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Economic Liberalism between Theory and Practice

by

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**Abstract**

Alfred Tovias argues that the EU's efforts to promote economic liberalization in the southern Mediterranean rely on the principles and instruments of economic liberalism within the so-called "second basket" of the Euro-Mediterranean Partnership. This paper focuses on the contradictions between the EMP's underpinning principle of economic liberalism, upheld by the EU on a theoretical and declaratory level, and both the methods suggested to achieve this principle and the EU's conduct of the economic dimension of the EMP in practice. The author argues that the EMP's economic component cannot attain its own declared objectives, namely the stabilization and growth of Arab Mediterranean economies. This is because the EMP's economic strategies do not lead to real economic integration of southern Mediterranean states into the European economy. In the absence of reforms of the EMP's economic tools, the author is dubious of their success. The full implementation of the Euro-Mediterranean free trade agreements will be the acid test of the economic rationale of the EMP and its initiators.

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## **ECONOMIC LIBERALISM BETWEEN THEORY AND PRACTICE**

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### **1. Declared objectives and principles of the Euro-Mediterranean Partnership in the economic realm**

As is well documented, it is because of the poor record of Maghreb and Mashrek countries combined with the demographic trends and the economic imbalances between the southern and northern shores of the Mediterranean that the European Commission, pushed along by its Southern European members highly concerned by all this, decided to launch a new initiative in late 1994, known as the Euro-Mediterranean Partnership (EMP), formally inaugurated in Barcelona in late November 1995. Note that it was a European initiative, not one made by the Mediterranean Non Member Countries (MNMCS heretofore). In the back of their minds, European policy-makers, mainly from Southern Europe, were quite impressed by what was perceived as the concrete translation of some of these imbalances in Northern Africa in the early 1990s, such as the sudden and violent developments in Algeria as well as the quite unexpected arrival of “boat people” from Morocco to the Southern coasts of Spain (i.e. the then new phenomenon of the “pateras”).

These economic circumstances explain that for the European architects of the EMP, its heart lied in its economic programme (or “basket” in the EMP jargon). The leading idea was to create an “area of shared prosperity” by promoting economic stability, followed

by growth in Northern Africa and the Eastern Mediterranean. Two guiding principles seem to have been behind: First the economic situation in that region had to improve in such a way as to deter as much as possible desperate and/or frustrated people from migrating North. Second, the way to improve the economic lot of the South was by “anchoring”, an idea taken from Bretton Woods institutions, with two possible meanings for the same principle: a) the deepening of the existing levels of asymmetric economic interdependence between the economic hegemon, namely the EU and each individual MNMC; b) shoring up efforts made by local MNMC governments to modernize their economies (in the Washington Consensus jargon “anchoring economic reforms”)<sup>1</sup>. This paper will discuss the contradiction between the liberal guiding principles of the Partnership just mentioned (on a theoretical and declaratory level) and the methods suggested to achieve these principles. This approach is in tune with the theoretical framework developed by Adler and Crawford in the introductory chapter to this book.

## 2. The economic tools suggested by the architects of the EMP

The main economic instruments by which the objectives and principles were to be achieved were 1) the creation of a Euro-Mediterranean Free Trade Area to be completed by about 2010; and 2) a substantial increase of the financial assistance given by the EU, drawn on the Community's own budgetary resources<sup>2</sup>.

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<sup>1</sup> The literature on external anchors is extensive particularly in relation to macroeconomic policy of developing countries. See e.g. recent contributions by Gros (2001) and Dollar and Svensson (2000). On anchoring reforms in MNMCs see Francois (1997), and Galal and Hoekman (1997).

<sup>2</sup> For early assessments of the economic basket of the EMP see Marks (1996), Alonso-Gamo et al. (1997), Aghrout and Alexander (1997), Havrylyshyn, O. (1997), Lawrence (1997), and Galal and Hoekman (1997).

To start with the second item, in practice the EC's Council of Ministers approved in 1996 a new EC Regulation called MEDA (Mesures d'Accompagnement) dealing with all the Mediterranean Non Member Countries (MNMCS) under a unified framework which had to deal with all cooperation activities on a multi-annual basis (see Philippart, 2001; Guggenbuhl and Theelen, 2000; Mira Salama 2002). Roughly speaking, slightly less than one billion Euros per year drawn from the EU's own budgetary resources were to be distributed on a bilateral basis among 8 of the 12 MNMCS, all of them belonging to the Arab world (namely 3 Maghreb and 5 Mashrek countries, including the Palestinian Authority). Turkey, Cyprus and Malta, all three candidate countries, although also beneficiaries of some MEDA funds, were to receive much pre-accession aid through other channels, whereas Israel was not supposed to receive any bilateral aid from the EU, in view of its own development level. Therefore when dealing with the EMP's anchoring capability one should really leave aside these 4 countries and focus on the other 8. To the annual one billion Euros of aid drawn from the EU budget, roughly another one was put at the disposal of the same 8 countries by the EIB (European Investment Bank) in the form of loans. In theory, MEDA bilateral amounts are not pre-determined and the concerned MNMCS are competing for the same multi-annual financial resources to be drawn on the EC's budget (e.g. 3435 million Euros for the MEDA I period of 1995 through 1999 or 5350 million Euros for the MEDA II period of 2000-2006).

In the field of trade, the establishment of a Euro-Mediterranean Free Trade Area by 2010 implied in relation to the previous agreements (which were basically in place since the mid-1970s when the first Global Mediterranean Policy of the EC took shape)

to oblige MNMCs, which had not done so already (i.e. Israel and Turkey), giving tariff- and quota-free access to industrial products originating both in the EC and partial liberalization in agricultural products as well. The reason is well known: the EC had already eliminated its own tariffs on practically all industrial imports originating from MNMCs in the late 1970s.

### 3. Effects deriving from the enforcement of the economic tools contained in the EMP initiative

Because of the discriminatory nature of the trade liberalization to be operated by Arab MNMCs and thus the inevitability of trade diversion effects, this author was the first to predict early on that they would benefit from small long-run welfare effects, in some cases negative for instance in the case of Mashrek countries (Tovias, 1997), in spite of the general enthusiasm in the early days of the Barcelona Process illustrated in studies produced by the World Bank (Rutherford et al. 1993, Konan and Maskus, 1997). Later on, however, econometric investigations have corroborated this author's forecast (Dessus and Suwa, 2000: 48; Ghesquiere, 1998).

Therefore what the new programme really meant was that the short-term adjustment effort had to be done mainly by the Arab MNMCs themselves. Some public officials in the Commission declared explicitly from the outset that the idea behind the economic programme contained in the EMP was "to shake up the MNMCs" and that the European role was to be a catalyst and a facilitator of needed change in North Africa and the Eastern Mediterranean. To shake up the manufacturing sectors of Arab Mediterranean countries, the EC wanted to encourage specializations, mergers, company

reorganizations, quality improvements, renewal of equipment, upgrading of management, privatizations, and so on. In other words, short term adjustment and restructuring costs to be borne by Arab Mediterranean countries were part and parcel of the economic basket of the EMP. For conservative, sometimes fossilized, economic and/or political regimes such costs are *per se* destabilizing. The programme meant as well fiscal reform since tariff revenue, an important economic source for governments' budgets in the region, was to be seriously eroded, implying therefore either introducing new taxes or lowering public expenditure (e.g. consumption subsidies). The programme also pointed in the direction of short-run external disequilibria since the trade deficit of the relevant MNMC with the EU was obviously expected to rise (on this see Ghesquiere, 1998).

The main supplementary effort to be made by the EU itself was financial, something favoured by Southern European members ("aid, not trade") over other more daring solutions ("trade, not aid"). To the adjustment efforts asked from the MNMCs, the EU came forward with a financial effort. The EU interpreted this effort both as a "concession" and as a "carrot" for the Arab MNMCs to grab. The idea underlying the economic component of the EMP was to use EU finance to help MNMCs to adjust to the new industrial free trade conditions contemplated in the EMP. The avowed intention of the European Commission was to promote (further) economic reform by inducing target countries to do so with rewards ("carrots") and not sanctions ("sticks"). In political economy terms it reflects a political compromise among the 15 member states, rather than among the 27 members of the EMP. The internal EC compromise consisted in being prepared to increase in relation to past efforts the amount of the bilateral Overseas Development Assistance (ODA) to 8 Arab countries of the Middle East and

North Africa (MENA) sub-region. The term “bilateral” is confusing, because as all ODA it is offered on a unilateral basis. There is no contractual obligation with each of the Arab MNMC to disburse a given amount in their favour. MEDA is an EC regulation, not part of the bilateral association agreements providing for industrial free trade between the EU and the 8 MNMCs under focus. It is important therefore to note that legally speaking the EU “carrots” (MEDA) and the commitment of MNMCs to eliminate their industrial tariffs on EU-originating products are not directly linked. At the most the link is indirect. Even more indirect, if not totally unconnected, is the link between MEDA and performance in “economic reform”. The link can be termed at most “soft conditionality”, if not “very soft conditionality” (Youngs, 2001).

In presenting its EMP initiative in 1994, the EU Commission should also have recognized openly that, apart from the short-term adjustment problems which the MNMCs would endure along the way to implementation, the stabilization of candidates to EU membership (namely Central and Eastern European countries) would contribute to the destabilization of those remaining outside, first and foremost the MNMCs. A clear link has been now established between the announcement of candidates for membership by the EU at the Essen Council in 1994 and subsequent foreign investment inflows into the candidate countries. Not only that. A second wave of foreign direct investment into some Central and Eastern European countries took place after negotiations for membership were announced by the EC in 1997 (Bevan et al., 2001; see also Tovas, 1994). What seems clear is that some of those capital flows are investments diverted away from other potential destinations in the EU’s periphery such as MNMCs (what economists call “investment diversion”), although it seems other areas of the world have been more affected by this effect (Tovas, 2000). In fact,



whether one likes it or not, if one thinks for a moment, already a previous enlargement of the EC (namely the Southern one) implied that the stabilization of three new Northern Mediterranean democracies (namely, Spain, Greece and Portugal) was obtained partly at the expense of the economic stability of Southern and Eastern Mediterranean non-members (e.g. through trade diversion, in the case of Morocco's citrus and tomato exports to the EU). This destabilizing effect would reproduce itself, as we are witnessing since the second half of the 1990s. In recognizing this fact, the EU would have been obliged to re-think its current Partnership strategies, which clearly have not been able to counteract investment and trade diversion in favour of past and future member states.

#### 4. Compatibility of the objectives with the tools

From the above, it is obvious that the economic component of the EMP was flawed from its inception, because the implementation of the programme could not possibly lead to the achievement of the objectives indicated above.

Take first the objective of creating a "zone of stability" around the Mediterranean including in the economic realm. How could the shaking up of the North African economies lead possibly to economic stability? How could the expected increase in the trade deficit of these countries lead possibly to their economic stabilization? Would not the introduction of consumer taxes to replace for lost customs duties lead possibly to a revolt of consumers and small businesses? How could stability in the EU's Southern periphery be attained if in parallel the EU intended to work full speed for the economic and political integration of its Eastern periphery using much more potent tools than the ones to be used in the context of the EMP?

Second, achieving a “shared prosperity” between the EU and the MNMCs does not seem possible without “shared efforts”. But, as implied from what was said above, the adjustment effort deriving from a correct implementation of the EMP was not meant to be reciprocal. The governments of EU member states did never declare their willingness to give the example and “shake their countries” even a little. Admittedly, on the EU's side, the Commission asked in its initial proposal of October 1994 from the member states a supplementary effort in the agricultural domain but, later on, the Declaration of Barcelona of November 1995, launching the so-called “Barcelona Process”, an outcome of the EMP, did not contemplate free trade in agricultural goods at all, unlike the North American Free Trade Agreement (Telo, 2001: 183) or the proposals made by President Bush shortly after the Iraqi war contemplating the establishment of bilateral Free Trade Agreements (FTAs) between the US and MENA countries (see the Introductory Chapter in this respect). In fact the only reciprocal concessions to be made by the EU in the domain of trade were, first, in terms of eliminating a few remaining restrictions on textile and clothing imports from some of the countries under focus. However this would be done at a time the EU had already previously agreed to phase out all the bilateral deals with other developing countries by 2005 signed in the context of the Multifiber Arrangement, according to what was agreed at the end of the Uruguay Round of Multilateral Trade Negotiations in 1994. The second concession would be in terms of “exploring the possibility” of cumulating value in different MNMCs for the purpose of defining the origin of products benefiting from duty-free treatment in the EU. “Exploring the possibility” is taking surprisingly a lot of time, since cumulation is still not put in place at the time of writing (Spring 2004). Regarding non-tariff barriers in trade between the EC and MNMCs, the Commission

stated from the beginning that it was prepared to engage in constant dialogue with the MNMCs on a wide range of trade- and investment-related matters such as indirect taxation, standards and customs procedures, but future membership in European standard institutions was and has not been ever mentioned.

In theory at least, the fact that the economic component of the EMP was not based on trade reciprocity did not preclude the EU from pretending that the efforts asked from the two sides to the Partnership were “shared”, since the EU was making as explained above a substantial financial disbursement. But can the effort asked from the MNMCs be at all compared with the one asked from the EU? To answer this question the next section focuses on the economic equation as seen from the South.

#### 5. Cost-benefit analysis by MNMCs in Political Economy terms

What were the costs and benefits of the FTAs provided for in the association agreements, as seen by the leadership of MNMC countries? Were the benefits sufficient to sustain the demand for the EU as an anchor? Were the countries to be anchored willing to incur loss of policy autonomy (i.e., “tie their hands”, using a commonly-used expression)?

For the leaders of the 8 MENA countries under focus the short-term benefit of the EMP, in political economy terms, was obviously the increased ODA from the EU in the form of MEDA grants and EIB loans and not the long-term benefits of the economic reform, which the EU said it wanted to “anchor”<sup>3</sup>. In fact for the non-democratic regimes of

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<sup>3</sup> A much more cynical interpretation of the EU’s intentions is also mentioned in the literature on the subject: 1) the EU had to re-equilibrate its external relations, too much tilting towards Eastern Europe in the early 1990s; 2) the EU had agreed with the

North Africa and the Middle East, economic reform is perceived as a cost, not as a benefit. Assuming this, the link between the expected benefits and expected costs for the governments of the MNMCs is only indirect, therefore uncertain. It could well be that they implement the trade liberalization steps to which they are committed according to strict timetables inscribed in the association agreements. Nothing guarantees them that the increased ODA will materialize. There is an asymmetry in conditionality. Whereas the EU can condition its increased ODA to implementation of the association agreement, the MNMC cannot condition implementing the tariff liberalization programme to previous MEDA disbursements or concession of EIB loans<sup>4</sup>. There is also time inconsistency since the MEDA calendars are administratively linked to the overall multi-annual financial programmes (so-called “Perspectives”) of the EU, which are formally and organically unconnected to the timetables provided for in the bilateral association agreements. Not only this. Being a “good domestic reformer” does not translate in more MEDA funding down the line later.

As for the economic “benefits” of the EMP as perceived by the political leaders of the MNMCs, can MEDA (admittedly a more than two-fold increase in ODA funding in relation to the EU’s own previous efforts) make a difference and have some real impact on the economic situation of Arab MNMCs? This is the assumption of many policy-makers in the EU. But is that so? It is easy to show that the amounts of aid

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US also in that period that discriminatory trade agreements they signed with third countries should take the form of Free Trade Areas to conform with World Trade Organization (WTO) rules and thus prevent (more) friction between the two trade superpowers; 3) increasing the EC’s market share in the 8 countries under focus; 4) filling the vacuum left in the Mediterranean by the collapse of the Soviet Union. On WTO rules and the EU see Messerlin (1999).

<sup>4</sup> Flaesch-Mougin (2001), p.86 says that “financial advantages of MEDA I have not been linked to the formal conclusion of the (association) agreement, but to the progress made with a view to this conclusion....”

needed to extract Maghreb, Mashrek countries as well as Turkey from their current predicament are both staggering and unavailable. But clearly, there is no political will in the EU to have the equivalent of the Marshall Plan for these countries. Some numbers: Using 1999 as a benchmark, the EU had committed itself to distribute to each of the citizens of the 9 relevant MNMCs (representing with Turkey included a population of 224 million people) about 9 Euros per year, half of it in the form of loans from the EIB, although in practice the amounts actually disbursed were much less than that mainly for administrative reasons. But even if the aid programs are streamlined, as was the case for MEDA II (stretching from 2000 to 2006), it is a view of the spirit that 9 Euros per year per capita can be instrumental in reforming or transforming economic reality. The argument heard in the EU whereby MEDA can be interpreted as “seed money” to function as a “signal” to foreign investors who will bring afterwards the “real money” is clearly far-fetched if one goes by the amounts allotted by MEDA just mentioned. As a point of reference, the US is transferring each year 2.2 billion US\$ (i.e. 2 billion Euros) to Egypt alone since 1979, just enough to keep the country afloat with no major effect in drawing massive inward foreign direct investment.

Of course, seen from an MNMC leader’s perspective, “little money” is better than none at all, particularly in the short run, to cover, even if only partially, increasing budget deficits. As indicated above, the implementation of the association agreements (i.e. the industrial free trade areas) is likely to increase the budget deficits in the short run at least for two reasons: 1) tariff revenue is going to be slowly eroded over a period of 12 years, the time allotted for the creation of full-fledged Free Trade Areas; 2) short-run unemployment in import-competing industries will necessarily rise as a

result of the implementation of the different tariff cuts applied on EU-originating exports. Clearly, any MNMC technocrat but also political leader understands perfectly well that MEDA is not there to create jobs or new incomes. The latter could only be expected in the short run by having the EU revamp its trade policies. This in turn would attract foreign investors, which is what is lacking.

What about the costs in political economy terms for the MNMC political leader? First, there is the issue of replacing fiscal revenue lost by the creation of a Free Trade Area with the EU. The leaders of MNMCs see this as a nuisance cost. Another nuisance is that contingent protection is not tackled really in the association agreements. How are these two costs perceived from the South?

Regarding the short-run costs to be borne by the MNMC, the only thing that seems to be amenable to fairly clear *a priori* evaluation is the amount of fiscal revenue to be foregone as a result of the elimination of customs duties on goods originating in the EU. As well known this is an important issue particularly for Lebanon (29 per cent of total tax revenues, 3.3 per cent of GDP) and Tunisia (16 per cent and 3.2 per cent of GDP), but also so for all remaining Arab MNMCs (Nienhaus, 1999: 509). There are some empirical studies produced by international institutions such as the World Bank, the IMF or some NGOs and academic independent researchers evaluating the trade, employment and welfare effects of the association agreements (see e.g. FEMISE, 2000; Ghesquiere, 1998; Havrylyshyn, 1997). What is far more important for the MNMCs leaders but much more difficult to assess are the short run costs and risks for them involved in the implementation of trade and other policy reforms. For instance, how to gauge the risks involved in having to replace customs duties by new

taxes, such as Value Added Tax (VAT)? How will the business community react to that? What about political parties and the public at large? Evidence from the case of Malta, where the introduction of VAT led to the downfall of the pro-EU conservative government to the benefit of the Labour Party in the mid-1990s, shows what might be at stake. What about cutting instead public expenditure, such as food consumption subsidies? Is that not likely to lead to riots, as was the case in Egypt or Algeria in the past?

On the other hand, although rules on market access to the EU are entirely specified in the association agreement, it is worthwhile mentioning here that contingent protection applied by the EU on MNMC-originating imports is still a possibility. And as is well known the EU has tended in the last decade to use more profusely anti-dumping legislation including on trade originating in MNMCs (e.g. Turkey). Of course it can be argued that this legislation is well known to MNMC economic operators, as well as to their governments at the time the association contract is signed. However it is the way this legislation is implemented which is not so transparent and for many outside observers quite arbitrary. To be fair, experts also indicate that there is a tendency by the European Commission to be more lenient in cases regarding countries with which the EU has a bilateral preferential deal, such as those currently benefiting from the Europe Agreements in Central and Eastern Europe. However it is not clear if this is due to the existence of these agreements or to the fact that those countries are candidates for membership in the EU in the future (see Pelkmans and Brenton, 1999).

#### 6. The impact of 9/11 on the economic component of the EMP

*A priori*, one would be tempted to say that the events of 9/11 should not have had a major impact on the EMP's economic basket, but rather on the other two ones. Clearly the mistrust among some of the 27 participants in the EMP could derail civil society projects launched as part of the third basket programme, as well as the imposition of new entry regulations by the EU for citizens of some MNMCs. There is no doubt as well that the political basket has been affected (e.g. the conclusion of a Stability Charter is even more compromised than it was well before 9/11). On the other hand, there were no reasons to suspend or revise operation of the MEDA aid instrument nor the bilateral free trade agreements between the EU and MNMCs. Indirectly, however, there has been an impact. The economic situation of some MNMCs (such as Egypt, Tunisia, Israel and Morocco) has deteriorated sharply as a result of the crisis of their tourism sectors, very sensitive to the security perceptions of citizens in the OECD area, although this has been compensated partially by an increase in intra-Arab countries tourism flows. The little foreign investment that was flowing before the events of 2001 has all but dried up. As a result it has become more difficult for unpopular governments in the Maghreb and the Mashrek to proceed with economic reform and liberalization. It can be assumed, therefore, that the final date for the achievement of free trade in industrial products will be further postponed by the governments of Arab MNMCs with the passive acquiescence of the EU.

#### 7. How can the discrepancy between objectives and tools be reconciled?

To begin with, to cope with the issue of reciprocity and shared efforts, a much more liberal EU trade policy than now addressed to MNMCs is what is called for. First, short-term adjustment costs deriving from import liberalization are less substantive and therefore more politically acceptable if new export markets develop simultaneously.



After all, reciprocity in trade concessions is what the WTO and GATT multilateral trade negotiations have always been based on. But regarding the new association agreements between the EU and the MENA countries under focus there is no new reciprocity in trade concessions. Second, given the demographic trends in the Maghreb and the Mashrek, there is an urgent need in creating jobs (otherwise unwanted people there will flow to the Northern shores of the Mediterranean or become alienated at home and causing trouble to the local non-democratic regimes). In passing, the assumption here is as for Spain, Greece and Portugal but that democratic reform and transition cannot be engineered from outside but economic reform can (Tovias, 1995). As indicated above, the possibility of anchoring economic reform and promoting growth in Maghreb and Mashrek countries exists. This much is clear to everybody, including policy-makers in the EU.

In terms of policy, it seems obvious that the best contribution of the EU to promote job creation would be to import more from MNMCs goods regarding which they have a comparative advantage. In turn this would induce a reduction in the trade deficit of MNMCs and thus in their external debt as well. Given the relative factor endowments of Southern Mediterranean economies compared to their industrialized neighbours (the EU) and the short distance to the latter, the former have a clear comparative advantage in the production of sun- and labour-intensive goods and services. They should therefore specialize in those products and export them to their developed neighbours (the EU).

Mediterranean agriculture, fishing and tourism services fall all in that category. Tourism is certainly very much job-creating; but as Spain and Italy are well aware since long

time, it is highly seasonal. People working in tourism must find complementary jobs for that time of the year where tourism is in the doldrums. This is where agriculture and fishing enters. It so happens that there is only partial overlap in time between agricultural and fishing activities on the one hand and tourism activities on the other. This is why agriculture or fishing (and not industry, which requires regular presence of the worker at his/her line of production) are well suited to complement tourism in terms of employment. Moreover, Mediterranean agriculture is, compared to other types of agriculture, very much labour-intensive, because fruit, flower, vegetable and wine production require, as Dutch, Spaniards and Italians know, a lot of attention and even affection; it is almost like gardening; this is what traditionally horticulture is about, which by the way was developed to an extreme sophistication by the Arab people themselves in Southern Spain. And for the moment, machines cannot in many instances replace humans yet in separating the right fruit from the bad one. Much of the same applies to fishing.

But any specialization and job-creation through specialization does not work without trade. The full realization of the agricultural and fishing potential of Southern Mediterranean countries requires as a necessary condition easier access to EU markets, which is not possible without some changes in the EU's Common Agricultural Policy and in the Common Fisheries Policy (the so-called "Blue Europe"). A job-creating economic strategy for the Southern Mediterranean countries would certainly require certain adjustments on the part of Northern Mediterranean states, such as France, Italy, Spain and Portugal, ultimately leading to entirely different patterns of division of labour around the Mediterranean. In passing, with appropriate technology transfer, much of current food processing activities operated in the Northern shores of the Mediterranean

could be transferred to the Southern shores. In order to soften the impact on Dutch and Northern Mediterranean farmers, fishermen and food processing manual workers, part of MEDA funds could be devoted to help the latter to adjust to the new situation. It is patently absurd to maintain European markets almost exclusively open to Dutch, Spanish and Italian food producers and then offer adjustment aid to Maghreb countries via MEDA to cope with their adjustment problems derived from the opening of their industrial markets to the EU.

In other words, there should not be anymore an "agricultural exception" in the free trade agreements between Europe and Arab countries, given the income levels attained by the former. What is called "*delocalisation*" in French should be accepted now also for Mediterranean agriculture, fishing and food processing, not only for textiles and travel goods, as already is the case now. MNMCs technocrats, particularly those of Morocco and Egypt, have been all along recent years insistent in asking more agricultural concessions from the EU, to no avail. One of the main reasons for delaying the signature of the Egypt- EU association agreement until 2001 was precisely this.

What about other job- and income-creating initiatives not taken (yet) by the EU? The Free Trade Area initiative launched in the context of the EMP has focused almost exclusively on tariffs. However, for the expansion of trade to be perceived as beneficial for the Mediterranean countries' leaders, it would have been important that the EU's trade liberalization measures would have included phasing out non-tariff barriers as well, since these are nowadays the real impediments to the exports from the southern Mediterranean countries to the EU. But none of the agreements signed until now has provided for the automatic removal of significant technical barriers faced by MNMCs

exports to the EU, such as obligatory testing or certification of conformity by local EU authorities for many goods, because mutual recognition agreements (MRA) are not part of the signed deals. Neither are MRAs on standards. In documents following the 1995 Barcelona Declaration there was some talk of standards harmonization in the future, but in fact the idea has been all along that MNMCs will have to accept the *acquis* as far as standards are concerned. Participation in European standards setting and membership of European standard institutions is out of question, even in the context of the far-more-generous new Wider Europe Initiative of the spring of 2003. This and other second-generation issues are not only important for Israel or Turkey (as one is tempted to think *a priori*), but also for Maghreb and Mashrek countries. Take for instance norms and standards relating to fish canning or relating to fishing methods. It is well known that Portugal, Spain and Morocco compete in the same canning products and in the same markets. Whereas Portugal and Spain are key-decision makers in the EU in these matters, Morocco is not even consulted under the current agreement.

In fact the association agreements that have been signed in the context of the EMP leading to industrial free trade areas must be criticized not because they have been too liberal (as some intellectuals in MENA countries have actually stated), but because they have not been liberal enough. Not only have agricultural tariffs and Non Tariff Barriers reductions as well as industrial Non Tariff Barriers been practically excluded, but also cumulation of origin is not for tomorrow and may enter into force too late to make a difference. Only in 2001 (thus six years after the Barcelona Conference), the Commission accepted in principle that MNMCs be incorporated in the so-called Pan-European cumulation system (which included well before accession all Eastern

European countries, most of which have entered the EU on May 1 2004)<sup>5</sup>. If implemented any time soon this could potentially be a huge bonus for Eastern Mediterranean countries in particular where input complementarities seem more prevalent than in the Maghreb because of the presence of fairly diversified economies such as Israel, Turkey or Egypt with a large industrial base. However cumulation makes sense only insofar as there is a sufficiently high preference margin justifying the time and money to be spent by Mediterranean industrialists in order to comply with (cumulated) rules of origin (e.g. maintaining separate stocks according to their origin, separate accountancy systems, lawyers' fees, etc.). The quite low post-Uruguay Round average Common Customs Tariff of less than 4% is bound to decrease further, should the WTO's Doha Round succeed, something which would further erode the value of any EU concession in the domain of origin rules. The same applies for agriculture. There is some talk of reforming (once again) the CAP in goods of interest to MNMCs but this would be clearly to accommodate the trade interests of the United States and Latin America, not at all those of MNMCs. The EU is actually working for multilateral trade ("Doha Round") and EU-Mercosur negotiations to succeed.

#### 7. How to restore the spirit of Partnership to the economic programme of the Barcelona Process?

It appears that the economic concessions the EU has been prepared to offer to make sense of the idea launched by the European Commission of establishing a "zone of

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<sup>5</sup> This procrastinating behaviour contrasts with the one of the US which has already positively answered to Israel and Jordan for the immediate application of cumulation of origin in Israeli or Jordanian exports benefiting from duty-free access in the US under the FTA treaties signed bilaterally by the US with Israel or Jordan respectively (the last one only signed recently). The US has insisted that these cumulation rules will also apply to any bilateral FTAs with MENA countries (see Adler and Crawford, introductory chapter in this book).

shared prosperity" through a "real Euro-Med Partnership" have been way out insufficient to entice MENA leaders to "tie their hands". In fact the EU has not applied to itself *de facto* the neo-liberal economic practices it has been preaching to its EMP partners in relation to agriculture, non-tariff barriers and cumulation of origin (something that the introductory chapter to this book seems to assume and which should not). The impression is that regarding MNMCs, Europe has been in the last decade in a mood of what musicians call: *Allegro ma non troppo*... Clearly, the way to strengthen the EU's anchoring power is via more trade concessions and not via a supplement of adjustment assistance. The opening of new export markets, not only in terms of sectors but also in terms of seasons, drastically diminishes the short-term adjustment costs for the MNMC and therefore the immediate political costs for the leader of the regime.

Moreover, if the goal of creating a zone of shared prosperity included in the EMP is to have any real meaning or substance and a sense of "ownership" of the Process be instilled to all its 27 participants, it is not sufficient for the EU to oblige the southern Mediterranean countries to proceed with economic reform and trade liberalization by asking them to eliminate tariffs and QRs (quantitative restrictions) on EU originating industrial exports, if there are no adequate rewards. This is even more so as a result of the events of 9/11 and the economic crisis developing in the Southern Mediterranean. Not surprisingly, more recently, the EU's Commission has tried to insufflate some life into the Partnership by working for the extension of the Internal Market in goods, business services and human capital to the MNMCs in the context of the new "Wider Europe Initiative". But even more urgent is to improve the terms of market access in the Euro-Med bilateral agreements, by implementing before becoming useless and irrelevant a system of cumulation of origin rules which would promote regional

economic cooperation among MNMCs, something the Commission has stated since 1995 that it was one of the Partnership objectives. In the medium run, the elimination of tariffs in MNMCs as a result of the implementation of the Free Trade Areas and the ensuing adjustment pressures will increase, not decrease, migration flows from the Southern Mediterranean to the North. The answer will have to come from those in Europe which will realize sooner or later that only by importing more primary and labour-intensive goods from MNMCs can the flow of MNMCs be stopped by peaceful means. There is also a moral dimension, something so important to many Europeans nowadays. “Anchoring” is an activity which consists in “demonstrating” and not in “sermonizing”. What is called for is a “demonstration effect” whereby the EU gives the example, not by telling MNMCs “to do what we ourselves already did”, but rather “to do what we do”, namely adjusting. This could be called the “we-are-in-the-same-boat” effect, reflecting thus better that the EU and MNMC are indeed involved in a “real Partnership”, something frequently questioned by Arab countries, particularly after 9/11.

#### 8. A decision-making structure likely to compromise the economic programme contained in the EMP and the bilateral association agreements

The decision-making procedures related to the Barcelona Process have been awkward and inadequate to cope with the immense tasks it wants to deal with. To begin with, decisions in the EMP are made by consensus, which means that the lowest common denominator tends to prevail. There is no formal voting, therefore no majority voting for the matter. Veto power by any of the 27 EMP members is the rule (Lannon et al., 2001: 117-8). Regarding financial matters, as indicated above, MNMC have no voice.

All is ultimately in the EU's hands. Regarding the association agreements they are inter-governmental, not supranational. This means that voting is inapplicable. Of course as in any reciprocal trade agreement, if one of the parties decides not to proceed with the tariff liberalization programme it is committed to implement by the agreement, the other side can always retaliate by suspending in turn its own "concessions". In the case of the EMP association agreements, a non-compliance of one of the 8 MNMCs with their tariff disarmament programme could lead, e.g., to a re-establishment by the EU of most-favoured-nation duties on imports originating from the violating MNMC. Nobody in the WTO would protest such a move, since such a step would be equivalent to reinstate non-discriminatory treatment for all other previously un-favoured WTO countries.

On a more micro-economic level the question arises to what extent the EU and MNMCs are likely to veto common decisions or impose decisions because of business/interest group lobbying. Here the answer is a little more optimistic overall. Before any EMP ministerial summit, each EMP member country prepares its national position on the different items on the agenda. In the case of the EU the position of the member states is coordinated by the Commission, although it must be stressed that each individual EU member state is represented by its own minister at the EMP bi-annual Summit, which is purely intergovernmental. Each partner in the EMP draws its position on the basis of the so-called national interest which is fashioned by the positions taken by the lobbies directly implicated. There is almost no leeway for the representative of the partner countries to negotiate its position once in the Summit. This is even less likely in the case of EU member states' representatives which not only are unlikely to move even one centimeter for fear of un-bundling finely-tuned compromises arrived at in the EU's



Council of Ministers (e.g. in terms of language to be used in official documents regarding changes in the CAP or in cumulation rules). In fact, the under-lying pressures of the lobbies lead to *de facto* paralysis at the level of the EMP bi-annual Ministerial Summit. This is not so much the case in the context of the annual association councils provided for in the bilateral association agreements. Here the MNMC minister in charge might reach a political deal with the EU representatives, knowing he might be opposed by some lobby back home. He will have to make his mind if he can cope with the pressure exerted by the latter on the government. But here one cannot speak of sheer veto power by lobbies. An example will suffice. The EU has been in conflict with Israel regarding the application of origin rules by the latter which considers the occupied territories since 1967 as part of Israeli customs territory. Therefore goods originating in settlements have been traditionally shipped to the EC duty-free. Lately the EC-EU has decided to strictly apply the association agreement to Israel in its frontiers of June 4 1967. Negotiations to look for a compromise have been stalling for a long period. The Israeli Minister of Industry and Trade has had to negotiate in late 2003 a compromise to enter into force in the year 2004, knowing that business interests in the territories (e.g. Golan wine-makers) or in Israel would strongly oppose it to no avail.

#### 8. Some conclusions

The main obstacles that have precluded the 1995 EMP initiative to act as a possible anchor to economic and (political) reform in MNMCs have been that:

- 1) The “carrots” offered by the EU have not been enough to make it worthwhile for an authoritarian regime in the Maghreb and the Mashrek to “tie its hands” (and the reader should not confuse the technocrats of the regime with its leader).
- 2) The “sacrifice” made by the EU to anchor Maghreb and Mashrek countries has been financial, not “real”. There has not been a “demonstration” effect. There has not been any “we-are-in- the-same-boat” effect.
- 3) The commitments made by the EU have been weak (e.g. exploring an issue for years without formal commitment at the outset) and reversible (e.g. contingent protection as a tool can be invoked by the EU).
- 4) The value of the “carrots” is likely to diminish with time (erosion of preferences by Enlargement, erosion of the value of cumulation of origin rules, etc)<sup>6</sup>.

The economic component of the EMP cannot in a substantial way attain its own declared objectives, namely the stabilization and growth of the Mediterranean Arab economies. The main reason is that the 1995 EMP initiative has not led to real economic integration of MNMCs in the European hub.

It might be that the EMP, as conceived by Brussels, had other than its own declared objectives. If not, then the conclusion is that it was not well conceived. If the EU had other reasons in favour of establishing industrial free trade areas and MEDA, then the question arises whether they still hold a decade after, at the time of writing. If yes, it

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<sup>6</sup> See Brenton (2000) on the increasing irrelevance of the EU’s pyramid of

makes still sense from the EU's perspective to proceed. If not, a thorough revision is what is called for. Some of those "historical" reasons are still valid. For instance, the consensus reached in 1993 between the US and the EU to respect the WTO rules on integration agreements (article 24 of the GATT) still holds, although if present tensions on trade issues between the two transatlantic trade partners do not dissipate soon, the above-mentioned consensus could unravel as well, leaving the EU with a freer hand. What about the perceived need of "rebalancing" the EU's external policies? It seems that progress done since 1994 on Enlargement issues plus the 1999 EU acceptance of Turkey at the Helsinki Summit as a candidate for membership will also diminish the urgency of "rebalancing" in coming years. For once, most countries called that have become members of the EU in 2004 do not have at all relations with MNMCs in their priority agenda (Tovias, 2000). Turkey will be even less enthusiastic then before about the EMP, lest it be considered by the EU as an alternative to membership. Most probably, though, the economic basket of the EMP will prevail as is until the time most Arab MNMCs have to start reducing tariffs on consumer and other final goods imported from the EU, something scheduled to happen only at the end of this decade or later<sup>7</sup>. This will be the acid test both for the EMP and its initiators.

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preference.

<sup>7</sup> Dates of entry into force of the association agreements are 1998 for Tunisia, 2000 for Morocco, 2002 for Jordan. No date is set yet for Egypt, Algeria, Lebanon and Syria. Add to this that immediate tariff cuts are only applied to inputs and intermediate products, all MNMCs having back loaded tariff reduction commitments on what they perceive as sensitive products. And the Free Trade Areas are supposed to be only in place after twelve years. Note that the Palestinian Authority has not (yet)

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