

**HELPING TO IDENTIFY THE  
POTENTIAL AND MODE FOR  
LIBERALIZATION OF TRADE IN  
SERVICES IN THE SOUTHERN  
MEDITERRANEAN COUNTRIES :  
THE CASE OF EGYPT**

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## **Abstract**

The potential of utilizing the liberalization of services for a number of Southern Mediterranean countries is great in a large number of sectors. Nevertheless, the importance of this potential is still not realized by those countries. The liberalization of trade in services has often been relatively neglected by the Southern Mediterranean countries in their trade liberalization efforts whether on unilateral, regional or multilateral levels. This paper aims to identify the comparative advantage of Egypt, as an example of a Southern Mediterranean country liberalizing its trade in services. This is undertaken by emphasizing two aspects: the comparative advantage that Egypt acquires in a number of services and the reduction in the transaction costs that liberalization of services can bring to many sectors of the economy. The paper then goes on to analyze whether Egypt should seek the regional or the multilateral mode. Finally, the paper provides some policy recommendations on which services sectors should be liberalized and whether to build on the comparative advantage or to reduce transaction costs and which mode of liberalization should be adopted.

## 1. Introduction

Liberalization of trade in services has gained great attention lately. The inclusion of services under the auspices of the World Trade Organization (WTO) represented in the General Agreement on Trade in Services (GATS) was a major starting point in this regard. For the first time, there was a general framework which countries could refer to in the liberalization of trade in services, an issue that has been considered non tradable for ages. The introduction of trade in services was a result of pressure from developed countries, particularly the U.S., to utilize their comparative advantage. Developing countries soon realized that they too could benefit from liberalization of trade in services. Hence, they started to liberalize their services' sectors. The Southern Mediterranean countries were also engaged in the liberalization process, at least as part of their obligations in being members of the WTO. This paper mainly addresses two issues: why should developing countries, taking Egypt as an example, liberalize services? And, what mode of liberalization (regional versus multilateral) should countries adopt in their liberalization process? The paper uses Egypt as a model of a developing country, while taking the Egypt-EU Partnership Agreement recently signed as a model of regional trade agreements. It is divided into five parts. Part one is the introduction. Part two poses the question of why developing countries should liberalize services. Part three addresses the relationship between liberalization of trade in services, regional trade agreements and the GATS. Part four evaluates Egypt's commitments in the GATS and its intentions of services' liberalization through the regional trade agreements it is party to, with special emphasis on the Partnership Agreement it has signed with the EU. Finally, conclusions and policy implications follow.

## 2. Why Should Developing Countries Liberalize Services?

In this part we tackle the phenomenon of the accelerated growth of trade in services, where we identify the main reasons behind it. We then move to the position of developing countries regarding liberalization of trade in services. Finally, we discuss Egypt's profile of the services sector identifying the strengths and weakness of this sector and how it affects the whole economy.

### 2.1 Reasons behind Accelerated Growth of International Trade in Services

There are two main reasons behind the phenomenon of accelerated growth of trade in international services, namely, the technological advances and the lowering and/or elimination of impediments to trade and foreign direct investment (FDI).<sup>1</sup> The technology advances, which were more evident in the information technology sector (e.g. the Internet), increased the feasibility of long-distance, equivalently called cross-border, provision of services at accelerating

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<sup>1</sup> For a similar set of determinants of increased trade in services see Hoekman (1997), p. 8. For rather a larger set of determinants of increased trade in services see Lawrence (1996), p. 9.

declining costs (e.g. the international telephony). In addition, it led to the introduction of new service products (e.g. financial derivatives, computer reservation systems for airlines, and telemedicine), and to qualitative changes in pre-existing services (e.g. distance learning). In sum, technology is rapidly expanding the tradability of services.<sup>2</sup> With declining impediments facing international trade flows and FDI, the role of services and especially producer services<sup>3</sup>, is underpinned. On the supply side, the service providers are becoming more specialized and competitive. On the demand side, inefficient services are hardly tolerated by exporters of merchandise goods, thus increasing their demands for an efficient and competitive services industry. Those two main factors (technology advance and lower impediments to trade and FDI flows), which have been the main features as well as engines of the globalization process, magnified the potential benefits that can be reaped from the liberalization of trade in services. Moreover, the economic structure of the major trading powers such as the United States (U.S.) and the European Union (EU) became largely dominated by services. For example, in the OECD countries services accounted for between 60-70 percent of employment and an equivalent share of GDP in the 1990s (Francois and Reinert, 1996). As a result, those leading trading powers in the world (mainly the US and the EU), which have the largest stake in liberalization of trade in services, pushed heavily for introducing services under the auspices of the GATT/WTO. Their trials succeeded in including the issue of trade in services in the framework of the WTO and the General Agreement on Trade in Services (GATS) was born with the main intention to enhance multilateral liberalization of trade in services.<sup>4</sup>

### 2.2 Position of Developing Countries Regarding the Liberalization of Trade in Services

Developing countries have often taken a conservative position regarding the liberalization of trade in services. This was evident in the Uruguay Round when a number of industrialized countries led by the U.S. suggested the inclusion of the liberalization of trade in services in the GATT/WTO, and many developing countries were reluctant to agree to such a suggestion<sup>5</sup>. This reluctance was

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<sup>2</sup> For more details on the role of technology in increasing the feasibility of trade in services see: Hoekman and Primo Braga (1997), pp. 2-3.

<sup>3</sup> Producer services are services used as intermediates in the production process. They include financial, business and professional services.

<sup>4</sup> For more details on the role of the U.S. and the EU in including services under the context of the GATT/WTO in the Uruguay Round see Hoekman and Sauvé (1994), pp. 42-43. For a short discussion on the intentions of the major trading powers in including the services under the context of the GATT/WTO see El-Naggar (1996) pp. 7-8.

<sup>5</sup> Before and during the 1986 Ministerial meeting at Punta del Este, establishing the agenda of the Uruguay Round, many developing countries defended the view that GATT negotiations should not address services. This position was defended by the so-called G-10, which included most of the large

mainly based on the belief that developing countries do not enjoy comparative advantage in services; along with the belief that liberalization of trade in services will ultimately affect national sovereignty as it influences the setting of their relevant domestic rules and regulations; and finally from a negotiating perspective, they were not eager to accept the extension of the GATT/WTO rules to new areas (services) when the old subjects of interest to them (agriculture and textile industries) continued to defy GATT discipline.<sup>6</sup> Nevertheless, as the negotiations of the Uruguay Round proceeded, the conservative position of developing countries regarding liberalization of trade in services relaxed, and by the conclusion of the Round, developing countries undertook several commitments to liberalize their services sectors.

The explanation for this change in the position of developing countries regarding liberalization of trade in services is mainly attributed to the political economy context of liberalization of trade in services and its development over the last decade. The political economy of liberalization of trade in services is analogous to trade liberalization of merchandise goods, where export-oriented industries (both manufacturing and services) and consumers will tend to support it, while service firms threatened by foreign competition are expected to oppose it. Notwithstanding this basic similarity, there are three important differences between liberalization of trade in services and liberalization of merchandise trade, namely: the impact of liberalization of trade in services on the employment level in the related economy; the rules governing liberalization of trade in services; and finally, the requirements of adopting an export-oriented strategy in developing countries. Those three differences have a substantial impact on the attitude of developing countries towards liberalization of their services sectors.

Regarding the first issue related to the impact of liberalization of trade in services on the employment level, there is a great difference between it and that of the impact of liberalizing merchandise trade on employment. Whereas in the case of liberalizing trade of merchandise goods there are short-term costs associated with increased imports in terms of jobs lost at home and domestic firms retreating from the market due to their uncompetitiveness, this is not necessarily the case in the services sector. Reasons for this dissimilarity are mainly embedded in the way services are provided. Contrary to the merchandise goods where cross-border provision is the main method of providing them, the most preferential mode of the provision of services is the physical establishment, through FDI, of the foreign producer in the domestic market of the consumer (Konan and Maskus, 2002; Primo Braga, 1996). To the extent that establishment is the mode of provision used for the provision of services, labor employed in domestic

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and more influential developing countries, including Argentina, Brazil, Egypt, India, Nigeria, and Yugoslavia. For more details see Hoekman and Sauvé (1994), pp. 42-43.

<sup>6</sup> For a similar argument see Hoekman and Primo Braga (1996), p. 154.

service industries can expect that net employment in the sector concerned will change less than it would if cross-border trade was possible. The establishment of foreign-owned firms will, to a large extent, offset any labor layoffs by domestic incumbents. Thus decreasing the extent of opposition from labor unions against opening up trade in services in the affected sectors.<sup>7</sup>

Rules governing liberalization of trade in services differ to a large extent from those governing liberalization of trade in goods. While the latter is mainly controlled on the borders through tariffs, the nature of the former and its special characteristics of intangibility<sup>8</sup> and non-storability<sup>9</sup> make cross-border trade in services limited and thus result in tariffs being rather an idle method to monitor and control their entrance to the national domestic market. The move towards liberalization and privatization in developing countries since the beginning of the 1990s opened up the opportunity for the provision of services, mainly through FDI, which gave them the chance to partake in many services activities that were forbidden for them to share in before<sup>10</sup>. Moreover, whereas regulators may have objections to liberalization of cross-boarder trade, because they perceive difficulties in monitoring and controlling industries that are located in foreign jurisdictions, they may prefer the establishment of foreign firms in the domestic market, as this ensures that they will remain under control of the activity involved (Hoekman, 1997). Thus, the general move towards deregulation and privatization in developing countries paved the way for developing countries to accept and perform liberalization of trade in services. This move was sometimes complemented by the preference of the regulators in developing countries to control the provision of services through domestic regulations rather than inefficient cross-border taxes which in turn reinforced such move (Konan and Maskus, 2002).

Finally, starting in the late 1980s, the commitment of a large number of developing countries to adopt an export-oriented strategy created pressures and motivations to liberalize services sectors. On the pressure side, policies that restrict the operations of foreign providers of services may raise the income of local sellers but act as a tax on local buyers for whom, in many cases, the services are inputs in the production and export of other goods and services (Heydon, 1990). Consequently, liberalization of trade in services is likely to result in efficiency gains as the quality of services become better, the costs of

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<sup>7</sup> For a similar argument see: Hoekman (1997), pp.14-15. See also: Heydon (1990) esp. pp. 159-160.

<sup>8</sup> Most of the services are invisible to customs agents and become visible only when they are produced and consumed thus making it impossible for customs agencies to detect their entrance in the domestic national market.

<sup>9</sup> Non-storability of most services implies that production cannot be separated from consumption in either space or time.

<sup>10</sup> For a similar argument in a general context see Lawrence (1996), p. 9.

production are lowered, and resources allocation is improved (for a practical example in the context of NAFTA, see Deadorff, 2000; for a more general context see Hoekman and Messerlin, 1999). In the longer term there are likely to be dynamic growth opportunities from the transfer of skills, frequently as a consequence of the operations of multinational service providers (Heydon, 1990; Primo Braga, 1996). In other words, the increasing share of the service content of exports makes efficient producer services increasingly relevant to the pursuit of an outward-oriented strategy of development. Moreover, the costs of liberalizing trade in merchandise goods and resisting liberalization of trade in services can be significantly high. For example, if a country was to be engaged in a reform program that would reduce tariffs of goods to zero and did not extend its reform and liberalization program to the services sector, distortions would continue to persist and resources allocation would be affected. As nations move to reduce tariffs and other barriers to trade substantially, effective rates of protection may become negative for manufacturing industries as they lose protection on their goods but continue to be confronted with services input prices that are higher than they would be if services markets were contestable. From this perspective it is, therefore, not surprising that liberalization and deregulation of service markets began to emerge as high profile policy reform issues in many developing countries where manufacturing industries need to have access to low-cost, high-quality service inputs in order to be competitive on both the domestic and world markets.<sup>11</sup>

On the motivation side, the labor-intensive character of a large number of services, supplemented by the nature of many services (intangibility and non-storability), which asserts that FDI is the most efficient mode of the provision of exported services, suggests that the increasing trade in services can result in substantial gains for developing countries. Examples of utilizing the comparative advantage of developing countries in the production of labor-intensive services are voluminous (UNCTAD and World Bank, 1994; Primo Braga, 1996; Hoekman and Sauve, 1994; Sauvart, 1990). Sectors where developing countries enjoy comparative advantage include tourism, construction, software programming, and “back-office” services, which include activities such as data entry<sup>12</sup> and transactions processing (e.g., insurance claims, airline reservations). *Table 1* reveals that in 2001 the list of the 40 world leading exporters in

commercial services<sup>13</sup> contained almost the same number of developing countries as in the case of the top 40 leading exporters in merchandise goods, which implies that the argument for absence of developing countries enjoying comparative advantage in services is refuted at least when compared to the case of merchandise goods.

To sum up, the position of developing countries regarding liberalization of trade in services has been experiencing a substantial liberal change since the beginning of the 1990s. It is likely that such a liberal attitude will continue in the future to exploit the potential comparative advantages possessed by developing countries in services, and to utilize the benefits of technological advance in lowering trade costs of services and in expanding the benefits that they can gain.<sup>14</sup> Moreover, such trend is expected to continue in the future so that developing countries are able to keep pace with the globalization process and with the export-oriented strategy adopted by the majority of them since the late 1980s.

### ***2.3 Profile of the Services Sector in the Egyptian Economy***

The services sector constituted 50 percent of GDP in Egypt in 1998. Given the fact that the share of services in GDP increases with the increase in income as shown in *Table 2*, the share of the services sector in the GDP in Egypt seems to be following the norm although lagging slightly behind the average of the low middle-income countries, of the category of income groupings of countries to which Egypt belongs. Moreover, such ratio of services to GDP in Egypt is comparable with other Mediterranean non-member countries (MNCs) after accounting for the income category to which they belong (see *Table 2*).

The importance of the services sector is underpinned when investigating its contribution to the current account. *Table 3* shows that the contribution of the services sector to the current account has always been positive. In other words, Egyptian exports of commercial services have always surpassed Egyptian imports of commercial services, though the gap between services exports and services imports has been declining over the last two years. Such positive contribution of the services sector to the current account has helped to alleviate the negative consequences of the chronic deficit in the balance of trade in

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<sup>11</sup> For a similar argument see: Hoekman and Primo Braga (1997), pp. 7-8.

<sup>12</sup> Data entry requires a low level of computer literacy and limited interaction between the customer and the supplier. The customer mails paper-based data forms or sends scanned images of data forms electronically to the foreign provider for processing. The supplier sends the computerized data back via telecommunication lines or by mailing magnetic tapes. Countries in the Caribbean have been quite active in exploring the market for offshore data entry. See Primo Braga (1996), p. 4.

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<sup>13</sup> According to the International Monetary Fund Balance of Payments Classification, Services constitute of transportation (sea, air and other); travel (business and personal); other services (communications, construction, insurance, financial, computer and information, royalties and license fees, other business services, personal, cultural and recreational and government services not identified elsewhere). Commercial services, however, exclude government services.

<sup>14</sup> Ongoing technological advances are making it easier to un-bundle the production and consumption of information-intensive service activities (e.g., research and development, software development, data entry, inventory management, quality control, accounting, personnel, secretarial, marketing, advertising, or legal services). As a result, the scope for international production of services has expanded significantly in recent years. See Hoekman (1997), p. 2.

merchandise goods, which is a common feature in countries undertaking economic and trade reforms and especially in the early years of the implementation of such reforms. However, over time the merchandise goods deficit should be reduced if the country is performing well (Egypt started to implement its structural adjustment and economic reform program in 1991). The highest share of exports of commercial services is concentrated in transportation services (mainly due to Suez Canal revenue), travel (tourism receipts) and in the other business services.<sup>15</sup>

The contribution of the services sector to the Egyptian economy is revealed by the position of Egypt among other major exporters of commercial services in the world. Thus, while Egypt does not appear in the international ranking of the forty leading exporters of world merchandise exports, it ranked 32 among leading exporters of commercial services in 2001 (see Table 1). Moreover, the revealed comparative advantage<sup>16</sup> (RCA) of Egypt in commercial services is relatively high when compared with other countries around the world as shown in Table 4.

To sum up, the magnitude and the importance of the services sector in the Egyptian economy is highly evident as apparent from the aforementioned tables. This overall evaluation, however, does not provide a clear view of the status of many key service sectors as telecommunications, transportation and financial sectors, so this will be addressed in the following discussion.

#### **2.4 Telecommunications**

Up to 1998, Public Law 153 granted the Arab Republic of Egypt National Telecommunications Organization (ARENTO) exclusive responsibility for establishment and operation of the national telecommunications network and for international interconnection. Despite the relatively high revenue of the

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<sup>15</sup> Other business services, according to the GATS classification, consist of: advertising services; market-research and public opinion polling services; management-consulting services; services related to management consulting; technical testing and analysis services; services incidental to agriculture, hunting and forestry; services incidental to fishing; services incidental to mining; services incidental to manufacturing; services incidental to energy distribution; placement and supply of services of personnel; investigation and security; related scientific and technical consulting services; maintenance and repair of equipment (not including maritime vessels, aircraft or other transport equipment); building-cleaning services; photographic services; packaging services; printing, publishing; convention services; others.

<sup>16</sup> The RCA of a certain commodity of a country considered is a measure that indicates the potential opportunities for expanded trade in that specific commodity and that the country is relatively specialized in exporting that commodity. It can take any number between 0 and infinity. If it is less than 1, it implies that the country has a revealed comparative disadvantage in that commodity. If it is greater than 1 it implies that the country has a comparative advantage in that commodity. Hence, an RCA of 4 means that this product's share in the total export structure of the country considered is 4 times the product's share in the overall world trade. It is given by the formula:  $RCA = (X_{ij}/Y_j) / (X_{iw}/Y_w)$ , where  $X_{ij}$  is total exports of product  $i$  by country  $j$ ,  $Y_j$  is total exports by country  $j$ ,  $X_{iw}$  is total world exports of product  $i$ , and  $Y_w$  is total world exports of all products.

telecommunications sector as a percentage of GDP (2.2 percent of GDP in 1994), the performance of ARENTO was judged to be suffering from a number of deficiencies. For example, ARENTO was able to fulfill only 65 percent of the applications for new basic telephone lines and was not able to address the large unexpressed demand (Mohieldin, 1997). In 2002, a new law for telecommunications was approved by the Parliament, which mainly aimed to provide more market forces and end the monopoly of ARENTO. Moreover, Egypt joined the Basic Telecommunications Agreement in 2002. As revealed by Table 5, the weak performance of ARENTO resulted in Egypt taking a lagging position, regarding its ability to satisfy the domestic demand, among other MNCs and when compared to the world as a whole. Previous studies on the cost of service/rate emphasized that almost all services provided by ARENTO require a price reform policy. The absence of such a policy and the continued transfer of revenues to other government ministries has jeopardized the required expansion and maintenance of the telecommunications sector (Mohieldin, 1997). Moreover, the price of obtaining a telephone line in Egypt has been considered relatively high. For example, the official price for obtaining a telephone line in Cairo in 1997 was 295 US\$ and the waiting time for obtaining the line was between one to two years. To obtain an urgent line the price was increased to 885 US\$ with the waiting time reduced to two to three months. However, these official prices underestimated the actual cost of obtaining a telephone line as when an apartment was purchased, the buyer had to pay an additional price of 1180-1770 US\$ for an operating telephone line. This price reflects the overall portfolio of transaction costs, including waiting time and other barriers associated with obtaining a telephone. The price of a telephone line is over 16 times as high as in Malaysia (Benham, 1997). Thus, it can be argued that the monopoly of ARENTO resulted in low efficiency of the basic telecommunications sector. Low quality and high prices were the main characteristics this service industry.

In 1998, Law 19 transformed ARENTO into a joint-stock company with the Egyptian government holding 80 percent of its shares. In addition, in 1998 the government signed contracts and awarded licenses to two private sector consortiums to provide mobile telephone services in the domestic market. Licenses to a larger number of companies in the field of mobile phones was expected to increase after the end of the four year grace period allowed for the two companies. Moreover, two consortia franchise licenses for public pay phone services were given to companies, which allotted 20,000 lines each, and some private sector participation was allowed in the provision of Internet services. A regulatory body within the Ministry of Transportation and Telecommunications was established to assign frequencies and rates, and to monitor interconnection rights and settle disputes (Tohamy, 2000). It is too early to evaluate the impact of these deregulation and privatization efforts, however, the experiences of other countries, which undertook similar efforts, show positive effects. For example, in

Argentina privatization and the introduction of foreign equity in the two telecommunications companies in the early 1980s had significant impacts on investment in upgrading infrastructure and improving the quantity and quality of services. Telefonica added some 66,000 lines to its network in the eleven months up to September 1991, and another 276,000 lines in 1992. Telecom, the other company created during the privatization of the telephone monopoly ENTel of Argentina, added 51,000 and 222,000 lines, respectively. This greatly exceeded the investment level required under the terms of the operating licenses granted to the two firms. In addition to this net expansion of their networks, both firms also upgraded their technology, moving towards digital systems. Telecom installed some 420,000 lines in 1992 alone, of which 95 percent were digital. The rival company also expanded the share of its lines that were digital. For purposes of comparison, ENTel had only added 98,000 lines a year in the five years before privatization (Hoekman and Primo Braga, 1997). Nevertheless, the prudent regulation required by the Egyptian government in the process of privatization of telecommunications is the key to obtaining satisfactory outcomes as asserted by the experiences of other countries. A study has shown that in the absence of adequate regulation in the privatized telecommunications sector, investment and productivity tend to be relatively low and private sector returns relatively high (Galal and Nauriyal, 1995; Galal, 1999).

### **2.5 Transport Services**

The importance of this sector is revealed by its share in GDP, which together with telecommunications reached 6.7 percent of GDP in 1994 and would rise to 10.5 percent if Suez Canal revenues were included (Mohieldin, 1997). Moreover, as mentioned above, it largely contributes to the Egyptian exports of services. Due to space limitations, the following discussion will concentrate on port services, which contribute largely to the efficiency of this sector.

Law 12 of 1964 created state monopolies across the board of port services<sup>17</sup>. This resulted in poor quality and high prices for the services in that domain. For example, the comparative cost of shipment and loading in Egypt in 1994 was higher than that of Jordan, Syria and Turkey by approximately 27 percent, 22 percent and 19 percent respectively (Moiling, 1997). Port service fees are some 30 percent higher than in other ports in the region. The costs of handling a container in the port of Alexandria was estimated to be up to two to three times higher than in other Mediterranean ports (World bank, 1995). Thus, while freight costs to Europe, for example, are lower than other countries, the costs of loading and stevedoring are higher, which make the total cost in Egypt the highest

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<sup>17</sup> Article 7 of this law determined that “maritime transport activities, including freight forwarding, loading and unloading, creating of vessels, maintenance of maritime supplies” shall be restricted to persons or entities registered by the Egyptian Public Organization for Maritime Transport, created by the Ministry of Transport to administer the law”.

compared to other countries in the Mediterranean region. Consequently, given these export inefficiencies Egypt's proximity to Europe does not count for much, especially when transport costs account for 11 percent of the CIF cost of imports and 10 percent of the cost of imported inputs, and hence reduce the ability of Egyptian exporting industries to compete internationally (Benham, 1997).

In 1998, the Egyptian government launched a reform and privatization program for the port services. Following the issuing of Law 1/1998, the Specialized Ports Law 1/1996 was amended by Law 22/1998 which allowed concessions to local and foreign investors, at home and abroad, for the establishment of general or specialized ports or platforms in existing ports. The Law also governs the management, exploitation and maintenance of these ports and regulates fees levied by the Egyptian government for their use. Moreover, the Holding Company for Inland Transport and the Holding Company for Maritime Transport have privatized fractions of their shares (17 percent and 20 percent) (Tohamy,2000).

Experiences of other countries show that benefits can be substantial from the deregulation and privatization of port services. For example, elimination of barriers to competition in the provision of port services in Chile led to substantial reductions in operating costs (by about 50 percent over two years). The same occurred in Mexico when entry into the relevant service activities was made free, service market segmentation was eliminated, and firms were allowed to subcontract freely, and to set prices according to market forces. Within one year, the cost of services in the port of Veracruz declined by some 30 percent, while container turnover went up by almost 50 percent. As noted by the World Bank, “the deregulation of transport services in Chile and Mexico has had an important effect on those countries' ability to compete internationally. By reducing the costs of shipping by almost 50 percent, small and medium sized firms that would otherwise be marginal, have been able to expand their export activities” (Hoekman and Primo Braga, 1997). Such experiences predict high benefits for Egypt, provided that prudential regulation is maintained on behalf of the government to avoid any monopolistic or oligopolistic market structures that can undermine the price/quality combination of the services produced. The preliminary results of the government efforts are evident despite the short time that has elapsed since the introduction of such reforms. For example, a study testing the perception of the Egyptian exporting community regarding the efficiency of the services and their impact on their exporting activities showed that port services have experienced a positive development in the last few years regarding quality. However, it still remains short of reducing transaction costs (Ghoneim, 2000). Nevertheless, there are positive signs as freight rates as a part of the value of goods decreased from 6.64 percent in 1980 to 5.27 percent in 1997 (Tohamy, 2000).

## 2.6 Financial Services

Developments in the financial sector followed the same path as the telecommunications and port services. Up to 1998, the banking business in Egypt was dominated by four commercial public banks, despite several reforms undertaken in this sector since the beginning of the Economic Reform and Structural Adjustment Program (ERSAP) launched in 1991.<sup>18</sup> The same is true for the insurance business, where three state-owned companies control about 90 percent of the insurance market (Mohieldin, 1997). Thus, despite the fact that the reforms in this sector started earlier than in other sectors, they remained short of providing competitive markets with high quality and low cost services.

Consequently, additional reforms and privatization moves were introduced in 1998. For example, Law 155/1998 allowed private sector entry and privatization of the four public commercial banks, with a maximum ceiling on shares owned by one person. In the insurance business, Law 156/1998 allowed for the privatization of the public insurance companies, including the three dominating ones. It also removed restrictions on majority private ownership (domestic or foreign) of insurance companies and allowed for foreign management of insurance companies (World Bank, 1999). However, till December 1999, no developments were announced to address the expected privatization (Tohamy, 2000).

Having said that, the above review of the services profile in Egypt underpinned three main observations: *First*, the services sector is a major sector in the economy and is highly contributing to the economy in terms of exports, and the prospects for the future built upon the RCA are promising. *Second*, the key service sectors investigated (telecommunications, transport and finance) suffer from high price and low quality symptoms that have resulted in an increase in the transaction costs for their users. *Third*, the reforms and privatization moves that have started to take place in these sectors are promising, but remain short of some institutional aspects related to the regulatory role of the government (e.g. controlling the dominant position of oligopolistic and monopolistic market structures) and in some cases endure lagged implementation.

### 3. Which Mode of Liberalization should Countries Chose in Liberalization: Regional or Multilateral?

This part addresses three main issues: The mutual relationship between liberalization of trade in services and regional trade agreements; the relationship between the GATS and RTAs; and the status of liberalization of services in different RTAs worldwide.

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<sup>18</sup> For a review of such reforms which included liberalization of lending and deposit rates, elimination in discrimination in favor of public banks, etc. see: International Monetary Fund (1998), esp. pp. 56-64. For a summarized discussion see: World Bank (1999), p. 16.

### 3.1 The Mutual Relationship between Liberalization of Trade in Services and Regional Trade Agreements (RTAs)

Liberalization of trade in services can proceed unilaterally or through bilateral, regional as well as multilateral reciprocal negotiations with trading partners. So far, most progress has occurred through autonomous liberalization programs, which often included privatization. Much less has been achieved through bilateral, regional and multilateral reciprocal negotiations, although regional trade agreements (RTAs) that liberalized both trade in goods and services have become prominent starting from the mid 1980s. Examples of RTAs that cover liberalization of trade in services include the US-Israel FTA, the Canada-US FTA Agreement (CUSFTA), the Australia-New Zealand Closer Economic Relationships Trade Agreement (ANZCERTA), the EU's Single Market program, numerous agreements between the EU and neighboring countries, the North America Free Trade Area (NAFTA), the Gulf Cooperation Council (GCC) and MERCOSUR (the Southern Cone Common Market). All of these agreements are relatively recent; the oldest was negotiated in the early 1980s.<sup>19</sup>

The common characteristics of both liberalization of trade in services and *new* RTAs suggest that liberalization of trade in services can accelerate in the context of a RTA maybe much faster than through multilateral or unilateral moves (for a similar point of view see Stephenson, 2002). For example, one of the major characteristics of new RTAs is their "deepness." That is, dealing with non-border measures including the harmonization of rules and regulations and/or mutual recognition agreements (for example, national treatment is provided for service suppliers of foreign partners as long as those suppliers meet the standards, requirements, regulations, etc. of the host country), which appears to be one of the major constituents required for the liberalization of trade in services. Since, as argued above, the limited tradability of a large number of services requires the physical establishment of the producer in the proximity of consumers (through commercial establishment or right of establishment)<sup>20</sup>, then domestic rules and regulations remain to a large extent the most effective method of controlling and monitoring liberalization of trade in services (a fact that differentiates trade in services from trade in merchandise goods and is important for any country aiming towards services liberalization). Thus, the requirements of effective

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<sup>19</sup> For a short review of some of these RTAs and their dimension of liberalization of trade in services see: United Nations Conference on Trade and Development (UNCTAD) and the World Bank (1994), op.cit., esp. pp. 151-154. See also Stephenson (2002) for an updated review of the RTAs with a service dimension.

<sup>20</sup> Commercial presence encompasses establishments that are necessary to facilitate cross-border trade in services. It falls short of a right of establishment. A right of establishment would allow a foreign bank to establish "agencies, branches, or subsidiaries" where the commercial presence refers only to the activities of representative offices and NOT agencies, branches, or subsidiaries". For such differentiation see: Hindley (1990), p. 16.

liberalization of trade in services (domestic rules and regulations and/or mutual recognition) are embedded in the main features of new RTAs (deepness). Another theme that is to a large extent common in both new RTAs and the issue of liberalization of trade in services is the exclusion of “sensitive” sectors. Contrary to the case of liberalizing merchandise goods where RTAs consisting of both developing and developed countries face the problem of “sensitive sectors” in which the developing countries acquire a comparative advantage whereas developed countries do not (e.g., textiles and agricultural goods), it is not the case in liberalization of trade in services. This is not to say that there are no “sensitive sectors”, but rather there are a number of “sensitive sectors” (e.g. basic telecommunications, temporary movement of natural persons, and domestic transport). However, with one main difference, which is that, both developing as well as developed countries are very reluctant to include them in their trade liberalization agenda (with one main exception which is the EU). The absence of friction regarding which sectors to include and which not among countries concluding a RTA facilitates the negotiations between partners and enhances the idea of the presence of “like-minded people” in RTAs.

Having said that, it appears that new RTAs are a suitable framework for the liberalization of trade in services. Nevertheless, confining liberalization of trade in services to bilateral or regional arrangements can result in “trade diversion”. For example, in 1986 Korea concluded an agreement with the US for improved market access of US insurance companies following an extensive section 301 investigation which showed that Koreans are discriminating against US insurance companies in their own Korean domestic market, which included Korean companies, joint ventures and two American companies. Responding to US pressures, Korea agreed to allow American firms to engage in more insurance activities and to receive the same rate of premiums Korean firms receive, however, such liberal treatment was not extended to other countries. The result was maintaining the cartelized-market structure of the insurance business with sharing the monopoly rents among both Korean and American companies. Prices in the insurance business remained high thus affecting negatively the Korean consumers as well as the economy as a whole.<sup>21</sup> Hence the main lesson learned is that partial liberalization in terms of the number of trading partners can result in trade diversion and can negatively affect the economy as a whole. Consequently, liberalization of trade in services within RTAs should be a step towards full liberalization. The liberalization under the auspices of a RTA can play the role of a “testing ground” or preparing for full liberalization. In other words, it should

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<sup>21</sup> For more details on the Korean case see: United Nations Conference on Trade and Development (UNCTAD) and the World Bank (1994), op.cit., esp. pp. 60-61. See also: Heydon (1990), op.cit., p. 163.

complement full liberalization of trade in services to all trading partners if the intention is to have efficient (low price and high quality) provision of services.

### **3.2 The General Agreement on Trade in Services (GATS) and Regional Trade Agreements (RTAs)**

Countries engaged in some form or another of a RTA have to comply with the GATS regulations regarding RTAs which are stated in Article V of the GATS entitled “Economic Integration”. This Article is equivalent to Article XXIV of the GATT entitled “Free Trade Areas and Customs Unions” and, for developing countries, the Enabling Clause.<sup>22</sup> In addition, agreements that provide for the full integration of labor markets may also be exempt from the MFN obligations under Article V *bis*.<sup>23</sup>

Analogous to Article XXIV of the GATT, Article V of the GATS imposes a number of conditions on RTAs between the members of the GATS: *First*, such agreements must have “substantial sectoral coverage” (Article V: 1(a)). An interpretive note states that this should be understood in terms of the number of sectors, volume of trade affected, and modes of supply. With respect to the latter, RTAs should not provide for *a priori* exclusion of any mode of supply. However, “substantial sectoral coverage” is not the same as “substantially all” sectors found in Article XXIV of the GATT but rather much weaker, suggesting that the intention of the drafters of Article XXIV of the GATT was perhaps more restrictive than that of those drafting Article V of the GATS.<sup>24</sup>

*Second*, RTAs have to provide for the absence or elimination of substantially all discrimination (defined as measures violating national treatment) among the parties to the agreement in sectors subject to multilateral commitments. This consists of the elimination of existing discriminatory measures *and/or* the prohibition of new or more discriminatory measures, and is to be achieved upon the entry into force of the RTA or on the basis of a reasonable time frame (Article V: 1(b)). In other words a mere *standstill* agreement may be sufficient. Moreover, Article V: 3(b) allows developing countries negotiating RTAs among themselves to give more favorable treatment to firms that are owned or controlled by natural persons belonging to the parties of the agreement. That is, it allows for discrimination against firms belonging to non-members, even if the latter are established within the RTA before its initiation.

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<sup>22</sup> This could be due mainly to the fact that tariffs and quotas on imports play little or no role in services trade, making it difficult to extend the concept of a customs union to the domain of services. For such an argument see: World Trade Organization (1995), op.cit., p. 22.

<sup>23</sup> For the review of Article V of the GATS see: the General Agreement of Trade in Services and/or World Trade Organization (1995), op.cit., pp. 21 -23.

<sup>24</sup> For similar arguments see: Hoekman and Sauv  (1994), op.cit., p.58 and Lawrence (1996), op.cit., pp. 103-104.

*Third*, such agreements must not result in higher trade and investment barriers against third non-member countries. These conditions constitute the “price” to be paid for the MFN obligation and specific commitments to be waived by GATS members. That is, for the implicit discrimination against non-members resulting from the agreement to be deemed acceptable. With respect to the export interests of third countries, this requirement is more advantageous than the GATT’s requirement that trade barriers may not be “on the whole” higher or more restrictive, since it applies specifically to individual sectors and sub-sectors. In addition, Article V clarifies that those service suppliers of a WTO member which is a third country to the agreement and who are already engaged in “substantive business operations” prior to the signature of the RTA in the territory of one of its parties, are entitled to the treatment granted under the agreement. Nevertheless, developing countries are exempted from such condition.<sup>25</sup>

*Fourth*, GATS Article V: 5 requires that the respective provisions for the modification of schedules apply if the establishment of a RTA leads to the modification of the members’ scheduled commitments. These negotiations are to be carried out in accordance with Article XXI entitled “Modification of Schedules”, which provides for a similar but not identical set of conditions as GATT’s Article XXVIII. In particular, arbitration is available if negotiations are unsuccessful, and retaliation may be carried out on a non-MFN basis.

*Fifth*, Article V: 7 contains requirements to ensure transparency of proposed RTAs. Agreements (and any enlargement or modification) are to be promptly notified to GATS, and members of such RTAs are required to make available information upon request. The Council of the GATS *may* (but need not) establish a working party to examine consistency of the agreement with Article V, in contrast to the automatic rule in the creation of the corresponding working party in the goods area. Moreover, regarding interim agreements, Article V: 7(b) specifies that reports on their implementation be provided periodically, that a working party *may* be established to examine these reports, and that working party reports *may* form the basis of recommendations to the members of agreements.

Considering all the aforementioned conditions, it appears that the GATS rules and Articles are much more flexible and loose than the corresponding rules and Articles of the GATT.<sup>26</sup> Summing up, the GATS’ provisions in relation to RTAs are arguably much weaker and more fragile than those of the GATT in both substantive and procedural terms with respect to loopholes allowed for members of a RTA to remain in compliance with the rules of the WTO. Some economists

argue that the explanation behind the weak Articles of the GATS concerning RTAs is that the GATS has been worded with a view to ensuring that existing RTAs would be consistent with GATS (Lawrence, 1996). Moreover, a number of the existing RTAs have gone further than the GATS in terms of mechanisms applied to liberalize services. This confirms that the GATS as a mechanism for liberalizing trade in services is still in its infancy stage. Abiding by the rules and regulations of the GATS alone, though still beneficial at least in bounding the standstill status of the protectionist measures applied in the field of trade in services, is still far from achieving its major intention of achieving free trade in the area of services.

### ***3.3 Review of Liberalization of Trade in Services in other Regional Trade Agreements (RTAs) Worldwide***

Liberalization of trade in services has featured prominently in a large number of RTAs signed over the last two decades. It was included in both “shallow” and “deep” agreements. It was adopted by RTAs incorporating developing and developed partners as well as in the agreements that were confined to developing or industrialized countries. The most notable example of the RTAs encompassing developing and developed countries that included liberalization of trade in services is the North America Free Trade Area (NAFTA) between the US, Canada and Mexico. In the case of RTAs among industrialized countries, liberalization of trade in services featured in the Australia-New Zealand Closer Economic Relationship Trade Agreement (ANZCERTA), the EU Single Market Initiative, the former Canada-US Free Trade Area (CUSFTA) and others. Among developing countries, the RTAs that incorporated liberalization of trade in services were the MERCOSUR between Uruguay, Paraguay, Brazil and Argentina, the Chile-Mexico free trade area agreement and the GCC between the Arab countries of the Gulf<sup>27</sup>. The following discussion will focus on the dimension of liberalization of trade in services in some of these RTAs.

The NAFTA resembles the proposed Egyptian-European Partnership Agreement in that it encompasses both developed as well as developing partners. However, the NAFTA can be characterized as a “deep” RTA as it deals with a large number of regulatory matters and is not confined to the elimination of tariffs “shallow integration” as is the case, to a large extent, in the Egyptian-European Partnership Agreement. Compared to the GATS, NAFTA went further to a large extent in terms of mechanisms employed to liberalize trade in services. For example, as mentioned before, the main core of the GATS are the specific commitments, and the GATS adopts a ‘positive list’ approach where the sectors listed are only the ones subject to liberalization. NAFTA adopts, on the contrary,

<sup>25</sup> See: World Trade Organization (1995), op.cit. p. 21.

<sup>26</sup> For more details see: Hoekman and Sauv e (1994), op.cit., pp. 57-61. For an evaluation of Article V see Feketekuty (2000)

<sup>27</sup> For a short review of the services dimension in these RTAs as well as others see United Nations Conference on Trade and Development (UNCTAD) and the World Bank (1994), op.cit., pp. 151-153.

a 'negative list' approach where, unless otherwise mentioned in the specific commitments, the liberalization extends to all services sectors. The difference between the two approaches is that the 'negative list' approach provides more transparency (since it forces governments to reveal all non-conforming measures and excluded sectors) and includes a built-in mechanism for liberalization of all services sectors that are likely to emerge in the future. In other words, the incentives for engagement in liberalization of services are greater under the 'negative list' approach when compared to the 'positive list' approach. Moreover, whereas in the GATS national treatment, market access or the right of non-establishment (i.e., the right to provide cross-border services without an established presence) are not general obligations, they are under the NAFTA (WTO, 1995). In addition, NAFTA goes beyond the GATS as far as it covers government procurement in services, in contrast to the GATS, which does not. This is not to say that services negotiations had no obstacles or 'sensitive sectors'. On the contrary, NAFTA contains sectors with "unbound" reservations as basic telecommunications, air and maritime transportation. Nevertheless, efforts were made to tackle such 'sensitive sectors'. Finally, the movement of temporary labor, especially of professional labor, has been one of the best achievements in the area of liberalizing trade in services under the NAFTA, including transparency on licensing procedures and certification requirements. NAFTA included rules of origin for services that were asserted to be more liberal than those of its predecessor, the CUSFTA, and was determined by residency of the service providers. Safeguard provision concerning balance of payments problems and denial of benefits are included in the agreement. In a nutshell, NAFTA was deemed by specialists to be "the most comprehensive package of services trade liberalization achieved in an inter-governmental trade agreement to date".<sup>28</sup>

The Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA) provides another example of successful introduction of trade in services as an area for regional liberalization. ANZCERTA was initially negotiated in 1983 and at that time it did not cover liberalization of trade in services. However, the new negotiations in 1988 included a Protocol on liberalization of trade in services. The goal of the Services Protocol was to establish a framework of transparent rules, remove barriers to trade in services and enhance competition in the provision of services. A 'negative list' approach was adopted for the sectoral coverage of services included. 'Sensitive' sectors were present in this RTA and also included basic telecommunications, air

transport and maritime services. Nevertheless, those sectoral exclusions were time bounded, as the RTA contained provisions aiming at bringing these sectors within the scope of the Protocol in the future, which were actually undertaken to a large extent in the review of the agreement in 1992. The agreement contained Articles concerning free movement of permanent labor and capital (i.e. common market) and thus special provisions for liberalizing free movement of temporary labor were not needed. Articles concerning harmonization of rules and regulations and mutual recognition based on minimum standards featured prominently in the agreement. The agreement contained rules of origin for service providers based on the nationality or residency of natural persons and incorporation for legal persons. Safeguard provisions were present in the transitional period of entering into force of the agreement, but were excluded afterwards (Hoekman and Sauve, 1994).

Contrary to the above-mentioned examples of NAFTA and ANZCERTA, which had a rich agenda for liberalization of trade in services, the case of the CUSFTA does not seem to have been successful. The first difference between the CUSFTA, on the one hand, and ANZCERTA and NAFTA on the other, is the positive list approach adopted by CUSFTA contrary to the negative list approach adopted by both NAFTA and ANZCERTA. The positive list contained a total of 60 sectors with several exceptions and market entry conditions. There was absence of general procedures for harmonization or mutual recognition of standards, and government procurement disciplines for services were not included. Nevertheless, the agreement was successful in founding a new approach in a number of services through the development of trade principles and rules for value added telecommunication services, licensing and certification of architects, and the temporary entry of business people. The agreement contained rules of origin for service providers, which were determined by nationality of ownership and control of the incorporation, and not by residency (implying that rules of origin in NAFTA and ANZCERTA were more liberal). In the area of safeguards, it was similar to the NAFTA (Hoekman and Sauve, 1994).

The review of the three examples of RTAs that have intended to liberalize trade in services reveals some important insights, namely, that there are two factors determining the success of such RTAs, which are the issues of *transparency* (provided by adopting a negative list approach in contrast to the positive list approach) and *regulatory harmonization and mutual recognition of standards*. The characteristics of services in terms of intangibility and non-storability imply that the rules governing their exchange are different from that of goods. Harmonization of regulatory regimes and/or mutual recognition agreements for minimum standards are important aspects in controlling and monitoring the trade in services. Since the CUSFTA failed to incorporate such dimension in its services area, it remained short of success. The issue of regulations becomes

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<sup>28</sup> Inter-governmental treatment refers to the case of all RTAs implemented till the year 2000. It excludes the European Union Single Market Initiative where a supranational power is responsible for the monitoring and implementation of such RTA. For more details see: Hoekman and Sauvé (1994), op.cit., p. 16. For an extensive discussion of the treatment of services trade related matters under the NAFTA see: *Ibid.* pp.15-25.

more evident when developing and industrialized countries are engaged in the same RTA. For example, a construction company from a developing country, using labor from that country and paying its workers on that country's terms, may be capable of constructing a highway or an airport of a given quality in Europe more cheaply than could a European company using European labor. But a company from developing country will have great legal difficulty in getting labor from the developing country into Europe. Even if it could do so, it might not be able to produce more cheaply if that labor, once in Europe, was subject to European employment laws. In other words, harmonization of regulations related to the service providers and/or mutual recognition agreements for the standards of service providers and/or services per se are the most important aspects in any bilateral or regional attempt to liberalize trade in services. Transparency regarding the services covered complements the requirements for a successful agreement as it decreases disputes and increases the scope of potential liberalization.

#### **4. Evaluation of Egypt's Commitments in GATS and the RTAs it has Joined**

In this part we discuss Egypt's commitments in both The GATS and the different RTAs it has joined with special emphasis on the European Partnership Agreement that Egypt has lately signed.

##### **4.1 Commitments of Egypt in the GATS and other RTAs**

Egypt's commitments in the GATS were concentrated in four main sectors (out of the twelve main sectors identified in the GATS). Egypt made a total of 28 commitments distributed among those four sectors and their related sub-sectors. The four sectors were construction (sector 3), financial services (sector 7), tourism (sector 9) and transportation (sector 11).<sup>29</sup> Moreover, in 2002 Egypt joined the Basic telecommunications Agreement and is in the process of joining the Information Technology Agreement. The choice of these sectors asserts that Egypt has chosen sectors where it enjoys comparative advantage (e.g. construction and tourism) and where the upgrading of some essential services is needed to reduce the transaction costs in order to increase the competitiveness of the Egyptian economy (telecommunications, financial services and transportation). Nevertheless, Egypt's strategy of liberalizing trade in services sectors according to its comparative advantage or needs to upgrade them was not universal. For example, despite the fact that it has a comparative advantage in other business services (sector 1) such as back office services and data entry, Egypt made no commitments to liberalize any of its sub-sectors. Hence, the intention of the Egyptian government in undertaking GATS commitments is not clear. However, confining our analysis to some sectors may give some

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<sup>29</sup> For the sectors where GATS members made commitments see: World Trade Organization website: <http://www.wto.org/services/websum.htm>

indications of the intended aims of the Egyptian policy makers in the process of reforming the services sector.

If the analysis is confined to the basic telecommunications sector, we observe on the one hand that the Egyptian government was and is currently undertaking a number of domestic policy and regulatory reform measures (see above) and finally joined the Basic Telecommunications Agreement in 2002. In the case of financial services, which is also experiencing domestic policy reforms, Egypt made very conservative commitments in the GATS. For example, in the insurance sector it introduced limitations on the commercial presence related to both the number of suppliers and foreign equity share<sup>30</sup>. Similar restrictions are to be found in the case of construction, transportation and tourism. Restrictions include limitations on the share of foreign personnel in foreign controlled enterprises (and even on the overall wage bill in the case of maritime transport); a maximum of 49 percent of foreign capital in several industries (construction and related engineering services, tourism projects in the Sinai region, and insurance); economic needs tests in the case of tourism, opening of branches by foreign banks, and insurance (for example, new companies should be able to work without "harmful" competition to existing companies); and restrictions on the operations of representative offices, and so on (Hoekman and Primo Braga, 1996). In other words, the commitments that Egypt made in the GATS are not in line with the domestic policy and regulatory reforms that it is undertaking. This implies that Egypt is using the GATS to anchor not even the standstill protectionist measures *currently* applied in the services sectors, but rather to anchor the *past* measures instead of using the GATS as a mechanism to signal future liberal reforms to the international community.

Another important fact that has to be emphasized is the use of the GATS as a mechanism that provides credibility for the governments' actions, which in turn increases the trust of foreign investors in those governments. When a government undertakes GATS commitments and binds its domestic reforms, it signals to foreign investors the credibility of its actions since backsliding on such commitments becomes rather difficult.<sup>31</sup> The aforementioned two examples in

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<sup>30</sup> See: *Ibid.*, p. 52.

<sup>31</sup> For the role of the international agreements in provision of credibility to governments' actions see: Mattoo (1999), *op.cit.* p. 15. See also: Hoekman and Primo Braga (1997), *op.cit.* The main point is that by binding the domestic reforms under the GATS, the country is not free any more to backslide on such reforms unless it provides concessions for other GATS members who are affected by such backsliding. The concessions do not have to be confined to the services sector, but rather can extend to agricultural and industrial goods where for example, lowering of tariffs on an industrial good that is of interest for the country asking for concession might be suitable. It has been argued in *Chapter Three* that the Egyptian-European Partnership Agreement might not perform the role of "anchoring" mechanism efficiently in case of merchandise goods because Egypt can always resort to safeguard mechanisms under the Agreement per se as well as under the GATT, for example by raising tariffs. However, in the case of services, the matter is different, simply because reforms normally are

the telecommunications and financial services reveal that the Egyptian government did not intend to use the GATS as a ‘credibility enhancing’ mechanism.

When comparing the commitments that Egypt has undertaken in the GATS to other selected MNCs, we observe that Egypt is lagging behind both in the number of sectors and the number of commitments, as shown in *Table 6*.

Turning to the RTAs that Egypt is engaged in, we find that the issue of liberalization of trade in services was not brought up rigorously in the spectrum of these agreements, or at least deterred for future negotiations. If we concentrate on two more recent examples, the Pan Arab Free Trade Area (PAFTA) and the Egyptian-European Partnership Agreement, we observe that there is no intention on liberalizing trade in services, at least as the Preamble of the agreements showed. In the PAFTA case, the Preamble declared that the services sector is excluded.<sup>32</sup> In the Egyptian-European Partnership Agreement, two Articles call for negotiations in the future to liberalize trade in services and include the right of establishment<sup>33</sup>, however, that will be applied upon entry into force (and at least for five years) of the Agreement. In the mean time and until further negotiations take place the commitments of each partner according to the GATS schedules will apply. This implies very minor liberalization, if any, on the behalf of Egypt. The reluctance to include liberalization of trade in services and the right of establishment came from the Egyptian side as evident by the documents reviewing the negotiations<sup>34</sup> and by the fact that Lebanon has included the liberalization of trade in services in its negotiations for its Partnership Agreement with the EU (Ghesquiere, 1998). Thus, it can be argued that use of RTAs as “anchoring” and/or “credibility enhancing” mechanisms by Egypt for liberalizing trade in services was foregone as was the case in its use of the GATS.

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regulatory and backsliding becomes more difficult especially if compared to the case of merchandise goods where backsliding can just be undertaken by a stroke of a pen to raise tariffs on that particular good.

<sup>32</sup> The services were not mentioned in the Declaration of Establishing the AFTA, with the exception of Article 8 that recommended consultation between AFTA members on issues related to services and especially those that are confined to trade. See: Arab League (1997), “The Declaration of Establishing the Larger Arab Free Trade Area”, Cairo: the Arab League (in Arabic). However, a new initiative for a separate agreement to liberalize services was made by Lebanon in 2002, but is still in its infancy stage.

<sup>33</sup> See: Articles 31 and 32 in the Tunisian-European Partnership Agreement. European Commission (1995b), Proposal for a Decision of the Council and the Commission on the conclusion of a Euro-Mediterranean Agreement establishing an association between the European Communities and their Member States, of the one part, and the Republic of Tunisia, of the other part, Brussels.

<sup>34</sup> Ministry of Supply and Domestic Trade, Trade Representative Sector (1997), “A Report on the Relations between Egypt and the EU and the Proposed Partnership Agreement”, Unpublished Report (in Arabic), see esp.: p. 29.

To sum up, Egypt neither made use of the GATS nor the RTAs that it is currently pursuing to enhance its efforts of liberalizing trade in services. It has not utilized the advantages of being a GATS and/or a RTA member in adding the “anchor” effect or the “credibility enhancing” mechanism in order to complement its domestic efforts of reforming the policies and regulations in the field of services. The foregoing of such advantages of being a GATS and RTA member can lead to substantial negative implications for the ability of Egypt in attracting FDI and can hinder the competitiveness of the Egyptian economy.

The following analysis reveals some of the negative impacts that are likely to follow the limited governmental efforts in liberalizing trade in services.

## **4.2 The Case of the Egyptian- European Partnership Agreement**

### *4.2.1 Benefits Foregone*

The non-liberalization of trade in services in the Egyptian-European Partnership Agreement is a loophole that will have negative consequences on Egypt. Egypt could have made use of the Agreement to foster the provision of efficient services domestically, which is urgently needed given the export-oriented growth path adopted by the Egyptian government. The availability of efficient services is a prime factor in determining the competitiveness of the Egyptian exports. Since the costs of services remain high and their quality low, it is an expected outcome that exporters who depend heavily on services as inputs in their production process will not be able to compete efficiently. Several studies have pointed out the impediments facing exporters in obtaining efficient domestic services (Ghoneim, 2000). Such impediments included excessive insurance fees, high port service costs, inefficient telecommunications services and losses caused by unnecessary waste and breakage of goods as a result of low quality transport and storage. Egypt is not expected to have a better market access for its exports in the EU, at least in the short run, upon implementing the Agreement because the majority of its manufactured products already enjoy a duty free access. Hence, what will determine the ability to have better market access will be the competitiveness of the Egyptian products, which in turn depends on the availability of efficient services domestically that ensure low costs and high quality. In other words, the non-liberalization of trade in services will reduce the competitiveness of the Egyptian exports in the EU market, which will result in the denial of a potential better market access.

Egypt was not able to utilize the Egyptian-European Partnership Agreement as a ‘testing ground’ for liberalizing its services sector. The methodology adopted by the Egyptian government to liberalize its services sector is highly conservative and the implementation pace is slow. The government announces domestic reforms which are implemented in a piece-meal way and does not anchor such reforms by locking them in a regional or international agreement. In many cases (e.g. telecommunications) it did not anchor its reforms by including them in its

GATS commitments. It could have used the Agreement to complement its domestic reforms and allow some kind of regional liberalization before announcing multilateral commitments. Certainly, the adoption of European institutions would have helped the Egyptian government to overcome some market failures. For example, though a competition law is not *urgently* needed in the field of merchandise goods due to the absence of monopolistic and oligopolistic market structures, it is *urgently* needed in the field of services, where a large number of services industries have monopolistic or oligopolistic structures, even after the domestic reforms that are currently taking place. Nevertheless, Egypt will adopt the European competition law in the merchandise goods and will not in the case of services. The absence of the competition law and/or sectoral regulations (The regulatory body in the telecommunications is headed by the Minister of Telecommunications!!) can have negative welfare consequences and can jeopardize all domestic reforms as long as those reforms are not translated into effective competitive and contestable service market structures. The availability of technical and financial assistance from the European side to Egypt and the flexibility in adding extra safeguard mechanisms, when compared to those under the GATS, are foregone opportunities that Egypt could have made use of if the services sector was liberalized within the context of the Agreement.

Egypt made no use of the Egyptian-European Partnership Agreement to ‘anchor’ its services-related domestic reforms. The role of international agreements and RTAs in ‘anchoring’ the domestic reforms in the services sector of a country engaged either in the international agreement and/or a RTA is evident (Lawrence, 1996). The reasons for such ‘anchoring effect’ are mainly due to the costs of backsliding on such reforms (e.g., in the GATS, a country retreating from its commitments has to pursue re-negotiations with all GATS members and provide concessions in other sectors to be able to modify its sectoral commitments). Such an ‘anchoring effect’ has positive externalities in helping the government avoid pressures from domestic interest groups that oppose liberalization and in sending positive signals to foreign investors that the concerned government is serious about the domestic reforms. In other words, it increases the credibility rating of the government concerned. The anchoring effect of the Agreement would have been idle if Egypt had undertaken wide commitments under the GATS, which would have been sufficient to provide the positive externalities mentioned above. Given the few commitments made by Egypt in the GATS, it could have utilized the Agreement to provide this ‘anchor effect’, which was unfortunately not the case.

To sum up, the failure of the Egyptian government to liberalize trade in services under the auspices of the Egyptian-European Partnership Agreement cannot be justified by economic reasoning. Due to this failure, Egypt had foregone three major benefits: *First*, Egyptian exporters would have certainly had better access

to efficient services; *second*, the Agreement *per se* could have acted as a ‘testing ground’ for extended liberalization efforts on the behalf of the Egyptian government which would have been backed up by additional safeguard mechanisms and provision of technical and financial assistance; and *finally*, the Egyptian government lost the ‘anchoring effect’ of international agreements and RTAs in adding the credibility dimension to its domestic reforms.

#### 4.2.2 Costs of Adjustment

There are three types of adjustment costs likely to face Egypt if it had made a decision to liberalize trade in services within the context of the Egyptian-European Partnership Agreement. These three types of adjustment costs are those due to balance of payments problems (macroeconomic-related type of adjustments), the specific sector adjustment costs and sensitive sector adjustment costs (microeconomic-related type of adjustments).

The costs of adjustment related to the balance of payments are likely to appear due to the increase in imports of services after the liberalization. However, this expected surge in imports of services should be weighted against the positive spillover effects from the liberalization of trade in services. *First*, while liberalization of trade in services will result in an increase in imports of services, it can also lead to an increase in the exports of services. Egypt enjoys a comparative advantage in many fields of commercial services. The recent phenomenon of ‘splintering’ or outsourcing of service activities,<sup>35</sup> where mother companies in the industrialized countries ask their affiliates (or sub-contractors) in developing countries to undertake the provision of services where such affiliates acquire some kind of comparative advantage, helps Egypt to utilize its own comparative advantage in services. Examples include back-office services and software development<sup>36</sup> where there are certainly positive prospects for the increase in the exports of services within the context of the Agreement. Moreover, if Egypt was able to negotiate a *fair* Agreement where the movement of temporary labor is allowed, then certainly this could boost some of its exports of services (e.g., construction) if conditioned by some kind of mutual recognition agreement on minimum standards (e.g., labor regulations) to avoid any kind of unexpected technical barriers from the EU. *Second*, Table 3 reveals that the main problem of the balance of payments lies in the chronic merchandise goods trade balance, and not in the services trade balance. Since the performance of Egyptian

<sup>35</sup> For the development of such trade see: Bhagwati (1984), for an updated analysis see Deadorff (2000).

<sup>36</sup> The Sakhr Software Company provides an excellent example, where it had showed excellent performance in the development of software employing more than 300 programmers with an average loan of US\$ 3000 per year per each. The high performance of Sakhr has already attracted the interests of specialized multinational companies as Lernour & Hauspie in Belgium, Acer in Taiwan and Davidson & Associates, Inc. in US. See: Delvin and Page (1999).

exports over the last five years has shown severe drawbacks, among which is the absence of efficient services, then an increase in the imports of services can result in an increase in the exports of merchandise goods since efficient services will decrease the costs of production of merchandise exports and will make them more competitive in the international markets.<sup>37</sup> *Third*, liberalization of trade in services will not always result in an increase in imports due to the nature of a large number of services that require the proximity of service providers and consumers, implying that FDI is the most reasonable mode of supply. Thus, the right of establishment and/or commercial presence will not result in an increase in imports of services, but rather their activities will be documented as increase in exports of services (Heydon, 1990) and will in many cases not cause employment demise (Hoekman and Messerlin, 1995). *Fourth*, the availability of financial assistance, which could back up any deterioration in the balance of payments, in addition to the safeguard mechanisms provided for that special reason should make any balance of payments problem easier to handle. This differs from unilateral liberalization (i.e., unilateral domestic reforms) and multilateral liberalization (i.e., under the auspices of the GATS) where financial assistance to back up any deterioration in balance of payments is absent.

Turning to the second point related to sector specific adjustment costs, there are two main kinds of losses that are likely to happen in the sectors that face liberalization, namely, lay-off of labor due to the closing firms that were unable to survive competition with European service providers and transfer of profits to the EU by the newly established European firms in the Egyptian domestic market. Regarding the lay-off of labor, it is unlikely to happen in the field of services with the same degree as it may exist in the case of merchandise goods. In many cases, the provision of services, as argued above, requires physical proximity of service providers and consumers, which in turn requires the establishment of the foreign service providers in Egypt. If European firms want to increase their profits, then they are likely going to depend on the cheap labor available in Egypt. Hence, even if labor was laid off due to the closing down of national-owned firms that were not able to survive the fierce competition with their European counterparts, most of the labor in the shut-down domestic firms will be employed by the newly established European firms. However, this argument applies only to such services that need the physical presence of service providers and does not apply to cross-border provision of services where the negative impact of laying off workers or shutting down uncompetitive firms cannot be avoided. Moreover, there is the possibility of Egypt applying restrictions to the number of foreign personnel (as in the specific commitment related to market access under the GATS), which will cushion the problem of laying off of labor. Regarding the transfer of profits to the European mother

companies, this could be controlled via restrictions on the ownership of European firms performing in Egypt (e.g., a joint venture with a maximum share of foreign partner) and through the adoption of a competition law and/or sectoral regulations that determine a ceiling on profits allowed.

Finally, turning to adjustment costs related to the 'sensitive sectors', it is not expected that they will appear in the first place, mainly because sensitive sectors in the area of services are likely to be similar in both the EU and Egypt, implying that negotiations on their liberalization will be kept at a low profile. This is evident from the experience of other RTAs, where the sensitive sectors for developing countries were shared by similar concerns among their developed partners (e.g., transportation and telecommunications sectors in the case of NAFTA). Moreover, they were the same sensitive sectors that appeared difficult to negotiate under the GATS (e.g., telecommunications and maritime services) (Hoekman, 1995). This is in contrast to the case of merchandise goods where agriculture and textiles have acted as stumbling blocks in the negotiations of the Egyptian-European Partnership Agreement. Nevertheless, a potentially sensitive issue that would have been expected to arise is the issue of 'movement of temporary labor, which the EU would certainly have not welcome and Egypt would have certainly insisted on, thus creating another area of friction in the negotiations.

In a nutshell, Egypt has foregone a number of benefits due to its reluctance to liberalize trade in services within the context of the Egyptian-European Partnership Agreement. Investigating the costs that would have been associated with liberalizing trade in services showed that they are rather minimal costs when compared to the pay-off expected from liberalization.

## **5. Conclusion and Policy Implications: Consequences of an Inefficient Services Sector in Egypt**

The analysis highlights some of the negative effects of having an inefficient services sector in the Egyptian economy. It includes high transaction costs, crowding out of FDI and/or skewed investment incentives, and a negative effect on the balance of payments.

### **5.1 High Transaction Costs**

Inefficient services in Egypt have resulted in high transaction costs. Several studies have pointed out that doing business in Egypt is costly. One of the main reasons behind this assertion was the presence of an inefficient services sector (high price and low quality) besides bureaucracy and red tape measures.<sup>38</sup> High transaction costs have negative impact on the welfare and undermine the ability of Egypt to attract FDI. Its negative impact on reducing the competitiveness of

<sup>37</sup> For a similar argument see: World Bank (1998), op.cit., pp. 14-15.

<sup>38</sup> See for example: Fawzy (1998) and Galal (1996).

exports is dramatic. Evidence from cross-country analyses show that inefficient services are a determinant factor in increasing production costs and reducing output (World Bank, 1998).

### **5.2 Crowding Out of FDI and Skewed Investment Incentives**

Inefficient protected services markets have negative effects on the allocation of resources and investment incentives. A study found that the structure of the effective rate of protection (ERP) is completely different when one considers the cost of inefficient services (Hoekman and Djankov, 1997). The simulation exercise, carried out in the aforementioned study, proved that a large number of industries, which currently enjoy high positive ERPs, will suffer negative ERPs during and after the implementation of the Egyptian-European Partnership Agreement. This means that the efforts of the Egyptian government to promote investment in certain sectors are hindered by the absence of an efficient services sector. Consequently, announcing and adopting an export-oriented strategy is likely to suffer from loopholes and unexpected outcomes as long as ERPs differ from the normal protection upon which the government builds its calculations. Moreover, there is substantial evidence that FDI in services accompany FDI in manufactures to provide the needed efficient services (Lawrence, 1996). As long as the Egyptian government willingness to liberalize its services sector is limited and/or unclear and/or not “anchored”, it is likely that Egypt will suffer from a dual effect of crowding out of FDI. *First*, existing FDI in non-services activities (industry and agriculture) will flow to other countries, which have efficient services infrastructure and other favorable conditions for FDI. The impact of the ‘hub and spoke’ argument for the EU-Mediterranean Partnership Agreements is highly relevant here. *Second*, the potential FDI in services will be diverted to other countries as long as it faces impediments in contesting the Egyptian services market. The race for attracting FDI among the MNCs will play a determinant role in this context.

### **5.3 Negative Impact on the Balance of Payments**

One of the main counter-arguments for not liberalizing trade in services is the fear from its negative impact on the balance of payments. Policy makers in developing countries often argue that liberalizing the services sector will increase the balance of payments deficit. This argument presumes that developing countries are at a comparative disadvantage in the provision of services.<sup>39</sup> If we concentrate on the case of Egypt, we find that such an argument is false as revealed by the RCA that Egypt enjoys in services (see *Table 4.*) and by the currently positive contribution of the services to the current account (see *Table*

3.). The curing of the chronic deficit in the balance of merchandise goods, which is increasing, can be embedded in the provision of efficient services, especially if they constitute a large share of the production costs. Thus, on the one hand, opening up the services sector in Egypt to foreign competition might have negative impact on the balance of trade in services (its final outcome will depend on many variables, including the development of the Egyptian exports of services which can increase if their cost of dependency on other services decrease as a result of liberalization, e.g. the decrease in the telecommunication costs for the hotel and tourism services). But, on the other hand, it is likely to have a positive effect on the balance of trade in merchandise goods, if the liberalization of the services sector is translated to competitive and contestable efficient services markets. Moreover, the GATS agreement allows for safeguard measures that can be utilized in the case of severe balance of payments problems. The point that has to be clearly made is that non-liberalization of the services sector can exacerbate the balance of payments problems rather than reduce it.

To sum up, the negative consequences of an inefficient services sector in Egypt are obvious. Despite the Egyptian efforts to eliminate the deficiency in the services sector, these efforts still remain short of being sufficient. Although, it is difficult to assess the domestic policy and regulatory reforms in the services sector due to the short time that has elapsed since the beginning of their implementation, it is evident that Egypt had foregone the possibility of “anchoring” them and providing them with “credibility” effect when observing its commitments under the GATS and the RTAs it is pursuing.

The liberalization of trade in services is still in its infancy stages in Egypt. The limited commitments that Egypt has made in the GATS agreement and the decision not to liberalize trade in services in the context of the Egyptian-European Partnership Agreement and confining it to the GATS commitments, are clear evidence on the decision of the Egyptian policy makers to choose a piece meal approach to liberalizing trade in services. Nevertheless, the Egyptian government has embarked on a comprehensive domestic reform program for increasing competitiveness in the services sector mainly through deregulation and privatization actions that remain to a large extent confined to the national private sector. A concrete evaluation of domestic reforms in the services sector cannot be undertaken due to the short time that has elapsed between the start of implementing such reforms and the time of pursuing this study. Consequently, the policy suggestions provided concentrate on specific issues that need to be taken into consideration in order to lessen the negative effects of not liberalizing trade in services within the context of the Agreement. Four issues are identified, namely: reaching an agreement on the rules of origin of services within the context of the Egyptian-European Partnership Agreement; upgrading the domestic regulatory system related to services; liberalization of trade in services with other MNCs and Arab countries; and finally, utilizing the potential

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<sup>39</sup> For a review of arguments in favor of not liberalizing services sector due to the misguided conception of its negative effect on the balance of payments see: World Bank (1998), op.cit., pp. 14-15.

comparative advantage in a number of services through the outsourcing processes between European firms and their Egyptian counterparts.

Contrary to the effort devoted to the rules of origin of merchandise goods within the context of the Egyptian-European Partnership Agreement, the rules of origin of services were completely neglected. Although services are not liberalized, reaching an agreement on rules of origin is a vital issue that needs to be negotiated and agreed upon in order to avoid any potential problems in the future, especially that rules of origin under the GATS differ from rules of origin of services within RTAs. The key issue in determining rules of origin of services is identifying the nationality of service providers. The nationality of service providers are determined, in turn, according to five main criteria which include: place of incorporation, nationality of ownership, headquarters location, principal place of business, and control of the incorporation (control is defined according to the GATS as a person having the power to name the majority of directors, or to otherwise legally direct the actions of the entity) (WTO, 1995). In some cases more than one criterion are used to identify rules of origin. Under the CUSFTA, for example, rules of origin for services were determined by ownership *and* control of the incorporation and not by residency. In the case of NAFTA, rules of origin are more liberal and are extended to include investments in services made by any resident or incorporated entity in a NAFTA country, regardless of the country of ownership or control. As far as the EU is concerned, Article 58 of the Treaty of Rome specifies that a corporation in order to be considered an EU company, not only must be incorporated in a member state, but *should also have* its headquarters/central administration *or* principal place of business within the EU (Hoekman and Sauve, 1994). The GATS adopts a broader and more flexible definition for the nationality of service providers as it defines juridical persons as entities constituted under the law of a signatory member and engaged in substantive business operations in the territory of that signatory or any other member; *or* owned *or* controlled by natural persons who are nationals under the law of a member. Ownership requires a person of a member country to have at least 50 percent of total equity (WTO, 1995). Consequently, the incompatibility of the rules of origin of services under the GATS and the EU can create problems for Egyptian service providers trying to penetrate the EU market. For example, an Egyptian service provider can satisfy the rules of origin of the GATS concerning the ownership condition that allows him to operate in the EU market (through double nationality or through joint venture), however, he could face the problem of the place of headquarters not positioned in the EU. Other potential problems could arise if no agreement is reached between the Egyptian negotiators and their European counterparts concerning the rules of origin of services. The problem is likely to escalate in the future due to the accelerating ongoing innovations in the provision of services.

The upgrading of the regulatory system that governs the services sector in Egypt is important for two main reasons. The first reason is the gaining of benefits of domestic reforms. Studies on specific service sectors in other countries show that privatization accompanied by inadequate regulation can lead to negative impacts on welfare as low productivity and high private sector returns may result in foregoing the main intention of the domestic reforms that aim mainly to provide efficient services (cost and quality wise) in a competitive environment.<sup>40</sup> The absence of a competition law is highly relevant here because of the nature of the market structure of the majority of the service sectors (monopoly or oligopoly). Privatization in the absence of a competition law and/or sectoral regulations can lead to negative results as long as the main forces driving efficiency, namely competitiveness and contestability of markets, are absent. The second reason behind the importance of the upgrading of the regulatory structure is confined to the outcomes of the Egyptian-European Partnership Agreement. Since there is a possibility of liberalizing trade in services in the future and since the strict regulations can act as non-tariff barriers, reaching some kind of mutual recognition agreement (for example, on minimum standards for services and service providers) is essential. Given the wide gap between the Egyptian domestic regulations and their counterparts in the EU (e.g. labor standards and child labor), the Egyptian government should devote extraordinary efforts to upgrade the domestic regulations. Such upgrading of domestic regulations in Egypt will facilitate the future negotiations on mutual recognition agreements and harmonization of standards. Regional agreements in this regard can be a better facilitator than the multilateral agreements if we consider regulations as a public good (see for a similar argument Mattoo and Fink, 2002). As asserted by Hoekman and Messerlin (1995, pp. 11-12), "Multilateral negotiations and institutions should be seen and used as a facilitating device to support the process of implementing the reforms, not as the driver of reform".

The liberalization of trade in services between Egypt and other MNCs and Arab countries is important for two main reasons. First, this may reduce the 'hub and spoke' effect between Egypt as well as other MNCs and the EU. The same arguments that apply for the likelihood of the 'hub and spoke' effect in the case of merchandise goods apply to the case of services as well. Consequently, to mitigate such a negative impact, liberalization of trade in services should complement liberalization of trade in merchandise goods between Egypt and other MNCs. The reluctance of Egyptian policy makers to liberalize trade in services should be reduced in this case because of the relative similarity in the degree of development of MNCs to Egypt especially when compared with the

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<sup>40</sup> See Galal and Nauriyal (1995), op.cit. for a study on the regulations related to the telecommunications sector in a number of developing countries including Chile, Argentina, Jamaica, Malaysia, Mexico, Philippines and Venezuela. For the importance of regulations in the field of service liberalization see Primo Braga (1996) and Deadorff (2000).

EU, which implies that the fear of other countries gaining all the benefit from such liberalization due to their degree of development is reduced. The second reason that should motivate Egypt to be engaged with other MNCs and Arab countries in liberalizing trade in services is the complementarity of factors determining trade in services in these countries. This in turn reduces the friction of negotiating liberalization of different modes of providing services and enhances the competition in the domestic market. For example, whereas Egypt and other North African countries (Tunisia and Morocco) enjoy a comparative advantage in tourism, hotel services and other labor-intensive services, countries in the Gulf area (e.g. United Arab Emirates and Bahrain) enjoy a comparative advantage in financial services (e.g. off-shore banking that is highly developed in those countries). The potential gains from utilizing the complementary nature of MNCs and other Arab countries, where labor is abundant in some and capital is abundant in others, suggest that the liberalization of trade in services among them is highly promising.<sup>41</sup>

Finally, Egypt should devote more efforts to benefit from the phenomenon of splintering or outsourcing of services. Several developing countries have made good use of outsourcing processes for services<sup>42</sup> though they were not necessarily engaged in RTAs with countries where the re-exported products were directed. RTAs definitely facilitate this type of trade if it includes a deeper dimension related to harmonization of standards and approximation of laws and regulations.<sup>43</sup> Within the context of the foreign trade policy of the EU, the Central and Eastern European countries (CEECs) have made good use of such outsourcing schemes, especially in the field of merchandise goods and are strong competitors to MNCs.<sup>44</sup> The availability of moderately trained human capital in Egypt complemented by low wage rates signal potential benefits in increasing such kind of trade in services as “back-office” activities and software programming. The recent improvements in telecommunications and data processing technologies facilitate the engagement in such kind of trade. This implies that exploiting market niches in such kinds of trade should be on the top of the agenda for Egyptian policy makers and export promotion agencies.

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<sup>41</sup> For a similar argument expecting optimistic payoffs among countries in the Middle East which encompass MNCs and Arab countries if they pursue RTA due to the complementarily nature of their economies where some are labor abundant and other enjoy possibility of exporting capital see Fisher (1993).

<sup>42</sup> The most notable examples are Jamaica in data processing and India in software development. For more details see: United Nations Conference on Trade and Development (UNCTAD) and the World Bank (1994), op.cit., p. 78. For a similar view see Deadorff (2000).

<sup>43</sup> For a similar argument see: Page and Underwood (1997), esp. pp. 111-113.

<sup>44</sup> For more details on the outsourcing trade and the competition between Eastern and Central European countries and the MNCs see: Alessandrini (2000).

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**Table 1: World-Leading Exporters in Commercial Services and Merchandise Goods, 2001**

Country	Rank	Share of total World Trade in Commercial Services	Country	Rank	Share of total World Trade in Goods
United States	1	18.1	United States	1	11.9
United Kingdom	2	7.4	Germany	2	9.3
France	3	5.5	Japan	3	6.6
Germany	4	5.5	France	4	5.2
Japan	5	4.4	United Kingdom	5	4.4
Spain	6	3.9	China	6	4.3
Italy	7	3.9	Canada	7	4.2
Netherlands	8	3.5	Italy	8	3.9
Belgium-Luxembourg	9	2.9	Netherlands	9	3.7
Hong Kong, China	10	2.9	Hong Kong, China	10	3.1
Canada	11	2.4	Belgium	11	1.8
China	12	2.3	Mexico	12	1.6
Austria	13	2.2	Korea, Rep. of	13	1.5
Korea, Rep. of	14	2.0	Taipei, Chinese	14	1.3
Denmark	15	1.8	Singapore	15	1.2
Singapore	16	1.8	Spain	16	1.8
Switzerland	17	1.7	Russian Fed.	17	1.7
Sweden	18	1.5	Malaysia	18	1.4
India	19	1.4	Ireland	19	1.3
Taipei, Chinese	20	1.4	Switzerland	20	1.3
Ireland	21	1.4	Sweden	21	1.2
Greece	22	1.3	Austria	22	1.1
Norway	23	1.1	Saudi Arabia	23	1.1
Turkey	24	1.1	Thailand	24	1.1
Australia	25	1.1	Australia	25	1.0
Malaysia	26	1.0	Brazil	26	0.9
Thailand	27	0.9	Norway	27	0.9
Mexico	28	0.9	Indonesia	28	0.9
Poland	29	0.8	Denmark	29	0.8
Israel	30	0.8	India	30	0.7
Russian Fed.	31	0.7	Finland	31	0.7%
<b>Egypt</b>	<b>32</b>	<b>0.6</b>	UAE	32	0.7%
Brazil	33	0.6	Poland	33	0.6%
Portugal	34	0.6	Czech Rep.	34	0.5%
Hungary	35	0.5	Philippines	35	0.5%
Czech Rep.	36	0.5	Turkey	36	0.5%
Finland	37	0.4	Hungary	37	0.5%
Saudi Arabia	38	0.4	South Africa	38	0.5%
Indonesia	39	0.4	Israel	39	0.5%
Croatia	40	0.3	Venezuela	40	0.4%

Source: World Trade Organization website: <http://www.wto.org/stat/stat.htm>

**Table 2: Share of Services to Gross Domestic Product in Egypt, Mediterranean Non-Member Countries (MNCs) and Income Groups Averages, 1980, 1998**

Services as Percentage of GDP	1980	1998
Egypt	45	50
Turkey	51	57
Morocco	51	54
Tunisia	55	58
Algeria	36	41
Jordan	64	72
Syria	56	NA*
Israel	NA	NA
Cyprus	NA	NA
Malta	NA	NA
Low Income Countries (average)	30	38
<i>Low middle Income Countries (average)</i>	NA	52
Upper middle Income Countries (average)	47	57
High Income Countries (average)	59	65
World (average)	56	61

\*NA stands for not available

Source: World Bank (1999/2000), *World Development Report*, New York: Oxford University Press published for the World Bank, p. 252-253.

**Table 3: Balance of Net Exports of Merchandise Goods, Balance of Net Exports of Commercial Services and Current Account in Egypt, 1991- 1998 (US \$ Million)**

	1991	1992	1993	1994	1995	1996	1997	1998
Balance on Goods	-5,667	-5,231	-6,378	-5,953	-7,597	-8,390	-8,632	-10,214
Balance on Services	3,419	2,849	2,528	2,425	3,717	4,187	2,610	1,649
Current Account	1,903	2,812	2,299	31	-254	-192	-711	-2,566

Source: International Monetary Fund (1999), *Balance of Payments Statistics Yearbook*, Washington D.C.: International Monetary Fund, p. 257.

**Table 4: Revealed Comparative Advantage (RCA) in Commercial Services in Selected Countries, 1985, 1990, 1992**

Country	1985	1990	1992
<i>Egypt</i>	2.42	2.96	3.10
Jordan	3.28	2.83	2.84
Turkey	1.32	1.76	1.65
Tunisia	1.98	1.58	1.49
Morocco	1.72	1.58	1.36
Mexico	0.84	0.81	0.76
Korea	0.96	0.74	0.66
Japan	0.65	0.66	0.61
United Kingdom	1.30	1.16	1.08
France	1.47	1.32	1.39
Italy	1.13	1.12	0.57
Germany	0.79	0.65	0.62
Greece	2.05	2.47	2.69
Spain	1.86	1.71	1.69

Source: Economic Research Forum for Arab Countries, Iran and Turkey (ERF) (1998), Economic Trends in the MENA Region, Cairo: ERF, p. 71.

**Table 5: Number of Basic Telephone Lines per 1,000 People in Mediterranean Non-Member Countries (MNCs), 1997**

Number of basic telephone lines per 1,000 people	1997
<i>Egypt</i>	56
Turkey	250
Morocco	50
Tunisia	70
Algeria	48
Jordan	70
Syria	88
Israel	450
Cyprus	NA*
Malta	NA
Low Income Countries (average)	32
<i>Lower Middle Income Countries (average)</i>	108
Upper Middle Income Countries (average)	179
High Income Countries (average)	552
World (average)	144

\*NA stands for not available

Source: World Bank (1999/2000), World Development Report, New York: Oxford University Press published for the World Bank, p. 266-267.

**Table 6: GATS Commitments of Selected Mediterranean Non-Member Countries (MNCs) made till year 2000**

Countries	Number of Commitments	Number of Sectors where Commitments were made
Turkey	72	9
Morocco	41	7
Egypt	28	4

Source: adapted from World Trade Organization website: [www.wto.org/services/websum.htm](http://www.wto.org/services/websum.htm)