Therefore, most of the importers believe that the RTAs have solved some problems on one hand but created new problems on the other.

The interviewed Egyptian importers further complain about the following; when the GAFTA tariffs were reduced by 80 percent, the importers were not yet informed about this reduction, so they already paid the tariffs of 30 percent at that time. According to them, they should have been reimbursed the difference, but this did not take place; they were still treated as if the reduction was only by 70 percent. Up to the date of the interviews, they have not been compensated for that and the problem has not been settled.

4.3.2. Taxation problems

The importers complain about the tax system as well. When the importer starts a new importing activity s/he automatically has to open a new tax file. If the first tax employee writes wrong information on this file from the beginning, the importers need to deal with it as long as s/he is in business and even after that. They always need to prove the opposite of the wrong information written in the file. Moreover, the tax employees overestimate their calculations, which brings the importers to trouble and diverts them from their importing activities. There are more than 65000 cases in the court between importers and the tax authorities.

[46] For example, acetone enters based on orders from certain pharmacies and only in limited quantities. This resolution has been taken by the Ministry of Health and the Ministry of Environment.

4.3.3. GAFTA and other RTAs

In general terms, the Egyptian importers are less motivated to import from Arab countries. They argue that they are already covered by cheaper and higher quality imports from the EU, the USA and Asian countries. Even the raw materials are largely imported from the two regions rather than from the GAFTA members. Many of the importers believe that the benefits of GAFTA would not be high, if any, since the tariffs are already very low.

4.3.4. Customs problems

Since the bureaucratic procedures on the borders are in many cases too complicated, some of the importers sacrifice the benefit of tariff eliminations, and pay the tariffs in order to avoid these complications. Hence, the potential benefits of the RTAs are not always fully utilized.

The big Egyptian importers do not distinguish between 'good' and 'bad' customs officials; they believe that if the importer is big in the market and experienced, the customs officials will cooperate and facilitate everything and vice versa. They also stress that corruption does not play a role for their companies, since an importer who knows her/his rights can avoid corrupting these officials. And in general, the big importers complain less about corruption, since the amounts they have to pay make up a little percentage of their revenues and profits as compared to the small importers. Moreover, the big importers are privileged in many aspects and dispose of more contacts in contrast to the rest.

The problems in the Egyptian customs are quite similar to the problems in the customs of the GAFTA countries; if there are slight differences between the information written on the invoices and the imported products, the latter may be stuck for days and even weeks in the customs. And if these products are agricultural goods, then they can be subject to spoilage or expiration, which happens in many cases. The importers consider this matter as an unjustified bureaucracy that causes waste of money and time.

When the imports are agricultural products, the Ministry of Agriculture is entitled to examine them before the customs clearance occurs. In several cases the examinations are run in a wrong way or the products are new for the laboratory technicians, and therefore the analysis wrongly give results that are not in favor of the products.

The interviewed companies reported that although customs duties and other import charges have been reduced, the reductions were being offset by increases in domestic taxes.

4.3.5. Freight costs

The importers stress that the country where they import from does not play a role in determining the tariff rates; it is rather the classifications of the products imported. They also confirm that the freight costs play a significant role in their overall costs; for example, although the USA is geographically among the farthest countries that Egypt trades with, the amounts paid to USA freight companies are very low as compared to others. In addition, the currency paid for freight plays a big role in determining the overall costs of importing.

4.4. The local producers

This section mainly deals with the external competition facing the local producers, due to the signed RTAs, their collective action towards that, their potential markets abroad, the government impediments facing them, the government support and commitment that they are missing and the corruption cases they report.

4.4.1. External Competition

Many producers fear the complete implementation of the RTAs, since they will have to face more external competition than before. But most of them set no great store on the competition from the countries of the RTAs; they are rather worried about the competition from South East Asian countries, especially after the full application of the GATT rules. They particularly feel threatened by China, where the labor is much cheaper than in Egypt and the productivity is much higher. The quality of their products is not necessarily better than the Egyptian products, but the Egyptian consumers do not pay much attention to the quality, as long as the products are provided in great quantities and for low prices. They claim that many other local producers had to shut down and exit the market because of this problem and many of the remaining producers in the market have cancelled some lines of production.

Even before completely applying the GATT rules, many of the producers are in trouble, since the corruption plays a big role in smuggling most of the Chinese imports into the Egyptian markets, and therefore they are not subject to any tariffs. Many importers sell the cheap Chinese products under Egyptian brands, in order to avoid legal complications. This is very harmful for the local producers who really use Egyptian inputs and labor and produce in national factories.

In Egypt it is forbidden to write foreign names, such as USA or European brands, on Egyptian products. The same applies to China. However, the Chinese government is stricter then the Egyptian one when it comes to application. The Chinese government even monitors the producers who undertake such actions and makes them subject to punishment. So, apparently, these Chinese producers escape with such products from China and distribute them widely in Egypt, where the government does not trace them as in the case of their home country. This leads to noticeable dumping in the prices in the Egyptian market.

According to the local producers, the external competition that follows trade liberalization does not only harm them, but would possibly also harm the importers who at the beginning prefer this liberalization; when the local producers are negatively affected by the cheap imports that threaten them, they are forced to reduce the salaries and wages of their employees and workers respectively or even dismiss some of them, in order to be able to cover the production costs after the demand for their local products decreases. These employees and workers represent a purchasing power in the economy. When the former weakens, this will have a negative impact on the importers when attempting to sell their imports in the local market. Therefore - according to the local producers - they need the government's support in order to be competitive and keep their workers in business.

4.4.2. Collective action

According to the individual interviews with the producers, no one of them is willing to lobby with the others in order to resist against the external competition. They believe that the general trend of all of them is not to cooperate with each other. In fact, their mindset makes them treat each other as enemies and there is no trust among them. Furthermore, each producer is concerned with her/his own enterprise and does not have the willingness to merge with others, in order to produce at a high scale and strongly face the external competition. They all believe that even if they lobby,

the government will go on with its policies, since the syndicate of workers is not powerful towards it.

4.4.3. Opening new markets abroad

When the local producers were asked whether they would like to open new markets abroad instead of having to deal with the external competition in the local markets, they argued that they are informed about the problems the Egyptian exporters face abroad and that they would definitely not have chances to be competitive internationally if they are not at the local level. They mentioned the example of some local producers who were willing to start an export activity with the countries of the RTAs and informed the Egyptian tax authority about that. When these producers found it too costly and hence cancelled these projects, they were 'chased after' by the tax authorities for many years later, although they did not actually export their products.

One important problem that the current local producers and potential exporters raise is the instability in the Egyptian markets and its price fluctuations. For example, it is hard for a producer to make a deal and determine the prices s/he would sell at in advance. Many producers had the chance to export to the countries of the RTAs, but when they informed the potential importers that they might not be able to stick to the prices agreed upon, due to the probable changes in the inputs prices, the deals were not signed by the importers. These examples discourage other producers from taking any new export initiatives and decrease the chances for international competitiveness, since they might lose and even exit the market if they agree in advance on selling the final products at certain prices and then be faced by sudden increases in the inputs prices.

4.4.4. Internal impediments

The local producers point out that it is unfair to treat them like the producers of the other countries of the RTAs, since in Egypt the producers are required to pay eighteen types of taxes, whereas the producers of the other countries do not. A new Egyptian tax law reduces the main production taxes from 40 percent to 20 percent, under the condition that the producers have to show the official invoices of the inputs and all other sorts of costs. But most of the producers do not receive such invoices from the input providers, since the latter prefer to avoid problems with the tax authorities, who would directly charge them sales taxes and open the door for

'negotiations' with them. In fact, the interviewed producers show understanding towards this situation, since they themselves do not report all their sales, avoiding hereby the same problem.

Another problem that discourages local producers is the prolonged procedures in the courts. For example, after having paid 18 percent sales taxes for four years, many textile producers discovered that they should have not paid them, since they had already been collected from the input providers, which lead to double taxing. When these producers asked for the money, it was not repaid to them. The cases are in court and have not been settled yet. Moreover, these procedures require time and money, which further creates an unhealthy environment for the producers and kills any incentives for opening markets abroad.

The tax employees themselves are not well informed and do their calculations in different ways. Therefore, a producer needs to deal with only one employee, and in case this employee is replaced by another the producer falls in trouble, since s/he has to start the calculations from the beginning and to submit the statements once again. Hence, there is no unified way of making the calculations, which leads in many cases to double accounting.

Due to all the problems that the producers face from the authorities, including the tax authorities, many of them shut down, close their tax files, and start new businesses in the informal sector. This proves that there is a general trend that discourages people from working in the forma sector. Hence, the profits that are gained in the informal sector do not enter the official income cycle, which negatively affects the economy.

4.4.5. The missing support

The textiles producers confirm that their industry needs much improvement and support from the government, in order to be competitive at local and international levels. For example, before privatization, they used to obtain high quality inputs from public companies, but after privatization, the quality of the inputs has deteriorated. They essentially blame the government for not selling the companies to qualified individuals. The latter dismissed at least 300 000 workers from the textiles industry, and the inputs' quality has deteriorated. Thus, apparently they did not have a proper strategy to improve their products. As a result, many textile producers stopped buying their inputs, which lead many of them to shut down, especially since they are also

faced by complicated tax laws. Hence, a vicious circle was created, further reducing the competitiveness of the local textile producers.

4.4.6. The missing commitment

On the other hand, a common complaint between the local producers, exporters and importers is the fact that the government does not commit itself in practice to the signed RTAs. The market representatives are very often impressed by the government press releases before being shocked by the obstacles in implementation. They agree that the Egyptian government has signed the RTAs just for political reasons and not really to benefit the Egyptian economic interests. When the government loses its credibility, the market representatives lose their predictability and future vision, which has a negative effect on the Egyptian economy in general and the Egyptian trade in particular.

4.5. Government officials

In the following, the outcomes of the interviews run in the Egyptian Ministry of Foreign Affaires, Customs Authority and Ministry of Industry and Foreign Trade are presented.

4.5.1. Ministry of Foreign Affaires

The interviews with officials in the Ministry of Foreign Affaires mainly concern Euro-Med versus GAFTA and COMESA, the concepts of national, regional and international liberalization, corruption, the enforceability of contracts and information asymmetries.

4.5.1.1. Euro-Med versus GAFTA and COMESA

The interviewed officials believe that the most serious RTA so far is the Egyptian-European Partnership Agreement, since it acts upon the rules of the WTO. This seriousness is imposed by the EU partners, who attain sounder regulatory framework and do not accept the weak ones existing in their partner countries. African and Arab countries in contrast are generally rather protective and encompass weak institutions in their economies.

There is a very important difference between Euro-Med and GAFTA. The former uses a model close to the NAFTA, where there is a compensation system. For example, the EU countries (developed countries) compensate Egypt (developing country), in the sense that the EU countries liberalize imports from the very beginning of implementing the Agreement, whereas Egypt liberalizes according to a schedule with a long transitional period. Thus, both are not treated similarly. The second sort of compensation includes a number of projects, programs and technical assistance, such as the European Program for South Mediterranean Countries *Mesures D'Accompagnement* (MEDA). But in the case of GAFTA, this compensation system is missing; for example, some less developed countries, such as Sudan and Yemen, are not yet prepared for opening their markets towards some other more developed Arab countries, since this would lead to great bankruptcies in their industries. Besides, the tariffs that their governments collect are a very important source of national income. They should be treated the same way that the EU countries treat a country like Egypt, including a right for a transitional period, while immediately opening the door for their products, especially that these products would not represent a threat for the Egyptian or other Arab countries' local production. They should also be supported by different assistance programs. This missing compensation mechanism might be one of the important reasons why some other Arab countries, such as Mauritania, Djibouti and Somalia have not joined GAFTA yet.

Only very few official meetings take place yearly in the frame of GAFTA. The responsible ministers of the member countries meet once in March and the other in October (a total of 10 hours a year), and in case a problem is not solved, the discussions are usually postponed till the upcoming meeting after 6 month. It is claimed that many of the attendants of the GAFTA committees do that as a routine and a source of income, whereas these committees do not really have a lot to do with the real trade occurring between the member countries. However, the EU ministers meet 12 times a year, and representatives for their ministries meet at least once every week.

Although the language and the history are similar among the GAFTA countries, still, the mind set of working together as one group, such as the EU, is entirely missing. The competition environment is highly dominating these countries. In addition, the problem of the leadership and the lack of political will are important constraints. On the other hand, most of the COMESA countries are landlocked and do not acquire enough information about each other, although they are located in one continent. There is a complaint about political disorders, high freight costs,

weak infrastructure and bad transportation among the African countries in general. Furthermore, many of the COMESA countries prefer and feel rather motivated and committed to deal with multinational companies and non-member countries. For example, although Egypt and Sudan have common borders, and Sudan is even member in GAFTA as well as COMESA, in many incidences the Sudanese authorities refuse to permit the entry of Egyptian cars carrying consignments to Sudan, since there are foreign enterprises dominating this business.

The reason for the relative success of the Egyptian-European Partnership could be referred to the fact that the EU countries are more experienced in RTA issues, since before the Partnership, the trade barriers among the EU countries themselves were diminished gradually till the union was complete. Another reason could be the fact that when Egypt deals with GAFTA and COMESA countries, it does not deal with a completely homogeneous group in each Agreement; despite the historical and cultural similarities of these countries, every country keeps its own characteristics. But having a look at the EU countries, they all apply unified tariff rates, there are no borders between them and they apply more or less similar policies. Hence, when trading with the EU, it is like rather trading with one big country.

4.5.1.2. National, regional and international liberalization

By signing the RTAs, Egypt is attempting to liberalize on regional and international basis, but it is more important to liberalize nationally; changing the rigid national policies is the most important and at the same time most difficult task. The same applies to other member countries of GAFTA and COMESA; Syria is member of GAFTA as well, which means that it signed an Agreement that supports free trade. Nevertheless, the national policies entail restrictions on capital movements, and therefore, the importers cannot afford paying in hard currency. Furthermore, foreign trade in Syria is dominated by the public sector, and hence, the government is entitled to determine the quantities and nature of imports entering the Syrian borders.

In order to import from Egypt, the Tunisian importers need import licenses from their government, which creates a new NTB. But the Tunisian government has called this measure off, since it was hindering transparency in trade. If these national NTBs remain, then there would be no difference if a country would liberalize regionally or internationally, with African, Arab or European countries, since the tight national policies would always be a burden and would not support and serve for the open regional and international policies.

4.5.1.3. Corruption

Corruption problems are countless in the case of COMESA. For example, the African economies are highly dominated by Asian traders who have already established their markets there and are against any free trade with other countries, such as Egypt. In short, they do not see any privilege for them from COMESA. These traders have a high influence on the decision makers and government officials in the COMESA countries. In many cases, bribes are paid, in order for the governments to limit or even ban the Egyptian imports in favor of the imports of Asian traders whose farms in their own countries mainly rely on the African demand. Although all this contradicts with the COMESA Agreement, there is no reference, commitment or penalty system in these countries.

The corruption problems are not limited to Arab and African countries, but they exist in some EU countries as well, even if not widely spread. For example, there are some reported cases in Italy, Spain and Greece, where the importers agreed to enter in their markets some Egyptian agricultural products that do not fully comply with the required standards of the EU. These are the cases where the Egyptian exporters are willing to exit the market and start new businesses, and accordingly, they send the remainders of their low quality products to these countries before the seasons are over, since they no longer need to be concerned about their reputation in the international markets. Nevertheless, such actions have a negative impact on the international reputation of the rest of the Egyptian exporters who plan to maintain their serious business. Noteworthy is the fact that such incidents would not take place without some of the Egyptian customs officials being disqualified or corrupt.

4.5.1.4. Enforceability of contracts

There are a number of complaints about the Egyptian exporters who start deals with African and Arab countries, and after receiving the money they do not commit themselves to these deals. In other cases they do not commit themselves to the guarantees agreed upon and do not provide the African importers with the necessary spare parts, etc.

Moreover, many Egyptian businessmen frequently change from one African or Arab country to the other and/or from one activity to the other. Accordingly, there is no stability and no real settling of markets and mutual trust.

Although the RoO are to a certain extent agreed upon in most of the RTAs, there are mainly two groups of Egyptian exporters who oppose the RoO in general and do not consider them. The first group is used to produce with certain inputs imported from non-member countries of the RTAs, mostly from South East Asian countries, since this is a precondition of their foreign customers for buying those products. The second are the producers who prefer the cheaper inputs also imported from non-member countries to the more expensive ones offered by the member countries, in order to reduce their total costs. Both groups of exporters do not stick to the RoO written in the RTAs.

There are many incidences where ships carry consignments and suddenly change their direction to pass by other countries for receiving more consignments. This reflects the disrespect of the contracts and the time factor especially that some products might be subject to spoilage. Hence, in many cases it is not only the bad transportation that causes the delays and infrequencies of the consignments, but rather the irresponsible behavior of some market representatives in the Arab and African countries. As a matter of fact, such behavior is widespread in these countries, as - in contrast to the case of the EU - it is hard to be penalized and there is a lack of enforceability of contracts.

4.5.1.5. Information asymmetries

Although the Egyptian exporters and importers assured that they still need to have their certificates of origin approved by the embassies or consulates of the GAFTA importing countries, officials in the Ministry of Foreign Affaires assured on their part that this procedure is no longer required. The latter argue that these importers and exporters might not have been informed and that the ministries cannot refuse the fees that the importers and exporters pay to them for approving the certificates, since these amounts are considered as an important source of income for the governments.

4.5.2. Customs officials

In this section the opinion of the customs officials concerning the RTAs, especially GAFTA, and the general trade environment are presented. It focuses on the problems facing the trade representatives when dealing with the customs authorities and the field teams that have been sent to monitor the customs in the GAFTA countries.

4.5.2.1. Customs problems

An interviewed official in the Egyptian Customs Authority admitted that he does not know how the CoO works; the latter is stamped by the Egyptian customs before it leaves the country together with the product, but it is not clear on what basis it is stamped. Moreover, the certificates are not stamped case by case and are not subject to control by third parties. This means that the procedure is a matter of routine, especially insofar as the GAFTA certificate for RoO is unified among the countries and it does not contain any details about the inputs used in the product.

Although a clear resolution was passed by the Minister of Foreign Trade which states that all the customs should be informed about the cancellation of the negative lists within GAFTA, many customs officials claim that they were not informed about that. Even if the negative lists are canceled in the frame of GAFTA, they may still exist in the frame of the BTAs, which is quite tricky and questionable with regard to the real benefits of GAFTA. The customs officials are confused about GAFTA and the BTAs of the Arab countries; they do not know which one to follow.

4.5.2.2. Field teams in the Arab customs

After there have been lots of complaints about the complicated and bureaucratic procedures in the customs of the GAFTA countries in general, the AL has sent official field teams to the customs of all these countries to investigate the application of unjustified NTBs, red tape and bureaucracy. However, no severe cases of violation were officially reported. In fact, this can be referred to the fact that it would be a bit sensitive to raise such issues publicly.

4.5.3. Ministry of Industry and Foreign Trade

Officials in the Egyptian Ministry of Industry and Foreign Trade were asked about problems occurring in Egypt in spite of the government control, low quality human resources in Egypt, Egyptian commercial delegations abroad, the lobbying system in Egypt, and the response of the local market towards the RTAs.

4.5.3.1. Problems occurring in Egypt in spite of the government control

The Ministry of Industry and Foreign Trade had to deal for a long time with the problem of the Egyptian potatoes infected by the brown rots disease. These potatoes entered the EU markets in the year 2004; a potatoes consignment was examined and directly rejected and sent back due to this infection. In conformity with the Egyptian-European Partnership Agreement, the EU determines the proper land to plant the potatoes and the basins where they are treated, according to certain technical standards with traceability. The maintenance and care for these basins is costly. One ton of the treated potatoes costs 200 Egyptian Pounds while the other costs only 50 Egyptian Pounds. The whole procedure is also controlled by the General Organization of Export and Import Control (GOEIC) and the Egyptian Health, Plants and Veterinary Quarantines. Therefore, there must be a leakage that led to this dilemma. After long investigations on the part of the Ministry, it was found out that some of the exporters bought normal potatoes from the local market and added them to potatoes that were treated according to the standards, in order to increase their profit margin.

The officials in the Ministry of Industry and Foreign Trade state that the problem must have been in the Health Quarantine or GOEIC. It is hard to find out whether the reason why it was not discovered is the ignorance, disqualification, non-interest or corruption of some employees. Hence, even if there is much official monitoring, it is not always guaranteed that this would work properly.

After the potatoes dilemma the Minister of Industry and Foreign Trade passed a new resolution stating that violating the export rules by certain exporters would automatically deprive them from any export activities for three following years as a penalty. This resolution was passed after the Egyptian exporters got a bad reputation world wide, which in turn has harmfully affected the Egyptian exports in general.

4.5.3.2. Low quality human resources in Egypt

According to the experience of the Ministry's officials, most of the exporters of agricultural and manufactured products are poorly qualified. Thus, they cannot make the best use of these RTAs, even though the latter look very promising on paper. These exporters do not have the future vision for establishing their markets abroad and prevailing a good reputation internationally. In addition, the Egyptian exporters concentrate on their own capabilities of producing certain products instead of keeping an eye on the international markets and the requirements of these markets concerning quantity, quality and timing.

The Ministry of Industry and Foreign Trade lacks the qualified personnel and there are no linkages and coordination between the qualified employees. The salaries are generally very low, which increases the probabilities of corruption. Moreover, there are no sufficient equipment, laboratories and skilled personnel who can handle them. All these labs and equipment need to be acknowledged from abroad in order to comply with the international standards.

In fact, the Ministry of Industry and Foreign Trade is committed to the signed RTAs. The budget at the disposal of the Ministry is large enough for improving the quality of personnel. However, it is rather a problem of misallocation of resources.

4.5.3.3. Egyptian commercial delegations abroad

According to leading officials in the Ministry of Industry and Foreign Trade, the Egyptian commercial delegations abroad do not always do their job accurately. The officials argue that many of the delegations personnel in 64 foreign countries are disqualified and have no future vision or incentives, since they are mainly selected according to their age in grade. For example, there is a complaint that these delegations do not inform the Egyptian exporters about their potential markets abroad. Furthermore, they are not capable of providing the Egyptian importers with information about their potential imports.

4.5.3.4. The lobbying system in Egypt

According to some officials in the Ministry, the lobbying system in Egypt is peculiar. For example, the local producers who believe to be harmed by the tariff reductions/eliminations do not get together in order to undertake an organized collective action, but everyone separately attempts to approach the government officials in order to achieve her/his target. Some of them even attempt to mislead the decision makers and provide them with wrong information or give currency to false rumors in the market, urging hereby for resolutions and measures that would at the end protect their individual interests.

4.5.3.5. The response of the local market to the RTAs

After the RTAs were implemented and the foreign products enter tariff-free, it was expected that the prices of the local and imported products would decrease. However, this decrease did not occur which could indicate that the local producers using foreign inputs have used the situation for their own interests by increasing their profit margins. Another explanation is the fact that the decrease in the tariff rates was overridden by the devaluation of the Egyptian Pound, and accordingly, the increase in the prices of the foreign inputs.

4.6. Common problems facing Egyptian importers and exporters

In this section the general opinion of the Egyptian importers and exporters concerning the common Egyptian institutional problems facing them when implementing the RTAs in general are summarized.

In general, the market representatives complain that the government decisions are often floundering and sudden, which leads to confusion and caution among the actors in the market. There is apparently no benchmark that the government uses when taking decisions. This leads to uncertainty. Market actors are hesitant before taking any step. This is not a healthy environment for investment, production, importing or exporting.

On average, the interviewed companies estimated the average costs of trading to be about 9 percent of the value of the total trade. The major sources of trading costs were ranked in

descending order as follows: customs clearance, public sector corruption, mandatory product standards, certification of conformity and transshipment regulations.

Concerning the time constraints for import clearance and inspection, it takes three to six days on average to release goods imported by air freight from customs; three to nine days for sea shipment; and one to four days for road shipment. In contrast, the international norm is less than six hours to clear air freight, less than twenty-four hours to clear sea freight; and less than four hours to clear shipment by road (Zarrouk, 2003). Regarding the number of documents and signatures required for processing a trade transaction, for the imports, it takes 12-19 signatures for air freight, 13-18 for sea shipment and 8-15 for road shipment. For the exports, it takes 7-9 signatures for air freight and sea shipment, and 12-17 for road shipment.

Important administrative costs are entailed in the number of workdays a year that Egyptian companies spend in resolving problems with customs and other government agencies. On average, this takes 90 workdays a year, and about 15 percent of the interviewees had daily contact (365 days a year) with customs and other government agencies. The companies regard these contacts as a clear encouragement to corruption and a source of 'extra amounts' of trading.

The interviewed companies were also asked whether difficulties in dealing with customs and other trade officials have decreased or increased in the late 1990s (after signing the RTAs). 30 percent of the interviewees thought that the difficulties had decreased, 22 percent believed that they had increased and 48 percent believed that they had remained about the same.

When asked about the obstacles to establishing and operating new importing and exporting businesses, the responding interviewees ranked these obstacles as follows: business licensing procedures; state monopoly of certain activities, such as insurance and mandatory employment of nationals; and public corruption.

When the interviewed companies were asked directly whether the RTAs signed by the government benefited their businesses, more than 60 percent of them replied that they had not benefited from any of the RTAs. According to the rest who benefited, the most beneficial RTA was the Egyptian-European Partnership Agreement, then came COMESA followed by GAFTA.

Moving on to the major constraints to trade, the interviewees ranked as the primary obstacle weak legal systems that fail to ensure that the terms of business contracts are honored. That was followed by direct state intervention to protect exclusive agents by giving territorial distributors monopoly over imports. Government limits on ownership of real estate and of equities are ranked third and fourth. That was complemented by traders' concern about corruption, domestic red tape, and bad governance, which was ranked fifth. Less transparent and complex tax systems were ranked sixth.

4.7. Summary and main findings

The previous sections demonstrated the important institutional obstacles hindering the full implementation of the signed RTAs, some of which can be summarized as follows:

- The awareness of the benefits of the RTAs is quite modest, since the public agencies do not make enough effort to keep the public informed. Information channels between ministries, traders and other concerned parties are completely absent.
- The information about foreign markets and the international promotion for the local products is poor.
- The guarantees system between the partner countries of the RTAs is missing in many cases.
- The competition from Asian countries is much stronger, offsetting the benefits of the RTAs.
- There exist diverse implementation problems; partner countries - including Egypt - do not always commit themselves to terms and conditions of the RTAs; the Articles of some RTAs are left to the interpretation of customs officials, who themselves lack knowledge about the operations of the RTAs and are not regularly informed about changes in rules, laws and resolutions.
- Although the RTAs look very promising on paper, they do not necessarily reduce the numerous administrative procedures, paperwork, red tape and corruption and do not improve the quality of human resources in Egypt.
- The transportation between countries of the RTAs is not always adequate.

CHAPTER 5

Assessing the Role of Institutional Factors within the Egyptian RTAs: A Gravity Model Approach

5.1. Introduction

Since this study is concerned with the institutional factors and their impact on facilitating/hindering the implementation of the RTAs that Egypt is member of, this chapter uses a gravity model, in order to assess the impact of institutions on trade flows between the countries where these trade flows are considered a proxy for a potential implementation of the different RTAs, where these trade flows are considered a proxy for a potential implementation. We analyze for each separate RTA, to which extent the quality of institutions affects the integration between the member countries. Additionally, for Egypt as a common country in the RTAs, we examine the impact of institutions on its trade volume with all the countries of the RTAs.

5.2. Empirical work

In the following, past empirical work that tackled the institutional factors and their relation with trade will be discussed.

5.2.1. The importance of institutions in trade

Economic literature has recently increased its interest in the role of institutions for the general functioning of markets[47]. Institutions embody different elements, such as formal and informal rules of behavior, ways and means of enforcing these rules, procedures for mediation of conflicts, and sanctions in the case of violation[48]. Institutions depend on the operation of these different features. The more the institutions are well-developed, the more likely the transaction costs for

[47] Examples for relevant literature are Frankel and Romer (1999), Acemoglu et al. (2001) and Rodrik et al. (2002).

[48] See North (1994) and World Bank (2002). North (1990) makes a distinction between institutions and organizations, referring to the first as the rules and the second as the players.

market participants would decrease and hence the efficiency of markets would increase. The channels through which well-developed institutions fulfill this are the following[49]:

1. The reduction of information asymmetries, since good institutions make information about market conditions, goods and participants more available.
2. Risk reduction, since good institutions define and enforce property rights and contracts.
3. Dampening the actions undertaken by politicians and interest groups.

According to the World Development Indicators (WDI, 2003), trade as a share of the world Gross Domestic Production (GDP) has increased from 25 per cent in 1960 to 58 per cent in 2001. This could be an indicator for deeper international specialization, which has in turn led to an increase in the number of international transactions per dollar of world GDP. At the same time, it reflects the substantial tariff reductions that took place since the 1960s, and hence, the observed global increase in trade.

Thus, one could expect that the trade volume should rather be higher among countries of one RTA, since in most cases, the tariffs are fully eliminated. However, even within one RTA, international trade might be about contracts between countries operating in different jurisdictions, different institutional environments, and different cultural and historical backgrounds. Moreover, the contracting countries are very often located in different geographic regions. Therefore, the decision to export or to import is connected with a large number of uncertainties; for example, it would take money and human effort to transport one good from one place to the other and it would even be questionable to which extent the quality and quantity of the shipment upon arrival complies with the one upon departure. The time gap between signing the contract and the payment involved is also a factor that should not be overlooked. An exporter may receive her/his money only upon the delivery of the good and not before sending it abroad. Hence, the exporter has to overtake the production and transport costs in advance, going through the risk that the expected payment will not be made. An important factor as well is the artificial over- and undervaluation of the currencies and the risks associated with such actions. These uncertainties and the resources involved in negotiating and enforcing contracts highly contribute to the transaction costs affecting the volume of trade between the member countries of any RTA. Needless to mention, the greater the difference between these countries concerning the

[49] World Bank (2002).

enforcement of contracts and further institutional structures, the more the transaction costs associated with trade between them could increase.

It is therefore not surprising to know that not all countries - whether they belong to RTAs or not - have experienced the same growth rate in trade, since the response of trade flows with respect to changes in tariffs may differ across countries, based on the differences between their institutions. A quite relevant explanation for this phenomenon could be the fact that tariff reductions increase trade flows only where other domestic factors - such as sound institutions - create a favorable environment for trade. A further explanation could be the fact that in the concerned countries transaction costs other than those related to tariffs have remained high or even increased over the years.

Institutions are supposed to be responsible for setting the rules for the interaction between private actors and for the interaction between public and private actors as well[50]. Well-functioning institutions reduce the level of uncertainty and in turn reduce transaction costs. Therefore, they are expected to have a positive impact on economic activity, and particularly on international trade.

In contrast, inefficient institutions can lead to serious obstacles for trade. *Bigsten et al.* (2000) give a good example on how an inefficient legal system can hinder interaction between manufacturing firms in a number of African countries on one hand and potential importers outside the continent on the other; after collecting survey data in Burundi, Cameroon, Côte d'Ivoire, Kenya, Zambia and Zimbabwe, the authors examined the contractual practices of African manufacturing firms. One of their findings is that a risky trade environment is usually associated with contract non-performance, and thus a higher probability of renegotiation of a contract. Due to the absence of an efficient legal system, the use of lawyers and courts to enforce the original contract can be rare. In this case, importers and exporters do not fulfill their contracts in the regular ways; imports may not arrive on time and/or their quality may not comply with what was ordered, and importers sometimes pay later than agreed upon. For instance, when Europeans deal with African firms, the former are often surprised by contractual renegotiations, delays or even sudden cancellations. It would be hard for those who are not used to functioning in this sort of environment to capture the fact that unpredictable behavior of African firms in such cases is nothing more than a 'rational' response to an inefficient system. This explains - to a

[50] For a detailed elaboration, see North (1990).

great extent - why firms of developed countries have a hard time dealing with Third-World firms and the chances for the latter to enter the export markets of the former are very low. Hence, we would expect domestic institutions to affect a country's overall level of openness; countries with better institutions are expected to trade more and inefficient institutions can be regarded as a cost factor for domestic exporters and therefore lower their international competitiveness, leading in turn to negative repercussions on export flows. On the other hand, transaction costs associated with inefficient institutions raise the final consumer price of imported goods, which negatively affects a country's import flows.

It is also worth mentioning that institutions are expected to influence the effectiveness of trade policy; even if we assume that the trade barriers of one country are lowered to the minimum, outsiders may still be reluctant to trade with that country if, for example, they are not sure whether contracts will be enforced or payments will be made.

Quite recent empirical studies have relied on more sophisticated measures for institutional quality in gravity equations. Take for instance *Anderson and Marcouiller* (2002) who use the survey data of the World Economic Forum on contractual enforcement and corruption as an index for institutional quality. Using a gravity equation, they conclude that lower institutional quality negatively affects trade.

Rauch and Trindade (2002) are concerned with the transnational networks and their impact on trade. Such networks include informal institutions that can either take the function of missing formal institutions or complement existing formal institutions. According to *Greif* (1993), the networks of traders can play an important role when it comes to contract enforcement in international trade[51]. Furthermore, they can contribute to the reduction of transaction costs through the reduction of information costs. In the study of *Rauch and Trindade* (2002), they find that the ethnic Chinese networks strongly and positively influence the bilateral trade, especially in the case of differentiated products. This result can be referred to the fact that information costs are more important in the case of differentiated rather than homogeneous products.

[51] See for instance Greif (1993) on the role of coalitions between traders that governed agency relations among the Maghribi traders in the Mediterranean are in the 11th century.

De Groot et al. (2004) use the measure for institutional quality to analyze the effect of institutions on bilateral trade flows. They find that a better quality of informal institutions tends to coincide with more trade. Their paper also includes a special dummy for RTAs.

5.2.2. Other factors affecting trade between countries

Numerous studies have focused on the geographical determinants of trade. These determinants are expected to affect the transaction costs a country faces in terms of international transport costs. A country's distance to its trading partners also has a negative effect on its propensity to trade. Hence, it is a standard result that measures of 'remoteness' have a negative and significant effect on openness (Jansen and Nordas, 2004; Rodrik, 1998; Frankel and Rose, 2000 and Wei, 2000)[52]. International transport costs are captured by the geographical distance between countries and by a border dummy[53]. It is also very common in the empirical literature to include dummies for islands and landlocked countries when explaining openness, since both types of countries are expected to face higher international transport costs (e.g., Frankel and Rose, 2000 and Wei, 2000).

The size of a country is likely to play a big role in determining openness, due to the fact that the small size limits the country's possibilities to diversify production. In order to satisfy their domestic demand, smaller economies rely to a larger extent on imports as compared to large-size countries[54]. Country size has indeed systematically been found to have a significantly negative impact on imports, and hence on the openness of any country (e.g., Rodrik, 1998; Frankel and Rose, 2000 and Wei, 2000). This country size is usually measured by population or landmass.

According to *Frankel and Rose* (2000), the literature considered for a long time the elasticity of trade with respect to output to be larger than unity. In other words, richer countries trade more. But according to some recent studies, when including measures for institutional quality and trade

[52] Very few papers, such as Baier and Bergstrand (2001) have used direct measures for transport costs. These measures included c.i.f./f.o.b ratios from the IMF International Financial Statistics, which was highly criticized in the literature for its low quality (Hummels, 2001). It should also be noted that the relevant data are no longer published in the International Monetary Fund (IMF).

[53] Trade between adjacent countries is expected to be characterized by lower transaction costs.

[54] See for instance Commonwealth Secretariat and Easterly and Kraay (2000) for the particularities of small economies.

policy in gravity equations, the effect of GDP on trade becomes either insignificant or turns negative[55].

The effect of institutional factors on bilateral trade flows is also captured by variables reflecting a shared historical, political and cultural background. The measures that have been most commonly used for this purpose are dummies that indicate the presence of cultural factors, such as a common language, a common dominant religion and/or a common colonial history. Each of these factors is likely to affect international transaction costs in its own way. For example, a common language facilitates communication in personal contact. A common religion may increase mutual trust and thus reduce the perceived risk of transactions, and a common colonial history has also been considered to affect international transaction costs in a way or another (Jansen and Nordas, 2004).

5.3. The gravity model

One of the most successful empirical trade devices of the past decades is the gravity model. It has long been recognized that bilateral trade patterns are well described empirically by this model, which relates trade between two countries positively to both of their incomes and negatively to the distance between them, usually with a functional form that is reminiscent of the law of gravity in physics (Deardorff, 1995).

In 1687, Isaac Newton introduced the "Law of Universal Gravitation". It held that the attractive force between two objects *i* and *j* is given by:

$$F_{ij} = G\frac{M_i M_j}{D^2_{ij}}$$

where F_{ij} is the attraction force, M i and M j are the masses, D_{ij} is the distance between the two objects and G is the gravitational constant depending on the units of measurements for mass and force.

The multiplicative nature of the gravity equation means that we can take natural logs and obtain a linear relationship between trade flows and the logged economy sizes and distances as follows:

[55] See for instance Anderson and Marcouiller (2002), de Groot et al. (2003) and de Groot et al. (2004).

$$ln\,(Fij) = \alpha 1\,ln\,(Mi) + \alpha 2\,ln\,(Mj) - \theta\,ln\,(Dij) + \varepsilon ij$$

where F_{ij} is measured as monetary flow such as exports, M is usually the GDP of each location. Thus M can also be related with population, D_{ij} is the distance between the locations measured from centre to centre.

When applied to a wide variety of goods and factors moving over regional and national borders under differing circumstances, the gravity model usually produces a good fit (Anderson and Wincoop, 2003). In the following, we briefly demonstrate the most important studies that used this model, particularly in assessing the impact of different factors on trade flows between countries.

5.3.1. Past studies using the gravity model

One of the very first studies that relied on the gravity model in the empirical literature was the one run by *Tinbergen* (1962) and *Pöyhönen* (1963). In fact, they ran the first econometric studies of trade flows based on the gravity equation, for which they gave some intuitive justifications. *Linnemann* (1966) added more variables and went further towards a theoretical justification in terms of a *Walrasian* general equilibrium system, but the *Walrasian* model tends to include too many explanatory variables for each trade flow to be easily reduced to the gravity equation. *Leamer and Stern* (1970) followed *Savage and Deutsch* (1960) in deriving this equation from a probability model of transactions. They applied their approach on trade. *Leamer* (1974) also used the gravity equation to motivate explanatory variables in a regression analysis of trade flows.

These contributions were followed by several more formal attempts to derive the gravity equation from models that assumed product differentiation. For example, *Anderson* (1979) was the first to do so, assuming Cobb-Douglas preferences. *Jeffrey Bergstrand* has explored the theoretical determination of bilateral trade in a series of papers. For example, in *Bergstrand* (1985) he derived a reduced form equation for bilateral trade involving price indices. *Helpman* (1987) used a correspondence between the gravity equation and the monopolistic competition model as the basis for his empirical work, i.e., he interpreted the close fit of the gravity equation with bilateral data on trade as supportive empirical evidence for monopolistic competition. *Helpman* applied his

test to data on trade of the Organization for Economic Co-operation and Development (OECD) countries, where most would agree that monopolistic competition is possibly present. *Hummels and Levinson* (1995) decided to attempt a sort of negative test of the same proposition by looking for the same relationship in the trade among a larger variety of countries, including those where monopolistic competition is less visible. *Anderson and Marcouiller* (2002), *de Groot et al.* (2004) and *Jansen and Nordas* (2004) observed a positive and robust relation between the quality of institutions and countries' openness to trade as measured by their trade flows.

This study attempts to detect the same relationship within the countries of COMESA, Euro-Med and GAFTA separately as well as between Egypt and the WTO member countries, including countries who are also members of the three RTAs.

5.3.2. The rationale and steps of the gravity model used in this study

The gravity model used in this study mainly relies on the following three indicators for institutional quality:

1. *Government Effectiveness*: It is an indicator for the quality of public service provision, the quality of the bureaucracy, the capability of civil servants, the independence of the civil service from political pressures, and the accountability of the government's commitment to different policies. It can also determine the importance of uncertainties related to policy changes in general and trade policy changes in particular.
2. *Rule of Law*: It is based on several indicators that measure the extent to which agents trust and bear the rules of society. These indicators contain the perceptions of the incidence of crime, the effectiveness and predictability of the judiciary, and the enforceability of contracts.
3. *Control of Corruption*: It measures the perceptions of corruption, usually defined as using the public power for private gain. Hence, high levels of corruption increase the uncertainty about the size of gains to be expected from economic activities. Corruption seems to be a widespread phenomenon with potentially large negative effects on trade[56].

[56] See for instance Ades and Di Tella (1999) and Wei (2000).

In a 1996 World Bank survey of 3,685 firms in 69 countries, for instance, corruption proved to be the second most important obstacle for doing business[57].

The three indicators are available in the *Kaufmann et al.* (2002) database[58]. Their indexes take values between -2.5 and 2.5; the higher the value the better the quality of the institutional factor. These indicators were chosen, since they can be expected to strongly affect the uncertainty involved with trade and hence the transaction costs.

In all the regressions, the dependent variable is the trade flows between the member countries of each RTA pair wise, and the main concern is estimating the coefficients of the three institutional independent variables and detecting their sign and significance in the model. We first add only the very basic independent variables - also used as control variables - of the gravity model (GDP[59] for the pair countries and the geographic distance between them) to the institutional variables, and in advanced steps, we add other complementary variables such as landmass or population of the importing partner country, border contingency with the partner country, common official language, common spoken language, common dominant religion[60], being colonized by a common colonizer, having a colonial relationship and being a same country[61] at a certain time of history[62], which are all independent variables that could have a certain influence on the trade flows between the countries of the RTAs.

[57] Brunetti et al. (1997) as cited in Anderson and Marcouiller (2002). The obstacle that ranked first was complaints about tax regulation and high taxes.

[58] The measures for institutional quality in de Groot et al. (2004) are taken from the same database.

[59] To avoid the endogeneity problem between the GDP on one hand and the exports and imports on the other, instrumental variables that explain the GDP were used, such as belonging to a certain continent, having colonized or having been colonized in the past, and using the languages used in the former colonies.

[60] Detailed data on the dominant religions in different countries were obtained from the World Fact Book, Central Intelligence Agency (CIA).

[61] For example, Jordan, Lebanon, Palestine and Syria used to be considered one country called 'Bilad-Es-Sham' before certain political divisions by Arab rulers took place.

[62] CEPII (2005).

5.4. The regression results

5.4.1. COMESA

Before including the three institutional variables in one regression, the correlation coefficients between the three variables are calculated. They confirm a very high multi-collinearity, as it is shown in *Table 5.1.*; the correlation coefficients for all combinations of pairs of the three indicators range between 0.8523 and 0.9060. An important reason for that could be the fact that they eventually reflect various aspects of the same thing, namely, the quality of one country's institutions. Thus, the three of them influence each other in a way or another. But usually, corruption, uncertainties related to entering and enforcing contracts, and ineffective provision of government services represent separate cost elements in international trade (Jansen and Nordas, 2004). Therefore, the regressions are run - with respect to each of the institutional indexes - separately.

Table 5.1.: Correlation coefficient matrix between the institutional variables in COMESA countries

	Government effectiveness	Rule of law	Control of corruption
Government effectiveness	1	0.8872	0.8523
Rule of law	0.8872	1	0.9060
Control of corruption	0.8523	0.9060	1

5.4.1.1. Using the minimum number of variables of a gravity model

5.4.1.1.1. Exports

Firstly, the exports of one member country *i* of COMESA to another member country *j* are regressed on the institutional variables existing in both countries (one at a time in the three different regressions) in addition to the GDP of the two countries and distance between them, using the following regressions:

$$log\text{-}exp\text{-}ij = \alpha 1 + \beta 1\ log\text{-}gdp\text{-}i + \gamma 1\ log\text{-}gdp\text{-}j + \delta 1\ log\text{-}distwces + \eta 1\ log\text{-}goveff\text{-}i + \theta 1\ log\text{-}goveff\text{-}j + \varepsilon 1 \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots 1$$

$log\text{-}exp\text{-}ij = \alpha 2 + \beta 2\ log\text{-}gdp\text{-}i + \gamma 2\ log\text{-}gdp\text{-}j + \delta 2\ log\text{-}distwces + \eta 2\ log\text{-}rullaw\text{-}i + \theta 2\ log\text{-}rullaw\text{-}j + \varepsilon 2$.....2

$log\text{-}exp\text{-}ij = \alpha 3 + \beta 3\ log\text{-}gdp\text{-}i + \gamma 3\ log\text{-}gdp\text{-}j + \delta 3\ log\text{-}distwces + \eta 3\ log\text{-}contco\text{-}i + \theta 3\ log\text{-}contco\text{-}j + \varepsilon 3$.....3

where:
exp-ij are country i's exports to country j
gdp-i is the GDP of the exporting country i
gdp-j is the GDP of the importing country j
distwces is the weighted average distance between countries i and j
goveff-i is the government effectiveness index for country i
goveff-j is the government effectiveness index for country j
rullaw-i is the rule of law index for country i
rullaw-j is the rule of law index for country j
contco-i is the control of corruption index for country i
contco-j is the control of corruption index for country j

$\alpha, \beta, \gamma, \delta, \eta, \theta$ are the respective estimated coefficients and ε is the error term[63].

The results are shown in *Table 5.2*. In the three cases, the GDP coefficients of the two partner countries give a positive sign at a five per cent level. The same applies to the coefficients of the institutional variables in both countries, although the institutional variables of the exporting country matter apparently more than the ones of the importing country. The distance coefficient gives in all cases the expected negative sign and is also significant. In general, the control of corruption matters less than government effectiveness and rule of law.

[63] Since the institutional indexes range between -2.5 and +2.5, the value 2.5 was added to them, in order to avoid zero and negative values, leading to undefined values when deriving the natural logarithms.

Table 5.2.: The impact of GDP, distance and institutional variables on exports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-22.23314 (-1.82)	-27.94181 (-2.28)	-34.67325 (-2.68)
GDP in country i	2.154103 (7.41)	2.35645 (8.32)	2.413375 (8.15)
GDP in country j	1.365371 (3.19)	1.522558 (3.45)	1.682377 (3.57)
Distance between country i and j	-6.970546 (-8.91)	-7.090463 (-9.14)	-6.937071 (-8.37)
Institutional variable in country i	6.735154 (3.91)	4.832982 (4.28)	4.027507 (2.14)
Institutional variable in country j	3.116435 (2.04)	2.615622 (2.38)	4.01008 (2.47)
R-squared	0.4875	0.5016	0.4560

5.4.1.1.2. Imports

To look at the other side of the coin, we regress the imports of one country (i) of COMESA on the GDP, the institutional variables of that country and its exporting partner (j) from the same Agreement and the distance between the two countries (i and j) in three separate regressions, as is shown in the three following regressions:

$$log\text{-}imp\text{-}ij = \alpha 4 + \beta 4\ log\text{-}gdp\text{-}i + \gamma 4\ log\text{-}gdp\text{-}j + \delta 4\ log\text{-}distwces + \eta 4\ log\text{-}goveff\text{-}i + \theta 4\ log\text{-}goveff\text{-}j + \varepsilon 4 \quad \ldots\ldots 4$$

$$log\text{-}imp\text{-}ij = \alpha 5 + \beta 5\ log\text{-}gdp\text{-}i + \gamma 5\ log\text{-}gdp\text{-}j + \delta 5\ log\text{-}distwces + \eta 5\ log\text{-}rullaw\text{-}i + \theta 5\ log\text{-}rullaw\text{-}j + \varepsilon 5 \quad \ldots\ldots 5$$

$$log\text{-}imp\text{-}ij = \alpha 6 + \beta 6\ log\text{-}gdp\text{-}i + \gamma 6\ log\text{-}gdp\text{-}j + \delta 6\ log\text{-}distwces + \eta 6\ log\text{-}contco\text{-}i + \theta 6\ log\text{-}contco\text{-}j + \varepsilon 6 \quad \ldots\ldots 6$$

where:

imp-ij are country i's imports from country j.

Hence, in this case, i is the importing country and j is the exporting country.

The results shown in *Table 5.3.* are quite similar to the ones in *Table 5.2.*, giving more weight to the government effectiveness and the rule of law as compared to the control of corruption. However, the latter still remains significant.

Table 5.3.: The impact of GDP, distance and institutional variables on imports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-49.35495 (-3.86)	-56.15734 (-4.36)	-55.2346 (-4.08)
GDP in country i	1.714901 (5.64)	1.862254 (6.25)	1.852866 (6.00)
GDP in country j	2.939151 (6.56)	3.228312 (6.95)	3.114785 (6.34)
Distance between country i and j	-6.667179 (-8.14)	-6.848802 (-8.38)	-6.710138 (-7.76)
Institutional variable in country i	3.767305 (2.09)	2.560623 (2.16)	3.383848 (2.82)
Institutional variable in country j	5.776103 (3.60)	4.505603 (3.90)	4.263756 (2.51)
R-squared	0.4725	0.4807	0.4429

5.4.1.2. Using the minimum number of variables of a gravity model in addition to the landmass or population of the importing country

In a following step, we add the landmass and population of the importing country one at a time as a further independent variable and expect the sign of the coefficient to be negative.

5.4.1.2.1. Exports

For the three institutional variables, we use the following regression on separate basis:

$$log\text{-}exp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}i + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \lambda\ log\text{-}size\text{-}j + \eta\ log\text{-}inst\text{-}i + \theta\ log\text{-}inst\text{-}j + \varepsilon \quad \ldots\ldots 7$$

where:
inst-i is the institutional variable in the exporting country i
inst-j is the institutional variable in the importing country j

size-j is the size of the importing country j (measured in terms of landmass or population one at a time).
λ is the estimated coefficient of the country size.

The results shown in *Table 5.4.* indicate that the GDP coefficients of both countries remain positive and significant, whereas the landmass coefficients are insignificant in the three cases. What is also noteworthy is the fact that the coefficients associated with the institutional variables in the exporting countries are positive and significant, while the same variables in the importing countries turn to be insignificant. This implies that the trade flows between two member countries of COMESA depend on the good or bad institutions in the exporting country rather than in the importing country.

Table 5.4.: The impact of GDP, distance, landmass and institutional variables on exports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-31.98795 (-2.28)	-33.58361 (-2.54)	-37.11433 (-2.68)
GDP in country i	2.169479 (7.48)	2.361787 (8.35)	2.41336 (8.13)
GDP in country j	2.202963 (2.98)	2.004189 (3.26)	1.922035 (2.90)
Landmass of country j	-0.5570618 (-1.39)	-0.3474317 (-1.12)	-0.1937438 (-0.52)
Distance between country i and j	-7.102365 (-9.04)	-7.153432 (-9.20)	-6.940776 (-8.36)
Institutional variable in country i	6.813302 (3.96)	4.830913 (4.29)	4.00035 (2.11)
Institutional variable in country j	0.3554717 (0.14)	1.624471 (1.15)	3.08593 (1.27)
R-squared	0.4950	0.5064	0.4571

Table 5.5.: The impact of GDP, distance, population and institutional variables on exports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-29.05389 (-2.30)	-32.52485 (-2.61)	-37.45125 (-2.85)
GDP in country i	2.195654 (7.60)	2.384131 (8.46)	2.433537 (8.22)
GDP in country j	2.488058 (3.37)	2.339004 (3.52)	2.295544 (3.28)
Population in country j	-0.9437221 (-1.85)	-0.7365251 (-1.64)	-0.5845353 (-1.18)
Distance between country i and j	-7.302963 (-9.18)	-7.315949 (-9.34)	-7.08345 (-8.47)
Institutional variable in country i	6.930711 (4.05)	4.900408 (4.37)	4.116302 (2.18)
Institutional variable in country j	.5147501 (0.25)	1.368502 (1.03)	2.496294 (1.21)
R-squared	0.5008	0.5118	0.4618

Replacing the landmass by the population as an indicator for the size of the importing country does not change the insignificance of the associated coefficients, as can be seen from *Table 5.5*.

5.4.1.2.2. Imports

After replacing the exports of regression 7 by the imports, the regression takes the following form:

$$log\text{-}imp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}i + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \lambda\ log\text{-}size\text{-}i + \eta\ log\text{-}inst\text{-}i + \theta\ log\text{-}inst\text{-}j + \varepsilon \quad \ldots\ldots 8$$

Table 5.6.: The impact of GDP, distance, landmass and institutional variables on imports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-66.02495 (-4.70)	-69.64503 (-5.15)	-68.14524 (-4.87)
GDP in country i	3.202826 (4.98)	3.110683 (5.73)	3.152361 (5.66)
GDP in country j	2.964749 (6.77)	3.281678 (7.23)	3.151919 (6.57)
Landmass of country i	-1.048322 (-2.61)	-0.9512979 (-2.72)	-1.011651 (-2.78)
Distance between country i and j	-6.966325 (-8.61)	-7.251933 (-8.94)	-7.064429 (-8.29)
Institutional variable in country i	-0.6016684 (-0.25)	0.4136521 (0.29)	-0.2996674 (-0.13)
Institutional variable in country j	5.925594 (3.78)	4.706003 (4.16)	4.58457 (2.76)
R-squared	0.4989	0.5089	0.4743

The results in *Table 5.6.* indicate that the GDP in both countries has a positive effect on trade flows between the partner countries of COMESA. And once again, the institutional quality in the exporting countries only has a positive effect on the trade flows. *Table 5.7.* gives the same results, but after substituting the population - which in itself does not have a significant effect - for the landmass.

Table 5.7.: The impact of GDP, distance, population and institutional variables on imports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-50.48576 (-3.93)	-56.9079 (-4.43)	-55.71572 (-4.13)
GDP in country i	2.235333 (3.64)	2.47185 (4.57)	2.494904 (4.53)
GDP in country j	2.940591 (6.57)	3.241984 (7.00)	3.128448 (6.39)
Population in country i	-0.4993383 (-0.98)	-0.6192088 (-1.35)	-0.6592732 (-1.41)
Distance between country i and j	-6.918498 (-8.06)	-7.228643 (-8.39)	-7.112444 (-7.84)
Institutional variable in country i	2.659239 (1.25)	1.954024 (1.54)	2.468388 (1.19)
Institutional variable in country j	5.851141 (3.65)	4.618811 (4.00)	4.470591 (2.63)
R-squared	0.4763	0.4880	0.4513

5.4.1.3. Dropping the institutional variables in the importing countries from the regressions

Since the regressions in the previous section proved that the institutional variable in the importing country does not have a significant effect on the trade flows between two countries, the same regressions are run after dropping this variable, while keeping the institutional variable in the exporting country. A slight change in the regressions occurs as follows:

$$log\text{-}exp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}i + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \lambda\ log\text{-}size\text{-}j + \eta\ log\text{-}inst\text{-}i + \varepsilon \quad \ldots\ldots 9$$

$$log\text{-}imp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}i + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \lambda\ log\text{-}size\text{-}i + \theta\ log\text{-}inst\text{-}j + \varepsilon \quad \ldots\ldots 10$$[64]

5.4.1.3.1. Exports

In the case of the exports and as it is shown in *Table 5.8.*, the GDP coefficients, the distance and institutional coefficients remain significant, and even the coefficient of the landmass as an indicator for the size of the importing country turns into significant. This means that the exports of one country to the other are negatively associated with the size of the importing country.

[64] Note that regression 9 reflects the situation of the exporting country, and therefore the institutional variables of country j (the importing country) were dropped. On the other hand, regression 10 reflects the situation of the importing country i and therefore its own institutional variables were dropped, while the institutional variables of country j remained in the regression.

Table 5.8.: The impact of GDP, distance, landmass and *institutional variables of the exporting countries* on exports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-32.59282 (-2.44)	-34.20385 (-2.59)	-37.89752 (-2.74)
GDP in country i	2.169549 (7.51)	2.339389 (8.28)	2.385815 (8.04)
GDP in country j	2.26332 (3.76)	2.175457 (3.64)	2.197096 (3.50)
Landmass of country j	-0.6022409 (-2.47)	-0.5712857 (-2.37)	-0.5475523 (-2.16)
Distance between country i and j	-7.101858 (-9.07)	-7.039638 (-9.12)	-6.763386 (-8.24)
Institutional variable in country i	6.805899 (3.98)	4.732816 (4.21)	3.754576 (1.99)
R-squared	0.4949	0.5013	0.4502

Table 5.9. gives the same results after substituting the population for the landmass. Again, the former becomes negatively significant after dropping the institutional variable of the importing country.

Table 5.9.: The impact of GDP, distance, population and *institutional variables of the exporting countries* on exports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-29.28283 (-2.33)	-31.3597 (-2.52)	-35.15209 (-2.70)
GDP in country i	2.19696 (7.63)	2.369976 (8.42)	2.415916 (8.16)
GDP in country j	2.574445 (3.96)	2.502868 (3.88)	2.503003 (3.69)
Population in country j	-1.02977 (-2.77)	-1.001409 (-2.72)	-0.9531934 (-2.45)
Distance between country i and j	-7.309648 (-9.22)	-7.25299 (-9.29)	-6.972739 (-8.37)
Institutional variable in country i	6.919552 (4.06)	4.834358 (4.32)	3.956018 (2.10)
R-squared	0.5005	0.5078	0.4557

5.4.1.3.2. Imports

Table 5.10. and *Table 5.11.* show - first using landmass and then population respectively - that not only the GDP in both countries, the distance between them and the institutional quality of the

exporting countries matter, but also the size of the importing country has an influence on the imports, a negative one, though, which was predicted by the theory and proven in most of the past empirical evidence.

Table 5.10.: The impact of GDP, distance, landmass and *institutional variables of the exporting countries* on imports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-64.62396 (-5.05)	-70.69572 (-5.44)	-67.81233 (-4.95)
GDP in country i	3.096306 (6.51)	3.18838 (6.73)	3.119147 (6.35)
GDP in country j	2.962714 (6.79)	3.285541 (7.27)	3.152943 (6.60)
Landmass of country i	-0.9799708 (-3.37)	-1.009297 (-3.50)	-0.9850449 (-3.30)
Distance between country i and j	-6.98241 (-8.69)	-7.2322 (-8.98)	-7.080081 (-8.42)
Institutional variable in country j	5.941948 (3.80)	4.691966 (4.17)	4.597304 (2.79)
R-squared	0.4987	0.5086	0.4743

Table 5.11.: The impact of GDP, distance, population and *institutional variables of the exporting countries* on imports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-53.14414 (-4.19)	-58.59173 (-4.55)	-55.77159 (-4.13)
GDP in country i	2.646794 (5.10)	2.728553 (5.28)	2.656134 (4.97)
GDP in country j	2.943771 (6.56)	3.251211 (6.98)	3.110168 (6.34)
Population in country i	-0.8392804 (-2.45)	-0.8702512 (-2.02)	-0.8356747 (-2.42)
Distance between country i and j	-6.875599 (-8.00)	-7.114964 (-8.24)	-6.946318 (-7.73)
Institutional variable in country j	5.745287 (3.58)	4.506109 (3.89)	4.293808 (2.53)
R-squared	0.4700	0.4785	0.4453

5.4.1.4. Adding the complementary variables to the regressions

In the following regressions, we add further complementary independent variables that might have an influence on the trade flows between the pair countries in COMESA. The regression takes the following form:

$$log\text{-}exp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}i + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \lambda\ log\text{-}size\text{-}j + \mu\ log\text{-}(1+contig) + \nu\ log\text{-}(1+comla\text{-}f) + \omega\ log\text{-}(1+comla\text{-}k) + \rho\ log\text{-}(1+comrel) + \pi\ log\text{-}(1+colony) + \sigma\ log\text{-}(1+comcol) + \partial\ log\text{-}(1+smctry) + \eta\ log\text{-}inst\text{-}i + \theta\ log\text{-}inst\text{-}j + \varepsilon \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots 11$$ [65]

where:
contig is the dummy for the contiguity (common border) between the pair countries.
comla-f is the dummy for the common official language between the pair countries.
comla-k is the dummy for the common spoken language between the pair countries.
comrel is the dummy for the common dominant religion between the pair countries.
colony is the dummy for a historical colonial relationship between the pair countries.
comcol is the dummy for being historically colonized by a common colonizer.
smctry is the dummy for country i and country j being one country at a certain time of history.
$\mu, \nu, \omega, \rho, \pi, \sigma, \partial$ are the estimated coefficients of the added variables to the model respectively.

5.4.1.4.1. Exports

It seems from *Table 5.12.* and *Table 5.13.* - using landmass and population respectively, as indicators for country size - that adding the complementary independent variables does not add much significance to the regressions. Moreover, the inclusion of these variables in the model makes the landmass and population lose their significance in most of the regressions. In other words, the impact of these variables - apart from the common colonizer in a few cases - on trade flows between the partner countries is insignificant, while the significance remains for the GDP, the distance between the pair countries and the institutional variables in the exporting countries.

[65] All the dummies were added to unity, in order to avoid zero values while deriving the natural logarithm.

Table 5.12.: The impact of GDP, distance, landmass, institutional *variables of the exporting countries* and further complementary variables on exports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-51.0476 (-3.58)	-50.87263 (-3.63)	-55.45756 (-3.91)
GDP in country i	2.329443 (7.09)	2.390419 (7.51)	2.45178 (7.56)
GDP in country j	2.32132 (3.97)	2.283382 (3.95)	2.302363 (3.89)
Landmass of country j	-0.4848667 (-1.93)	-0.4970283 (-2.01)	-0.4278911 (-1.69)
Distance	-5.575068 (-5.25)	-5.59768 (-5.37)	-5.315152 (-4.97)
Institutional variable in country i	3.637215 (3.05)	3.09331 (2.52)	1.963493 (2.07)
Common borders	0.7977753 (0.32)	0.9044068 (0.37)	0.5584883 (0.22)
Common official language	0.9238935 (0.46)	0.5295622 (0.27)	0.961233 (0.47)
Common spoken language	2.34796 (1.22)	2.224976 (1.17)	2.993986 (1.57)
Common dominant religion	2.375906 (1.50)	2.443034 (1.56)	2.375025 (1.47)
Colonial relationship	-4.592283 (-0.60)	-5.099866 (-0.67)	-4.332491 (-0.56)
Common colonizer	3.286137 (1.99)	3.580117 (2.21)	3.880818 (2.34)
Same country in the past	0.6035055 (0.15)	0.6495024 (0.16)	0.7227115 (0.17)
R-squared	0.5568	0.5661	0.5466

Table 5.13.: The impact of GDP, distance, population, institutional *variables of the exporting countries* and further complementary variables on exports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-47.55241 (-3.44)	-47.36355 (-3.49)	-52.3164 (-3.81)
GDP in country i	2.373488 (7.24)	2.437728 (7.66)	2.492596 (7.67)
GDP in country j	2.447669 (3.81)	2.417308 (3.82)	2.386764 (3.67)
Population in country j	-0.7126236 (-1.87)	-0.7341386 (-1.96)	-0.6059327 (-1.58)
Distance	-5.791426 (-5.34)	-5.819023 (-5.48)	-5.485479 (-5.03)
Institutional variable in country i	3.724635 (2.87)	3.149504 (2.55)	1.965488 (2.06)
Common borders	0.5393156 (0.22)	0.6403426 (0.26)	0.3186997 (0.13)
Common official language	1.079696 (0.55)	0.6817053 (0.35)	1.121431 (0.55)
Common spoken language	2.445541 (1.27)	2.32808 (1.23)	3.096914 (1.62)
Common dominant religion	2.261977 (1.43)	2.327642 (1.49)	2.265993 (1.41)
Colonial relationship	-5.53731 (-0.72)	-6.076411 (-0.80)	-5.139977 (-0.66)
Common colonizer	2.769991 (1.67)	3.059051 (1.90)	3.441184 (2.09)
Same country in the past	0.9131196 (0.22)	0.9674887 (0.24)	1.019027 (0.25)
R-squared	0.5560	0.5655	0.5453

5.4.1.4.2. Imports

Having a look at *Table 5.14.* and *Table 5.15.*, we obtain similar results for the imports as the other side of the coin. The GDP in all the member countries and the institutional variables in the exporting countries have a significant positive influence on the trade flows and the distance between the countries has a significant negative influence. Adding the complementary variables to the model reduces the significance of the size of the pair countries. The only additional variable in the model that appears to have a positive significant effect on the trade between COMESA countries pair wise is the common spoken language between them.

Table 5.14.: The impact of GDP, distance, landmass, institutional *variables of the exporting countries* and further complementary variables on imports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-70.38249 (-5.10)	-75.34138 (-5.47)	-71.44055 (-4.96)
GDP in country i	2.14831 (3.77)	2.242991 (3.98)	2.190906 (3.71)
GDP in country j	3.157728 (7.11)	3.53928 (7.77)	3.381934 (7.05)
Landmass of country i	-0.3814769 (-1.11)	-0.3985101 (-1.18)	-0.3661224 (-1.03)
Distance	-5.246463 (-4.68)	-5.839076 (-5.21)	-5.784434 (-4.87)
Institutional variable in country j	5.730216 (3.59)	4.613606 (4.14)	4.270489 (2.53)
Common borders	3.63075 (1.40)	3.112241 (1.23)	2.249968 (0.86)
Common official language	-1.230766 (-0.60)	-1.071217 (-0.53)	-1.097274 (-0.52)
Common spoken language	5.032236 (2.38)	5.36345 (2.57)	5.004277 (2.30)
Common dominant religion	0.6498707 (0.40)	-0.3993645 (-0.25)	-0.0917447 (-0.05)
Colonial relationship	-3.789437 (-0.48)	-3.300599 (-0.42)	-3.274277 (-0.40)
Common colonizer	2.784267 (1.64)	2.956782 (1.77)	3.503907 (2.01)
Same country in the past	-1.363165 (-0.32)	-1.906274 (-0.45)	-2.039242 (-0.45)
R-squared	0.5578	0.5712	0.5356

Table 5.15.: The impact of GDP, distance, population, institutional *variables of the exporting countries* and further complementary variables on imports within COMESA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-67.52521 (-4.95)	-72.21497 (-5.31)	-68.39883 (-4.83)
GDP in country i	1.746273 (2.93)	1.830802 (3.11)	1.791013 (2.91)
GDP in country j	3.197826 (7.19)	3.567491 (7.80)	3.397304 (7.05)
Population country i	-0.1072275 (-0.23)	-0.1220685 (-0.27)	-0.0931163 (-0.20)
Distance	-4.951887 (-4.28)	-5.519001 (-4.78)	-5.44985 (-4.47)
Institutional variable in country j	5.474477 (3.44)	4.434988 (3.99)	3.948334 (2.36)
Common borders	3.411982 (1.31)	2.913828 (1.15)	2.087637 (0.79)
Common official language	-1.530663 (-0.73)	-1.382998 (-0.67)	-1.382508 (-0.64)
Common spoken language	5.823189 (2.81)	6.161405 (3.01)	5.77475 (2.72)
Common dominant religion	0.8019029 (0.49)	-0.1943821 (-0.12)	0.0904495 (0.05)
Colonial relationship	-2.900969 (-0.36)	-2.413031 (-0.31)	-2.431168 (-0.30)
Common colonizer	3.065199 (1.80)	3.235552 (1.93)	3.732564 (2.13)
Same country in the past	-0.5372537 (-0.13)	-1.051581 (-0.25)	-1.118828 (-0.25)
R-squared	0.5535	0.5666	0.5317

5.4.2. Euro-Med

As it is in the case of COMESA, the results of the correlation coefficients between the three institutional variables show high multi-collinearity. This is shown in *Table 5.16.*; the correlation coefficients for all combinations of pairs of the three indicators range between 0.9601 and 0.9748, which is even higher than in the case of COMESA.

Table 5.16.: Correlation coefficient matrix between the institutional variables in Euro-Med countries

	Government effectiveness	Rule of law	Control of corruption
Government effectiveness	1	0.9714	0.9601
Rule of law	0.9714	1	0.9748
Control of corruption	0.9601	0.9748	1

5.4.2.1. Using the minimum number of variables of a gravity model

5.4.2.1.1. Exports

Based on regressions 1, 2 and 3, where the exports of one country of Euro-Med are regressed on the institutional variables in both countries (one at a time in the three different regressions) in addition to the GDP of the two countries and distance between them, the results are shown in *Table 5.17.*; the GDP coefficient of the two partner countries give a positive sign at a five per cent level. The same applies for the coefficients of the institutional variables in the exporting countries. Even the T-statistics of these institutional variables take far higher values than in COMESA. The distance coefficient gives in all cases the expected negative sign and is also significant.

Table 5.17.: The impact of GDP, distance and institutional variables on exports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-26.73784 (-6.63)	-27.37909 (-6.89)	-25.76946 (-6.31)
GDP in country i	0.9417883 (10.07)	0.9376598 (10.42)	0.9069599 (9.71)
GDP in country j	1.074476 (11.04)	1.080175 (10.79)	1.079121 (10.79)
Distance between country i and j	-1.362673 (-5.51)	-1.365542 (-5.55)	-1.384374 (-5.73)
Institutional variable in country i	3.426911 (3.50)	4.033129 (3.64)	3.433159 (3.88)
Institutional variable in country j	-0.5614666 (-0.76)	-0.650373 (-0.79)	-0.531699 (-0.85)
R-squared	0.4651	0.4682	0.4692

5.4.2.1.2. Imports

When the imports of one country of Euro-Med are regressed on the GDP, the institutional variables of this country and its partner, and the distance between them in three separate regressions, according to equations 4, 5, and 6, we obtain the results that are shown in *Table 5.18*. They are quite similar to the results obtained when taking the exports as dependent variables. It is worth mentioning that for the imports and exports in the case of Euro-Med, the T-statistics for the GDP coefficients are much higher than in the case of COMESA.

Table 5.18.: The impact of GDP, distance and institutional variables on imports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-29.31725 (-7.27)	-28.80771 (-7.33)	-28.51348 (-6.83)
GDP in country i	1.103473 (9.16)	1.110294 (9.43)	1.101573 (8.60)
GDP in country j	1.086853 (13.56)	1.050999 (12.99)	1.06385 (13.42)
Distance between country i and j	-1.311676 (-5.73)	-1.306708 (-5.73)	-1.325777 (-5.91)
Institutional variable in country i	-1.570038 (-1.82)	-1.902276 (-1.89)	-1.396735 (-1.63)
Institutional variable in country j	2.781182 (3.51)	3.270775 (3.78)	2.555835 (4.06)
R-squared	0.4218	0.4243	0.4188

Table 5.19. and *Table 5.20.* show the results after dropping the institutional variables of the importing countries. The coefficients are all significant and give the expected signs. In this case, the regressions take the following forms for the exports and imports respectively:

$$log\text{-}exp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}i + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \eta\ log\text{-}inst\text{-}i + \varepsilon \ldots\ldots\ldots 12$$

$$log\text{-}imp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}i + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \eta\ log\text{-}inst\text{-}j + \varepsilon \ldots\ldots\ldots 13$$

Table 5.19.: The impact of GDP, distance, the *institutional variables of exporting countries* on exports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-26.51262 (-6.47)	-27.10538 (-6.69)	-25.30604 (-6.04)
GDP in country i	0.9403609 (10.04)	0.9364206 (10.40)	0.905855 (9.70)
GDP in country j	1.031094 (12.61)	1.030216 (12.67)	1.029558 (12.66)
Distance between country i and j	-1.33302 (-6.03)	-1.33543 (-6.03)	-1.359874 (-6.05)
Institutional variable in country i	3.446276 (3.49)	4.054617 (3.63)	3.448802 (3.87)
R-squared	0.4643	0.4673	0.4684

Table 5.20.: The impact of GDP, distance, the *institutional variables in the exporting countries* on imports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-27.63892 (-7.24)	-27.35308 (-7.21)	-26.51721 (-6.97)
GDP in country i	0.9555437 (11.96)	0.9561125 (11.98)	0.9561022 (11.95)
GDP in country j	1.081213 (13.57)	1.044214 (12.99)	1.057792 (13.48)
Distance between country i and j	-1.280925 (-5.52)	-1.276094 (-5.54)	-1.309633 (-5.75)
Institutional variable in country j	2.822501 (3.48)	3.320926 (3.74)	2.590805 (4.03)
R-squared	0.4167	0.4183	0.4141

5.4.2.2. Using the minimum number of variables of a gravity model in addition to the landmass or population of the importing country

As was done in COMESA, we first start with the exports followed by the imports after adding the size factor of the importing country. But the difference here is that we directly drop the institutional variables of the importing country, since they proved to be insignificant in the very first regressions in Euro-Med.

5.4.2.2.1. Exports

We use again regression 9 and the results are shown in *Table 5.21*. They indicate that the GDP coefficients of both countries remain positive and significant, whereas the landmass coefficients are negative and significant in the three cases.

Table 5.21.: The impact of GDP, distance, landmass and the *institutional variables in the exporting countries* on exports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-26.28133 (-6.46)	-26.87143 (-6.68)	-25.10173 (-6.03)
GDP in country i	0.9427243 (10.11)	0.9392096 (10.48)	0.9093804 (9.76)
GDP in country j	0.9061163 (10.99)	0.9058668 (11.04)	0.9055924 (11.03)
Landmass of country j	-0.2940041 (-4.10)	-0.2925692 (-4.07)	-0.2917036 (-4.09)
Distance between country i and j	-1.39341 (-6.31)	-1.395567 (-6.32)	-1.419533 (-6.33)
Institutional variable in country i	3.403052 (3.51)	3.999225 (3.65)	3.398675 (3.88)
R-squared	0.4785	0.4814	0.4824

Replacing the landmass by the population as an indicator for the size of the importing country does not change the significance of the associated coefficients, as can be seen from *Table 5.22*. This implies that the size of the importing countries in Euro-Med does have a significant impact on the trade between them.

Table 5.22.: The impact of GDP, distance, population and the *institutional variables in exporting countries* on exports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-28.32798 (-6.89)	-28.89696 (-7.10)	-27.1457 (-6.46)
GDP in country i	0.9493616 (10.23)	0.9449376 (10.61)	0.9155793 (9.86)
GDP in country j	0.7548923 (8.71)	0.7543487 (8.74)	0.7543298 (8.73)
Population in country j	-0.5792559 (-5.74)	-0.5785824 (-5.73)	-0.5772961 (-5.76)
Distance between country i and j	-1.417855 (-6.28)	-1.419994 (-6.29)	-1.443668 (-6.30)
Institutional variable in country i	3.351635 (3.54)	3.950569 (3.69)	3.35624 (3.92)
R-squared	0.4929	0.4958	0.4968

5.4.2.2.2. Imports

When applying regression 10 and demonstrating the results in *Table 5.23.* and *Table 5.24.*, we observe that all the coefficients are significant and give the right sign.

Table 5.23.: The impact of GDP, distance, landmass and the *institutional variables of the exporting countries* on imports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-29.4721 (-7.81)	-29.1953 (-7.79)	-28.39543 (-7.56)
GDP in country i	0.8784092 (10.77)	0.8787496 (10.79)	0.8779906 (10.79)
GDP in country j	1.082866 (13.91)	1.045868 (13.34)	1.057744 (13.81)
Landmass of country i	-0.3973433 (-4.48)	-0.3984795 (-4.50)	-0.4024063 (-4.53)
Distance between country i and j	-1.37389 (-6.13)	-1.36863 (-6.16)	-1.401305 (-6.39)
Institutional variable in country j	2.709469 (3.43)	3.206964 (3.71)	2.51441 (4.02)
R-squared	0.4398	0.4414	0.4378

Table 5.24.: The impact of GDP, distance, population and *institutional variables of the exporting countries* on imports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-30.75701 (-8.16)	-30.47784 (-8.14)	-29.67419 (-7.92)
GDP in country i	0.6797058 (7.27)	0.6802294 (7.28)	0.6787578 (7.28)
GDP in country j	1.082285 (14.20)	1.045888 (13.64)	1.05785 (14.17)
Population in country i	-0.6737922 (-6.61)	-0.6738716 (-6.61)	-0.6774728 (-6.64)
Distance between country i and j	-1.363465 (-5.91)	-1.358422 (-5.93)	-1.390759 (-6.15)
Institutional variable in country j	2.727335 (3.49)	3.217356 (3.76)	2.522452 (4.09)
R-squared	0.4567	0.4583	0.4546

5.4.2.3. Adding the complementary variables to the regressions

In a next step, we include all the complementary independent variables that might have an influence on the trade flows between the pair countries in Euro-Med. The regression used is the one already used in COMESA in a similar case (regression 11), using the exports and then the imports as dependent variables respectively.

5.4.2.3.1. Exports

After including all the complementary variables in the model and showing the results in *Table 5.25.* and *Table 5.26.*, we observe that the number of complementary variables that matter for trade between the countries of Euro-Med are more than in COMESA. Moreover, these variables differ in the two Agreements. The main four variables that have a significant effect on trade between the Euro-Med countries are the common official language, the colonial relationship, the common historical colonizer and the common dominant religion. All the other basic variables of the gravity model, in addition to the institutional variables of the exporting countries also give significant results with the expected signs.

Table 5.25.: The impact of GDP, distance, landmass, institutional *variables of the exporting countries* and further complementary variables on exports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-28.85147 (-7.30)	-29.41782 (-7.60)	-27.63806 (-6.91)
GDP in country i	0.9589567 (9.50)	0.9433118 (10.04)	0.9211448 (9.31)
GDP in country j	0.8420667 (9.91)	0.8430346 (9.89)	0.8403534 (9.86)
Landmass of country j	-0.3577601 (-4.46)	-0.3566012 (-4.43)	-0.3567332 (-4.46)
Distance	-1.04423 (-4.32)	-1.035574 (-4.28)	-1.068696 (-4.37)
Institutional variable in country i	3.14576 (3.07)	3.870427 (3.43)	3.198871 (3.50)
Common borders	-1.115134 (-1.08)	-1.110118 (-1.07)	-1.171076 (-1.12)
Common official language	1.828818 (3.30)	1.935005 (3.59)	1.869793 (3.34)
Common spoken language	-0.7713269 (-0.43)	-0.8345655 (-0.47)	-0.7921094 (-0.44)
Common dominant religion	1.656572 (3.59)	1.670371 (3.65)	1.67849 (3.62)
Colonial relationship	1.741627 (2.44)	1.765302 (2.51)	1.685656 (2.34)
Common colonizer	2.74403 (2.97)	2.928195 (3.18)	2.690764 (2.89)
Same country in the past	0.9908104 (0.82)	0.9378818 (0.77)	1.080637 (0.88)
R-squared	0.5071	0.5116	0.5114

Table 5.26.: The impact of GDP, distance, population, institutional *variables of the exporting countries* and further complementary variables on exports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-31.23051 (-7.75)	-31.69777 (-8.02)	-30.05809 (-7.38)
GDP in country i	0.9775923 (9.86)	0.956937 (10.41)	0.936178 (9.64)
GDP in country j	0.6102981 (6.86)	0.6120867 (6.84)	0.6093337 (6.80)
Population in country j	-0.7408708 (-6.46)	-0.7396432 (-6.44)	-0.7403481 (-6.47)
Distance	-1.019422 (-4.27)	-1.010788 (-4.23)	-1.04124 (-4.31)
Institutional variable in country i	2.824396 (2.86)	3.561734 (3.27)	2.947219 (3.34)
Common borders	-1.257342 (-1.23)	-1.250456 (-1.23)	-1.306766 (-1.27)
Common official language	1.839101 (3.52)	1.942901 (3.83)	1.88317 (3.58)
Common spoken language	-1.194306 (-0.67)	-1.240632 (-0.71)	-1.201228 (-0.67)
Common dominant religion	2.148553 (4.45)	2.152444 (4.51)	2.16021 (4.46)
Colonial relationship	1.689925 (2.38)	1.704145 (2.44)	1.630221 (2.27)
Common colonizer	2.875039 (3.04)	3.047969 (3.24)	2.829808 (2.96)
Same country in the past	1.036978 (0.87)	0.9931482 (0.82)	1.125085 (0.93)
R-squared	0.5290	0.5336	0.5335

5.4.2.3.2. Imports

The results of the regressions concerning the imports - after including all the complementary variables - are shown in *Table 5.27.* and *Table 5.28*. In fact, the results resemble and confirm the results obtained when taking the exports as dependent variables.

Table 5.27.: The impact of GDP, distance, landmass, institutional *variables of the exporting countries* and further complementary variables on imports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-30.5907 (-8.19)	-30.47288 (-8.17)	-29.82038 (-7.97)
GDP in country i	0.8409601 (10.29)	0.8453248 (10.33)	0.8400294 (10.34)
GDP in country j	1.089908 (13.33)	1.065005 (12.87)	1.067984 (12.97)
Landmass of country i	-0.4305145 (-4.86)	-0.4286756 (-4.84)	-0.4352693 (-4.87)
Distance	-1.116374 (-5.04)	-1.123518 (-5.07)	-1.13075 (-5.15)
Institutional variable in country j	1.790047 (2.37)	2.208129 (2.65)	1.687853 (2.86)
Common borders	-1.286645 (-1.45)	-1.314892 (-1.47)	-1.33744 (-1.48)
Common official language	3.078263 (2.49)	3.139334 (2.54)	3.054825 (2.45)
Common spoken language	-2.620521 (-1.71)	-2.599781 (-1.70)	-2.658392 (-1.72)
Common dominant religion	1.610428 (3.89)	1.534742 (3.70)	1.661422 (4.04)
Colonial relationship	2.066257 (3.14)	2.044926 (3.10)	2.115813 (3.22)
Common colonizer	1.600259 (1.80)	1.710221 (1.92)	1.71039 (1.94)
Same country in the past	0.9991919 (0.95)	0.9587857 (0.91)	0.9744576 (0.92)
R-squared	0.4713	0.4724	0.4709

Table 5.28.: The impact of GDP, distance, population, institutional *variables of the exporting countries* and further complementary variables on imports within Euro-Med countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-32.13232 (-8.51)	-32.02146 (-8.50)	-31.44191 (-8.33)
GDP in country i	0.5969429 (6.62)	0.601958 (6.67)	0.5950064 (6.62)
GDP in country j	1.088549 (13.75)	1.067153 (13.32)	1.068175 (13.41)
Population in country i	-0.7842106 (-7.67)	-0.7805355 (-7.63)	-0.7891116 (-7.61)
Distance	-1.081164 (-4.87)	-1.087735 (-4.91)	-1.093262 (-4.97)
Institutional variable in country j	1.601345 (2.20)	1.962492 (2.44)	1.519468 (2.66)
Common borders	-1.568582 (-1.80)	-1.592719 (-1.81)	-1.613762 (-1.82)
Common official language	3.188633 (2.58)	3.242693 (2.62)	3.168338 (2.54)
Common spoken language	-3.065399 (-1.99)	-3.045923 (-1.99)	-3.100357 (-2.01)
Common dominant religion	1.907683 (4.67)	1.841767 (4.51)	1.95186 (4.79)
Colonial relationship	2.151206 (3.36)	2.131552 (3.33)	2.197305 (3.45)
Common colonizer	1.918993 (2.08)	2.015245 (2.19)	2.020878 (2.20)
Same country in the past	1.398326 (1.37)	1.360866 (1.33)	1.377006 (1.34)
R-squared	0.4959	0.4967	0.4957

5.4.3. GAFTA

As shown in *Table 5.29.*, the correlation coefficients between the three institutional variables in GAFTA range between 0.9135 and 0.9691, which indicates an obviously high multi-collinearity, requiring the separation of these variables in three different regressions.

Table 5.29.: Correlation coefficient matrix between the institutional variables in GAFTA countries

	Government effectiveness	Rule of law	Control of corruption
Government effectiveness	1	0.9341	0.9135
Rule of law	0.9341	1	0.9691
Control of corruption	0.9135	0.9691	1

5.4.3.1. Using the minimum number of variables of a gravity model

5.4.3.1.1. Exports

Firstly, the exports of one country of GAFTA are regressed on the institutional variables in both countries (one at a time in the three different regressions) in addition to the GDP of the two countries and the distance between them, using regressions 1, 2 and 3).

Table 5.30.: The impact of GDP, distance and institutional variables on exports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-37.21875 (-1.02)	-31.89001 (-0.92)	-19.62417 (-0.55)
GDP in country i	2.74821 (1.42)	2.663006 (1.46)	2.180067 (1.67)
GDP in country j	-0.6554167 (-0.89)	-0.8009012 (-1.05)	-0.8769396 (-1.00)
Distance between country i and j	-1.178323 (-2.17)	-0.9729094 (-2.13)	-0.9559365 (-2.05)
Institutional variable in country i	6.552246 (3.95)	5.860611 (3.78)	6.003474 (3.30)
Institutional variable in country j	4.508506 (2.41)	3.389296 (2.19)	4.220502 (3.41)
R-squared	0.3011	0.2917	0.2363

As shown in *Table 5.30.*, in contrast to COMESA and Euro-Med, the GDP coefficients of partner countries in GAFTA have an obviously insignificant effect on the trade between these countries. In addition, the institutional variables in both the exporting and importing countries of GAFTA significantly influence the trade flows between them. The distance coefficient is negatively significant.

5.4.3.1.2. Imports

Using regressions 4, 5 and 6, and demonstrating the results in *Table 5.31.*, we obtain similar results, but this time, taking the imports as dependent variables to the GDP of pair countries, the distance and the institutional variables.

Table 5.31.: The impact of GDP, distance and institutional variables on imports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-48.46667 (-1.27)	-42.90933 (-1.17)	-33.53861 (-0.88)
GDP in country i	2.479182 (1.80)	2.47438 (1.84)	2.128661 (1.54)
GDP in country j	0.3069074 (0.36)	0.0370005 (0.04)	-0.0472835 (-0.05)
Distance between country i and j	-1.634595 (-2.48)	-1.402226 (-2.18)	-1.398457 (-2.10)
Institutional variable in country i	3.812832 (2.08)	3.619773 (2.15)	3.540224 (3.85)
Institutional variable in country j	4.797885 (2.77)	4.057149 (2.90)	4.924103 (2.45)
R-squared	0.2188	0.2299	0.1937

5.4.3.2. Using the minimum number of variables of a gravity model in addition to the landmass or population of the importing country

In the following step, we add the landmass and population one at a time as a further independent variable and expect the sign of the coefficient to be negative.

5.4.3.2.1. Exports

Once again, regression 7 is used, in order to assess the impact of the institutional variables on the exports of GAFTA countries to each other, taking into account the landmass and population respectively.

The results shown in *Table 5.32.* indicate that the landmass as an indicator for the size of the importing country is insignificant. However, the population in *Table 5.33.* gives significant results.

Table 5.32.: The impact of GDP, distance, landmass and institutional variables on exports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-18.46869 (-0.49)	-16.50983 (-0.45)	2.875156 (0.07)
GDP in country i	2.529713 (1.95)	2.560561 (2.03)	1.967413 (1.55)
GDP in country j	-1.414182 (-1.50)	-1.512772 (-1.53)	-1.841255 (-1.48)
Landmass of country j	0.4987585 (1.20)	0.409634 (1.01)	0.4888499 (1.07)
Distance between country i and j	-1.554832 (-2.50)	-1.216515 (-2.04)	-1.229724 (-4.68)
Institutional variable in country i	6.609275 (4.00)	5.878568 (3.78)	6.05856 (3.31)
Institutional variable in country j	6.343546 (2.63)	4.68308 (2.39)	6.406384 (2.06)
R-squared	0.3107	0.2978	0.2437

Table 5.33.: The impact of GDP, distance, population and institutional variables on exports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-33.18108 (-0.96)	-28.58698 (-0.85)	-9.32299 (-0.28)
GDP in country i	2.262575 (1.86)	2.356238 (1.95)	1.706872 (1.44)
GDP in country j	-1.154649 (-1.60)	-1.355963 (-1.82)	-1.720316 (-1.93)
Population in country j	-1.337881 (-2.61)	-1.160168 (-2.36)	-1.333187 (-2.39)
Distance between country i and j	-1.715004 (-2.99)	-1.332778 (-2.34)	-1.338353 (-2.25)
Institutional variable in country i	6.570782 (4.14)	5.849546 (3.88)	6.011645 (3.37)
Institutional variable in country j	7.489894 (3.50)	5.494567 (3.23)	7.751353 (2.89)
R-squared	0.3435	0.3246	0.2747

5.4.3.2.2. Imports

After taking the imports as an independent variable, the main observation is that the only significant coefficients are the ones of the institutional variables in both countries and the distance between these countries. All the other coefficients prove to be insignificant. Substituting the

population for landmass fails to increase the significance of these variables. The results are demonstrated in *Table 5.34.* and *Table 5.35*.

Table 5.34.: The impact of GDP, distance, landmass and institutional variables on imports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-31.09366 (-0.76)	-23.75076 (-0.61)	-14.33673 (-0.32)
GDP in country i	1.682055 (1.01)	1.599938 (0.99)	1.241757 (0.65)
GDP in country j	0.2966233 (0.35)	0.0249774 (0.03)	-0.0444621 (-0.05)
Landmass of country i	0.2206337 (1.12)	0.2361773 (1.31)	0.2089886 (0.96)
Distance between country i and j	-1.727978 (-2.73)	-1.498397 (-2.40)	-1.479881 (-2.31)
Institutional variable in country i	4.536585 (2.03)	4.295795 (2.17)	4.344645 (2.95)
Institutional variable in country j	4.785534 (2.74)	4.049726 (2.87)	4.882116 (2.39)
R-squared	0.2243	0.2365	0.1982

Table 5.35.: The impact of GDP, distance, population and institutional variables on imports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-46.74153 (-1.30)	-41.21374 (-1.19)	-27.09025 (-0.76)
GDP in country i	2.082618 (1.55)	2.128733 (1.64)	1.502617 (1.03)
GDP in country j	0.308727 (0.36)	0.0370888 (0.04)	-0.0331983 (-0.04)
Population in country i	-0.4954012 (-1.43)	-0.4270479 (-1.47)	-0.5114682 (-1.40)
Distance between country i and j	-1.728435 (-2.70)	-1.478552 (-2.34)	-1.480847 (-2.29)
Institutional variable in country i	4.895619 (2.19)	4.38077 (2.31)	4.857712 (3.32)
Institutional variable in country j	4.82063 (2.83)	4.071789 (2.95)	4.920332 (2.48)
R-squared	0.2292	0.2384	0.2034

5.4.3.3. Adding the complementary variables to the regressions

In the next regressions, we add the rest of the complementary independent variables that might have an influence on the trade flows between the pair countries in GAFTA[66].

5.4.3.3.1. Exports

It seems from *Table 5.36.* - using landmass as an indicator for the country size in the importing countries - that adding the complementary independent variables does not add any significance to the regressions. And apparently, the landmass itself does not matter for the trade between the partner countries in GAFTA. In other words, when talking about GAFTA, the impact of these complementary factors on trade flows between the partner countries is - except for the dummy for a past colonial relationship - insignificant, while the significance remains only for the institutional quality of both the exporting and importing countries and the distance between them.

[66] Due to the similarity in the common dominant religion, the official and spoken language within the Arab countries, these three variables were not included in the regressions concerning GAFTA.

Table 5.36.: The impact of GDP, distance, landmass, institutional variables and further complementary variables on exports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-3.712962 (-0.09)	-11.25243 (-0.28)	15.20996 (0.34)
GDP in country i	2.193774 (1.52)	2.416607 (1.72)	1.725007 (1.20)
GDP in country j	-1.62939 (-1.72)	-1.569646 (-1.58)	-2.076094 (-1.63)
Landmass of country j	0.4861677 (1.06)	0.3474415 (0.77)	0.5027501 (1.03)
Distance	-1.774046 (-2.37)	-1.195225 (-2.93)	-1.432542 (-3.79)
Institutional variable in country i	6.962996 (4.10)	6.010179 (3.77)	6.354158 (3.43)
Institutional variable in country j	6.712562 (2.70)	4.762051 (2.37)	6.929632 (2.17)
Common borders	0.1520045 (0.06)	0.8051164 (0.34)	-0.1063059 (-0.04)
Colonial relationship	6.582805 (2.75)	5.497489 (2.23)	7.745883 (2.77)
Common colonizer	-1.039399 (-0.57)	-0.0346131 (-0.02)	-0.7851437 (-0.42)
Same country in the past	-2.949382 (-1.21)	-2.972778 (-1.12)	-2.700322 (-1.08)
R-squared	0.3257	0.3073	0.2567

When the landmass of the importing countries is replaced by the population, the latter has a significant negative effect on the trade. The results can be seen in *Table 5.37*.

Table 5.37.: The impact of GDP, distance, population, institutional variables and further complementary variables on exports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-24.35112 (-0.55)	-27.99757 (-0.64)	-4.295188 (-0.09)
GDP in country i	2.113694 (1.54)	2.406478 (1.77)	1.65978 (1.21)
GDP in country j	-1.282938 (-1.55)	-1.404466 (-1.64)	-1.825072 (-1.81)
Population in country j	-1.287946 (-2.27)	-1.110666 (-2.01)	-1.314114 (-2.18)
Distance	-1.923502 (-2.87)	-1.34453 (-2.08)	-1.525704 (-2.27)
Institutional variable in country i	6.807396 (4.15)	5.875551 (3.79)	6.186933 (3.44)
Institutional variable in country j	7.72979 (3.51)	5.649411 (3.22)	8.0904 (2.94)
Common borders	-0.2115886 (-0.09)	0.3815734 (0.17)	-0.4402996 (-0.17)
Colonial relationship	6.876721 (2.75)	5.832439 (2.30)	8.148346 (2.78)
Common colonizer	-0.7378057 (-0.40)	0.2997947 (0.16)	-0.4967977 (-0.26)
Same country in the past	-2.636368 (-1.26)	-2.810374 (-1.38)	-2.260607 (-1.02)
R-squared	0.3547	0.3316	0.2852

5.4.3.3.2. Imports

As demonstrated in *Table 5.38.* and *Table 5.39*, whether including the landmass or the population as indicators for the size of the importing country, the only variables that have a significant effect on the trade between GAFTA countries are the institutional variables in the exporting and importing countries, the distance between them and a past colonial relationship.

Table 5.38.: The impact of GDP, distance, landmass, institutional variables and further complementary variables on imports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-54.46772 (-1.06)	-53.43189 (-1.07)	-40.56543 (-0.73)
GDP in country i	2.588143 (1.30)	2.689256 (1.38)	2.25582 (1.01)
GDP in country j	0.5784316 (0.62)	0.3468273 (0.37)	0.2421838 (0.23)
Landmass of country i	0.2015048 (0.99)	0.2128268 (1.13)	0.1874621 (0.81)
Distance	-2.39816 (-3.23)	-2.043794 (-2.83)	-2.12815 (-2.94)
Institutional variable in country i	4.170176 (3.31)	3.804372 (3.47)	3.930636 (1.96)
Institutional variable in country j	5.025189 (2.77)	4.249334 (2.91)	5.120352 (2.40)
Common borders	-3.566033 (-1.38)	-3.198696 (-1.24)	-3.638127 (-1.34)
Colonial relationship	11.59256 (3.90)	11.15168 (3.67)	12.32555 (3.87)
Common colonizer	0.3731139 (0.24)	1.028606 (0.69)	0.4412894 (0.28)
Same country in the past	-4.251286 (-1.33)	-5.186551 (-1.64)	-5.399636 (-1.64)
R-squared	0.2551	0.2641	0.2300

Table 5.39.: The impact of GDP, distance, population, institutional variables and further complementary variables on imports within GAFTA countries

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	-68.32822 (-1.44)	-68.78741 (-1.48)	-52.43646 (-1.07)
GDP in country i	2.984937 (1.73)	3.18426 (1.90)	2.571634 (1.40)
GDP in country j	0.5752745 (0.61)	0.3429648 (0.36)	0.2361823 (0.23)
Population country i	0.3749239 (1.03)	0.329748 (1.07)	0.3654848 (0.95)
Distance	-2.337088 (-3.10)	-1.971415 (-2.69)	-2.069237 (-2.81)
Institutional variable in country i	4.331793 (2.14)	3.790342 (2.01)	4.152821 (2.03)
Institutional variable in country j	5.053881 (2.85)	4.279668 (2.99)	5.151655 (2.47)
Common borders	-3.260808 (-1.28)	-2.904041 (-1.14)	-3.345776 (-1.26)
Colonial relationship	10.77908 (3.37)	10.55521 (3.30)	11.52548 (3.39)
Common colonizer	0.5136774 (0.34)	1.180201 (0.79)	0.5648542 (0.37)
Same country in the past	-5.400012 (-1.70)	-5.434374 (-1.76)	-5.507433 (-1.70)
R-squared	0.2563	0.2638	0.2313

5.4.4. Egypt and the WTO

This section takes a different perspective from the three previous sections, since it deals with Egypt as a common partner country of all the countries of the RTAs of the study in addition to the WTO countries. In order to distinguish between the countries of the RTAs and the rest of the countries, in certain regressions, dummies for belonging to these RTAs are created and included in the regressions.

5.4.4.1. Using the minimum number of variables of a gravity model

In this section, we only include the GDP of the partner country of Egypt, the distance between the two countries and the institutional variables of the partner countries in different regressions one at a time. We do this for the exports and the imports separately.

5.4.4.1.1. Exports

The following regression is used:

$$log\text{-}exp\text{-}ij = \alpha + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \theta\ log\text{-}inst\text{-}j + \varepsilon \quad \ldots\ldots 14$$

assuming that *i* represents Egypt and *j* represents the partner country, i.e. *log-exp-ij* is Egypt's exports to the partner country and *inst-j* is the institutional variable in the partner country.

Table 5.40. shows that the GDP of the partner countries of Egypt has a significant positive impact on the trade with Egypt and the shorter the distance between Egypt and its partner countries the more the trade flows. The institutional quality has a significant positive effect on the trade relations.

Table 5.40.: The impact of GDP, distance and institutional variables on the Egyptian exports to the countries of the RTAs and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.0022368 (0.03)	0.0020326 (0.03)	0.0013339 (0.02)
GDP in the partner country	0.4368208 (6.04)	0.4450949 (6.13)	0.4442202 (6.14)
Distance between the two countries	-0.2015331 (-2.89)	-0.2015117 (-2.87)	-0.2042963 (-2.92)
Institutional variable in the partner country	0.1574182 (2.18)	0.1296016 (2.08)	0.1354222 (2.18)
R-squared	0.2774	0.2701	0.2717

5.4.4.1.2. Imports

The previous regression is run, but after substituting the imports for the exports, in order to assess the other side of the coin:

$$log\text{-}imp\text{-}ij = \alpha + \gamma\ log\text{-}gdp\text{-}j + \delta\ log\text{-}distwces + \theta\ log\text{-}inst\text{-}j + \varepsilon \quad \ldots\ldots 15$$

We obtain similar results for all the variables included in the regressions so far, as can be seen in *Table 5.41*.

Table 5.41.: The impact of GDP, distance and institutional variables on the Egyptian imports from the countries of the RTAs and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.0023905 (0.05)	0.0022021 (0.04)	0.0012711 (0.02)
GDP in the partner country	0.6841807 (12.37)	0.6908063 (12.40)	0.690189 (12.44)
Distance between the two countries	-0.1183521 (-2.22)	-0.1175284 (-2.18)	-0.1213208 (-2.26)
Institutional variable in the partner country	0.1940436 (3.52)	0.1729065 (3.11)	0.1786097 (3.24)
R-squared	0.5771	0.5700	0.5721

5.4.4.2. Adding dummies for the membership in the RTAs

In the following regressions, we simply add dummies for belonging to one of the four RTAs that are included in the study.

5.4.4.2.1. Exports

In the case of Egypt's exports to the other countries, we use the following regression:

$$log\text{-}exp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}j + \gamma\ log\text{-}distwces + \delta\ log\text{-}inst\text{-}j + \eta\ COMESA\text{-}j + \theta\ GAFTA\text{-}j + \lambda\ EURO\text{-}MED\text{-}j + \kappa\ AGHADIR\text{-}j + \varepsilon \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots 16$$

where:
COMESA-j is the dummy for Egypt's partner country's membership in COMESA.
GAFTA-j is the dummy for Egypt's partner country's membership in GAFTA.
EURO-MED-j is the dummy for Egypt's partner country's membership in Euro-Med.
AGHADIR-j is the dummy for Egypt's partner country's membership in Aghadir.

The results are demonstrated in *Table 5.42*. The GDP of the partner country is still positively significant. However, and as was also observed in the three RTAs separately, the institutional variables in the importing countries do not have a significant influence on their trade with Egypt. The distance loses its significance after including these dummies. Moreover, being a member in

Euro-Med increases the possibility for the trading partner to trade more with Egypt as compared to members of other RTAs.

Table 5.42.: The impact of GDP, distance and institutional variables on the Egyptian exports to the countries of the RTAs (including dummies for their membership) and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.000918 (0.01)	0.000677 (0.01)	0.0006545 (0.01)
GDP in the partner country	0.4447747 (6.20	0.4529223 (6.32)	0.4489409 (6.28)
Distance between the two countries	-0.0962809 (-1.08)	-0.0910723 (-1.02)	-0.0947369 (-1.06)
Institutional variable in the partner country	0.0446847 (0.53)	0.0071901 (0.09)	0.0258546 (0.32)
GAFTA	0.0320498 (0.39)	0.0292493 (0.36)	0.0280845 (0.34)
COMESA	-0.0236361 (-0.32)	-0.0298541 (-0.40)	-0.0281117 (-0.38)
Euro-Med	0.2365585 (2.47)	0.2558425 (2.68)	0.2466217 (2.62)
Aghadir	-0.0680681 (-0.87)	-0.0697249 (-0.88)	-0.0672559 (-0.85)
R-squared	0.3093	0.3080	0.3084

5.4.4.2.2. Imports

We use the following regression:

$log\text{-}imp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}j + \gamma\ log\text{-}distwces + \delta\ log\text{-}inst\text{-}j + \eta\ COMESA\text{-}j + \theta\ GAFTA\text{-}j + \lambda\ EURO\text{-}MED\text{-}j + \kappa\ AGHADIR\text{-}j + \varepsilon$ 17

As shown in *Table 5.43.*, the institutional variables in the partner countries of Egypt, when the former are regarded as exporters to Egypt, positively influence the trade flows. The rest of the results are the same like in the case of the Egyptian exports.

Table 5.43.: The impact of GDP, distance and institutional variables on the Egyptian imports from the countries of the RTAs (including dummies for their membership) and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.0012576 (0.02)	0.001038 (0.02)	0.0006534 (0.01)
GDP in the partner country	0.6896267 (12.65)	0.6964007 (12.74)	0.6937006 (12.75)
Distance between the two countries	-0.025826 (-0.38)	-0.0217395 (-0.32)	-0.0270925 (-0.40)
Institutional variable in the partner country	0.1061155 (2.28)	0.0760153 (2.22)	0.0886796 (2.14)
GAFTA	0.0321223 (0.51)	0.0262318 (0.42)	0.0215744 (0.35)
COMESA	0.0054745 (0.10)	0.0003389 (0.01)	-0.002076 (-0.04)
Euro-Med	0.205188 (2.82)	0.2209099 (3.04)	0.215485 (3.00)
Aghadir	-0.093 (-1.56)	-0.0916693 (-1.52)	-0.0877883 (-1.46)
R-squared	0.6011	0.5976	0.5994

5.4.4.3. Adding the size of the importing country

In this section, we only consider Egypt as an exporting country, since what concerns us as an additional control variable is the size of the importing country and its impact on the trade flows. Hence, if we look at Egypt as an importing country, we cannot include its size in the regression, since it will always be a fixed size, apart from which country it trades with. In other words, this variable will be automatically dropped from the regression.

Therefore, we use the following regression:

$$log\text{-}exp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}j + \gamma\ log\text{-}distwces + \delta\ log\text{-}inst\text{-}j + \eta\ COMESA\text{-}j + \Upsilon\ size\text{-}j + \theta\ GAFTA\text{-}j + \lambda\ EURO\text{-}MED\text{-}j + \kappa\ AGHADIR\text{-}j + \varepsilon \quad \ldots\ldots 18$$

Since Egypt is looked at as an exporting country, the impact of the institutional variables of the importing countries is insignificant, like it has been the case in previous regressions concerning the different RTAs. This can be seen in *Table 5.44.* and *Table 5.45*. The distance does not have a significant effect on trade either. In all cases, the membership of an Egyptian trade partner in

Euro-Med matters in contrast to its membership in any of the three other RTAs. When comparing the significance of the landmass and population of the Egyptian partner countries, we easily find out that the landmass does not give significant results, while the population does.

Table 5.44.: The impact of GDP, distance, landmass and institutional variables on the Egyptian exports to the countries of the RTAs (including dummies for their membership) and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.0008087 (0.01)	0.0005772 (0.01)	0.0005501 (0.01)
GDP in the partner country	0.4230916 (5.19)	0.4302952 (5.26)	0.4263554 (5.23)
Distance between the two countries	-0.1015541 (-1.13)	-0.0967454 (-1.08)	-0.1003805 (-1.11)
Landmass	0.0454841 (0.56)	0.0465831 (0.58)	0.0466716 (0.58)
Institutional variable in the partner country	0.0435392 (0.51)	0.0079677 (0.09)	0.026237 (0.32)
GAFTA	0.0294352 (0.36)	0.0266575 (0.32)	0.0254618 (0.31)
COMESA	-0.0242825 (-0.32)	-0.030195 (-0.40)	-0.0285374 (-0.38)
Euro-Med	0.2423317 (2.51)	0.2607558 (2.72)	0.2517512 (2.65)
Aghadir	-0.0680727 (-0.86)	-0.0695997 (-0.88)	-0.0671541 (-0.85)
R-squared	0.3108	0.3096	0.3100

Table 5.45.: The impact of GDP, distance, population and institutional variables on the Egyptian exports to the countries of the RTAs (including dummies for their membership) and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.0004439 (0.01)	0.0002616 (0.00)	0.3610456 (5.10)
GDP in the partner country	0.3623777 (5.13)	0.3683079 (5.20)	0.3610456 (5.10)
Distance between the two countries	-0.079095 (-0.94)	-0.0754368 . (-0.89)	-0.0817938 (-0.97)
Population	-0.2874856 (-4.23)	-0.2873638 (-4.21)	-0.291371 (-4.26)
Institutional variable in the partner country	0.0615084 (0.76)	0.0348257 (0.44)	0.0637265 (0.82)
GAFTA	0.0536818 (0.69)	0.0501397 (0.64)	0.0473345 (0.61)
COMESA	-0.0014085 (-0.02)	-0.0059025 (-0.08)	-0.0041316 (-0.06)
Euro-Med	0.2640281 (2.91)	0.2778379 (3.07)	0.2643404 (2.96)
Aghadir	-0.0776545 (-1.04)	-0.0777037 (-1.04)	-0.0732917 (-0.98)
R-squared	0.3846	0.3829	0.3850

5.4.4.4. Including all the complementary variables in the regressions

In the following we add the other complementary variables that were used for the RTAs separately. But in this regression, we add two dummies that reflect whether the Egyptian partner country is an island or landlocked[67]. We rewrite the regression once again, so that it takes the following form:

$$log\text{-}exp\text{-}ij = \alpha + \beta\ log\text{-}gdp\text{-}j + \gamma\ log\text{-}distwces + \delta\ log\text{-}inst\text{-}j + \eta\ COMESA\text{-}j + \Upsilon\ size\text{-}j + \theta\ GAFTA\text{-}j + \lambda\ EURO\text{-}MED\text{-}j + \kappa\ AGHADIR\text{-}j + \sigma\ log\text{-}(1+isl) + \partial\ log\text{-}(1+landl) + \mu\ log\text{-}(1+contig) + \nu\ log\text{-}(1+comla\text{-}f) + \omega\ log\text{-}(1+comla\text{-}k) + \rho\ log\text{-}(1+comrel) + \pi\ log\text{-}(1+colony) + \varepsilon \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots 19$$

where *isl* is the dummy variable for being an island country and *landl* is a dummy variable for being a landlocked country.

[67] Data on the island and landlocked countries were obtained from the Free Dictionary 'Encyclopedia'.

The same regression is used for the exports and imports (by replacing this dependent variable one at a time). However, the size of the importing country is dropped when considering the Egyptian imports for the reason mentioned above.

In principal, the results in *Table 5.46.*, *Table 5.47.* and *Table 5.48.* do not differ from the previous results. The complementary variables do not add much significance to the regressions; only having a colonial relationship with Egypt matters for trade. Belonging to Euro-Med and acquiring high institutional quality rather positively affect the trade between Egypt and other countries.

Table 5.46.: The impact of GDP, distance, landmass, the institutional variables and the complementary variables on the Egyptian exports to the countries of the RTAs (including dummies for their membership) and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.0011429 (0.02)	0.0009264 (0.01)	0.001074 (0.02)
GDP in the partner country	0.4012459 (5.02)	0.4071633 (5.08)	0.4036747 (5.05)
Distance between the two countries	-0.1551092 (-1.60)	-0.1560445 (-1.61)	-0.1553543 (-1.61)
Landmass	0.0451226 (0.57)	0.046215 (0.58)	0.045815 (0.58)
Institutional variable in the partner country	0.0090856 (0.10)	-0.0228407 (-0.25)	-0.0045994 (-0.05)
Landlocked	-0.099455 (-1.33)	-0.0990591 (-1.33)	-0.0996189 (-1.34)
Island	-0.0185385 (-0.23)	-0.0105621 (-0.13)	-0.0153317 (-0.19)
Common borders	-0.1338026 (-1.74)	-0.1369952 (-1.78)	-0.1353294 (-1.75
Common official language	0.0079581 (0.06)	0.0043827 (0.03)	0.0063733 (0.04)
Common spoken language	0.0552086 (0.68)	0.0592101 (0.73)	0.0567533 (0.70)
Common dominant religion	-0.0924999 (-0.91)	-0.0972688 (-0.96)	-0.0945383 (-0.93)
Colonial relationship	0.2327415 (3.22)	0.2317018 (3.20)	0.2324032 (3.21)
GAFTA	0.037246 (0.27)	0.0408943 (0.30)	0.0388709 (0.28)
COMESA	-0.0450972 (-0.58)	-0.0514619 (-0.66)	-0.0474943 (-0.62)
Euro-Med	0.2042214 (2.05)	0.2195252 (2.21)	0.2107391 (2.15)
Aghadir	-0.0645917 (-0.81)	-0.0672647 (-0.84)	-0.0657006 (-0.82)
R-squared	0.3750	0.3752	0.3749

Table 5.47.: The impact of GDP, distance, population, the institutional variables and the complementary variables on the Egyptian exports to the countries of the RTAs (including dummies for their membership) and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.000892 (0.01)	0.0007423 (0.01)	0.0006448 (0.01)
GDP in the partner country	0.3399964 (4.87)	0.3445768 (4.92)	0.3376527 (4.83)
Distance between the two countries	-0.1144115 (-1.26)	-0.1149416 (-1.26)	-0.1156533 (-1.27)
Population	-0.2800418 (-4.18)	-0.2792148 (-4.15)	-0.2835366 (-4.20)
Institutional variable in the partner country	0.0431821 (0.50)	0.0216991 (0.25)	0.0504457 (0.61)
Landlocked	-0.0814709 (-1.16)	-0.0825156 (-1.17)	-0.0810429 (-1.15)
Island	-0.0542111 (-0.72)	-0.0498201 (-0.66)	-0.0565441 (-0.75)
Common borders	-.01300595 (-1.79)	-0.1322955 (-1.82)	-0.1282394 (-1.77)
Common official language	0.0408746 (0.31)	0.0379444 (0.28)	0.0405491 (0.30)
Common spoken language	0.0577103 (0.76)	0.0602907 (0.79)	0.0583473 (0.77)
Common dominant religion	-0.0946208 (-0.99)	-0.0972819 (-1.02)	-0.0921394 (-0.96)
Colonial relationship	0.2311775 (3.39	0.2311951 (3.39)	0.2319686 (3.40)
GAFTA	0.0400166 (0.31)	0.0403715 (0.31)	0.0334553 (0.26)
COMESA	-0.0219653 (-0.30)	-0.0260867 (-0.35)	-0.0233348 (-0.32)
Euro-Med	0.2232428 (2.39)	0.2333877 (2.50)	0.2212152 (2.41)
Aghadir	-0.0754629 (-1.01)	-0.0757856 (-1.01)	-0.0715378 (-0.95)
R-squared	0.4435	0.4428	0.4440

Table 5.48.: The impact of GDP, distance, population, the institutional variables and the complementary variables on the Egyptian imports from the countries of the RTAs (including dummies for their membership) and WTO

(T-statistics in parenthesis)

	Government effectiveness	Rule of law	Control of corruption
Constant	0.0019889 (0.04)	0.0017933 (0.03)	0.0012693 (0.02)
GDP in the partner country	0.6740043 (12.30)	0.6792752 (12.35)	0.6785178 (12.39)
Distance between the two countries	-0.0273874 (-0.37)	-0.0277415 (-0.37)	-0.0314664 (-0.42)
Institutional variable in the partner country	0.1212075 (2.02)	0.0954257 (4.61)	0.0995836 (2.13)
Landlocked	-0.0800402 (-1.39)	-0.0835537 (-1.44)	-0.0800902 (-1.39)
Island	-0.0673064 (-1.10)	-0.0639844 (-1.04)	-0.0631041 (-1.03)
Common borders	-0.0896281 (-1.51)	-0.0926011 (-1.55)	-0.0895741 (-1.50)
Common official language	0.0143249 (0.13)	0.0098172 (0.09)	0.0089029 (0.08)
Common spoken language	-0.0243459 (-0.39)	-0.0214461 (-0.34)	-0.0187638 (-0.30)
Common dominant religion	-0.0196471 (-0.25)	-.00218492 (-0.28)	-.00196128 (-0.25)
Colonial relationship	0.1197693 (2.14)	0.1210498 (2.16)	0.1207684 (2.16)
GAFTA	0.0450812 (0.43)	0.0418191 (0.40)	0.0344726 (0.32)
COMESA	0.0232285 (0.38)	0.0187429 (0.31)	0.0130864 (0.22)
Euro-Med	.1774833 (2.33)	.1899083 (2.48)	0.189606 (2.52)
Aghadir	-.0971947 (-1.58)	-.0949618 (-1.54)	-0.0911188 (-1.47)
R-squared	0.6241	0.6211	0.6220

5.5. Summary and main findings

The institutional quality - which is the main concern of this chapter - has a positive impact on trade flows, and hence, on the potential implementation of COMESA, Euro-Med and GAFTA. When controlling for other variables that are supposed to influence the trade between partner countries, we find out that in COMESA and Euro-Med, the institutional variables that really matter are the ones existing in the exporting rather than in the importing countries. This means that in a commercial deal between two countries in COMESA or Euro-Med, it is mainly the institutional quality of the exporting country that influences the deal, which in turn indicates that

institutional factors affecting the quality, quantity and timeliness of providing the goods are more important than the financial settlements occurring within this deal. However, in GAFTA, the institutional variables in both the exporting and importing countries play a significant role in the trade volume. In the trade between Egypt on one hand and all the WTO countries and the countries of the four RTAs of the study on the other, the institutional variables in these partner countries play a positive significant role as well.

The GDP in the exporting and importing countries within COMESA and Euro-Med has a positive impact on the trade flows between the countries of both RTAs. It also plays a positive role in trade between Egypt and its partner countries of the WTO and the four RTAs of this study collectively. However, it seems that in GAFTA the GDP does not have any significant role in the trade between the member countries. The geographical distance is a factor that negatively affects the trade flows between countries of the RTAs on a general basis. However, when analyzing the trade between Egypt, on one hand, and its WTO partner countries and the countries of the four RTAs collectively, on the other, we find out - especially when including the other control variables in the regression - that there are some factors other than the geographical distance that influence the trade. Two other factors highly related to the geographical distance which are also included in the regressions concerning the trade between Egypt and the WTO countries are the dummies that categorize the partner country for being landlocked or an island. These two variables also proved to be insignificant. The size of the importing country measured in terms of population and landmass plays the greatest role in trade in the Euro-Med area as compared to COMESA and GAFTA.

The rest of the complementary control variables differ in their importance and significance among the different RTAs. For example, whereas the only additional control variable that in most cases significantly affects the trade between partner countries of COMESA is the common spoken language, the officially used language is an important factor that positively affects trade between the Euro-Med countries. Within the latter RTA the common dominant religion, the past colonial relationship and the existence of a common colonizer in the past also play a significant positive role in trade between the partner countries. As for GAFTA, it would be expected that the similar dominant religion and official as well as spoken language would have a great positive effect on trade between the partner countries. However, these variables are dropped from the model, due to the fact that their dummies would take the same value in the regressions. The

colonial relationship in the past significantly affects the trade within these countries, as was noticed after running the regressions.

Last but not least, being a member in Euro-Med increases the possibility for the trading partner to trade more with Egypt as compared to members of other RTAs.

CHAPTER 6

Problems of the Implementation of the Egyptian RTAs resulting from Overlapping Rules of Origin

6.1. Introduction

The concept of RoO has become increasingly important for international trade. In fact, the implementation of preferential trade regimes and the application of trade measures such as import bans and prohibitions, discriminatory restrictions, tariff quotas, among others, depend to a great extent on the application of RoO.

Various studies[68] mentioned the Spaghetti Bowl problem of *Bhagwati* (1996) concerning the overlapping RoO that might result from the involvement of one country in several RTAs. However, none of these studies - to the knowledge of the researcher - tackled the problem on commodity level with a thorough analysis that identifies the problems of implementing the overlapping RoO and the expected impact of the latter on the flows of these commodities among the countries of the RTAs.

The contribution of this study would therefore be tracing the detailed production process of the twenty most important Egyptian exports to the countries of the different RTAs, taking into account the necessary inputs and raw materials used in the production. We detect to what extent applying the RoO of the three RTAs could constrain the potential exportation of these goods and whether there would be an observable conflict between the three RTAs in this regard.

We focus on the Egyptian exports rather than imports, due to the fact that - from any country's point of view - usually the exports are the goods that face problems while crossing the boarders when it comes to RoO. If a country considers some certain imports extremely important, it could on purpose be less strict with applying the RoO. But exporting a commodity and facilitating its access to the market of another country is more complex, if there is an agreement on the RoO.

[68] See for example Schiff and Winters (2003) and Palmeter (1993).

Moreover, promoting the exports is important for the Egyptian Balance of Payments which is already suffering from a deficit with many countries of the world.

6.2. Empirical work

The literature provides different ways of observing the impact of being part of different RTAs with their RoO on the economy in general. Among others, *Duttagupta and Panagariya* (2001) introduce a general equilibrium model of trade to analyze the economic and political characteristics of the initial equilibrium, based on a nondiscriminatory tariff. They incorporate intermediate inputs into the analysis and derive the implications of the RoO for the political feasibility of RTAs. Then they discuss the welfare implications of RTAs in the presence of intermediate inputs and RoO. Their model has three final goods and an intermediate input used in the production of one of the final goods. A key welfare result they derive is that, in general, the RoO may lower or raise the joint welfare of the RTA. On the one hand, a RoO diverts trade in the intermediate input by substituting within-union supply for outside-union supply. On the other, it can undo trade diversion in the final good using the input. Thus, the net effect is ambiguous. *Krishna* (2004) developed a way of looking at the effect of conditional policies, such as RoO, in general equilibrium setting under the assumption of perfect competition. His study looks at the effects of such restrictions on the factor price frontier and shows how this can be derived quite simply for certain kinds of RoO. It is shown that when RoO are set at ex ante binding levels, they need not be binding ex post. In general, the difficulty of validating general equilibrium models to examine their ability to replicate reality forms a main drawback.

Krueger (1993) measures the impact of RoO of an RTA on the profitability in a member country of this RTA. She measures the profitability of Mexico when it is subject to certain RoO agreed upon with the USA in the frame of NAFTA. In a study by *Cadot et al.* (2005) they run a full analysis of the market-access implications of RTAs, taking into account both tariff preferences and compliance costs mainly related to RoO. They also apply this on NAFTA by estimating the combined effects of NAFTA's tariff preference and RoO on the direction of Mexican exports.

A comparative approach was taken by *Schiff and Winters* (2003), when they were examining the RoO of NAFTA and their impact on Japanese investment plans. Although trade between Canada, Mexico, and the USA had a high regional content even before the three countries formed NAFTA, the latter's RoO have serious protective effects in certain sectors, shifting their trade and

investment patterns from lower-cost to higher-cost sources. Most clothing produced in Mexico gains tariff-free access to the North American market only if its inputs are virtually 100 percent sourced in North America. In the automobile industry, the requirement of 62.5 percent local content has induced Japanese automobile manufacturers with plants in Canada to produce components in the USA rather than use cheaper components from Japan. The RoO also require the tubes in color televisions to be of North American origin if the televisions are to receive duty-free treatment. Since the inception of NAFTA in 1994, five television tube factories have been planned or established in North America by Japanese or Korean firms, probably at the expense of expansion in Southeast Asia.

The same approach has also been used by *Palmeter* (1993) when he assessed the role of NAFTA RoO in creating trade obstacles. To Chile's dismay, the rules for tomato ketchup changed when the Canada-USA Free Trade Agreement (CUSFTA) evolved into NAFTA. Under CUSFTA, ketchup processed from imported tomato paste qualified for duty-free treatment in internal trade, but under NAFTA rules the tomato paste itself must be produced within a NAFTA member in order for the ketchup to qualify for free entry. In 1992 Chile was the leading foreign supplier of tomato paste to the USA, and the ketchup produced from the tomato paste enjoyed free entry under CUSFTA. Mexico and Chile together accounted for over 80 percent of USA tomato paste imports, in roughly equal quantities. Under NAFTA, ketchup made out of Chilean paste can no longer circulate duty-free, and Chile's share dropped to 5 percent, while Mexico's share rose to 75 percent. Now, if we assume that the USA and Chile had signed a separate FTA where duty free trade is granted, implementing this FTA would to a certain extent be hindered, if the USA were to comply with the rules of NAFTA.

6.3. The Harmonized Commodity Coding System

The analysis used in this chapter is based on the Harmonized Commodity Coding System (HS). It is intended to serve as a universally accepted classification system for goods, so that countries can administer customs programs and collect trade data on exports and imports. It was designed to replace the local systems used by countries, allowing them to have a common classification system by which to track trade and apply tariffs[69].

[69] Canada-Saskatchewan Business Service Center –Business InfoSource

This system uses a 6-digit code to identify basic commodities. Each country is allowed to add additional digits for statistical purposes.

The HS was developed under the auspices of the Customs Cooperation Council (CCC) now known as the World Customs Organization (WCO). It is a commodity classification system in which articles are grouped largely according to the nature of the materials of which they are made, as has been traditional in customs nomenclatures. The HS contains approximately 5000 headings and subheadings covering all articles in trade. These provisions are organized in 96 chapters arranged in 21 sections which - along with the interpretative and legal notes to the chapters and sections - form the legal text of the HS.

The 6-digit code consists of three parts. The first two digits identify the chapter the goods are classified in. The next two digits identify groupings within that chapter and the last two digits identify sub-groupings within this grouping. This is also the last point at which different countries' classification codes are identical. After this point countries can add more digits to make the HS classification numbers even more specific. This study uses a 4-digit code as it is used in most of the RTAs that Egypt is part of.

6.4. Egypt as a member of three RTAs

If we assume that no RoO exist in any of the RTAs, the Egyptian producers would theoretically be capable of producing as much as they can and export to the countries they wish, without giving lots of consideration to the origin of their inputs. But if they are used to export to a certain country that now belongs to one of the RTAs and they import the inputs from a country that belongs to another, then they are put in a situation where they have to be more selective either in choosing the country they export to or the country that provides them with the inputs of the product. Therefore, if the RoO of the RTAs contradict with each other, this might discourage the production and exportation of certain products, which could at the end negatively affect the total exports of the country.

We start our analysis with Euro-Med, which has the clearest, most detailed and best defined RoO, followed by COMESA and GAFTA, respectively.

6.4.1. Euro-Med

General requirements of the Euro-Med RoO:

"1. For the purpose of implementing this Agreement, the following products shall be considered as originating in the Community:

(i) Products wholly obtained in the Community;

(ii) Products obtained in the Community incorporating materials which have not been wholly obtained there, provided that such materials have undergone sufficient working or processing in the Community;

2. For the purpose of implementing this Agreement, the following products shall be considered as originating in Egypt:

(i) Products wholly obtained in Egypt;

(ii) Products obtained in Egypt incorporating materials which have not been wholly obtained there, provided that such materials have undergone sufficient working or processing in Egypt.

Meaning of wholly obtained products:

1. The following shall be considered as wholly obtained in the Community or Egypt:
(a) Mineral products extracted from their soil or from their seabed;
(b) Vegetable products harvested there;
(c) Live animals born and raised there;
(d) Products from live animals raised there;
(e) Products obtained by hunting or fishing conducted there;
(f) Products of sea fishing and other products taken from the sea outside the territorial waters of the Community or Egypt by their vessels;
(g) Products made aboard their factory ships exclusively from products referred to in subparagraph (f);
(h) Used articles collected there fit only for the recovery of raw materials;

(i) Waste and scrap resulting from manufacturing operations conducted there;
(j) Products extracted from marine soil or subsoil outside their territorial waters provided that they have sole rights to work that soil or subsoil;
(k) Goods produced there exclusively from the products specified in subparagraphs (a) to (j).

Meaning of sufficient working and processing:

Products which are not wholly obtained are considered to be sufficiently worked or processed when certain conditions are fulfilled. These conditions differ from each single product to the other according to the different headings as will be discussed in detail in the analysis run later in this section. It should be noted that if a product, which has acquired originating status by fulfilling these conditions is used in the manufacture of another product, the conditions applicable to the product in which it is incorporated do not apply to it, and no account shall be taken of the non-originating materials which may have been used in its manufacture.

However, materials which, according to these conditions should not be used in the manufacture of a product may nevertheless be used, provided that:
(a) their total value does not exceed 10 percent of the ex-works price of the product;
(b) any of the percentages given in the list for the maximum value of non-originating materials are not exceeded through the application of this paragraph.

Meaning of insufficient working and processing:

The following operations shall be considered as insufficient working or processing to confer the status of originating products, whether or not the requirements of Article 6 are satisfied:

(a) operations to ensure the preservation of products in good condition during transport and storage (ventilation, spreading out, drying, chilling, placing in salt, sulphur dioxide or other aqueous solutions, removal of damaged parts, and similar operations);
(b) simple operations consisting of removal of dust, sifting or screening, sorting, classifying, matching (including the making-up of sets of articles), washing, painting, cutting up;
(c) (i) changes of packaging and breaking up and assembly of packages;
(ii) simple placing in bottles, flasks, bags, cases, boxes, fixing on cards or boards, etc., and all other simple packaging operations;

(d) affixing marks, labels and other like distinguishing signs on products or their packaging;
(e) simple mixing of products, whether or not of different kinds, where one or more components of the mixtures do not meet the conditions laid down in this Protocol to enable them to be considered as originating in the Community or Egypt;
(f) simple assembly of parts to constitute a complete product;
(g) a combination of two or more operations specified in subparagraphs (a) to (f);
(h) slaughter of animals.

Bilateral cumulation of origin

1. Materials originating in the Community shall be considered as materials originating in Egypt when incorporated into a product obtained there. It shall not be necessary that such materials have undergone sufficient working or processing.

2. Materials originating in Egypt shall be considered as materials originating in the Community when incorporated into a product obtained there. It shall not be necessary that such materials have undergone sufficient working or processing.

Diagonal cumulation of origin

Materials originating in the other Mediterranean countries of Euro-Med *within the meaning of the Agreements between the Community and Egypt and these countries* shall be considered as originating in the Community or Egypt when incorporated into a product obtained there. It shall not be necessary that such materials have undergone sufficient working or processing.

The cumulation provided here may only be applied where the materials used have acquired the status of originating products by an application of RoO identical to the RoO in the Protocol between the Community and Egypt. Both parties shall provide each other, through the European Commission with details of Agreements and their corresponding RoO which have been concluded with the other Mediterranean countries of the Agreement. Once these requirements have been fulfilled, and a date for the entry into force of these provisions has been agreed, each party shall fulfill its own notification and information obligations."

In an annex attached to the Protocol for RoO of the Agreement, there is a list that sets out the conditions required for all products to be considered as sufficiently worked or processed within the meaning of the Protocol.

The twenty most significant Egyptian exports to the EU and their RoO[70]

HS 2710: Petroleum oils and oils obtained from bituminous materials, other than crude; preparations not elsewhere specified or included, containing by weight 70 percent or more of petroleum oils or of oils obtained from bituminous materials, these oils being the basic constituents of the preparations ($142,699,880 in 2003):

Manufacturing should contain operations of refining or other operations in which all the non-originating materials used are classified within a heading other than that of the product. However, materials classified within the same heading may be used provided their value does not exceed 50 percent of the final factory price of the product.

The raw oil itself is obtained from Egypt ($92,265,929 was the local production in 2003) and the refining process exists in Egypt as well. The local material used in the process is far more than 50 percent of the final factory price of the product[71]. Hence, exporting the product that belongs to this tariff heading to the Community shall not be affected by the RoO of the Agreement.

HS 5205: Yarn and thread of cotton ($75,001,638 in 2003):

The working or processing carried out on non-originating materials that confers originating status is manufacturing from raw silk (HS 5007) or silk waste (HS 5003) carded or combed or otherwise prepared for spinning.

Egypt imports raw silk mainly from South Korea ($5,934 in 2003) and imports silk waste mainly from China ($56,225 in 2003) and Saudi Arabia ($11,136 in 2003). Although these three countries are not members of Euro-Med, this shall not constraint exporting the final good to the

[70] In the following analysis, where the sources are not indicated, the main source is the Central Authority for Public Mobilization and Statistics (CAPMAS 2004).

[71] This information is based on interviews with officials in the Ministry of Industry and Foreign Trade.

Community, since the manufacturing process of these materials fully takes place in Egypt till the final product comes out.

HS 5201: Raw cotton ($74,666,395 in 2003):

The product must be wholly obtained, in order to confer origin. This condition is fulfilled in the Egyptian raw cotton (1,000,000 bales local production in 2003)[72].

HS 7601: Unwrought aluminum ($72,844,186 in 2003):

In the case of non-originating materials, the required process is the manufacturing of these materials by thermal or electrolytic treatment from unalloyed aluminum or waste and scrap of aluminum. This process indeed takes place in the *Egyptalum* aluminum plant situated at Nag Hammady[73]. Also in this case, the RoO are not violated.

HS 2523: Cement Clinkers ($53,999,591 in 2003):

The process required is the manufacturing in which the value of all the non-originating materials used does not exceed 50 percent of the final factory price of the product.

Limestone (HS 2521) is the most common material used although chalk (HS 2509) and calcium carbonate (HS 2836) can also be used in the production process. The importance of limestone is that it makes up around 80 percent of the approximately 1.65 tons of raw material input needed to

[72] The Nation Master Data Base

[73] Egyptalum's Aluminum plant is situated in Nag Hammady, some 100 kilometers north from Luxor (Upper-Egypt) . Serveral factors were taken into consideration in the selection of Nag Hammady as the site of the Egypt Aluminum complex. One was its proximty to the High Dam and to the Nag Hammady electrical substation 326 km. from Aswan . Another was its easy access to the port of Safaga, 210 km . And third important factor was the availability of skilled and semi-skilled labor in the area. In addition to the foregoing, there was a social consideration : an attempt to raise the standard of living of this part of upper Egypt Hence the choice of the location of Nag Hammady in 1972, and the construction of the first two pot lines which took place in October 1975 and reached 5 pot lines in July 1983.

make one ton of clinker. Approximately 50 percent by weight of the lime-bearing material is lost as carbon dioxide in the manufacturing process (Cement Industry Federation).

Limestone exists in the Egyptian ground in generous amounts (15 Million Cubic Meters in 2003). However, Egypt also imports it from China ($350,968 in 2003) and Saudi Arabia ($342,000 in 2003). Therefore, in order to cope with the RoO of the Agreement, Egypt needs to rely more on its own inputs of limestone. As for the chalk, it is mainly imported from Germany ($47,139 in 2003), which is a member of the Agreement. Last but not least, Egypt imports large amounts of calcium carbonate from other members of the Agreement, such as Italy ($218,607 in 2003), Turkey ($185,173 in 2003), France ($98,923 in 2003), Spain ($54,641 in 2003), Germany ($23,744 in 2003), UK ($12,484 in2003) and Belgium ($10,131 in 2003). Therefore, obeying the Euro-Med RoO is not a hard task concerning this product.

HS 2803: Carbon ($50,211,330 in 2003):

In order for the final product to confer origin, the non-originating materials used shall be classified within a heading other than that of the product. However, materials classified within the same heading may be used provided their value does not exceed 20 percent of the final factory price of the product.

Carbon in Egypt is derived from graphite (HS 2504) (Jefferson Lab Data Base). The latter is mainly imported from China ($680,294 in 2003), which is not member of the Agreement. However, since the headings of graphite and carbon are different, and the rest of the production process is done in Egypt, the export of carbon to the Community shall not be negatively affected by the RoO of the Agreement.

HS 0701: Potatoes ($45,548,270 in 2003):

The necessary working and processing requires manufacturing in which all the materials used must be wholly obtained. The local production of potatoes covers the exports abroad[74] and therefore this does not represent a problem in relation with the RoO of the Agreement.

[74] This information has been obtained from officials in the Ministry of Industry and Foreign Affaires and not from the official website.

HS 4205: Leather articles ($28,152,694 in 2003):

The process required is the manufacturing from non-originating leather inputs of headings (HS 4104 to 4107) (leather without hair or wool).

All the following process is undertaken in Egypt: Warehousing and sorting in controlled cool rooms, soaking the skin, de-fleshing, liming (adding lime and sulphur compound), bating, pickling, tanning, splitting, skiving, sorting to various quality levels, neutralizing, filling out, dyeing and greasing, drying, staking, finishing, quality control, dispatching[75]. This indicates that if Egypt uses the inputs that belong to the above mentioned headings, there should be no problem concerning the RoO of the Agreement. Nevertheless, Egyptian leather factories use leather inputs that belong to headings other than these headings. For example, they sometimes rely on leather inputs of headings HS 4109 and HS 4111. If we have a look at the first heading, we find that its leather inputs are mainly imported from member countries, such as France ($368,700 in 2003), Italy ($196,092 in 2003) and Spain ($118,932 in 2003). Consequently, the category of product relying on leather inputs of this heading should not face enormous problems when entering the EU markets. As for the leather inputs that belong to the second heading, they are mainly imported from China ($18,566 in 2003), USA ($6,973in 2003), the Netherlands ($3,692 in 2003), Italy ($3,084 in 2003) and Sweden ($632 in 2003). Therefore, the Egyptian leather factories should in this case rather rely on inputs from member countries or rely on local inputs, in order to fulfill the RoO and benefit from the preferential treatment of the expected FTA with EU countries. However, the volume of imports of this heading (HS 4111) is quite modest as compared to the imports of heading (HS4109). Hence, all in all, the leather exports should not be affected by the Euro-Med RoO.

HS 0712: Dried onions ($22,521,954 in 2003):

The necessary working and processing requires manufacturing in which all the materials used must be wholly obtained.

[75] These information were obtained by the researcher while running an interview in a leather factory located in Old-Cairo.

Egypt imports the fresh onions - in addition to the local production ($9,987,367 in 2003) - from Australia ($884,658 in 2003), which is not member of Euro-Med. Therefore, this could to some extent dampen the export volume to the Community.

HS 6109: Knitted T-Shirts of cotton ($20,245,421 in 2003):

Manufacturing should be starting from yarn, in order to confer origin. According to the Egyptian producers interviewed in the frame of this study, this condition is fulfilled in most of the Egyptian production of T-Shirts and therefore should represent no problem in exporting to the Community.

HS 1703: Molasses resulting from the extraction or refining of cane sugar, flavored or colored ($18,449,580 in 2003):

The necessary working and processing requires manufacturing in which the value of any non-originating materials of sugars and sugar confectionery (HS 1700) does not exceed 30 percent of the final factory price of the product.

Egypt produces most of its own raw sugar ($7,235,896 in 2003) and the imported sugar originates mainly from Turkey ($528,003 in 2003), Spain ($304,798 in 2003), Germany ($236,277 in 2003) and Ireland ($43,183 in 2003), which are all members of Euro-Med. Applying the RoO should therefore make no observable change in the export volume of this product.

HS 2515: Marble ($14,939,362 in 2003):

The process required is the manufacturing in which all the non-originating materials used are classified within a heading other than that of the product.

The main material used in producing marble is the rock, which can be massively found in the Galala mountain, 75 kilometers northeast of Cairo near Suez (The Business Today Data Base)[76] . As for the complementary machines used for that purpose, they are mainly imported from

[76] The majority of the quarries use explosives to extract rock from the mountain, a method largely abandoned abroad that leads to a great deal of waste and sometime causes damage to the product itself. Very few companies are able to afford the price of machinery (rock cutters and drillers) that treats the rock existing in the mountain.

member countries of the Agreement; rock drillers (HS 8207) are imported from Germany ($80,727 in 2003), Sweden ($76,300 in 2003), Ireland ($12,978 in 2003), France ($7,534 in 2003), Italy ($4,424 in 2003) and the UK ($1,849 in 2003). Rock cutters (HS 8430) are imported from Germany ($84,034 in 2003) and Belgium ($65,129 in 2003). Other member countries of the Agreement exported to Egypt rock cutters worth of $427,094 in 2003. Hence, the main material used for producing marble is fully obtained in Egypt and the machines used are mainly imported from member countries of the Agreement. Accordingly, the RoO are not expected to be a constraint on the way of exporting Egyptian marble to the EU countries.

HS 2712: Mineral waxes ($14,103,765 in 2003):

The required process is any operations of refining or other operations in which all the non-originating materials used are classified within a heading other than that of the product.

These waxes are a mixture of hydrocarbons and occur in association with petroleum; some varieties are used in making ceresin and candles. Hydrocarbon is an organic compound containing only carbon (HS 3801) and hydrogen (HS 2804) (The Free Dictionary by Farlex). Hence, the only two materials used are classified within a heading other than that of the product. Moreover, the hydrogen is mainly imported from the countries of the EU ($460,200 in 2003), whereas the carbon is mainly imported from Norway ($250,710 in 2003), China ($141,898 in 2003) and New Zealand ($95,424 in 2003). However, since the condition of the different heading is fulfilled, then this product should not face problems in continuing to enter the EU markets.

HS 3926: Plastic articles ($12,984,022 in 2003):

The process required is the manufacturing in which the value of all the non-originating materials used does not exceed 50 percent of the final factory price of the product.

Oil and natural gas are the major raw materials used to manufacture plastics. The plastics production process begins by heating components of crude oil or natural gas in a "cracking process." This process results in the conversion of these components into hydrocarbon monomers such as ethylene and propylene. Further processing leads to a wider range of monomers, which

are then chemically bonded into chains called polymers. The different combinations of monomers yield plastics with a wide range of properties and characteristics[77].

The plastics industry in Egypt is growing and modernizing steadily. In 2003, Egypt consumed approximately 1.2 million tons of plastic materials and resins worth $750 million, and this rate of consumption is expected to grow at 6 percent annually for the next 5 years at least. However, Egypt's plastics market is supplied 65 percent from imports and 35 percent from domestic sources (Canada's Business and Consumer Site). The main suppliers of plastic inputs (HS 3916) are Germany ($1,179,683 in 2003), China ($1,130,172 in 2003), Turkey ($889,731 in 2003), Italy ($888,802 in 2003), USA ($782,370 in 2003), Belgium ($159,846 in 2003), Sweden ($144,521 in 2003), Taiwan ($124,781 in 2003), India ($117,815 in 2003) and France ($117,120 in 2003).

Both, the crude oil ($22,265,929 local production of 2003) and natural gas ($4,337,389 was the local production of 2003) are available locally. Thus, there should be no problem concerning the local production of plastic articles where local inputs are used. However, the local production of plastic articles that relies on imported inputs could be problematic in the case where the exporting countries are non-members of the Agreement, such as China, USA, Taiwan or India. If Egypt is to fulfill the RoO of the Agreement, it should consider this matter and rely more on its local inputs or inputs from member countries of the Agreement.

HS 1006: Polished rice ($10,041,738 in 2003):

The process required is the manufacturing in which all the materials used must be wholly obtained.

Beside the locally harvested rice in Egypt (3,900 thousand metric tons in 2003)[78], the latter imports it also from India ($102,986 in 2003), Pakistan ($81,412 in 2003), Switzerland ($74,638 in 2003), Australia ($15,404 in 2003), and Ghana ($1,896 in 2003). All these countries are not members in the Agreement. Thus, if Egypt plans to sustain or increase its exports of polished rice to the EU-countries, it needs to rely more on its locally obtained rice.

[77] These information were obtained by interviewing local producers in Egypt.

[78] The Nation Master Data Base.

HS 7202: Steel ($8,510,117 in 2003):

The required process is the manufacturing in which all the non-originating materials used are classified within a heading other than that of the product.

Iron (HS 7216), coke (HS 2713), limestone (HS 2521) and dolomite (HS 2518) are the major raw materials used in producing steel[79]. All these raw materials are obtained from Egyptian ground (Iron: 2399000 Tons in 2003, Coke: 9.4 Million Cubic Meter in 2003, Limestone: 15 Million Cubic Meters in 2003, Dolomite: 1508000 Tons in 2003). Nevertheless, Egypt additionally imports iron from Libya ($122,529 in 2003) and the European Economic Community ($86,245 in 2003), coke from Kuwait ($2,144,174 in 2003), Australia ($949,253 in 2003) and Italy ($4,179 in 2003), limestone from China ($10,968 in 2003) and Saudi Arabia ($342 in 2003), and it imports dolomite from France ($55,132 in 2003) and Norway ($6,457 in 2003). Many of these countries are not members of the Agreement, but at the same time, the headings of the materials are all different from the final product. Hence, this does not violate the RoO of the Agreement.

HS 9403: Furniture ($5,613,826 in 2003):

The process required is the manufacturing in which all the non-originating materials used are classified within a heading other than that of the product.

The processes used in the manufacture of furniture include the cutting, bending, molding, laminating, and assembly of such materials as wood (HS 4403), iron (HS 7216), glass (HS 3207), plastics (HS 3916) and rattan (HS 1401) (USA Census Bureau). From the headings of these materials we can see that they belong to different classifications from the final product. Moreover, most of the materials are either obtained locally or are imported from member countries of the Agreement. For example, Egypt imports wood mainly from Finland ($5,825,067 in 2003), Estonia ($1,146,971 in 2003), Latvia ($ 170,116 in 2003), Croatia ($98,151in 2003), Sweden ($68,891 in 2003) and Belgium ($ 33,843 in 2003). Egypt also highly relies on its imports of iron on the EU ($86,245 in 2003). The glass is produced locally and imported from Spain ($3,379,110 in 2003), Italy ($1,853,232 in 2003), United Kingdom ($650,628 in 2003), Germany ($575,646 in 2003), Belgium ($118,374 in 2003) and the Netherlands ($33,845 in 2003).

[79] The information is based on interviews with local producers.

Plastics are mainly imported from Germany ($1,179,683 in 2003), Turkey ($889,731 in 2003), Italy ($888,802 in 2003), Belgium ($159,846 in 2003) and Sweden ($144,521 in 2003). The only material that Egypt imports from countries that are non-members of the Agreement is rattan, which it mainly imports from Singapore ($ 825,470 in 2003), China ($11,896 in 2003) and Indonesia ($2,158 in 2003). However, this material belongs to a heading completely different from the heading of the final product. Therefore, this product is not expected to face problems concerning the RoO when entering the EU countries.

HS 6910: Ceramic products ($3,665,720 in 2003):

The required process is a manufacturing in which all the non-originating materials used are classified within a heading other than that of the product. According to the local producers, the raw material that ceramic is obtained of is plastic clay body[80]. This material is not imported from other countries but is obtained in the Egyptian ground ($11,956,415 is the local production of 2003). Therefore, ceramic products are fulfilling the RoO of Euro-Med.

HS: 2714: Bitumen ($2,443,352 in 2003):

The process required is operations of refining and/or one or more specific process (es) or other operations in which all the non-originating materials used are classified within a heading other than that of the product.

Bitumen is a naturally-occurring, inflammable organic matter formed in the process of petroleum (HS 2709) generation. Bitumen also includes mineral wax (HS 2712) (School Science Website). Both products originate in Egypt. Hence, Bitumen is not expected to face problems in entering the EU markets, due to the RoO of the Agreement.

[80] This information is also obtainable in the Glendale Community College District (California) and Maricopa Community Colleges (Arizona) and the Thai Ceramics Online websites.

HS 1512: Vegetable oils and their fractions ($2,401,569 in 2003):

The process required is the manufacturing in which all the non-originating materials used are classified within a heading other than that of the product.

The main four sorts of vegetable oils that Egypt produces and exports to the EU countries are the olive oil, the maize oil, sunflower oil and soy bean oil. Sunflower isd planted and harvested locally[81]. Egypt relies on local production of olives[82] and maize (6,400,000 tons was the local production in 2003)[83] as well, but part of these two plants is imported from abroad; maize (HS 2001) is mainly imported from Brazil ($2,171,370 in 2003), Russia ($1,061,752 in 2003), the USA ($180,174 in 2003), Argentina ($34,533 in 2003), Greece ($2,358 in 2003), Mexico ($171 in 2003), Syria ($163,106 in 2003), Uruguay ($53,414 in 2003), Italy ($29,632 in 2003) and Turkey ($22,865 in 2003). Olives (HS 1005) are mainly imported from Greece ($219,116 in 2003). Finally, the soy beans (HS 1201) are mainly imported from Argentina ($16,160,387 in 2003), Brazil ($10,884,861 in 2003), USA ($5,689,474 in 2003), Colombia ($1,477,269 in 2003) and South Africa ($1,063,325 in 2003). As can be seen, most of the imports come from non-member countries of the Agreement. However, the tariff headings of these non-originating inputs are different from the heading of the final product as required. Therefore, the RoO are not expected to have a negative impact on the access of Egyptian vegetable oils to the EU markets.

As can be observed in the case of the twenty most significant exported Egyptian goods to the EU, the RoO should not really limit or constrain the exports. The very few exceptions would mainly occur where the requirement for conferring origin is for the product to be wholly obtained in Egypt or in one of the member countries of the Agreement. But even in these cases, Egypt could work on intensifying its local production of these products. It is also worth mentioning that the interviewed government clerks stated that there are no real problems facing them concerning the Euro-Med RoO.

[81] Accurate numbers about Sunflower production in Egypt are not available, but Egypt produces 9.5 percent of world production (The National Information Resource for Value Added Agriculture).

[82] Egypt belongs to the top 10 Countries of world production of olives (5.2 percent in 2003) (Fruit Crops Encyclopedia, The University of Georgia).

[83] World Corn Growers Association.

6. 4. 2 COMESA

In 1994, the COMESA members agreed on the RoO for products to be traded between themselves, as provided for under Article 4(1)(e) of the Treaty. The COMESA RoO are the cornerstone of the COMESA trade regime and serve to prevent non-COMESA members from benefiting from preferential tariffs for them to access the COMESA market. The determination of the eligibility of products to COMESA origin and the granting of preferential tariffs to goods originating in the member states are important processes in the implementation of the COMESA trade regime. The effective and uniform implementation of the provisions of the Protocol on RoO by the member states is important as it helps in strengthening the COMESA trade regime.

COMESA provides that goods shall be accepted as eligible for CM treatment if they originate in the member states, and the definition of such products is provided in a Protocol on RoO that is attached to the Treaty.

Product coverage

Under the COMESA trade regime, goods qualify for preferential tariff treatment if they originate in the member states. This means that all goods that meet the requirements of the COMESA RoO qualify for preferential tariff treatment when they are traded within COMESA.

Definition

COMESA RoO are a set of criteria which is used to distinguish between goods that are produced within the COMESA member states and are therefore entitled to preferential tariff treatment on one hand and those that are considered to have been produced outside the COMESA region. Since COMESA RoO are used for granting tariff preferences, they are referred to as preferential RoO.

Cumulation of origin

"For the purposes of implementing the Protocol on RoO, the member states shall be considered as one territory. Raw materials or semi-finished goods originating in any of the member states and undergoing working or processing either in one or more states of COMESA shall, for the purpose

of determining the origin of a finished product, be deemed to have originated in the member state where the final processing or manufacturing takes place. In applying this rule, the evidence of originating status of raw materials or semi-finished goods imported from another member state is given by a CoO issued by the Designated Issuing Authority in the exporting member state."

Determination of origin

Article 48 of the Treaty establishing COMESA provides that goods shall be accepted as eligible for CM tariff treatment if they originate in the member states. For the goods to be considered originating in a member state of COMESA, any of the following five independent criteria has to be met:

(i) The goods should be wholly produced in a member state, such as mineral products extracted from the ground or sea-bed of the member states, vegetable products harvested within the member states, live animals born and raised within the member states, products obtained from live animals within the member states, products obtained by hunting or fishing conducted within the member states, products obtained from the sea and from rivers and lakes within the member states by a vessel of a member state, products manufactured in a factory of a member state exclusively from the former products, scrap and waste resulting from manufacturing operations within the member state, and goods produced within the member states exclusively or mainly from materials containing no element imported from outside the member states or of undetermined origin. Used articles fit only for the recovery of materials, provided that such articles have been collected from users within the member states[84]; or

(ii) The goods produced wholly or partially from imported materials should be produced in the member states and the c.i.f. value of any foreign materials should not exceed 60 percent of the total cost of all materials used in their production[85]; or

[84] Electrical power, fuel, plant, machinery and tools used in the production of goods shall always be regarded as wholly produced within the CM when determining the origin of the goods.

[85] The formula used is:
Import material content = c.i.f. value of imported materials/ (cost of local materials + c.i.f. value of imported materials) This rule can also be expressed in terms of domestic materials, where a minimum of 40 percent local content should be achieved for the finished goods to qualify as originating in a member state,

(iii) The goods should be produced in the member states and attain a value added of at least 35 percent of the ex-factory cost of the goods[86]; or

(iv) The goods should be produced in the member states and should be classifiable under a tariff heading other than the tariff heading of the non-originating materials used in their production; or

(v) The goods should be designated by the Council of Ministers as "goods of particular importance to the economic development of the member states" and should contain not less than 25 percent value added, notwithstanding the provisions of paragraph (iii) above.

Processes not conferring origin

The Protocol for RoO contains a list of operations and processes, which shall be considered as insufficient to support a claim that goods originate from a member state. The list includes packaging, bottling, placing in flasks, bags, cases and boxes, fixing on cards or boards, mixing of ingredients imported from outside member states, simple assembly of components and parts imported from outside the member states to constitute a complete product, marking, labeling or affixing other like distinguishing signs on products or their packages, removal of dust, sifting or screening, sorting, classifying and matching, including the making up of sets of goods, washing, painting and cutting up and slaughtering of animals.

Products resulting from these operations and processes retain their foreign origin and are thus not entitled to preferential tariff treatment.

In the following analysis, we essentially stick to the following two criteria:

1. The condition of the final good to be wholly produced in a member state of COMESA; or
2. The condition of the difference in the tariff heading classifications between the final product and the non-originating materials.

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such that: Local material content = cost of local materials/ (cost of local materials + c.i.f. value of imported materials).

[86] The formula used is:Value added =(ex-factory cost of the finished product - c.i.f. value of imported materials used in production)/ex-factory cost of the finished product.

The reason therefore is the difficulty of relying on any criterion that considers the percentages of the materials used or the value added of the final product[87]. The tariff heading used is according to the HS, also used in the analysis concerning Euro-Med and GAFTA.

The twenty most significant Egyptian exports to the COMESA countries and their RoO

HS 7202: Steel ($13,745,598 in 2003):

As has been mentioned before, the main raw materials used in producing steel are iron (HS 7216), coke (HS 2713), limestone (HS 2521) and dolomite (HS 2518). All these raw materials are obtainable from Egyptian ground. However, Egypt additionally imports iron from Libya ($122,529 in 2003) and the EU ($86,245 in 2003), coke from Kuwait ($2,144,174 in 2003), Australia ($949,253 in 2003) and Italy ($422,179 in 2003), limestone from China ($10,968 in 2003) and Saudi Arabia ($8,425 in 2003), and it imports dolomite from France ($55,132 in 2003) and Norway ($6,457 in 2003). Neither of these countries are members of COMESA. Nevertheless, the headings of coke, limestone and dolomite are far different from the heading of the final product. Thus, if Egypt relies more on its locally extracted iron, it can fulfill this criterion of the COMESA RoO. Otherwise, the export volume of this heading might be slightly affected.

HS 1703: Molasses resulting from the extraction or refining of cane sugar ($ 13,723,899 in 2003):

In addition to the local Egyptian raw cane sugar ($7,235,896 in 2003), the imported sugar originates mainly from Germany ($ 236,277 in 2003), Turkey ($528,003 in 2003), Spain ($304,798 in 2003) and Ireland ($43,183 in 2003). These are not COMESA members, and accordingly, the Egyptian export volume of this final product could highly be affected, if Egypt further relies on the sugar imported from these non-member countries as an input for that product.

[87] Many of the companies that were interviewed considered the percentages of material usage highly confidential, and therefore, it was hard to obtain accurate information concerning these percentages.

HS 1006: Polished rice ($7,725,231 in 2003):

Egypt imports raw rice from India ($102,986 in 2003), Pakistan ($81,412 in 2003), Switzerland ($74,638 in 2003), Australia ($15,404 in 2003), and Ghana ($1,896 in 2003). Since all these countries do not belong to the Agreement, Egypt needs to rely more on its locally harvested rice (3,900 thousand metric tons in 2003). Otherwise, the exports of the final product could be negatively affected, if the RoO are to be applied according to the Treaty.

HS 2523: Cement Clinkers ($6,069,334 in 2003):

As referred to above, limestone (HS 2521) makes up around 80 percent of the approximately 1.65 tons of raw material input needed to make one ton of cement clinker. In addition, its heading is fairly close to the heading of the final product. Hence, in order to cope with the RoO of the Agreement, Egypt needs to rely more on its own inputs of limestone, especially that it also imports it from other non-COMESA countries, such as China ($350,968 in 2003) and Saudi Arabia ($342,000 in 2003). Chalk (HS 2509), another material used in producing cement clinkers, also belongs to a close heading of the final product. Therefore, Egypt shall enhance its local production of this material, especially that it greatly relies on importing it from Germany ($47,139 in 2003), another non-COMESA country.

HS 3004: Medicaments or therapeutic purposes ($4,187,480 in 2003):

It is hard to judge whether the COMESA RoO would affect the Egyptian exports of this heading, since the medicaments industry is highly sensitive and complex, concerning the processes and the inputs. Egypt relies heavily on inputs imported from countries other than the COMESA members. Moreover, from the experience of the researcher in interviewed medicament companies, the components used in the medicine and their exact percentages remain confidential in most of the factories.

HS 1512: Vegetable oils and their fractions ($3,216,821 in 2003):

As already indicated in the frame of Euro-Med the main four sorts of vegetable oils that Egypt produces and exports are the olive oil, the maize oil, the sunflower oil and the soy bean oil. Sunflower is planted and harvested locally. Egypt relies on local production of olives and maize as well, but part of these two vegetables is imported from abroad; maize (HS 2001) is mainly

imported from Brazil ($2,171,370 in 2003), Russia ($1,061,752 in 2003), the USA ($180,174 in 2003), Argentina ($34,533 in 2003), Syria ($163,106 in 2003), Uruguay ($53,414 in 2003), Italy ($29,632 in 2003) and Turkey ($22,865 in 2003) and Greece ($2,358 in 2003). Olives (HS 1005) are mainly imported from Greece ($219,116 in 2003). Finally, the soy beans are mainly imported from Argentina ($16,160,387 in 2003), Brazil ($10,884,861 in 2003), USA ($5,689,474 in 2003), Colombia ($1,477,269 in 2003) and South Africa ($1,063,325 in 2003). Neither of these exporting countries are COMESA members. However, the tariff headings of these non-originating inputs are different from the heading of the final product as required. Therefore, no enormous problems concerning the RoO should be expected.

HS 3401: Bar soaps ($3,182,675 in 2003):

Bar soaps are made from fats and oils or their fatty acids which are reacted with inorganic water-soluble bases. Palm, olive and coconut oils are the principal oils used in soap-making (The Soap and Detergent Association[88]). In general, the vegetable oils are classified under a totally different heading (HS 1512) than the one that bar soaps belong to[89]. Two very important inputs that are used in producing bar soaps are the caustic soda (HS 2815) and the citric acid (HS 2918). In addition to the local production of caustic soda in Egypt[90] the latter imports it from Libya ($318,551in 2003), Rumania ($221,330 in 2003), China ($119,372 in 2003), Turkey ($81,787 in 2003), UK ($56,644 in 2003), Belgium ($45,280 in 2003) and Ukraine ($35,354 in 2003). Citric acid is mainly imported from China ($1,074,357 in 2003), Austria ($47,390 in 2003), Belgium ($40,614 in 2003), UK ($33,263 in 2003), Germany ($26,073 in 2003) and India ($25,692 in 2003). Neither of these exporting countries belongs to COMESA. Nonetheless, the headings of these two inputs are far different from the final product heading. For that reason, these inputs shall not be a hindrance for exporting the final good in COMESA markets.

HS 3926: Plastic articles ($2,366,403 in 2003):

As has been mentioned early in this chapter, the plastics industry in Egypt is growing and modernizing steadily. However, the main suppliers of plastic inputs (HS 3916) are Germany

[88] This association represents manufacturers of household, industrial and institutional cleaning products, their ingredients and finished packaging.

[89] More about vegetable oils has been demonstrated in the Euro-Med section.

[90] Market Research Website.

($1,179,683 in 2003), China ($1,130,172 in 2003), Turkey ($889,731 in 2003), Italy ($888,802 in 2003), USA ($782,370 in 2003), Belgium ($159,846 in 2003), Sweden ($144,521 in 2003), Taiwan ($124,781 in 2003), India ($117,815 in 2003) and France ($117,120 in 2003).The heading of these inputs is quite close to the heading of the final product, and at the same time, these inputs do not originate in Egypt, according to the COMESA RoO. Hence, the plastic articles must be reconsidered once again, if Egypt is to sustain its exports to COMESA countries. For example, Egypt should then rely more on its locally extracted crude oil and natural gas in producing plastic, in order to comply with the COMESA RoO.

HS 2803: Carbon ($2,290,155 in 2003):

The Egyptian Carbon is derived from graphite (HS 2504) (Jefferson Lab Data Base). The latter is mainly imported from China ($680,294 in 2003), which is not member of the COMESA. Nonetheless, since the headings of graphite and carbon are different, and the rest of the production process is done in Egypt, the export of carbon to the other COMESA countries shall not be affected by the RoO of the Agreement.

HS 6910: Ceramic products ($1,923,924 in 2003):

The main raw material that ceramic is obtained of is plastic clay body, which is obtained in the Egyptian ground ($11,956,415 the local production of 2003). Therefore, Egyptian ceramic products can be considered wholly produced in Egypt, fulfilling in turn the COMESA RoO.

HS: 2714: Bitumen ($1,700,853 in 2003):

Bitumen is formed in the process of petroleum (HS 2709) generation. Bitumen also includes mineral wax (HS 2712). These two materials are classified in headings very close to the final product. Therefore, both materials should be originating in Egypt or in any other COMESA country, in order for Bitumen to confer origin. Petroleum is obtained in the Egyptian ground ($22,265,929 in 2003). However, the mineral wax, which is a mixture of hydrocarbons, cannot be considered originating in Egypt, according to the COMESA Agreement, although it fulfills the RoO of Euro-Med. The reason therefore is the fact that the hydrocarbon is an organic compound containing carbon (HS 3801) and hydrogen (HS 2804). The first material is mainly imported from Norway ($250,710 in 2003), China ($ 141,898 in 2003) and New Zealand ($95,424 in 2003) and

the hydrogen is mainly imported from the countries of the EU ($54,200 in 2003). Consequently, applying the COMESA RoO could negatively affect the export volume of Bitumen, unless Egypt wholly relies on its own materials or materials imported from the COMESA countries when producing this final product. However, this would clash with the Euro-Med RoO.

HS 2712: Mineral waxes ($1,698,865 in 2003):

The inputs used are carbon (HS 3801) and hydrogen (HS 2804). The hydrogen is mainly imported from the countries of the EU ($460,200 in 2003) and the carbon is mainly imported from Norway ($250,710 in 2003), China ($141,898 in 2003) and New Zealand ($95,424 in 2003), which are all non-COMESA members. But due to the fulfillment of the different-heading-classifications condition, the final product should be accepted as originating in Egypt.

HS 9403: Furniture ($1,456,199 in 2003):

Cutting, bending, molding, laminating, and assembly of wood (HS 4403), iron (HS 7216), glass (HS 3207), plastics (HS 3916) and rattan (HS 1401) are the main processes used in the manufacture of furniture. Although all these materials - apart from the local production - are imported from non-COMESA member countries, such as Finland and Estonia for wood, the European Economic Community ($86,245 in 2003) for iron, Spain and Italy for glass, Germany and Turkey for plastics, and last but not least Singapore and China for rattan, this does not really conflict with the COMESA RoO, since the headings of these inputs are completely different from the heading of the final product.

HS 1905: Bakery products ($1,318,608 in 2003):

The input that represents the largest percentage of the final product (at least 70 percent) is flour (HS 1208) and/or wheat (HS 1001). The rest of the materials are water, backing powder and some additional secondary inputs.

Egypt mainly imports flour from Syria ($15,738,355 in 2003) and Lebanon ($7,935,363 in 2003). The wheat is imported in massive quantities from the USA ($223,187,022 in 2003), France ($96,149,337 in 2003), Russia ($77,830,887 in 2003), Australia ($58,665,699 in 2003), Syria ($25,798,323 in 2003), Germany ($8,405,300 in 2003), Poland ($4,634,650 in 2003), Ukraine

($3,591,045 in 2003), Cyprus ($3,518,016 in 2003), Sweden ($2,634,486 in 2003), Pakistan ($2,566,772 in 2003), Slovakia ($1,838,578 in 2003), Bulgaria ($886,382 in 2003), the Czech Republic ($775,120 in 2003), Spain ($724,493 in 2003), Rumania ($637,881 in 2003), Croatia ($530,288 in 2003), Canada ($525,947 in 2003), Slovenia ($366,021 in 2003), Jordan ($191,728 in 2003), Somalia ($108,417 in 2003) and Taiwan ($78,771 in 2003). Although no COMESA country is included in the list of exporters, the final product should enter the COMESA markets, since it obeys the rule of the different headings that is stated in the Protocol of the Agreement.

HS 7615 Aluminum articles ($1,262,477 in 2003):

The principal ore of aluminum is bauxite, widely abundant in Egypt. It is normally mined by open cut techniques. The bauxite is purified by the Bayer process which involves heating in caustic soda. The aluminum cryohydrate dissolves leaving a residue of insoluble iron and titanium oxides. The aluminum cryohydrate is dried to produce alumina. The iron and titanium oxide residue is called `red mud'. Two tons of bauxite yield one ton of alumina[91]. The rest of the processes is undertaken in the *Egyptalum* aluminum plant situated at Nag Hammady. Therefore, Aluminum can be considered wholly produced in Egypt.

HS 0703: Chilled onions ($1,245,365 in 2003):

Besides the local production, Egypt imports the fresh onions from Australia, which is not member of COMESA. If Egypt keeps relying partly on the Australian onions, this would violate the rule of wholly obtained products. At the same time, the headings of fresh and chilled onions are very close to each other, which - in the case of relying on the imported fresh onions - clashes with the rule of sufficient transformation. Therefore, this could to a certain extent limit the exports of this heading to the other member countries of COMESA.

HS 0701: Potatoes ($1,154,869 in 2003):

The local production of potatoes covers the exports. This complies with the rule that the product must be wholly obtained in the COMESA country, and therefore, this does not harm the RoO of the COMESA Agreement.

[91] The AZO Online Journal of Materials.

HS 2515: Marble ($1,145,862 in 2003):

As mentioned in the frame of Euro-Med, rock, the main material used in producing marble, can be massively found in the Galala mountain of Egypt. As for the rock drillers (HS 8207) and rock cutters (HS 8430), they are imported from various countries, most of them European, and none of them African. However, since the main material originates in Egypt and the headings of the rest of the materials used belong to completely different headings from the one that the final product belongs to, the production of this product and its exportation to COMESA countries shall not be violating the RoO of the Agreement.

HS 2009: Fruits juice ($1,115,507 in 2003):

In addition to Egypt's local production of fresh fruits (HS 0800), it also imports them from different countries of the world. For example, fresh apples (HS 0808) are mainly imported from Lebanon ($5,999,140 in 2003) and Syria ($2,558,883 in 2003), cherries (HS 0809) from Lebanon ($323,452 in 2003) and Syria ($83,575 in 2003), fresh figs (HS 0804) from Syria ($31,179 in 2003), fresh grapes (HS 0806) from Lebanon ($279,343 in 2003), fresh peaches (HS 0809) from Italy ($4,760 in 2003), fresh pears (HS 0808) from Lebanon ($84,616 in 2003) and China ($71,071 in 2003), fresh pineapples (HS 0804) from Ghana ($20,209 in 2003) and Indonesia ($7,211 in 2003). Although all of these exporting countries do not belong to COMESA, using their inputs is not problematic, since the fruits that they export to Egypt are classified under different headings from the heading that the final product is classified under. The rest of the production processes is undertaken by - among others - the two main Egyptian juice factories MEGA, in Smouha, Alexandria, and Egypt-Africa-Co., Cairo[92], which in turn makes the final product eligible for entering COMESA countries duty free.

HS 7403: Refined copper ($1,032,314 in 2003):

Copper ores are mainly mined and melted in the eastern desert and in Sinai[93]. The production is in the form of small-scale refining of scrap metal. In the public sector, the Egyptian Copper Works in Alexandria is reportedly one of the main producers. In the private sector, the largest

[92] The Aliba. Website on Global Trade.

[93] The Digital Egypt for Universities, University College London.

refiner is Egyptian Metal Works Co. in Helwan, which has capacity to produce at least 6,000 t/yr of a medium purity product by fire refining[94]. Therefore, the refined copper can be considered originating in Egypt and hence, it should not face problems entering the countries of COMESA, if the RoO of the latter are to be applied.

The COMESA Protocol for the RoO seems to be a bit more problematic for the Egyptian exports than in the case of Euro-Med. The lack of inputs imported from COMESA countries is the most visible reason for that. Most of the inputs are imported from the EU, and therefore, what is in favor of the Egyptian exports to the EU might at the same time be against the Egyptian exports to COMESA countries. But within the twenty goods that have been chosen for each Agreement, this occurs only in a few cases.

6.4.3. GAFTA

The general RoO introduced by GAFTA indicate that the value added within the boundaries of one or more member countries should be no less than 40 percent of the final ex-factory price of the goods and this percentage can be lowered to 20 percent in case of joint Arab production. The 40 percent value added rule is a general rule and is supposed to be a temporary one till detailed RoO are agreed upon.

So far, a comprehensive and detailed protocol on RoO has not been agreed upon among the member countries of GAFTA. The former are still in the process of designing a protocol that is quite similar to the Euro-Med Protocol for the RoO. We build our analysis here on the draft that has been submitted for that purpose and where the conservations of different countries on each separate RoO are also noted.

Definitions in the GAFTA draft for RoO

Manufacture: means any kind of working or processing including assembly or specific operations.

Material: means any ingredient, raw material, component or part, etc., used in the manufacture of the product

[94] The United States Geological Survey (USGS), Mineral Resources Program.

Product: means the product being manufactured, even if it is intended for later use in another manufacturing operation.

Goods: means both materials and products.

General requirements according to the GAFTA draft for RoO:

Cumulation with originating materials:

1. The materials originating in any Arab member state shall be considered as if originated in any other Arab member state when included in a product manufactured in this latter state. It is not necessary that these materials are sufficiently worked and processed.
2. The products originating in any Arab member state shall be considered as originating in that latter Arab state where the value added there is greater than the value of the materials used originating in any one of the other member states. If this is not the case, the product obtained shall be considered as originating in any of the GAFTA member states which accounts for the highest value of originating materials used in the manufacture in that latter state. And when the national value added of a product being produced in more than one country is equal, the product shall acquire the originating status of the last member state in which the product has been worked and processed.

"For the purpose of implementing the Agreement to Facilitate and Develop Trade among the Arab states and the Executive Program of GAFTA, the following products shall be considered as originating in the exporting Arab member state:

1. Products wholly obtained in the member countries of the Agreement; the details of this condition resemble the ones included in Euro-Med.
2. Products obtained inside that state containing materials not wholly obtained inside such a state provided that these materials have undergone sufficient preparation, working or processing in the state. These conditions differ from each single product to the other as will be discussed in detail in the following analysis. In general, the rules related to the sufficient and insufficient working or processing operations quite resemble the ones included in Euro-Med."

The twenty most significant Egyptian exports to the GAFTA countries and their RoO

HS 1006: Polished rice ($89,990,423 in 2003):

The process required is the manufacturing in which all the materials used must be wholly obtained.

Beside the locally harvested rice in Egypt, the latter imports it also from India ($102,986 in 2003), Pakistan ($81,412 in 2003), Switzerland ($74,638 in 2003), Australia ($15,404 in 2003), and Ghana ($1,896 in 2003). All these countries are not members of GAFTA. Thus, considering the GAFTA RoO, if Egypt is willing to maintain the same volume of its polished rice exports to the GAFTA countries, it needs to rely more on its locally obtained rice; especially that polishing is an insufficient transformation process. As indicated above, the same problem rises when considering Euro-Med, since all these exporting countries are not members of the latter Agreement either.

HS 2710: Benzene ($72,022,902 in 2003):

The required process is any operations of refining or other operations in which all the non-originating materials used are classified within a heading other than that of the product.

Benzene is a natural part of crude oil (HS 2709) (Agency for Toxic Substances and Disease Registry). Since the latter is obtained in Egypt ($22,265,929 in 2003) and the rest of the process is undertaken in Egypt, this product should face no problems concerning RoO. All the member countries agreed on the provision.

HS 2523 Cement clinkers ($69,001,636 in 2003):

The process required is the manufacturing in which all the non-originating materials used are classified within a heading other than that of the product. As referred to in the RoO of Euro-Med, limestone (HS 2521) is the most common material used although chalk (HS 2509) and calcium carbonate (HS 2836) can also be used in producing cement clinkers.

Besides the local limestone, Egypt also imports it from China ($350,968 in 2003) and Saudi Arabia ($342,000 in 2003). The chalk is mainly imported from Germany ($47,139 in 2003) and the calcium from Italy ($218,607 in 2003), Turkey ($185,173 in 2003), France ($98,923 in 2003), Spain ($54,641 in 2003), Germany ($23,744 in 2003), UK ($12,484 in2003) and Belgium ($10,131 in 2003). It is clear that most of the raw materials do not originate in GAFTA countries. Furthermore, these inputs - apart from calcium carbonate - belong to a heading very close to the final product. Thus, Egypt should increase its local inputs in the production process or rely on inputs imported from GAFTA member countries[95], in order to comply with the RoO of this Agreement. This might be the reason why Egypt - in addition to Morocco, Libya and Tunisia - has not yet voted for the RoO of this heading, which further complicates the problem.

HS 3004: Medicaments for therapeutic purposes, excluding goods of heading HS 3002 (human blood; animal blood prepared for therapeutic, prophylactic or diagnostic use; antiserum and other blood fractions and modified immunological products, whether or not obtained by means of biotechnological processes; vaccines, toxins, cultures of micro-organisms (excluding yeasts) and similar products) ($24,733,416 in 2003):

The process required is the manufacturing in which all non-originating materials used are classified within a heading other than that of the product. However, materials of heading (HS 3003) or (HS 3004) may be used provided their value, taken together, does not exceed 20 percent of the final factory price of the product.

It is hard to judge whether the RoO of GAFTA would affect the Egyptian exports of this heading, since the medicaments industry is highly sensitive and complex concerning the processes and the inputs. Egypt relies heavily on inputs imported from countries other than the GAFTA members and, therefore, the probability that the RoO could have a negative impact on the exports of this heading remains high. In addition, a number of GAFTA members refused to vote for the RoO related to this heading, which further complicates the problem; the opposing countries are Saudi Arabia, Oman, Kuwait, Lebanon, UAE, Bahrain, Libya and Qatar.

[95] This solution might not be simple to reach, since as can be seen from the figures, Egypt has been mainly relying on inputs from EU countries, which either indicates that these inputs are not abundant in Arab countries or that they are more expensive as compared to EU countries, which makes it more reasonable for Egypt to import them from the latter.

HS 2711: Raw and liquefied natural gas ($17,043,076 in 2003):

In the case of non-originating materials, the process required is the refining and/or one or more specific processes.

The natural gas originates in Egypt, since the raw material is directly extracted from Egyptian ground - mainly in the north coast - and later transported in interstate or intrastate pipelines ($4,337,389 was the local production of 2003)[96]. As for the liquefied natural gas, it is first formulated in an amino unit, and then it is subject to molecular absorption unit. In a gas clean up unit, the Carbon dioxide (CO2) is removed. Then the gas is treated in a so-called Merox unit, where Ethane, Propane and Butane are obtained. This process takes place in Egyptian factories[97]. Hence, the raw and liquefied natural gas is not expected to face problems concerning RoO in GAFTA, especially that all the countries of the Agreement have no objections with regard to this heading.

HS 0703: Chilled onions ($15,151,603 in 2003):

The necessary working and processing requires manufacturing in which all the materials used must be wholly obtained. Egypt obtains the fresh onions - in addition to the local production from Australia, which is not member of GAFTA. Therefore, this could to a certain extent limit the exports of this heading to the other member countries of GAFTA.

HS 8424: Agricultural machinery (even if manually operated) to sprinkle, disperse and spittle powders and liquids, fire extinguishers even if filled, sprinkling guns, and similar machines ($14,774,644 in 2003):

The process required is the manufacturing in which all non-originating materials used are classified within a heading other than that of the product. However, materials from the same heading may be used provided that their value shall not exceed 20 percent of the final factory price of the product.

[96] Interstate pipelines carry natural gas across governorates, in some cases clear across the country. Intrastate pipelines, on the other hand, transport natural gas within a particular governorate (Natural Gas Supply Association).

[97] UOP LLC official homepage.

Detailed information about the origin of materials used in producing these machines in Egypt is still very scarce. Moreover, it is most likely that the machines that are exported from Egypt to other countries are either re-export or even used machines. Most of the imported machines would be originating in member countries of the EU or in the USA. Therefore, in the case of applying the RoO of GAFTA on the Egyptian machinery exports to other GAFTA countries, the latter exports could face enormous problems concerning the certificates of origin. What makes this rule more complicated is the fact that there are two proposed scenarios; the first proposal, which Egypt strongly calls for is applying 40 percent instead of 20 percent of the final factory price product. The only two countries that agree on that scenario are Morocco and Algeria, whereas Saudi Arabia, UAE, Qatar, Kuwait, Oman, Jordan and Lebanon refuse. The second proposal which is proposed by the latter countries and refused by the former is applying 60 percent of the final factory price of the product.

HS 0406: Cheese ($11,677,261 in 2003):

The necessary working and processing requires manufacturing in which all the materials used must be wholly obtained.

All natural cheeses go through a similar production process. The basic ingredient for cheese is milk. After the thickening of the latter, the temperatures and the enzymes used determine the shape and sort of the produced cheese[98]. For that reason, the main stress in this analysis should be on the milk as an essential input. The Egyptian cheese producers rely on the local milk as an input as well as the milk powder imported from different countries that are all non-GAFTA members. The major exporting countries are New Zeeland ($2,621,243 in 2003), Ireland ($1,453,015 in 2003), Canada ($713,281 in 2003), the Netherlands ($620,341 in 2003), France ($612,339 in 2003), Denmark ($377,669 in 2003), the Czech Republic ($165,626 in 2003), Germany ($118,932 in 2003), Poland ($ 68,242 in 2003) and Australia ($23,367 in 2003). Clearly, cheese (HS 0406) does not originate in Egypt or in any of the GAFTA countries, and hence, applying the GAFTA RoO would be quite problematic. Therefore, it is not surprising that Egypt - in addition to Tunisia - has voted against this provision.

[98] ESSORTMENT Information Website.

HS 1703: Molasses resulting from the extraction or refining of sugar, flavored or colored ($9,732,239.00 in 2003):

The necessary working and processing requires manufacturing in which the value of any non-originating materials of sugars and sugar confectionery (HS 1700) does not exceed 40 percent of the final factory price of the product.

Egypt produces most of its own raw sugar. Nevertheless, it also imports sugar from Germany ($236,277 in 2003), Turkey ($528,003 in 2003), Spain ($304,798 in 2003) and Ireland ($43,183 in 2003), which are non-members of GAFTA. Accordingly, applying the GAFTA RoO might negatively affect the Egyptian exports of heading HS 1703 to its Arab neighbors. In fact, this could be the reason why Egypt is still opposing the RoO of this heading. Noteworthy is that Sudan - which might face a similar problem - takes the same position as Egypt.

HS 0902 Packed black tea ($8,023,684 in 2003):

The necessary working and processing requires manufacturing in which all the materials used must be wholly obtained.

Egypt mainly imports the black tea from Kenya ($58,781,135 in 2003), Tanzania ($ 1,179,837 in 2003), Malawi ($530,804 in 2003), Sri Lanka ($280,487 in 2003), India ($ 134,311 in 2003), Indonesia ($107,726 in 2003) and Hong Kong ($19,277 in 2003), which are all non-members of GAFTA. And since mere packing of the products is considered an insufficient working or processing to confer the status of originating products, packed black tea in Egypt would be expected to face problems entering the GAFTA markets, if the RoO of the latter are to be applied properly.

HS: 2714: Bitumen ($7,914,702 in 2003):

The process required is operations of refining and/or one or more specific process (es) or other operations in which all the non-originating materials used are classified within a heading other than that of the product. As indicated above, bitumen is formed in the process of petroleum (HS 2709) and mineral wax (HS 2712) generation.

Petroleum originates in Egypt, while Bitumen should be re-considered, in order for it to confer origin, especially that most of its inputs originate in the EU, as has been mentioned early in this chapter. Other than this problem, all the GAFTA countries agreed on the provision concerning this heading.

HS 0701: Potatoes ($7,836,764 in 2003):

The necessary working and processing requires manufacturing in which all the materials used must be wholly obtained. As has been mentioned in the Euro-Med and COMESA RoO, the local production of potatoes covers the exports abroad and therefore this does not represent a problem in relation with the RoO of the Agreement.

HS 2709: Crude Petroleum ($5,470,745 in 2003):

The process needed here is the destructive distillation of bituminous materials. According to the interviewed officials in the Ministry of Industry and Foreign Trade, this process is fully done in Egypt. All the member countries agreed on the provision.

HS 2710: Petroleum oils and oils obtained from bituminous materials, other than crude; preparations not elsewhere specified or included, containing by weight 70 percent or more of petroleum oils or of oils obtained from bituminous materials, these oils being the basic constituents of the preparations ($5,235,729 in 2003):

Manufacturing should contain operations of refining or other operations in which all the non-originating materials used are classified within a heading other than that of the product. However, materials classified within the same heading may be used provided their value does not exceed 20 percent of the final factory price of the product.

The raw oil itself is obtained in Egypt and the refining process exists in Egypt as well. The local material used in the process is far more than 20 percent of the final factory price of the product. Hence, exporting the product that belongs to this tariff heading to GAFTA members shall not be affected by the RoO of the Agreement. All the GAFTA members agreed on that provision.

HS 2712: Mineral waxes ($5,125,311 in 2003):

The required process is any operations of refining or other operations in which all the non-originating materials used are classified within a heading other than that of the product.

As mentioned before in this chapter, waxes are a mixture of hydrocarbons and occur in association with petroleum. Hydrocarbon is an organic compound containing only carbon (HS 3801) and hydrogen (HS 2804). Thus, the only two materials used are classified within a heading other than that of the product. Since the condition of the different heading is fulfilled, then this product should not face problems in continuing to enter the GAFTA markets.

HS 3102 Urea ($3,342,729 in 2003):

The necessary working and processing requires manufacturing in which all the non-originating materials used are classified within a heading other than that of the product. However, non-originating materials classified within the same heading may be used provided their value does not exceed 20 percent of the final factory price of the product.

Urea is an organic compound of carbon, nitrogen, oxygen and hydrogen[99]. Carbon in Egypt is mainly derived from graphite (HS 2504)[100]. Nevertheless, the latter is mainly imported from China ($68,294 in 2003), which is not member of GAFTA. This clashes with the rule stating that if a product, which has acquired originating status by fulfilling these conditions is used in the manufacture of another product, the conditions applicable to the product in which it is incorporated do not apply to it, and no account shall be taken of the non-originating materials which may have been used in its manufacture. Consequently, if Egypt does not fully rely on its local graphite in producing carbon, the latter cannot be considered as an originating material in the process of urea production. As for the three left inputs, they are obtained locally, but a certain amount is imported from non-GAFTA countries; nitrogen is imported from Canada ($41,156 in 2003), Germany ($28,701 in 2003), France ($21,414 in 2003) and China ($16,612 in 2003). Oxygen is mainly imported from the USA ($26,940 in 2003) and hydrogen from Belgium ($8,236 in 2003). As can be seen from the figures, the import volumes of non-GAFTA countries are not

[99] Wikipedia, The Free Encyclopedia.

[100] Jefferson Lab Data Base.

too large, especially in the case of oxygen and hydrogen. This indicates that Egypt could principally rely on its own inputs. Otherwise, applying the GAFTA RoO would constrain the Egyptian export volume of this heading.

HS 5201: Raw cotton ($2,784,298 in 2003):

The product must be wholly obtained, in order to confer origin. This condition is fulfilled in the Egyptian raw cotton ($1,000,000 bales in 2003).

HS 2202: Mineral water ($1,866,532 in 2003):

The process required is the manufacturing in which all non-originating materials used are classified within a heading other than that of the product.

Bottled mineral water sales in Egypt maintained positive volume growth in 2003, with sales reaching 370.5 million liters, making it the second largest sector by volume in the Egyptian soft drinks market (The Fine Waters Website). The relative stability of unit prices over the review period contributed to positive growth. An important reason for that is the fact that Egypt has the highest kidney failure rate in the world, mainly because of the lack of a reliable source of clean drinkable water. Most Egyptians believe tap water is contaminated and very unhealthy. Therefore, the Egyptian market for mineral water is growing and there are about 12 Egyptian independent factories for producing mineral water, which is mainly extracted from Helwan, Siwa, The New Valley, Notron Valley, as well as different oasis in the Western dessert of Egypt (State Information Service, Cairo)

The factories are mainly located in the following regions: El Sadat City and Kafr El-Arbein Region. Hence, this product complies with the GAFTA RoO. However, Morocco, Tunisia and Sudan have not yet agreed on that provision.

HS 0710: Frozen vegetables ($1,431,685 in 2003):

The process required is the manufacturing in which all the materials used must be wholly obtained. Egypt mainly depends on its own vegetables, and the imported vegetables are mainly obtained from the EU countries ($3,656,000 in 2003). Therefore, on the contrary to Euro-Med,

Egypt as a member of GAFTA might face the problem of limited possibilities of exporting frozen vegetables that do not originate in it or in other GAFTA member countries.

HS 0851: Fresh citrus fruits ($1,295,498 in 2003):

The process required is the manufacturing in which all the fruits used must be wholly obtained. Since Egypt mainly relies on its locally planted and harvested citrus fruits[101], this RoO does not clash with further exporting this product to the GAFTA member countries, especially that these countries did not show any objection against this provision.

6.5. Summary and main findings

It is quite noticeable that the most problematic case regarding RoO is the case of GAFTA. Out of the twenty examined Egyptian exported products to the countries of this Agreement, at least eight would face constraints in entering these markets, if the RoO would be applied according to the proposed draft, due to imported inputs from non-GAFTA countries. In addition, there are several member countries objecting the application of certain RoO for specific reasons. Hence, the first challenge would be agreeing on a unified protocol for RoO, and the second challenge would be Egypt's capability of applying the RoO without harming the volume of its exports to its Arab neighbors. This brings us to the concept of intra-Arab trade, which is urgently needed - at least within the inputs and raw materials - in order for the final products to confer origin and hereby easily move from one Arab country to the other, as it is the case among the EU countries and even between the EU countries on one side and Egypt and its Mediterranean partners on the other.

In general, the RoO problems identified in the analysis are not necessarily problems of overlapping between the RTAs; in most of the cases where the products do not confer origin according to the RoO of one RTA, the inputs are imported from non-member countries of the RTAs under study, such as China, India and Indonesia. In other words, the RoO could constrain the trade flows between Egypt and the member countries of each separate RTA, but do not necessarily lead to a conflict between the three RTAs.

[101] Food and Agriculture Organization for the United Nations (FAO), official website.

Where the overlap exists, it is mostly where the inputs are of European origin. A good example for that are the Egyptian cane sugar molasses. They do not originate in Egypt according to the COMESA definition of RoO, since most of the inputs are European. Hence, in order to confer origin in COMESA, the quantities of the European inputs have to be reduced, which would in turn clash with the Euro-Med RoO. The same applies to the Egyptian plastic articles and to the Egyptian bitumen exported to COMESA countries.

An example where the COMESA and GAFTA RoO overlap is the Egyptian steel exported to the COMESA countries, where some inputs originate in GAFTA countries. This implies that reducing the contribution of these inputs in order to comply with the COMESA RoO could clash with applying the GAFTA RoO. However, the problem is not too severe, since the imported GAFTA inputs do not represent a high percentage of the total inputs for producing steel. Besides, the same inputs are obtainable in Egypt. The second example would be the Egyptian cement clinkers exported to the COMESA countries in which some inputs from GAFTA countries are used. But at the same time, Egyptian cement clinkers could face RoO problems when entering the GAFTA countries, since most of the inputs originate in the EU countries. Reducing these inputs could have a negative effect on the compliance with the Euro-Med RoO. Therefore, a good solution could be the Egyptian reliance on its local inputs, which is not always so simple. Other Egyptian exports to GAFTA that face similar problems in association with EU inputs are re-exported machines, cheese, sugar cane molasses, urea and frozen vegetables.

Egypt relies to a great extent on the Kenyan tea when re-exporting it packed to GAFTA countries. Since Kenya is not a GAFTA but a COMESA member, this might create problems for Egypt when exporting this tea to the GAFTA countries, especially that there is no alternative local tea production in Egypt.

CHAPTER 7

Concluding Remarks

The institutional factors serve as an important catalyst for implementing the RTAs in general. Egypt as a common country in different RTAs faces the challenge of benefiting from all of them without being subject to potential conflicts in implementation.

The lack/delay of implementation of the Egyptian RTAs cannot really be referred to organized lobbies or to certain ministries who officially object the RTAs but rather to the lack of the missing awareness of the potential benefits of the RTAs, to the weak institutions, low incentives, and to a lesser extent, to the overlapping RoO.

Chapter 1 of the study gave a theoretical background about some important concepts related to RTAs, such as trade diversion, trade creation, RoO, and institutional aspects associated with international trade.

Chapter 2 attempted to identify the differences between the four RTAs that Egypt is member of: within GAFTA and COMESA, many provisions need more development, elaboration and editing, and even many of the clear provisions have not been implemented to date. For example, the negative lists and exemptions of tariff reductions in both RTAs represent a considerable problem and is one of the important reasons that hinder the WTO from acknowledging GAFTA. Creating an FTA among only ten out of the nineteen COMESA countries, although a complete Custom Union was planned for the year 2004, proves that there is still much to be done in this RTA.

Despite the fact that the Egyptian-European Partnership Agreement seems to be promising, and its provisions have been implemented so far, the time that passed since the implementation was too short to have a broad view of the gap of implementation. It is too early to find this out in the case of the Aghadir Agreement as well, since it has not entered into force yet, due to the Jordanian delay in ratification.

Since the Egyptian RTAs are shallow of nature, their overlapping does not seem to generate a lot of costs in general terms. Even in the cases where clashes between GAFTA and COMESA or

GAFTA and the Arab BTAs could occur, - for the purpose of simplification - the Egyptian authorities give the importers and exporters space to choose which RTAs to follow. Although the EU makes up one independent trading bloc, Egypt still faces the challenge of dealing with the differences between the specific standards of each separate EU member, in addition to the common standards written in the Egyptian-European Partnership Agreement. If the Egyptian exporters keep not being aware of these conditions and standards, Egypt might miss many opportunities of entering the EU markets broadly.

Chapter 3 dealt with the static, dynamic and institutional effects that might influence Egypt as a consequence of its membership in the different RTAs. GAFTA takes the first ranks in most of the criteria concerned with the expected static gains, followed by COMESA. The reasons therefore are - among others - the shorter geographic distance, the relative similarities in production structures, the relative high tariff barriers among the member countries and the common historical and cultural factors.

GAFTA and COMESA can have a very high potential considering the dynamic effects as well, since there is still a huge unutilized space for investment stimulation, increased competition and economies of scale within both RTAs as compared to the Agreement with the EU countries.

Hence, from a pure theoretical economic and even cultural point of view, Euro-Med does not necessarily have the best potential for trade creation - at least for Egypt -, compared to COMESA and GAFTA. However, the lack of sound institutions in the two latter RTAs make them seem less advantageous.

Chapter 4 demonstrated the important institutional obstacles hindering the full implementation of the signed RTAs, such as the unawareness of the potential benefits of the RTAs, the lack of information about other potential markets abroad, the missing guarantees systems between the partner countries of GAFTA and COMESA, the lack of commitment at the side of the importers, exporters and the governments, the numerous administrative procedures, paperwork, red tape and corruption and the bad transportation, especially among the COMESA countries.

Chapter 5 showed that the institutional quality - which is one of the main concerns of the study - has a positive impact on trade flows, and hence, on the potential implementation of COMESA, Euro-Med and GAFTA. The other complementary factors and control factors differ in their

influence from one RTA to the other. It should be stressed that the institutions included in the gravity model of this chapter, which are the government effectiveness, rule of law and control of corruption, are usually non-debated institutions. However, there are other intangible institutions that are hard to measure. They can differ from one country to the other and even from one generation to the other and might include social norms, values and morals. Noteworthy is the fact that these institutions most probably do not play a less important role in the developing countries than the institutions included in the model. Nonetheless, in an attempt to overcome the unavailability of concrete data about these hidden institutional factors, the latter were still tackled to a certain extent in a descriptive approach, based on the interviews run with the Egyptian government officials, importers and exporters and local producers, as was shown in the *Chapter 4* of the study.

Chapter 6 traced the detailed production process of the important Egyptian products that are exported to the countries of the different RTAs, taking into account the necessary inputs and raw materials used in the production, in order to assess the potential implementation problems of the Egyptian RTAs resulting from the overlapping RoO. Most of the inputs that are used in the Egyptian products originate in Egypt, in the EU or in countries other than GAFTA or COMESA. Therefore, the RoO problems that Egypt faces when exporting to countries of Euro-Med are far less than exporting to countries of the two other RTAs.

The RoO are indeed a NTB for Egypt as a common country in Euro-Med, COMESA and GAFTA; when the Egyptian exporters feel 'squeezed' between the RoO of the different Agreements, they are forced to specialize in the countries they are exporting to rather than specialize in the products, which makes the RTAs an obstacle on the way of fulfilling multilateral free trade. An alternative option for the exporters would be sacrificing the privileges of the RTAs (tariff reduction) or even saving the whole effort and concentrating their production on the local market in order to avoid the complications of the RoO, which has a negative effect on international trade.

The RoO problem can to a great extent be regarded as an independent concern in each separate RTA, since in many cases, the inputs originate in countries other than the countries of the three RTAs, such as Asian countries, and hence, it is to a lesser extent an overlapping problem between these particular three RTAs.

All in all, and within the 20 most significant Egyptian exports within each RTA, most of the RoO problems in Egypt could be manageable by increasing the inputs originating in Egypt. Evidently, this would not be for free, as input substitution needs money, time and relevant experience.

Apart from the problems that could face Egypt while implementing the RoO of GAFTA, the latter RTA is a special case; the new suggested GAFTA protocol for RoO is indeed almost identical to the one adopted by Euro-Med, but the Arab countries disagree on many items in it, and therefore, the protocol has not been signed to date. In fact, the analysis run in this study was based on the assumption that Egypt would apply the suggested protocol. But assuming that this would not be the case, then applying the simple GAFTA RoO could contradict more with the RoO of Euro-Med and hence be more problematic.

Even if we assume that all the GAFTA countries would establish FTAs with the EU, using the same RoO of Euro-Med, and hereby solving the RoO problem within GAFTA, the problem of the COMESA RoO would remain unsolved, since if the latter would contradict with the RoO of GAFTA and Euro-Med, the Egyptian exporters would fall in the overlapping mess.

A look into the future

The analysis above shows that, economically, both GAFTA and COMESA could be promising Agreements, if the concerned countries would improve the institutions deeply rooted in their economies. This does not necessarily need a miracle, but rather time and a proper strategy, since the experience of the EU proves that achieving an Economic and even Currency Union is possible, let alone an FTA. An essential issue is strengthening the linkages between the different countries. These include - among others - the availability of market information and also the improvement of the transportation between countries.

Fulfilling deep integration by harmonizing the domestic policies of the members of the different RTAs could also help more in improving the institutions existing in these countries including Egypt. It must be mentioned, however, that deep integration does not automatically lead to more free trade on global basis or improve the members' welfare; on the contrary, harmonization may be on wrong policies, which would in turn reduce welfare[102]. Moreover, the harmonization of policies and regulations might result in the loss of national autonomy on domestic policies,

[102] Lawrence (1997).

carrying negative consequences to some members, especially the developing countries. Thus, it would make sense to make a balance between shallow and deep integration, leading to a compromise that would benefit all the member countries as much as possible.

Signing RTAs in Egypt is often and mistakenly regarded as a rather political end in its own. Nonetheless, it should be considered a start for penetrating global markets. In order to carry out the latter, Egypt should be able to export high quality and low price products to these markets. As long as efficient institutions are missing, it is hard to fulfill this end. As mentioned before, the exporters mangle the export-oriented mentality. They should not only focus on the production suitable for them but suitable for the external markets they target with their production (outward orientation) with the help of the commercial delegations abroad. It is essential for them to realize that in order to make profits they first need to arrange campaigns for marketing their products abroad and send there professional representatives of their companies. This is costly in the short run, but it establishes their markets abroad and increases their returns in the long run. And once they have settled, they should not change their businesses but strengthen and even improve their markets abroad in order to maintain the good reputation. All this needs knowledge and public awareness. Therefore, it could be useful for Egypt not only to rely on the traditional ministries of industry and trade, but establish additional powerful bodies that complement their jobs and duties. These bodies can either be public or private. In addition, the Egyptian Federation of Industries - which is still week in this regard - can play an important role in creating a sound environment for industry and trade. The private sector - where there are stronger incentives - could take the lead, while the government could still act as an important regulator; Self Regulatory Organizations that exist in many developed countries could be established in Egypt to monitor and positively influence the markets. Moreover, the Exporting Councils should have a strong role in informing and making the exporters aware of the international standards and the consequences of any cheating and fraud activities.

Moving back to the example of the ‘brown rot’ potatoes consignment, the exporters among themselves should be capable of identifying the exporter(s) who brought their international market in trouble, relying hereby on the monitoring, tracing, enforcement and ‘code of ethics’ system. For instance, the Council of Exporting Agricultural Products, one of the Export Councils established by the Ministry of Industry and Foreign Trade, includes some of the potato exporters. The latter should at least set the rules for hindering a repeated occurrence of such an incidence by positive lobbying activities.

There should be more cooperation between the employees in the Egyptian commercial delegations abroad and the Ministry of Industry and Foreign Trade. Courses should be offered to them in order to improve their knowledge, mindset and qualifications.

It should not be an impossible task to form a data base for all the potential markets in Arab, African and European countries. There should be information channels between all the concerned parties of trade in order to achieve the high level of transparency existing in developed countries. For example, the fact that the Egyptian exporters assure that they still have to have the certificates of origin approved by the concerned embassies or consulates of the importing GAFTA countries and hereby bear high costs, whereas the officials of the Ministry of Foreign Affaires confirm that the compulsory approval has been called off, but approving still takes place due to the ignorance of the importers about the new resolution, this fact in itself is a strong evidence for lack of transparency, unorganized work among the concerned parties and unnecessary waste of resources.

In general, there is a great need of mobilizing the Egyptian investors for investing in freight companies, in order to help the exporters avoid dealing with quotas on board and high charges associated with national or foreign airlines.

The Egyptian government sets certain regulations for exporting manufactured goods, which many Egyptian exporters consider to be complicating the export procedures. Since these exporters have to cope with the stricter EU standards in any case, there should be a harmonization between the European and Egyptian standards. In fact, the EOQS has started such a program, but not all the products had been covered till the date of the interviews (September 2005).

As for Egypt, the common country of the Agreements tackled in the study, there is a great need of a flexible system that enhances the incentives of the business community instead of dampening its motivations. Egypt could make a big use of the fact that it is involved in several RTAs. One experience could positively affect the other. For example, the MEDA which is offered by the EU in the frame of the Egyptian-European Partnership Agreement is an important form of financial and technical assistance. The more Egypt makes use of it, the more it can increase its benefits from the Agreement. Furthermore, this could indirectly be in favor of Egypt's performance within the other RTAs it is part of, since it would help improve the general trade environment in Egypt.

Therefore, MEDA could be regarded as a positive externality. In addition, the Egyptian local producers could take the Chinese enterprises - which are even not part of the signed RTAs - as an example for them; they could merge their small factories and import the machines and inputs used in production in bulk. Hence they could make use of the economies of scale and, on average, their inputs would get much cheaper due to the decrease in average costs. Moreover, Chinese industry experts could be imported in the Egyptian industrial zones in order to benefit from the Chinese experience in that aspect and hereby help in pushing all the Egyptian RTAs towards proper implementation.

On the other hand, Egypt is - and will be - facing the challenge of competing with foreign production; if the local producers are concerned about the competition facing them from the Asian countries which are not part of the RTAs, then their worries should grow by knowing that the tariffs applied on products from countries involved in the RTAs will completely fade away sooner or later, due to the commitments of the RTAs. Therefore, improving the quality of production and increasing its productivity is no longer a matter of choice.

More transparent exchange rates would reduce the uncertainties of the importers and exporters and their transaction costs. The purpose of the export subsidies should be the promotion of high quality export products and not only the increase of foreign currency receipts of the government by asking exporters to exchange the obtained hard currency for the local currency which is the primary condition for receiving such subsidies now.

There is a need of a better long run strategy for collecting taxes; if the government gives the producers space to produce at cheap costs, they would increase their production, employ more labor, the purchasing power would increase, they can even start to be export-oriented, and the probability for the whole economy to benefit would increase. It is also important to strictly monitor and trace the poles of corruption. The customization and automation in the customs and the rest of the authorities dealing with trade issues could also be a key technique for conquering this phenomenon.

If Egypt and the rest of the GAFTA and COMESA countries commit themselves more to the Agreements, the guarantees system will automatically come into effect, and the traders in both sides will feel backed by their governments and will be encouraged to run mutual deals with the traders of the other RTAs.

The Arab and African countries are relatively new in the field of free trade, and they thus still cannot fully grasp the real concept of 'liberalization'. Therefore, even though GAFTA and COMESA apparently open the door for free trade, the importers and exporters of the two RTAs are squeezed by the different sorts of NTBs and the administrative and bureaucratic problems. When the institutional problems are deeply rooted, then it takes time for the countries to adapt to new systems and accept and implement the reforms.

The bureaucracy existing in Egypt and many other GAFTA and COMESA members is a matter of cultural and historical process that accumulated over the years and became part of their political and economic systems. For example, the common concept of the Egyptian bureaucratic system is to detain the people and their activities instead of encouraging them and giving them incentives. Therefore, changing this mind set needs radical actions, such as intensively creating a public awareness against bureaucracy and red tape, punishment in the cases of exaggerating or abusing the concept of 'bureaucracy' and reward in the case of facilitating the course of productive and legal activities, taking into consideration that these actions could only pay off in the medium if not long run, since as mentioned above, it is a matter of a long process and accumulation.

In general terms, Egypt's performance is better when it deals with the EU countries in contrast to its performance with GAFTA and COMESA countries. This could be referred to the weak institutions existing in the Arab and African countries as compared to the EU countries and, therefore, there should be a reason for Egypt to apply what it learns from the EU on its deals with GAFTA and COMESA. For example, Egypt's trade size with the EU is the largest. However, this could be referred to the sound institutions existing in the EU and missing in the countries of the other RTAs. If these institutions are improved, given the good economic incentives, the implementation of the other RTAs could be successful and flows between Egypt on one hand and Arab and African countries on the other could boost.

It is observable from the analysis that almost every Arab country would prefer to export to the other Arab countries rather than to the EU countries, since the standards that the latter set for importation are higher than the capabilities of the Arab producers and exporters. However, the same Arab country would prefer to import from the EU countries, mainly due to the better institutions existing in these countries, which would guarantee the high quality and timeliness of

providing the goods, in addition to the more different production structures as compared to the Arab countries. This pattern has also been proven by the gravity regressions run in *Chapter 5* where it was found out that the institutions existing in the exporting countries matter more than the institutions existing in the importing countries when deals take place. This means that the Arab countries - as importers - hope to benefit from these good institutions existing in most of the EU countries, but at the same time - as exporters to the EU - they fail to be adequate to applying these institutions. Consequently, their product quality does not comply with the quality required by the EU countries, and they prefer to export to other Arab countries which in turn prefer the European imports, leading hereby to this vicious circle. For solving this problem the Arab countries need to improve the quality of their existing institutions - as mentioned above - and/or follow the *Viner* (1950) and *Salvatore* (1998) model (*Chapter 3*) of trade creation by making use of the similar production structures and diversifying and specializing within the similar good that they produce, which could create the economies of scale and lead to a cheaper joint production and increase the competitiveness of the Arab producers as one block towards the rest of the world. Again, this requires lots of information about all the countries of the RTA.

Although it has similar institutions to them, Egypt does not have the reason to be protective towards the imports from GAFTA and COMESA countries, since it possesses one of the greatest industrial bases in the two regions. At the same time, many of the GAFTA countries are committed to other Agreements with the EU, which is a stronger trade partner than Egypt. Hence, they principally do not have a strong reason to close their doors towards the Egyptian products either.

Since the Egyptian product standards and quality are very hard to accept by the EU countries, but can more easily be accepted by the African countries, Egypt should be able to benefit more from the trade with COMESA countries because it mainly imports raw materials from them and exports manufactured products, where the latter do not face the high standard requirements existing in the EU markets.

The COMESA countries need to have their transportation and infrastructure problems solved in order to facilitate the trade with Egypt. By helping them to solve these problems, Egypt could make benefits, since Egypt has a comparative advantage in the field of construction and can accordingly run procurements for developing their infrastructure. In this case, Egypt would get a double benefit; it would firstly benefit from the construction activities in the rest of the COMESA

countries and secondly widen the exports market of its manufactured products in these countries which are mainly providers of raw materials. In other words, Egypt could apply the European-Egyptian model, where the EU countries assist Egypt financially and in construction activities, and at the same time open up a huge export market.

There is a sea route that connects Egypt with some COMESA countries. It also connects East African countries with each other and is extended to Lusaka, Nigeria. When this route came into effect, the demand on it was weak, but now the demand has increased and this route reached the break even in its operations. For example, it covers Egypt, Kenya, Nigeria and Tanzania, which are not all COMESA countries.

The strongest economies in Africa are the following by order: South Africa, Egypt and Nigeria. There should be an Egyptian strategy to intensify the trade with these two poles of development in Africa, although they do not belong to COMESA, but through them, Egypt can find its outlets to the rest of COMESA countries.

Although many of the African countries in general and COMESA countries in particular are landlocked, there are harbors in Djibouti (Djibouti), Mombassa (Kenya), Darussalam (Tanzania), Antananarivo (Madagascar) and Dakar (Senegal). Each harbor serves for a number of countries. By having access to these harbors, many possibilities for trade with African COMESA and non-COMESA countries could be opened up. This means that the landlocked factor should no longer be a hindrance on the way of trade especially that this factor proved to be insignificant in the gravity regressions run in *Chapter 5* of this study.

Regarding the GAFTA-RoO problem, negotiations between GAFTA countries on sectoral basis could be very useful. The Arab Federations of Industries should get together in order to agree on a comprehensive protocol on RoO. For instance, they should be able to decide whether a garment produced with Taiwanese textiles confers origin. If this is the case, then the probability of many Arab factories changing their activities from producing textiles to producing ready made garments would increase. However, many countries such as Egypt, Syria and Morocco might disagree, since they are already specialized in producing textiles. In fact, when the Egyptian textile producers and exporters just heard a rumor about the possibility of bringing up such an issue, they were fully against it, since it obviously clashes with their interests. On the other hand Jordan might agree, since producers of this country are not the best in this field. In any case, a

compromise has to be reached. Therefore, the ministerial GAFTA meetings need to be more frequent, intensive and active.

According to one of the interviewed Ministry of Trade officials, a reason for the EU customs not being strict about the RoO could be the fact that the Euro-Med RoO were formulated mainly according to the requirements of the EU industries. Hence, the main purpose was for the EU products to find a way to enter the Mediterranean markets rather than the opposite case. And therefore, there might not be a strong reason for them to strictly control the Mediterranean imports, as long as the volume of these imports is modest as compared to the exports. Nevertheless, the Egyptian exporters should not take this flexibility for granted and keep relying on it. And even if it would be guaranteed that the EU will not be strict in applying the RoO, there is no guarantee that COMESA and GAFTA countries will be as flexible, too. Therefore, the Egyptian customs authority is in need of well-trained and informed personnel for dealing with the RoO in the case of imported as well as exported products.

One option for solving the overlapping problem could be the countries of GAFTA and COMESA signing Agreements with the EU countries - as one block - like it is the case in the Partnership Agreements between a number of separate Mediterranean countries and the EU. In this case the RoO could be unified and the overlapping problems could be overcome to a great extent. Since at least 40 percent of the Egyptian exports already go to the EU countries, and the countries of the two other RTAs trade in general more with the EU countries than trading among themselves, then the adoption of the Euro-Med RoO in GAFTA and COMESA could be a good way for facilitating trade between countries and avoiding complexities in implementation. The optimal option would certainly be establishing a broader RTA between all the countries of these three RTAs in the long run, moving hereby closer towards multilateralism. However, achieving this broad RTA is not as simple as it might sound, especially that managing each RTA separately already has its own problems.

It is also worth mentioning that the Arab and African countries are still receivers in the international market; they are not in a situation where they can impose their conditions. For example, the Egyptian industry is mainly based on direct ‘piece orders’ and consignments from other countries, including the EU. The Egyptian exporters are not yet well represented in exhibitions abroad and do not use the concept of mass production, where the importers adapt to their conditions. Therefore, they are incapable of imposing their own conditions, concerning the

inputs used….etc. Hence, following the Euro-Med RoO could be a good start for them to be more involved and well-represented in international markets.

An important advantage of following the Euro-Med RoO is the fact that it is based on detailed, clear and concrete tariff line definitions; although the value added concept that is used so far in the GAFTA RoO sounds simple, it is quite hard to measure, especially when the exchange rates change frequently, and when it is hard to calculate the value of labor used in the production. This problem gets more sophisticated in the cases of the informal sector and child labor.

Obviously, the question 'with whom did Egypt sign the RTAs' is not as important as the question 'how do the institutions in Egypt work and how can Egypt improve these institutions'. By solving the institutional problems Egypt can handle the real challenge it is - and will be - facing in order to make the best out of its RTAs.

APPENDIX I

List of Bilateral Arab Preferential Trade Agreements concluded between Egypt and a number of Arab Countries

Libya: The Agreement was signed in 1990, for a period of 5 years, to be renewed automatically unless else notified. This Agreement entered into force on 18/06/1991.

Syria: The Agreement was signed in 1990, for a period of one year, to be renewed automatically unless else is notified. This Agreement entered into force on 01/12/1991.

Tunisia: The Agreement was signed in 1998 with no specified time limit unless else is notified. This Agreement entered into force on 15/03/1999.

Morocco: The Agreement was signed in 1998 with no specified time limit unless else is notified. This Agreement entered into force on 28/04/1999

Lebanon: The Agreement was signed in 1998 with no specified time limit unless else is notified. This Agreement entered into force on 15/03/1999

Jordan: The Agreement was signed in 1998 with no specified time limit unless else is notified. This Agreement entered into force on 21/12/1998.

Iraq: The Agreement was signed in 2001 with no specified time limit unless else is notified. This Agreement entered into force on 08/07/2001.

APPENDIX II

Table (A)
Number of goods having RCA in Egypt and in the partner countries

Country	Number of common goods where Egypt and the concerned country have RCA
Bahrain	11
Iraq	1
Jordan	14
Kuwait	4
Lebanon	22
Libya	5
Morocco	21
Oman	3
Qatar	5
Saudi Arabia	4
Sudan	11
Syria	15
Tunisia	15
United Arab Emirates	10
Yemen	5
Angola	2
Burundi	4
Comoros	5
Congo (Democratic Republic of)	2
Djibouti	14
Eritrea	15
Ethiopia	12
Kenya	14
Madagascar	18
Malawi	11
Mauritius	11
Rwanda	3
Seychelles	6
Uganda	7
Zambia	11
Zimbabwe	22
Algeria	5
Austria	13
Belgium and Luxembourg	20
Cyprus	15
Czech Republic	17
Denmark	10
Estonia	14
Finland	6
France	18
Germany	9
Greece	26
Hungary	12

Ireland	3
Israel	14
Italy	20
Latvia	19
Lithuania	24
Malta	3
Netherlands	19
Poland	24
Portugal	21
Slovakia	21
Slovania	15
Spain	23
Sweden	6
Turkey	26
United Kingdom	9
Minimum value	***1***
Maximum value	***26***
Mean	***12.328***
Median	***12***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table (B)

Correlation coefficients between the adjusted RCA index of Egypt and that of each other country

Country	Correlation coefficient between Adj. RCA index of Egypt and that of other countries
Bahrain	0.3433771
Iraq	0.1541142
Jordan	0.364551
Kuwait	0.2105459
Lebanon	0.4163299
Libya	0.2780089
Morocco	0.4328484
Oman	0.2441518
Qatar	0.1568432
Saudi Arabia	0.194415
Sudan	0.3101455
Syria	0.572122
Tunisia	0.4060961
United Arab Emirates	0.3781809
Yemen	0.2128603
Angola	0.1032572
Burundi	0.0601067
Comoros	0.0529863
Congo (DR)	-0.0475817
Djibouti	0.1836367
Eritrea	0.1962783
Ethiopia	0.2488923
Kenya	0.3484812
Madagascar	0.4424426
Malawi	0.3817834
Mauritius	0.273978
Rwanda	0.0705498
Seychelles	0.0917837
Uganda	0.1455947
Zambia	0.2467344
Zimbabwe	0.4308707
Algeria	0.2065
Austria	-0.0458146
Belgium and Luxembourg	0.0840581
Cyprus	0.3374288
Czech Republic	0.0829524
Denmark	-0.0097989
Estonia	0.2193237
Finland	-0.1598336
France	-0.00565
Germany	-0.1843055
Greece	0.4688536

Hungary	0.1036196
Ireland	-0.089241
Israel	0.2023515
Italy	0.0900692
Latvia	0.3327036
Lithuania	0.3339744
Malta	0.129329
Netherlands	0.0975302
Poland	0.2295766
Portugal	0.2335385
Slovakia	0.1575446
Slovenia	0.0565211
Spain	0.1164912
Sweden	-0.1924951
Turkey	0.4293941
United Kingdom	-0.1118101
Minimum value	***-0.192495138***
Maximum value	***0.572121952***
Mean	***0.189951648***
Median	***0.199314943***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table (C)

Correlation coefficients between the dummy RCA index of Egypt and that of each other country

Country	Correlation coefficient between the RCA dummy index of Egypt and that of other countries
Bahrain	0.237766
Iraq	0.129303
Jordan	0.189664
Kuwait	0.138966
Lebanon	0.278574
Libya	0.19703
Morocco	0.344794
Oman	0.09874
Qatar	0.139099
Saudi Arabia	0.103885
Sudan	0.26338
Syria	0.470744
Tunisia	0.262933
United Arab Emirates	0.1253
Yemen	0.123865
Angola	0.097424
Burundi	0.042521
Comoros	0.097322
Congo (DR)	-0.028131
Djibouti	0.126138
Eritrea	0.226869
Ethiopia	0.227353
Kenya	0.251392
Madagascar	0.35494
Malawi	0.277361
Mauritius	0.237766
Rwanda	0.039415
Seychelles	0.171691
Uganda	0.12293
Zambia	0.193812
Zimbabwe	0.381359
Algeria	0.175147
Austria	-0.113482
Belgium and Luxembourg	0.006752
Cyprus	0.127311

Czech Republic	-0.005918
Denmark	-0.170115
Estonia	0.139134
Finland	-0.129372
France	-0.056651
Germany	-0.24646
Greece	0.257109
Hungary	0.013535
Ireland	-0.109822
Israel	0.139134
Italy	0.006752
Latvia	0.324685
Lithuania	0.294305
Malta	-0.0315
Netherlands	0.006901
Poland	0.127706
Portugal	0.19787
Slovakia	0.192141
Slovenia	-0.01038
Spain	0.070455
Sweden	-0.169479
Turkey	0.297713
United Kingdom	-0.160358
Minimum Value	***-0.24646***
Maximum Value	***0.470744***
Mean	***0.122368***
Median	***0.128504***

Source: Researcher's calculations from World Bank *Trade CAN* 2002

Table (D)
Weighted average tariffs of the member countries in the four Agreements

(Figures are in percent and in the year 2002)

Country	**Weighted average tariff**
Bahrain	7.7
Iraq	5
Jordan	11.3
Kuwait	3.6
Lebanon	8
Libya	15.9
Morocco	28.2
Oman	6.7
Palestine	8.5
Qatar	4.2
Saudi Arabia	10.5
Sudan	4.4
Syria	35
Tunisia	27.4
United Arab Emirates	4
Yemen	12.6
Angola	10
Burundi	23.5
Comoros	38.9
Congo	15.6
Djibouti	21
Ethiopia	16.5
Kenya	14.4
Madagascar	2.9
Malawi	12.5
Mauritius	15.8
Rwanda	6.6
Seychelles	28.3
Swaziland	3.6
Uganda	6.8
Zambia	8.4
Zimbabwe	12
Algeria	15.3

Austria	2.4
Belgium	2.4
Cyprus	2.4
Czech Republic	4.1
Denmark	2.4
Estonia	0.053
Finland	2.4
France	2.4
Germany	2.4
Greece	2.4
Hungary	7.5
Ireland	2.4
Israel	4
Italy	2.4
Latvia	2.5
Lithuania	0.5
Luxembourg	2.4
Malta	2.4
Netherlands	2.4
Poland	2.9
Portugal	2.4
Slovakia	6.1
Slovenia	1.59
Spain	2.4
Sweden	2.4
Turkey	4.5
United Kingdom	2.4
Minimum weighted average tariff	***0.053***
Maximum weighted average tariff	***35***
Mean	***8.148186***
Median	***4.4***

Source: Researcher's calculations based on data from the Index of Economic Freedom 2005.

Table (E)
Historical and cultural factors in GAFTA

(Unity is given if there is a common factor and zero if this common factor does not exist)

	Common border with Egypt	Common official language with Egypt	Common ethical/spoken language(s) with Egypt	Colonized by or colonized Egypt	Colonized by a common colonizer like Egypt	Common dominant religion
Bahrain	0	1	1	0	1	1
Iraq	0	1	1	0	1	1
Jordan	0	1	1	0	1	1
Kuwait	0	1	1	0	1	1
Lebanon	0	1	1	0	0	1
Libya	1	1	1	0	1	1
Morocco	0	1	1	0	0	1
Oman	0	1	1	0	0	1
Palestine	1	1	1	0	1	1
Qatar	0	1	1	0	1	1
Saudi Arabia	0	1	1	0	0	1
Sudan	1	1	1	1	1	1
Syrian Arab Republic	0	1	1	0	1	1
Tunisia	0	1	1	0	1	1
United Arab Emirates	0	1	1	0	1	1
Yemen	0	1	1	0	1	1

Source: CEPII 2005

Table (F)
Historical and cultural factors in COMESA

(Unity is given if there is a common factor and zero if this common factor does not exist)

	Common border with Egypt	Common official language with Egypt	Common ethical/spoken language(s) with Egypt	Colonized by or colonized Egypt	Colonized by a common colonizer like Egypt	Common dominant religion
Angola	0	0	0	0	0	0
Burundi	0	0	0	0	0	0
Comoros	0	1	0	0	0	1
Congo (D.R.)	0	0	0	0	0	0
Djibouti	0	1	1	0	0	1
Eritrea	0	0	1	0	1	1
Ethiopia	0	0	0	0	0	1
Kenya	0	0	1	0	1	0
Madagascar	0	0	0	0	0	0
Malawi	0	0	1	0	1	0
Mauritius	0	0	1	0	1	0
Rwanda	0	0	1	0	0	0
Seychelles	0	0	1	0	1	0
Sudan	1	1	1	1	1	1
Swaziland	0	0	0	0	1	0
Uganda	0	0	1	0	1	0
Zambia	0	0	1	0	1	0
Zimbabwe	0	0	1	0	1	0

Source: CEPII 2005

Table (G)
Historical and cultural factors in Euro-Med

(Unity is given if there is a common factor and zero if this common factor does not exist)

	Common border with Egypt	Common official language with Egypt	Common ethical/spoken language(s) with Egypt	Colonized by or colonized Egypt	Colonized by a common colonizer like Egypt	Common dominant religion
Algeria	0	1	1	0	0	1
Austria	0	0	0	0	0	0
Belgium	0	0	0	0	0	0
Cyprus	0	0	0	0	1	0
Czech Republic	0	0	0	0	0	0
Denmark	0	0	0	0	0	0
Estonia	0	0	0	0	0	0
Finland	0	0	0	0	0	0
France	0	0	0	0	0	0
Germany	0	0	0	0	0	0
Greece	0	0	0	0	1	0
Hungary	0	0	0	0	0	0
Ireland	0	0	1	0	1	0
Israel	1	0	1	0	0	0
Italy	0	0	0	0	0	0
Jordan	0	1	1	0	1	1
Lativa	0	0	0	0	0	0
Lebanon	0	1	1	0	0	1
Lithuania	0	0	0	0	0	0
Luxembourg	0	0	0	0	0	0
Malta	0	0	1	0	1	0
Morocco	0	1	1	0	0	1
Netherlands	0	0	0	0	0	0
Palestine	1	1	1	0	1	1
Poland	0	0	0	0	0	0
Portugal	0	0	0	0	0	0
Slovakia	0	0	0	0	0	0
Slovenia	0	0	0	0	0	0
Spain	0	0	0	0	0	0
Sweden	0	0	0	0	0	0
Syria	0	1	1	0	1	1
Tunisia	0	1	1	0	1	1
Turkey	0	0	0	1	0	1
United Kingdom	0	0	1	1	0	0

Source: CEPII 2005

Table (H)
Historical and cultural factors in Aghadir

(Unity is given if there is a common factor and zero if this common factor does not exist)

	Common border with Egypt	Common official language with Egypt	Common ethical/spoken language(s) with Egypt	Colonized by or colonized Egypt	Colonized by a common colonizer like Egypt	Common dominant religion
Jordan	0	1	1	0	1	1
Morocco	0	1	1	0	0	1
Tunisia	0	1	1	0	1	1

Source: CEPII 2005

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