

ERF Policy Brief

Aid for Trade and Exports in the MENA Region: When Institutions Matter

Nora Aboushady, Georges Harb and Chahir Zaki

About the authors

Nora Aboushady is Associate Professor of Economics at the Faculty of Economics and Political Science, Cairo University and Senior Researcher at the German Institute of Development and Sustainability, Bonn, Germany.

Georges Harb is Associate Professor of Economics at the Adnan Kassab School of Business, Department of Economics, Lebanese American University, Beirut, Lebanon.

Chahir Zaki is a Chaired Professor of Economics, University of Orléans, Laboratoire d'Economie d'Orléans, and Economic Research Forum.

In a nutshell

- Aid for Trade (AfT) is found to increase the probability to export and the volume of bilateral exports of aid-recipients.
- The difference in the quality of institutions (institutional distance) between recipient and donor countries dampens the positive effect of AfT on both margins of recipient's exports.
- AfT for trade policy is the most important aid type for promoting both margins of exports of recipients.
- Strengthening the quality of institutions in recipients would enhance the positive impact of AfT on their exports.

Aid for trade, exports, and institutions

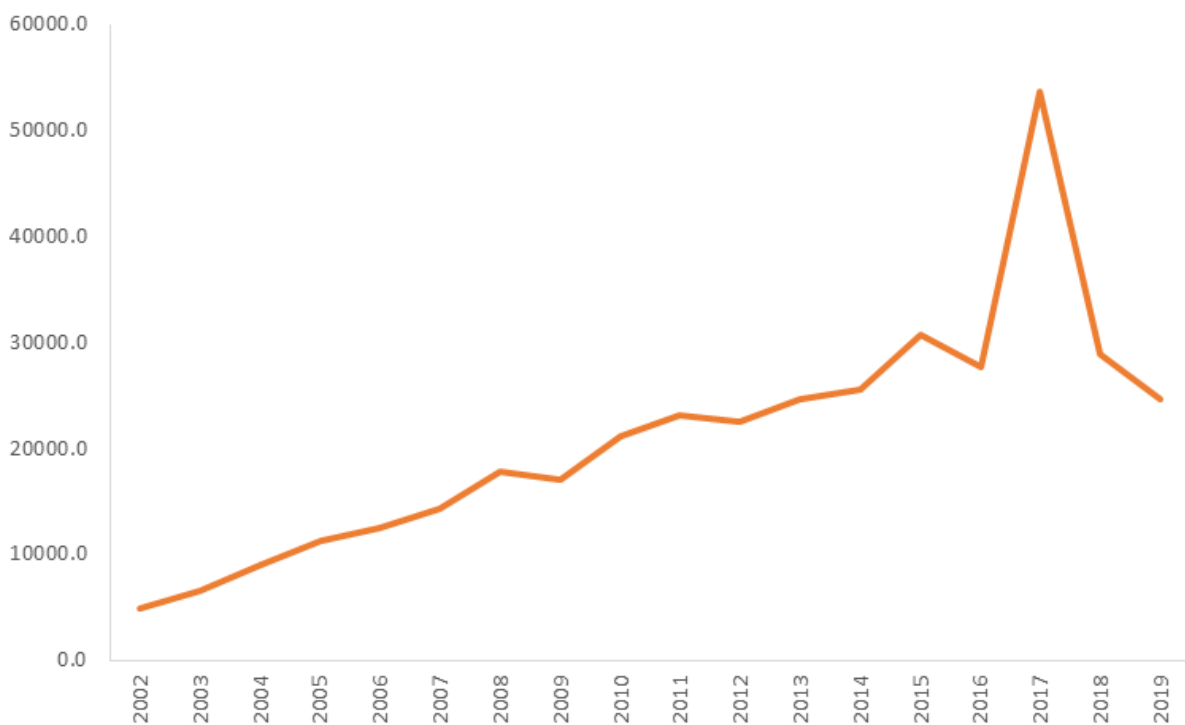
With the launching of the “Aid for Trade Initiative” in 2005 by the World Trade Organization, donor countries started funneling larger volumes of “Official Development Assistance” that aim at enhancing trade capacities of recipient countries. Such aid, labeled “Aid for trade” (AfT), increased from 11.3 billion USD in 2005 to 53.7 billion USD in 2018 (see Figure 1). AfT can be divided into three categories: aid for economic infrastructure, aid for productive capacity, and aid for trade policy. The first category includes aid flows targeting infrastructure like transport and storage, communications, energy, in addition to banking and financial services. The second category regroups all flows related to economic sectors including agriculture, forestry, fishing, industry, and mining. The third category of AfT includes all flows pertaining to trade policy administrative management, trade facilitation, enhancing regional trade agreements and multilateral negotiations, and trade-related adjustments.

The MENA region has benefited from AfT inflows since 2002, before such aid flows were officially labelled as AfT (see Figure 2). Between 2002 and 2019, MENA countries received AfT amounting to 20 billion USD on average per annum. Moreover, the AfT obtained

by MENA countries represented around 13 percent of total disbursed AfT over the same period. Many MENA countries were pursuing parallel reforms aiming at less restrictive trade policies, opening up their markets to foreign investments, with crucial repercussions on their development prospects.

In view of the increasing importance of AfT in the international agenda of donors, and of the mounting evidence of its positive effect on trade of recipients (Lemi, 2017; Gnangnon, 2019; Lee and Oh, 2022; Nishitaten and Umetani, 2023), our recent research (Aboushady et al., 2024) investigates the following: i) did AfT promote exports of recipient countries at the intensive and extensive margins (i.e. on the changes in the volume of exports from an AfT-beneficiary to a donor country, and on the likelihood of exporting by an aid-recipient country to a donor country, respectively)?; ii) what AfT categories matter more for exports of recipients?; and iii) does the quality of institutions in recipient countries impact the way AfT affects recipients’ exports? Our investigation is particularly informative to the MENA countries, given the importance of trade for development and job creation, and the trade and governance-related reforms implemented by several MENA countries over the recent decades.

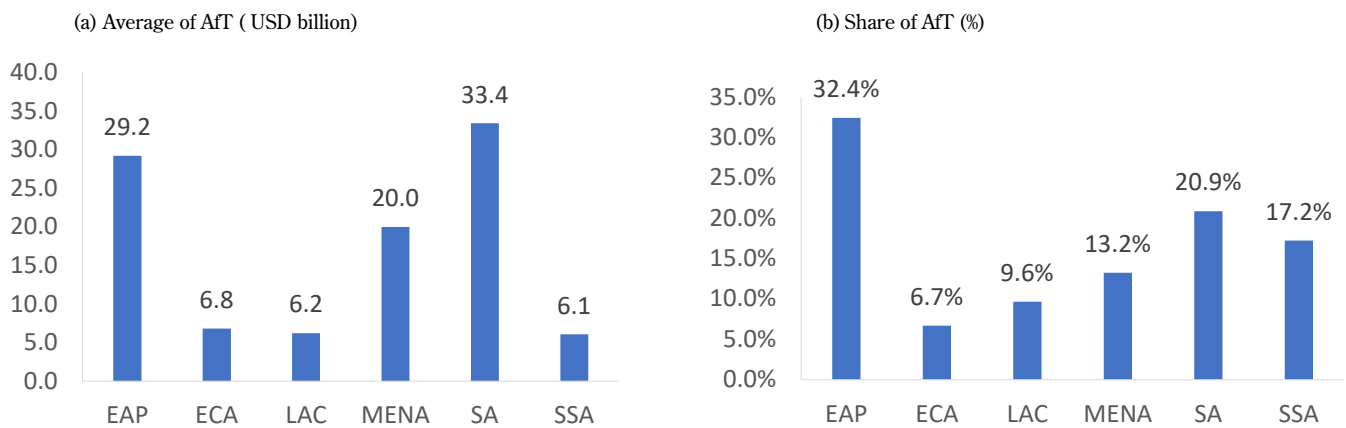
Figure 1: Evolution of aggregate AfT (in USD millions)



Source: Aboushady et al. (2024).



Figure 2: Average AfT and share in total AfT flows by region



Source: Aboushady et al. (2024).

Note: EAP (East Asia and Pacific), ECA (Europe and Central Asia), LAC (Latin American and the Caribbean), MENA (Middle East and North Africa), SA (South Asia), SSA (Sub-Saharan Africa).

Methodology and findings

To answer the three above-mentioned questions, we empirically test for the impact of AfT on the exports of recipient countries at the extensive and intensive margins. We use a gravity model to implement our empirical analysis. Our explanatory variable of interest is AfT (aggregate AfT, AfT for economic infrastructure, AfT for trade policy, AfT for productive capacities). We also include a variable reflecting the “the institutional distance” between the recipient and the donor countries and an interaction term between the latter and AfT to account for the possible moderating role of institutions (i.e. the role such difference in institutional quality between donor and recipient countries can play in strengthening/weakening the impact of AfT on the exports of recipients). Finally, we account for the geographical and income heterogeneity of the recipient countries by adding regional and income-based dummy variables.

Our key findings are as follows. First, the effect of AfT is overall positive on both trade margins and decreasing with the institutional distance between recipients and donors: the larger the distance (i.e. the lower the quality of institutions in recipients), the smaller the effect of AfT on the extensive and intensive export margins. Second, the marginal effect of AfT on exports varies significantly across regions. Remarkably, the MENA region performs well in comparison to the other regions: with the second-highest impact on the extensive margin, and the highest impact on the intensive margin, among

all regions. Third, the magnitude of the effect of aid on both trade margins differs substantially across the different AfT sub-categories. Overall, AfT for trade policy comes first in terms of its impact on recipients’ exports. Given its role in promoting trade facilitation and trade-related negotiations, and streamlining trade policy, this result comes as no surprise. By and large, AfT for productive capacities is particularly relevant for stimulating exports at the intensive margin, whereas AfT for economic infrastructure is especially important for fostering exports at the extensive margin. In line with our general findings, AfT for trade policy is by far the aid category that matters the most for both margins of trade in MENA countries. AfT for productive capacities is especially relevant for the intensive margin, while AfT for economic infrastructure is notably important for the extensive margin.

Policy implications

A number of policy recommendations stem from our research. First, given the important role of institutions, recipient countries would further enhance the benefits of AfT if they ameliorate their governance quality and reduce their institutional gap vis-à-vis donor countries. This is particularly relevant for MENA countries, in view of their comparatively weak institutions and in light of our findings on the large impact of AfT on their exports. Second, in the light of the positive contribution of AfT to the expansion of the prospects of trade and to the trade volume in aid-recipients, donor countries should consider increasing the amount of disbursed AfT,



especially in regions that did not historically benefit from large aid inflows. Lastly, since institutions in aid-recipient countries were found to condition the efficacy of AfT, tying the amount of aid disbursed by donors to reforms undertaken in recipients to strengthen the quality of their institutions would be advisable.

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Contact Information

ERF Office

Address: 21 Al-Sad Al-Aaly St. Dokki, Giza, Egypt

PO Box 12311

Tel: +202 333 18 600 - 603

Fax: +202 333 18 604

Email: erf@erf.org.eg

Website: <http://www.erf.org.eg>

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