Economic and Social Implications of Globalization for the Arab Countries

GOUDA ABDEL-KHALEK AND KARIMA KORAYEM[1]

I. Introduction

Globalization has economic and social implications, particularly for Third World countries. The Arab countries, being part of the latter group, are subject to those likely impacts. The objective of this paper is to assess the most important economic and social implications of globalization on the Arab countries, and to suggest appropriate policies that can be applied to reduce the negative impacts, and maximize the positive ones, on those countries.

This study will focus on assessing the likely impacts of globalization on economic growth (and sectoral structure) in the Arab countries, and their vulnerability. Two aspects of the countries' vulnerability will be investigated in the study: (i) the implications of globalization on the evolution of the countries' international trade relative to their GNP; and (ii) the implications for the financial markets and their likely impact on the countries' economies. With regard to the social implications of globalization, we shall be concerned with their potential impact on employment and poverty.

From a socio-economic perspective, the Arab countries are not homogenous in many respects. There are considerable differences among them in economic size and structure, population size, income per capita, balance of payments, labour market, poverty, etc. Such differences will be reflected in the type of problems those countries may face, and in the policies they may adopt to address the challenges of globalization. Thus, to assess the likely economic and social impacts of globalization on the Arab countries, one has to get acquainted, first, with their main socio-economic features.

The literature offers various definitions of the term 'globalization' which perhaps reflect different perceptions of the phenomenon. Thus, we must first define the concept of globalization, before attempting to assess its implications for the Arab countries.

The study consists of five parts following the Introduction. Part Two will include a review of different definitions and perceptions of globalization as derived from the literature. In Part Three, we shall identify the main features of the Arab countries that are relevant to our assessment. Part Four will include the assessment of the economic implications of globalization with respect to economic growth (and sectoral structure) and economic vulnerability. Part Five will comprise the assessment of the social implications of globalization regarding employment and poverty. Finally in Part Six, some policies will be suggested to enable the Arab countries to deal with globalization more effectively.

II. The Concept of Globalization[2]

Globalization is at the same time an old and a recent phenomenon. It is an old phenomenon if we confine it to the volume of international trade, since for the industrial countries the level of merchandize trade relative to GDP prevailing in 1913 was not obtained again until the late 1960's or 1970's, and some countries have not reached the earlier level yet, such as Australia, Denmark, Japan and the United Kingdom (Feenstra, 1998). However, it is a recent phenomenon if we broaden it to include trade and financial flows, outsourcing of production, etc. based on the outcome of the Uruguay Round of the General Agreement on Tariffs and Trade (GATT 1994), whose implementation started with the establishment of the World Trade Organization (WTO) in 1995.

We are more concerned in this study with the recent vintage of globalization, embodied in GATT 1994 and implemented by the WTO through the enforcement of its rules and regulations. Since there is no universal definition of globalization, the literature will be reviewed to select the appropriate and operational concept to be adopted for our analysis.

Globalization is perceived by some authors as an abstract concept that does not refer to a concrete object but to an interpretation of a societal process (Lubbers, 1998). Others define it as the process by which nationality becomes increasingly irrelevant. According to this perception, two types of globalization exist: globalization of consumption, referring to

the situation where the nationality of the consumer becomes independent of the nation in which a product was made; and globalization of production/ownership, indicating that the nationality of the owner and controller of productive assets is independent of the nation hosting them (Head, 1997).

Michel Camdessus, the former managing director of the International Monetary Fund (IMF), described globalization as an architecture made up of seven building blocks that will lead to the prosperity of the world.

The seven blocks are: The tremendous potential for growth and prosperity globalization provides countries fully integrating into the global economy; integration (by integrating themselves, the poorest countries will accelerate development); the universal consensus on the importance of an increasingly open and liberal system of capital flows; the golden rule of transparency; good governance; a set of standards and codes of best practices; and the option for the multilateral approach to handle problems that are now more global in nature (Camdessus, 1998).

Another definition in the literature differentiates globalization from internationalization. According to this perspective, the world at present is undergoing an "internationalization" phenomenon and not a "globalization" phenomenon. In the international economy, trade and financial flows take place between nations and under the regulations and laws of those nations, while in the global economy all the international relations (trade, capital flows, etc.) take place under unified international laws and regulations issued and enforced by international institutions (Hirst and Thompson, 1996).

Perhaps the most operational definition of globalization for our purpose is the one which characterizes globalization in terms of its major dimensions. Globalization is a process which involves trade liberalization, financial liberalization, outsourcing of production, and the increased harmonization of economic institutions and the regulatory framework in the countries of the globe (Cardoso, 1996; Sachs, 1998).

To study the implications of globalization for the Arab countries, we should, first, get acquainted with the current state of globalization in terms of its four dimensions and the major players (developed *vis-à-vis* developing countries) in each of them. This will clarify the present picture of globalization which will enable us to assess its likely economic and social impact on the Arab countries.

International Trade

International trade, one of the four major aspects of globalization, has as its main actors the Triad countries (North America, European Union (EU) and Japan) and the multinational corporations (MNCs)[3]. In 1992, 69.9% of world exports took place within the Triad countries[4], which have only 14 percent of the world's population (Hirst and Thompson, 1996, Tables 3.2 and 3.3). MNCs are also major players in international trade; about 80% of US trade was conducted by MNCs, which is typical for the developed countries as a whole. Also, 90% of MNC headquarters are located in the developed countries (Hirst and Thompson, 1996, p.53).

North-South trade has fallen as a proportion of world trade due to the decline of the share of raw materials in total trade. This decline is attributed to the fall in oil prices after 1985 and to the deterioration of the terms of trade of raw materials (Jilberto and Mommen, 1998). The fall in North-South trade, and the small share of the intra-trade of the developing countries indicate the marginalization of the Third World with respect to this dimension of globalization.

Financial Liberalization

Financial liberalization is the second aspect of globalization. Liberalization involves short-term capital flows and foreign direct investment (FDI). The latter is the most important component of financial liberalization because of its impact on economic development in the Third World countries. Looking at the world distribution pattern of FDI, one finds that it is concentrated in the developed countries. The Triad countries—North America, Europe and Japan—attracted 75% of the FDI flows over the 1980's; and at the beginning of the 1990's, 75% of the total accumulated FDI stock and 60% of the FDI flows were attracted by these three players (Hirst and Thompson, 1996). The MNCs are also the main channel for global FDI. The 100 largest MNCs accounted for a third of the total FDI stock and 14% of the total flow in 1990; 60% of the MNC FDI stock was associated with manufacturing, 37% with services, and only 3% with the primary sector (Hirst and Thompson, 1996).

The South is left behind in this dimension of globalization as well. Only 5% of the stock of FDI had its origins with MNCs in the developing countries. Moreover, two thirds of the FDI flowing to the developing

countries are concentrated in ten countries only[5], leaving the majority of the developing countries in a disadvantageous situation (Hirst and Thompson, 1996). What is striking is the large increase in FDI relative to exports since the 1980's. For example, between 1983 and 1990, FDI flows grew at an average annual rate of 34% compared with an annual rate of 9% for world merchandise trade; i.e., FDI grew almost four times faster than trade over the eight-year period (Hirst and Thompson, 1996). In another estimate, FDI flows grew three times faster than trade flows and almost four times faster than output (Jilberto and Mommen, 1998). Despite the difference in estimates, both sources agree that FDI grew at a much faster rate than did trade.

Liberalization of short-term capital flows minimizes risks and maximizes profits for the investors in the financial markets. International financial markets allow residents of different countries to pool various risks, achieving more effective insurance than domestic markets would allow (Obstfeld, 1998). On the other hand, liberalization of short-term capital has its negative impact on investment and production. Despite the positive impact of financial liberalization, the quick and large profits that short-term capital may realize in a relatively short period of time by moving globally between financial markets reduces the supply of funds available for direct investment. It has been observed that the increase in profits achieved by the globalization of production does not translate into increased investment in production as would have been expected, since a good part of these profits find their way to financial markets instead of being re-invested in production.

Internationalization of Production

Globalization is also characterized by the internationalization of production. At present, it is quite common for the production of one good to be allocated among several countries to lower costs and maximize profits. The MNCs are also leaders in the outsourcing of production. It is estimated that one third of the total trade in the US is intra-MNC trade (Hirst and Thompson, 1996). The integration of production itself leads to more trade as intermediate inputs cross borders several times during the manufacturing process (Feenstra, 1998). Outsourcing the production of some goods or some intermediate products to developing countries where wages are low has generated a body of literature that investigates the impact of this phenomenon on the labour market in the developed economies. These countries are currently experiencing rising

unemployment of unskilled labour and a deterioration in income distribution due to the growing income gap between the wages of unskilled and skilled workers (Kim, 1997).

There is more than one factor responsible for this phenomenon in the developed countries, and the studies differ among themselves with respect to the relative weights they give to those factors. Some studies attribute the main cause of the rising unemployment of unskilled labour and the deterioration in income distribution in the developed countries to the outsourcing of some products to developing countries (Feenstra, 1998; Feenstra and Hanson, 1997). Others argue that the impact of this factor on the labour market of the advanced economies is minor, and they maintain that the main cause is the rapid technological development which has led to less demand for unskilled labour and an intensified use of capital and skilled labour (IMF, 1997; Burtless 1995). Outsourcing of some products to developing countries can be viewed as highly beneficial for the developed countries if their economies have flexible labour markets and effective adjustment mechanisms to shift their production to sectors with higher value added per unit of input than low value-added manufacturing (IMF, 1997).

Despite the fact that the developed countries produced more than two-thirds of the global GDP from 1970-1989[6], and that the flow of FDI to the developing countries, even in periods of peak flow, is a tiny portion of the capital stock in the developed world[7], the developed countries perceive the outsourcing of unskilled labour-intensive products to the developing countries as a threat to their economies. If this threat is real in the sense that the advanced economies are confronted with the prospect of the collapse of employment and output, then they may go so far as to reintroduce tariff barriers and exclude Third World products. In such an eventuality, to quote Hirst and Thompson (1996; p.119), "GATT would be swept away by political necessity".

The Spread of the Global Market Economy

The fourth dimension of globalization is the spread of the global market economy. The state was a major player in the economic system adopted by many developing countries in the sixties and seventies. In the eighties and nineties, this system was abandoned by many Third World countries and substituted by the free-market system which was based on the International

Monetary Fund (IMF) and World Bank (WB) tailored structural adjustment programmes (SAPs). In many cases the SAPs were not successful in achieving the economic objectives of the developing countries (increasing production, raising incomes, reducing unemployment, etc.). The success of these programmes was confined mainly to the financial objectives, such as reducing government deficits and inflation rates. In many countries, including the Arab countries, these IMF-WB SAPs produced negative results, such as raising unemployment, increasing poverty, and worsening the income distribution pattern. Thus, although the institutionalization of the market-economy system worldwide will help to speed up globalization, the fruit of this process may not be equally shared by the developed and developing countries. The already wide economic and social gaps between the parties involved may grow even wider.

III. Main Features of the Arab Countries

The countries in the Arab region are not homogenous in their economic structure or their size, and this has significant implications for the policies they adopt and the problems they face. Therefore, some classification of these countries into homogeneous sub-groups should be made according to a chosen criterion. Two types of classification are adopted by the organizations working in the region. The first is the classification used by the Economic and Social Commission for Western Asia (ESCWA), which divides the member countries into two groups: the Gulf Cooperation Council (GCC) members, which include Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates (UAE); and the non-GCC countries, which include the rest of the Arab countries. The second classification is adopted in the Unified Arab Economic Report, produced by the Arab League, the Arab Fund for Economic and Social Development, the Arab Monetary Fund, and the Organization of the Arab Oil Exporting Countries (Arab League et al, 1994). This classification divides the Arab countries into two groups: the major oil-exporting countries (which include the GCC members plus Algeria, Iraq and the Libyan Arab Jamahiriya) and the rest of the Arab countries (which have more diversified economies). We shall adopt the latter classification since the major oil-exporting countries with their special characteristics—the relatively high income per capita, the heavy dependence on one commodity (oil), less diversified economies and the small population in most of them—might be affected differently by the economic and social implications of globalization from the other Arab countries.

One may point out the following features and differences among the countries of the region:

The major oil-exporting countries, especially the GCC members, are small in terms of population, but relatively large with respect to the GNP; the reverse is true in the other Arab countries with more diversified economies. Based on the data in Tables 1 and 2, Group 1 countries have 32.7% of the population and claim 66.2% of the total GNP of the region. The GCC countries as a subgroup of Group 1 have 10.9% of the population and claim 39.2% of the GNP in the region. Saudi Arabia has the largest GNP in the Arab region (21% of the total). Group 2 countries have 67.3% of the population and 33.8% of the total GNP in the Arab region. This has been reflected in the considerably higher income per capita in Group 1, especially in the GCC countries, as compared to the average income per capita in Group 2 countries.

As shown in Table 1, in the major oil-exporting countries population is below 3 million in each of the GCC countries in 1998, with the exception of Saudi Arabia whose population is close to 20 million. Among the non-GCC countries in Group 1, Algeria has the largest population (close to 30 million). In Group 2 countries, the population is less than 10 million in half of them (Lebanon, Tunisia, Jordan, Djibouti and Mauritania), while below 20 million in two countries (Syria and Yemen), around 30 million in Morocco and Sudan, and about 61 million in Egypt.

The average annual population growth rate is the highest in the GCC countries (2.9%), as compared to an average growth rate of 2.5% in Group 2 countries and 2.0% in the non-GCC countries in Group 1 (Table 1). This average population growth rate in the Arab region is considerably higher than the comparable rate over the period 1990-98 in the world's low-income countries (2.0%), middle-income countries (1.5%) and high-income countries (0.7%) (World Bank, 2000a, Table 3).

One of the consequences of the high population growth rate in the Arab region is the low ratio of labour force to total population as compared to other groups of countries. In 1998, the participation rate was about 37% in the GCC countries and Group 2 countries, and 31% in the non-GCC countries in Group 1 (Table 1). This is much lower than the comparable ratio in the low-, middle- and high-income countries in 1998, which is 50.0%, 44.0% and 48.6%, respectively (calculated from: World Bank, 2000a, Table 3). This low participation rate results in a high dependency ratio in the Arab region, which is one of the primary causes of poverty[8].

This ratio is between 3 and 4 in all the Arab countries (with the exception of Somalia and the UAE) as compared to a value of 2 in the developed countries (e.g., France, Germany and the USA) and the newly industrialized countries (NICs), such as Hong Kong and Singapore (Korayem, 1998). Another consequence of the relatively high population growth rate is that a high percentage of the population is below 15 years of age, which implies a potential increase in the rate of growth of the supply of labour in the coming generations. This will increase the potential for unemployment in the region, especially given that one of the likely impacts of globalisation on the Arab countries, (as developing countries), is an increase in unemployment (see section V.1 in this paper). The ratio of the population below 15 years of age in total population in 1998 in the Middle East and North Africa (MENA) region, which is representative of the Arab region according to the World Bank classification[9], is 42.1% as compared to 38.7% in the low-income countries, 36.5% in the middle-income countries, and 33.1% in the high-income countries[10].

As can be seen from Table 2, all the countries in Group 1 (with the exception of Algeria) as well as Lebanon in Group 2 have a GNP per capita in 1998 that ranges between $3650 and $16,900. Algeria and more than half of the countries in Group 2 (Tunisia, Jordan, Egypt, Morocco, Djibouti and Syria) have a GNP per capita that ranges between $1000 and $2050. The rest of the Arab countries in Group 2 (Mauritania, Sudan and Yemen) have GNP per capita less than $400. This means that three out of the nineteen Arab countries have per capita GNP below $1000. This implies an improvement in the average income in the Arab region, specifically in Group 2 countries[11], since five out of the nineteen countries had income per capita below $1000 in 1993 (Korayem, 1996).

Looking at the structure of production in the Arab countries in 1998, Table 2 shows that the extractive industries—which are mainly oil—represent about one-quarter or more of the GDP in the GCC countries, with the exception of the UAE and Bahrain in which the share of the extracting industries in GDP is 22.0% and 13.5%, respectively. Excluding Iraq, which is presently subject to international sanctions, the relative share of the extractive industries in GDP in the non-GCC countries in Group 1 is 16% in Libya and 23% in Algeria. The manufacturing sector in most of the major oil-exporting countries is involved in producing oil-related commodities, such as petrochemicals and oil products, etc. (see the manufacturing sector in the GCC countries in: The Inter-Arab Investment Guarantee Corporation (1994)). Bahrain, Algeria and Iraq have more

diversified production structures than other countries in Group 1. In all the GCC countries excepting Saudi Arabia, the agricultural sector is insignificant (3.4% or lower of GDP). In Saudi Arabia and Libya, the relative share of agriculture in GDP is around 7%, while its relative share is as high as 11% and 33% in Algeria and Iraq, respectively.

The countries in Group 2 have a more diversified structure of production (see Table 2). With the exception of Djibouti and Jordan, the relative share of the agricultural sector ranges between 8% in Lebanon and 49% in Sudan. The relative share of the manufacturing sector in GDP ranges between less than 4% in Djibouti and 18% in Tunisia. The relative share of the extractive industries is in the range of 11% and 19% in three countries (Mauritania, Syria and Yemen), and 6% in Egypt. It falls to 4% and less in the rest of the countries in the group.

Reviewing the ratios of government revenue and expenditure in the two groups of countries in the Arab region as reported in Table 3, one finds the following: In 1998, the ratio of government revenue to GDP in all the major oil-exporting countries (Group 1), with the exception of Libya and Kuwait, falls within the range of 24% and 34%. In Group 2, all the countries, with the exception of Lebanon and Sudan, have a ratio of government expenditure to GDP that ranges between 22% and 32%. This shows that, with few exceptions, the ratio of government revenue to GDP falls between one-fourth and one-third in the two groups of countries. This is quite a convergence between the two groups of countries as compared to 1993, when the difference between them in this ratio was significant[12]. On the other hand, there is a considerable difference in the ratio of government expenditure to GDP in the two groups of countries. In 1998, government expenditure in GDP was around 40% and more in the major-oil exporting countries, with the exception of Bahrain and Algeria. In the Group 2 countries, the ratio was below 30% for all of them, with the exception of Lebanon, Jordan and Yemen.

This close range between the two groups of countries in the government revenue ratio and the considerable differences in the government expenditure ratio is reflected in the difference in the size of government budget deficits in the major oil-exporting countries as compared to the other Arab countries in Group 2. In Group 1 countries, the budget deficit in 1998 was 5% and higher in the GCC countries, while it was lower in the non-GCC countries (zero deficit in Libya and 4% in Algeria). The budget deficit was below 5% for all Group 2 countries, with the exception of Lebanon (16%) and Jordan (7%) (Table 3).

Table 4 shows the trade and current account balances in the Arab region in 1998. Looking at the balance of trade in Group 1, one finds that all the countries, with the exception of Oman, have a trade surplus. The ratio of trade surplus to GDP is 3% and below in four countries (Qatar, Bahrain, Libya and Algeria), and 7% and higher (up to 9%) in the UAE, Kuwait and Saudi Arabia. In Oman, the trade deficit amounts to 2.2% of GDP. In Group 2, all the countries have a deficit in the balance of trade, with the exception of Mauritania. The ratio of the trade deficit to GDP is 9% and higher in all the countries in the group with the exception of Syria, and reaches 22% and 36% in Jordan and Lebanon, respectively. The current account in 1998 was in deficit in both groups of countries, with the exception of the UAE and Kuwait in Group 1, and Jordan, Syria and Mauritania in Group 2. However, the current account deficit was considerably higher in the GCC countries as compared to the other major oil-exporting countries and all the countries in Group 2, with the exception of Lebanon and Sudan; it is 10% and higher in the GCC countries as compared to 5% and lower in the other Arab countries.

IV. Economic Implications of Globalization for the Arab Countries

As already mentioned in Part Two, globalization is a multi-dimensional process. It amounts to redefining borders in time and space. For the purpose of discussing the economic implications of globalization for the Arab countries, it may be useful to focus on its four specific dimensions: trade liberalization, financial liberalization, outsourcing of production and standardization of institutions and regulatory frameworks. Due to space considerations, we shall confine our discussion of the economic implications to two aspects only, namely: growth/sectoral structure of GDP, and vulnerability.

IV.1. Implications for Growth and Sectoral Structures

Conventional wisdom dictates that overall economic growth combines growth in factor inputs and the growth in total factor productivity. The implications of globalization for economic growth will depend on the prospects of the growth in factor inputs and in total factor productivity under globalization. A clear distinction has to be made of various categories of countries: in particular developed *versus* developing, open-

border *versus* land-locked or isolated[13]. More than two centuries ago, Adam Smith observed that the great geographical discoveries at the turn of the 15th century were the "greatest and most important events recorded in the history of mankind" (Sachs, 1998). They paved the way for the first "global" division of labour, with Smith providing the theoretical model expounding the benefits of trade liberalization. New mathematical models of endogenous growth have lately been developed which emphasize that long-run growth depends on increased productivity and innovation, which in turn depend on the scope of the market. If outsourcing raises productivity and cuts unit costs, a "new division of labour" emerges within the context of the MNCs. Sachs observed that early postwar development economists could not conceive of such a division of labour in manufacturing. According to him, those economists "simply couldn't conceive of the production process being a complementary relationship between advanced and developing countries…..both sides of the great income divide stand to benefit from globalization" (Sachs, 1998, p.101)[14]. It should be stressed, however, that the standard theory rests on some critical assumptions—most notably competition in factor and product markets (Stiglitz, 1998).

There is currently a heated debate regarding the relation of openness and growth (Edwards, 1998; Greenaway *et al*., 1977; Frankel and Romer, 1999; de Mello, Jr., 1999). Part of the debate is related to conceptual issues—trade liberalization *versus* outward orientation. Part of it relates to methodological issues—particularly the measurement of openness and hypothesis-testing based on cross-section regression analysis. Another methodological problem is the difficulty in establishing trade-growth causality due to the endogeneity of both trade and GDP growth.

We shall not go into the details of this debate. One may only point to the difficulty of answering the question regarding the implications of trade liberalization for economic growth. By necessity, the broader issue of the implications of globalization for growth will be much more difficult to clarify. The reason is that globalization, as already indicated in Part Two above, involves trade liberalization, financial liberalization, outsourcing of production, and the standardization of institutions and regulatory frameworks around the world. Against this background, one may ask: What does globalization imply for growth of the Arab economies?

A. Implications for growth Growth depends on changes of both factor inputs and total factor productivity. With regard to the latter, we can only say that globablization may be expected to raise total factor productivity.

Factor inputs represent mainly labour and capital. With regard to labour input, it may be safe to assume that the change in labour input will depend on the behaviour of the demand for labour under globalization. The demand for labour and employment is discussed in detail in section V.1 below. With regard to the supply of labour (availability of labour input), this should not be a constraining factor to economic growth in the light of existing high rates of unemployment in most of the Arab countries and the high rate of labour force growth. Thus, although accurate and regular data on unemployment are rather scarce in the Arab countries, available evidence shows high rates of unemployment in the region (see section V.1 below).

The total labour force amounted to 92.6 million out of a population of about 270 million, making an overall participation rate for the Arab countries of 36% (Table 1). The average annual growth rate of the labour force from 1990-1998 is estimated at 3.4% in the MENA region (World Bank, 2000a, Table 3). For the purpose of judging the prospects of labour supply in the Arab countries, therefore, it is interesting to note that they have the lowest labour force participation rate and the highest labour force growth rate of any regional group (Karshenas, 1997; Arab League *et al.*, 1999)[15].

We conclude this part on labour input by saying that as far as long-run growth is concerned, Arab economies need not worry about the availability of labour. In fact, they may have to consider structural changes to enhance the labour intensity of economic activity. They also have to improve the quality of their labour force through education and training. That way, they can ensure that growth will be labour-absorbing.

What about the other factor input in the growth process – capital? Available data suggest that the 1970's were perhaps the golden decade in terms of the rate of capital accumulation in the Arab countries. Thus, while fixed investment during the 1970's grew annually at rates averaging from 10% to 15%, its growth was mostly negative during the 1980's. Consider the illustrative cases of a number of Arab countries (Table 5). The data show that the decade of the 1970's witnessed a boom in investment. In every country in the region, investment accelerated. One may explain this by the oil booms of 1973-74 and 1979-80[16]. The dollar value of oil exports from the Arab countries rose by 2385% in nominal terms, and by 794% in real terms during the 1970's[17]. On the other hand, the 1980's witnessed an absolute decline in many of the Arab countries. Again this was strongly

correlated with rather dismal oil fortunes during the decade. Since 1980, the real price of oil was subject to steady decline with fluctuations in the range of $15 – $20 per barrel in 1995 prices. In fact it never regained its 1974 level throughout the period following 1984. This may explain the very significant drop in the economic growth rate of the Arab countries from 1980 to 1991 corresponding to the fall in investment reported in Table 5.

In terms of macro balances, the fall in investment implies a particular pattern of adjustment to the fluctuations in the price of oil and oil revenue. Analysis of saving behaviour for the oil-exporting countries during the 1980's and 1990's may throw some light on this adjustment pattern. Thus, during the boom, savings increase at a rate lower than the rate of increase in real income; but during the bust, savings fall by the full extent of the decline in real income. For example, during the oil boom of 1996-97, real income resulting from terms-of-trade improvement increased by 4.6% of GDP for all oil exporters taken together. But savings increased by only 2.5% of GDP. During the oil bust of 1998, while oil exporters as a group sustained a terms-of-trade related drop in their real income of 5.4% of GDP, their savings fell by 5.3% of GDP (World Bank, 2000b, Table 4.1). At the same time the rate of investment was almost constant at about 22% in 1998 and 1993[18]. This means, correspondingly, that consumption rises faster than income throughout the oil-price cycle; the adjustment to the fall in income is made through the reduction in savings. If the trend in the long run is a decline in the real price of oil, this pattern, if it persists, has disturbing implications for investment, growth and employment.

So far, our analysis of macro adjustment to boom and bust in world markets has focussed on Arab oil-exporting countries. But what about the non-oil exporting ones? In an attempt to address this question, we make the following observations. First**,** oil is important as a source of foreign-exchange revenues to non-GCC countries in Group 1 (such as Libya, Iraq, and Algeria), and to some of the more diversified economies in Group 2 (such as Egypt, Syria and Yemen). There are indications that Sudan may soon join this club. According to 1998 data, oil exports accounted for about 40%, 44% and 46% of the value of total exports of Egypt, Yemen and Syria respectively (Table 4). Second**,** labour movement within the region and related remittance income has forged a very strong link between oil and non-oil economies in the region. This has tempted some analysts to talk about remittance sensitive states (RSS). Sullivan (1998) observed that not only oil shocks (such as in 1985-86) but also other non-oil shocks to the oil states, such as the Gulf crisis of 1990-91, can affect RSSs rather

significantly (Sullivan, 1998)[19]. Third**,** capital flows from the oil states to non-oil states in the region represent yet another link, which proved rather sensitive to oil-related developments. Fourth**,** in the case of certain strategically located countries such as Egypt, transport activities related to the oil trade contribute significantly to the economy. We conclude, therefore, that macro-economic adjustments to oil booms and busts apply to oil and non-oil economies in the Arab world.

How then does globalization affect the growth of the Arab countries? The answer is neither easy nor straight forward; remember that globalization can be a vague—if not fuzzy—term. However, it may be useful for organizing one's thinking to make a distinction between two types of considerations which may have bearing on the question raised. There are general considerations and specific considerations. The first category represents factors that may apply to all developing countries in general. The second category represents factors that apply to the Arab countries specifically. Let us address the first category first:

1.Globalization may be viewed as a new stage in the development of the capitalist system. At this stage the world economy suffers a multi-dimensional crisis: a crisis of structural over-accumulation and financial anarchy. In the industrialized countries, which are the locomotive of the world economy, the rate of gross fixed capital formation (i.e., fixed investment as a proportion of GDP) has been falling since the mid-seventies. For example, the rate of investment has fallen from 30% to 19% in Germany and from 20% to 14% in the United States between the mid-fifties and the mid-nineties (Kisker, 1996). For the group of countries which now constitute the European Union, the investment rate fell from about 25% to about 19% and for Japan from 36% to 28% over the period 1965 to 1994 (Hirst and Thompson, 1998, p.126). The other side of the coin is secular decline in the world economy (Table 6).

The overall picture is quite clear. There is a downward trend in real world GDP growth since the mid-sixties. The growth rate achieved in 1998 was almost one-third of the average for the period 1966 to 1973. The regional variations in GDP growth rates do not change the overall picture, but rather confirm it. With regard to growth prospects in developing countries, it is more likely that their growth from 1999 to 2008 will be lower than the growth rates achieved before the financial crises of 1997 to 1999 (World Bank, 2000, p.3). Several factors contribute to this outcome: most notably, a significantly less favorable and more fragile external

environment and a prolonged working-out of structural weakness in the developing countries' financial sectors and fiscal balances[20].

The financial crises of 1997-99 revealed the fragility of the international financial system, or rather the lack of an adequate system. Due to the tremendous development in the financial industry, particularly the creation of derivatives and the expansion of forward exchange-rate transactions, it is becoming possible for some agents to create money or liquidity in offshore markets without control by any national authority. This has created imbalance between the real side and the financial side of the world economy. It is estimated that the value of annual foreign-exchange transactions is almost one hundred times the value of international trade[21]. Financial liberalization in many countries taking place within the context of structural adjustment programmes through the Bretton Woods institutions, facilitated the movement of hot money between various markets. Against this background, one observes the recurrence of financial and foreign exchange crises at an accelerating pace: 1987, 1992, 1995, 1997-99.

Among the general considerations in the context of the growth implications of globalization, special mention should be made of GATT/WTO discipline. Most important, by emphasizing liberalization as the dominant issue, it has created a regime which may be appropriate for trade but perhaps not as appropriate for governing the flows of FDI. The current ungoverned and skewed distribution of FDI threatens to limit the growth of the entire world economy and tilt the terms of trade against developing countries (Hirst and Thompson, 1998, p.52).

2. With regard to the specific considerations relevant to the case of the Arab countries for discussing the growth implications of globalization, we must emphasize oil and foreign investments. The Arab countries together have more than 60% of the world's proven oil reserves, and at least one-fifth of the natural gas reserves[22]. Oil has played a crucial role in the recent economic history of the region. We have discussed the macro adjustment problem posed by booms and busts related to oil. Although it may be difficult to rigorously link oil prospects to globalization, one may relate the prospects of oil to world growth in the context of globalization. We have already noted the apparent likely trend toward decline in world growth and its relation to globalization. That should mean slower growth in demand for oil, other things being equal. If we also assume that technological advance as part of globalization may reduce energy intensity of output in general, and oil intensity in particular, we reach the conclusion that the observed

trend in the real price of oil since 1980 will most probably continue (see data in Arab League *et al.*, 1999, p.260 and p.262).

The price of oil experienced a very hard landing in 1998, falling to a twenty-year historical low (World Bank, 2000b, Table A2.11). With regard to long-term prospects, the World Bank forecasts oil prices to remain under downward pressure in the longer run. The main factors behind this development are limited growth in demand for OPECs crude oil, increased competition from both oil and other energy producers, falling production costs for crude oil and other energy sources in the light of technological advances (in oil shale and liquefied natural gas). These factors may effectively set a price ceiling for crude oil in the neighborhood of $20 per barrel for the foreseeable future (World Bank, 2000, p.25). This is almost the same nominal price which prevailed during the oil booms of the early- and mid-nineties, but significantly below the price experienced during the oil boom of 1979-85 (see World Bank, 2000, Table A2.11; the Arab League *et al.*, 1999; Annex Table 5/4). It is important to note that these forecasts should be revised downward when Iraq resumes oil production and export[23].

It should be observed that, according to some energy experts, oil and natural gas fall under the GATT/WTO discipline, although they were not explicitly mentioned in GATT 1947. GATT 1994, including the agreement on trade in goods, Trade Related Investment Measures (TRIMS) and Trade Related Intellectual Property (TRIPS), has a clear bearing on oil and gas by the force of its three basic principles, particularly the tariff-only principle (Abdalla, 1999). If putting a ceiling on oil production (in order to protect its real price and to conserve) is successfully challenged within WTO, this would mean that the long-run oil price forecasts mentioned above would have to be revised downward.

Foreign investment MNCs are playing an increasingly important role in the context of globalization. GATT 1994 included a separate agreement on foreign investment, the agreement on TRIMS. The essence of this agreement is deregulation. This means that member countries commit themselves to remove various regulations put in place previously to ensure that foreign investment brings maximum benefit (contribution) to the economic development of the host country. Thus, national investment codes will eventually have to be revised to drop such stipulations as domestic content requirements, balance-of-payments requirements, and employment-of-nationals requirements. This is a good example of the

fourth dimension of globalization mentioned in Part Two above (harmonization of regulatory framework).

The Arab countries as a group send much larger investments abroad than what they receive. There are no accurate data on the outflow of Arab investment. But an estimate may be made for the first half of the 1990's. The stock of Arab investments abroad rose from $400 billion in 1990 to $750 billion in 1995 (Kharioush and El-Hamoury, 2000**)** One may infer from this information that the net outflow of Arab investments averaged about $50 billion annually during 1990-95. About 80% of Arab investments are based in the developed economies in Europe, Japan and the United States, the bulk of which is bank deposits and government securities. The flow of Arab investment to Arab countries is just a trickle, representing $1.5 – $2.0 billion annually (Kharioush and El-Hamoury, 2000).

The Arab countries have attracted only limited amounts of FDI, fluctuating around 0.5% of GDP during the decade from 1985 to 1994. The bulk of this investment was concentrated in the energy sector. In the first half of the nineties, a number of Arab countries opened up to foreign capital by liberalizing the capital account in the balance of payments (Egypt is the most important example). Egypt successfully experienced the first global deposit receipts (GDR) placement of private sector equities in industrial markets. Lebanon has also successfully placed GDRs and sovereign bonds to attract foreign-investment participation in its massive reconstruction effort. Tunisia has already placed international bond issues in the Euro and Samurai markets. At the same time there has also been a dramatic increase in the number of equity mutual funds directed at the region (El-Erian and Sheybani, 1997).

As a result of these and other changes in the international financial setting, the flow of net private capital to the group of Arab countries included in Table 7 reached $4.3 billion of which $2.4 billion FDI, $2.1 billion portfolio investment and $ -0.24 billion of net debt flows. The data in Table 7 reveal two interesting results. First**,** the MENA region, which consists mainly of Arab countries[24], compares rather unfavourably both with developing countries as a group and with each regional group in the developing world, with the exception of sub-Saharan Africa. As a group, these Arab countries for which data are available attracted private capital only to 1.6% of their GDP in 1997. This is less than one-third the corresponding ratio for the developing countries.

The data in Table 7 also show that private foreign-investment flows to the majority of Arab countries amounted to less than 1.5% of total private flows to developing countries. So the magnitude of private investment flows to the Arab countries is extremely low. An interesting question is why this rather modest rate of capital inflow to the Arab countries, and what are the prospects for future investment in the context of globalization?

Second, the data reveal a highly skewed pattern of inflow. Inflows in the form of portfolio investment for the Arab countries included in Table 7 in 1997 was 48.6% of total private flows and 85.6% of FDI. This compares with only 10% and 18.5% respectively for developing countries. In the case of Egypt, portfolio investment represented 70% of total private capital flows, and more than double the magnitude of FDI. The example of Egypt epitomizes the dangers involved in the indiscriminate opening of the economy to foreign capital inflows. If foreign capital is necessary to complement domestic saving and increase the rate of domestic investment, efforts should be directed to attract FDI. Portfolio investment by its very nature is highly volatile and may constrain the conduct of monetary and exchange-rate policy[25]. It may even have troubling fiscal consequences. In short, portfolio investment should be seen as engendering economic vulnerability of a modern vintage.

The upshot of the foregoing discussion is that in terms of the growth of the Arab economies, the globalized economic environment may be less enabling. We now turn to the issue of the implications for sectoral structure.

B. Implications for sectoral structural change The economies of the Arab countries may be characterized as resource-based to varying degrees (see Table 2). At one end we find the GCC countries in Group 1, where the share of extractive industries in GDP averaged 27% in 1998. This is followed by the more diversified oil countries in Group 1, Libya, Iraq and Algeria, where extractive industries contributed about 12% of GDP. This figure would have been higher were it not for the economic sanctions imposed on Iraq following its invasion of Kuwait in 1990. At the other end, we have Group 2 countries where the share of extractive industries is the lowest, averaging 5% of GDP. However, if we add the contribution of agriculture, the share of resource-based sectors is also high even in this group of non-oil economies (about 23% of GDP)[26]. Manufacturing accounts for some 10%-15% of GDP, lower in many oil countries, but

about 17-18% in some of the non-oil countries, specifically Egypt, Morocco and Tunisia.

Table 2 also reveals the pattern of sectoral distribution of GDP in terms of the familiar commodity-service sector dichotomy. On this basis we find that in 1998, there was an even (50-50%) split of GDP between commodity and service sectors for Group 1 countries together and about a 46%-54% split in Group 2 countries. It is interesting to observe that Group 1 includes high- and upper-middle income countries (except for Iraq and Algeria) according to World Bank classification by per capita GDP. Group 2 is composed of lower-middle and low-income countries (see Table 2). One would have expected the share of the tertiary sector to be higher in Group 1 than in Group 2 —this is from an Engel's Law perspective[27]. But the situation depicted in Table 2 does not obey the economic logic of Engel's Law. The reason is that in Group 2 countries, the service sector is a bundle of formal and largely informal activities reflecting the fact that the service sector in a poor developing economy performs the function of a reserve and buffer.

What are the implications of globalization for sectoral structure of GDP? In answer to this question we offer the following observations regarding dimensions of globalization.

1. Trade liberalization is likely to put the manufacturing sector in the Arab countries under relatively stronger competitive pressure due to the more open trading regime. Trade liberalization under GATT/WTO discipline does not totally preclude government intervention to promote industry. Although such discipline prohibits subsidies to exports, most preferential measures to protect infant industries and to diversify manufacturing are still permissible (Amsden, 2000). GATT 1994, like GATT 1947, allows members to protect themselves against competition from aggregate imports that destabilize their balance of payments (Article XVIII), and also against competition which threatens individual industries.

With regard to support for industrial development, GATT 1994 makes a distinction among three categories of subsidies: prohibited, actionable and permissible. The latter include those for the promotion of research and development (RandD), for regional development, and for environmentalism (Amsden, 2000).

The most important industries in the Arab countries are chemicals (including oil refining), food processing, textiles and clothing, and

machinery and transport equipment. According to the most recent figures (for 1997), these industries accounted for 23%, 22%, 15% and 13% of value added in manufacturing for the Arab countries as a group. There are significant country variations. For example, the chemical industry appears to be of growing importance in Saudi Arabia[28]. Food processing contributes a much higher share in the manufacturing value added in Mauritania (41%), Morocco (31%), Lebanon, Iraq and Syria (about 25-27%). Textiles and clothing play a more important role in Tunisia (36%), Syria (31%) and Egypt (23%) (Arab League *et al.*, 1999; Appendix Table 4/5).

In addition to the trade liberalization in the globalized context of GATT, the manufacturing sector in the Arab countries will be also affected by two important developments toward regionalism. The first is the partnership agreements between some Arab countries (those in the southern Mediterranean) and the European Union (EU) within the framework of the Euro-Mediterranean Association Agreements (EMAAs). So far, four association agreements have been signed between the EU and each of Tunisia, Morocco, Jordan and the Palestinian Authority. Egypt appears to be in the final stages of reaching an agreement, while Algeria, Lebanon and Syria are currently negotiating to conclude association agreements. The second is the Greater Arab Free Trade Area (GAFTA), initiated on 17 February 1997 by the executive programme of the Economic and Social Council of the Arab League to set up a free trade area over ten years (1998-2007). To date, 14 countries have participated in this effort: Jordan, UAE, Bahrain, Tunisia, Saudi Arabia, Sudan, Syria, Iraq, Oman, Qatar, Kuwait, Lebanon, Egypt and Morocco[29] (Arab League *et al.*, 1999; Ch.12).

Such a plethora of regional multilateral and bilateral trade agreements raises serious issues of trade diversion and trade creation. But for our purposes, we would like to underscore the point that a pan-Arab integration effort is important for securing better terms for the Arab countries in the global economy. One should not push the point about trade diversion vs trade creation too far, since it is based on static welfare comparisons. The dynamic growth effects, though difficult to measure, may be more important.

On this basis, we argue that expansion of the manufacturing sector in the Arab countries within the context of globalization will depend to a great extent on the ability of the Arab countries, through integration and other measures, to take advantage of some aspects of the present GATT /

WTO discipline to promote manufacturing. Moreover, pan-Arab integration will also, among other things, enhance the position of the Arab countries in the competition for FDI on more reasonable terms. The critical mass guaranteed by establishing a regional Arab block is a precondition for maximizing the gains and minimizing the losses related to globalization.

2. The other sector which is bound to be directly affected by the trade liberalization dimension of globalization is agriculture. One of the consequences of the Agreement on Agriculture in GATT 1994 is the increase in the world prices of many agricultural commodities—notably wheat, sugar, edible oil and dairy products. Net-food-importing countries stand to lose in the process, and their vulnerability may increase if the liberalization of agricultural prices generates greater instability. However, the higher prices for the main agricultural commodities should provide better incentives for local producers, if the right policies are followed. Further, increased market access under GATT 1994 in the area of agricultural trade may encourage expansion of agricultural production in the region, considering its proximity to the European market. Also, if globalization frustrated the efforts of the Arab countries to develop manufacturing, then the weight of the agricultural sector may increase by necessity.

3. The prospects of the service sector in the Arab countries under globalization will depend on the overall growth rate of their economies in relation to population growth. If economic growth outpaces population growth, then we may expect the share of the service sector in GDP to fall initially in relative terms, given the biased structure of this sector towards informal activities as mentioned above. The composition of service activities will change significantly in the process.

IV.2. Economic Vulnerability

What does globalization imply for the Arab countries in terms of economic vulnerability? By economic vulnerability, we mean the degree of sensitivity of the country's economic conditions (i.e., exports, GDP level and growth, inflation, unemployment, poverty and inequality, etc.) in the face of external shocks, whether these shocks are positive or negative. In this context, we may ponder the risks inherent in the integration of capital markets, volatility of international commodity prices (especially oil and food), in addition to changes in world interest rates and exchange rates.

We first examine the current degree of vulnerability. Two measures of vulnerability are used–one narrow, the other broad. The *narrow* (Measure 1), is the ratio of merchandise trade (exports and imports) to GDP. The *broad* (Measure 2), is expressed in three different variants because of data limitations[30]: merchandize trade plus remittances (for 1993)[31]; the ratio of merchandize trade plus net income (for 1998, alternative a); and the ratio of merchandize trade plus net current transfers (for 1998, alternative b). Thus, the results for 1993 and 1998 are comparable for Measure 1, but not for Measure 2. The two measures are reported in Table 8.

According to Measure 1 of vulnerability, a general pattern prevails in 1993 and 1998. GCC countries generally tend to exhibit a larger degree of vulnerability compared to countries of Group 2 and the non-GCC countries of Group 1. For all GCC countries, the ratio of merchandise trade to GDP was significantly higher than 50%, shooting up to more than 100% in a number of cases. In the non-GCC countries of Group 1 and Group 2 (excepting Mauritania, Jordan and Tunisia), the ratio of merchandise trade to GDP is below 50%. This points to a basic difference in the economic structure of the GCC countries on one side and the rest of the Arab countries on the other. The dependence of GCC countries on oil appears to be a major source of vulnerability; such countries are expected to face greater challenges in adjusting to external shocks related to oil.

The incorporation of workers' remittances in the measure of vulnerability leads to a significant increase in the value of the indicator (see Measure 2 for 1993 in Table 8). The increase in the value of the vulnerability indicator as a result of including workers' remittances applies to all countries; but the examples of Jordan and Egypt are outstanding. For Jordan in 1993, Measure 2 produces a value of 131 percent compared to 107 percent for Measure 1. For Egypt, the corresponding values are 43 percent and 29 percent respectively. Although intra-regional labour movement has forged strong links among the labour-receiving and the labour-sending countries, they continue to be a source of vulnerability for the latter in particular. Reduced demand for labour in the Gulf impacts strongly on the labour markets and the balance of payments of these countries, making the adjustment to such shocks rather more difficult.

According to Measure 2 of vulnerability, a similar pattern prevails in 1998. In addition to exports and imports we include both net compensation of non-resident workers and investment income (Measure 2,

alternative a in Table 8); we obtain values for the indicator significantly above 50% in the GCC countries where data are available, as well as in more than half the countries of Group 2. Taking into account net current transfers rather than net income (Measure 2, alternative b in Table 8) does not change the situation.

We conclude that, because of the relatively strong vulnerability of most of the Arab economies to external shocks, macroeconomic policies have to include an anti-cyclical component. It would be more prudent to deal with oil-related booms (or booms in commodity prices in general), not as permanent shocks, but as temporary ones. The brunt of the adjustment would have to be through changes in consumption rather than changes in saving and investment.

In a globalized environment, external shocks may be expected to increase. With such high levels of vulnerability as those of the Arab economies, macroeconomic management plays a more critical role in stabilizing those economies in the face of external shocks. When we look at the implications of globalization in terms of vulnerability, we have to extend the measures to consider recent changes in exchange rates and financial aspects (financial liberalization or capital mobility).

Consider Table 9 which summarizes major changes in the foreign-exchange regimes of the Arab countries in the second half of the nineties. Quite significant changes took place. The number of countries adopting floating exchange-rate regimes increased from 6 to 8 countries. Correspondingly, the number of those adopting a fixed exchange-rate regime fell from 14 to 12 between 1995 and 1998. Nevertheless, 12 countries still have pegged exchange rates, with some change in the anchor away from the American dollar and towards special drawing rights (SDRs). Furthermore, by 1998, all countries but one had moved towards a unified exchange rate.

The liberalization of the foreign exchange regime was accompanied by liberalization of the capital account in a number of Arab countries, alongside restrictive monetary and fiscal policy for stabilization in an attempt to attract foreign capital (Arab League *et al.,* 1999, Ch. 7). The ultimate result may be portfolio inflows driven by interest arbitrage, which may lead to a real appreciation of the national currency and a consequent loss of competitiveness. The experience of Egypt under the Economic Reform and Structural Adjustment Programme, ERSAP, is a vivid example (Abdel-Khalek, 1998). It may not have been a coincidence,

therefore, that the ratio of portfolio investment to total net private capital flows to the Arab countries in 1997 was about five times that for developing countries as a group; it was 48.6% in the Arab countries as compared to 10.1% in the developing countries (calculated from Table 7).

The simultaneous liberalization of the capital and current accounts often produces an uncomfortably high domestic interest/strong currency combination. Such a combination of macro prices does not provide a solid base for improved trade performance or investment to support economic growth. In the process, continuing trade deficits resulting from this interest/exchange combination can ultimately lead to a dynamically unstable situation: actors may suddenly realize that the risks associated with domestic assets are too high. This may very well spark massive capital outflow, devaluation and stagflation. Glaring examples of this scenario were provided by Mexico in 1994 and East Asian NICs in 1997 (Ocampo and Taylor, 1998).

The trend in the Arab countries during the nineties has been to liberalize the current and capital accounts of their balance of payments. For example, in Egypt, there are virtually no restrictions on the flow of capital in either direction (El-Ektessadia, 1996). In Kuwait, GCC nationals can purchase stocks up to a certain limit, non-Kuwaitis can purchase local treasury bills and bonds through local banks and investment companies, and both Kuwaitis and non-Kuwaitis can freely buy or sell foreign exchange (Lain and Dashti, 1999). Issues of Euro bonds and GDRs have been on the rise during the 1990's. In 1998, there were new issues of Euro bonds and GDRs placed by companies and banks in Tunisia and Lebanon; thus joining Jordan, Bahrain, Egypt and Morocco which had already placed a total of about $4 billion in foreign money and financial markets. This may be rather modest, but it points to a new and fundamentally important development.

It should be observed that the question of portfolio investment flows to the Arab countries has been the subject of heated debate. Some argue that FDI may be welcome but not portfolio investment in view of its volatile nature. Others tend to stress the benefits of foreigners' participation in Arab financial markets[32]. We are more inclined to doubt the net benefit of portfolio flows for the development of the Arab economies.

V. Social Implications of Globalization for the Arab Countries

Globalization with its four dimensions—trade liberalization, financial liberalization, outsourcing of production, and the widespread institutionalization of the market-economy system—has social implications for the Arab countries. We shall focus here on the likely impact of globalization on employment and poverty.

V.1. Implications for Employment

Globalization affects employment through its likely impacts on investment, economic growth and the demand for labour.

A. The direct impact of the liberalization of financial flows on employment in the Arab countries is through the amount of foreign direct investment (FDI) flowing to them. FDI has both direct and indirect effects on employment creation in the recipient countries (Lall, 1995).

The direct employment effect of FDI depends on several factors. Among those factors are: (i) the size and type of investment: "greenfield" or acquisition. A "greenfield" investment creates a new productive unit, which adds to the productive capacity of the economy and creates new employment; while the acquisition of an existing enterprise may not necessarily result in an addition to production and employment. (ii) The type of technology adopted. Although it is widely accepted that the transnational corporations (TNCs) usually adopt the latest technology, the investment effect on employment depends on the ability of the host country to master the imported technology and adapt it to its needs. (iii) Other factors also have direct effects on employment, like the strategy of the foreign investor regarding the level and speed of technology upgrading, the export-orientation of the project, the corporate integration strategy of the TNCs concerned, and the economic and market conditions in the host economies[33].

FDI also has indirect effects on employment. Among them are employment creation in firms which are vertically linked to the TNCs, and there may also be spillover effects of TNCs on local science and technology, education and training. Lall (1995) concluded that the employment effects of FDI are complex, and that policies can play a crucial role in stimulating and guiding them.

The likely impact of globalization on employment creation in Arab countries will be positive if a good part of the world FDI is flowing to this region thus raising the investment rates in the economies. The Arab countries already suffer from high unemployment rates. According to the latest data available, the unemployment rate in the early nineties was 14% in Egypt, 18.8% in Jordan, 15%-17% in Lebanon, 12.3% in Yemen and 14.8% in the GCC countries (UNESCWA, 1997a, Table II.3). According to other estimates, the unemployment rate reached 20% in Algeria, Jordan, Lebanon and Tunisia, 15% in Egypt and Morocco, and 60% in the Gaza Strip (UNESCWA, 1997b, p.73). Lately other countries with no unemployment (notably GCC countries) have also started to experience this problem. Furthermore, unemployment has been wide spreading among graduates of university and higher institutes over the past decade (Arab League *et al*., 1999, p.23).

Investment in the Arab countries amounted to 22.1% of GDP on average in 1998 (Table 2). At the country level, the range varies considerably. In the nine major oil-exporting countries (Group 1), the investment rate is above 20% of GDP in four GCC countries (United Arab Emirates (UAE), Qatar, Saudi Arabia and Oman) and Algeria, and in the range of 17% to 19% of GDP in the other countries in the group with the exception of Kuwait (Table 2). In Group 2, the investment rate is above 20% in seven countries (Lebanon, Tunisia, Jordan, Egypt, Morocco, Syria and Yemen), and ranges from 15% to 19% in the three other countries. This implies that the major oil-exporting countries in the Arab region compare less favorably to other Arab countries with respect to the investment rates in 1998, since less than 50% of the countries in Group 1 have investment rates higher than 20% as compared to 70% of the countries in Group 2. This may be explained by the pattern of adjustment to the fall in oil prices and revenue (see section IV.1 above).

The direct impact of the of liberalization financial flows on employment in the Arab region is through the amount of FDI flowing to it. As mentioned in Part II above, most of the world FDI is allocated to the advanced economies, North America, Europe and Japan. A tiny fraction of the already small share of the world FDI flowing to the developing countries is received by the Arab countries. Out of a total amount of $163,423 million (net FDI flows to all the developing countries in 1997), $5368 million was received by the Middle Eastern and North African (MENA) countries (Table 7). This means that only 3.3% of the FDI flowing to the Third World countries

is received by the MENA region. Since MENA consists mainly of Arab countries as shown above, and since flows to the eight largest Arab recipients of FDI as reported in Table 7 totaled $ 2446 million in 1997 (i.e. 1.5% of total flows), the share of Arab countries seems in fact much less than the 3% of flows to developing countries. As a matter of fact, UNCTAD estimates imply total net FDI flows to all Arab countries of about $2874 million in 1997 (UNCTAD, 1998, Annex Table 1); i.e., about 1.8% of total flows to developing countries. Consequently, the likely impact of financial liberalization on employment in the Arab region is negligible, judging by the global distribution of FDI so far.

Looking at the country level, the three largest recipients of the FDI in the Arab region in 1997 were Morocco ($1200 million), Egypt ($891 million) and Tunisia ($316 million) (Table 7); i.e., the three countries together received 44.8% of the FDI flows to the MENA region in 1997[34]. Comparing the ratio of FDI to total investments in the three countries to find out its relative importance to output and employment creation in the economy, one finds that in 1997 it represented 17.4% of total investment in Morocco, 5.8% in Egypt and 6.2% in Tunisia[35]; i.e., in terms of the relative importance of FDI in total investment in the three major recipient countries in the Arab region, Morocco comes first, followed at a distance by Tunisia and Egypt. Yemen, which is one of the low-income countries in the region (see Table 2), had a net outflow of FDI of $138 million in 1997 (Table 7), amounting to 8.6% of its total investment[36].

It might be argued that the potential of the Arab countries to attract FDI in the future is greater than at present, when more economic and financial liberalization takes place in the region, and all the Arab countries become members in the WTO. At present only nine of the Arab countries are members of GATT/WTO: Egypt, Tunisia, Morocco, Djibouti, Mauritania, Kuwait, Bahrain, UAE and Qatar. Lebanon and Yemen are *defacto* members, and three countries are negotiating for membership: Saudi Arabia, Jordan and the Sudan (Zarrouk and Zallio, 2000). Even if the Arab countries succeed in achieving high rates of economic performance and liberalization, it is unlikely that the pattern of global distribution of FDI will be changed considerably in their favour in the short and medium term. In the eighties and early nineties, the FDI flows were strongly biased towards the developed countries as explained in Part II above, despite the high economic performance of some developing countries, such as the NICs.

B. The average annual growth of real GDP in the MENA countries over the period 1991-98 was lower than that of the other groups of countries in the Third World, with the exception of the group designated as Europe and Central Asia[37]; it is 2.9% as compared to 7.6 % in Asia, 3.6% in Latin America and the Caribbean, and 4.1% in Sub-Saharan Africa (World Bank, 2000b, Table A2.1). Taking the population growth rate into consideration, the real per capita growth rate in the MENA region falls to 0.6% during the period 1991-98, as compared to 6.0% in Asia, 1.6% in Latin America and the Caribbean, and 0.1% in Sub-Saharan Africa. The GDP growth rate of the higher income economies was 2.3% over the same period, and their real per capita GDP growth rate was 1.6% (World Bank, 2000b, Table A2.2). Will globalization increase this modest rate of growth in the Arab region?

There are two views—optimistic and pessimistic—regarding the impact of globalization on economic growth in the developing countries in general, and its consequent impact on employment in particular. Within the optimistic view there are two variants. One variant predicts rapid growth in a substantial part of the Third World, in East and South Asia and, possibly, in Latin America (Hirst and Thompson, 1996). The other variant holds that all countries will share the benefits of globalization according to the standard theory. This implies an increase in the economic growth of Third World countries through innovations and access to large markets, with the consequent positive impacts on employment. Three exceptions are mentioned in this respect: land-locked countries, tropical-climate countries, and major producers of natural resources, such as oil (Sachs, 1998).

The pessimistic view predicts that capital mobility and free trade will shift manufacturing investments from the industrial countries to the low-wage developing countries without benefiting the workers in the developing countries. This is because authoritarian governments and repressive labour laws will hold wages down in the Third World. Some even argue that economic growth in developing countries which is driven primarily by foreign capital is not stable, since FDI is highly volatile and leads to highly uneven development[38] (Hirst and Thompson, 1996).

Based on the above arguments, we maintain that according to both variants of the optimistic view, quite a few of the Arab countries will fall within the group of countries that will not benefit from globalization. This is because they are major natural resource producers and, furthermore, some have also extreme climates that make them subject to severe adverse effects that impede their economic growth. On the other hand, according to

the pessimistic view, globalization is not likely to have positive impacts on the economic growth of the developing countries and, hence, of the Arab countries as part of this group.

We have also concluded in section IV.1 above that, on balance, the economic environment under globalization may not be favourable to the growth of the Arab countries. This conclusion was based on two sets of considerations: general (the crisis of structural over-accumulation, financial crises, and GATT/WTO discipline) and specific (oil and foreign investment) (see part A of section IV.1 for details).

Moreover, as labour costs typically represent no more than about 20% of the cost of the final product in manufacturing in advanced countries, the benefits of cheap labour are unlikely to attract products for which RandD costs or marketing costs are as significant (or more significant) than labour costs (Hirst and Thompson, 1996). In addition, average gross labour productivity can be considerably lower in the Arab countries. Despite the very low wages in Morocco and Tunisia as compared to the EU countries —about ten times lower—the very low average gross labour productivity raises the unit labour cost considerably. For example, in 1989, the labour cost per unit—defined as the average wage per unit of value added or the wage/productivity ratio—was higher in Tunisia than in Germany, although lower than in France and Italy (Boughzala, 1997).

C. The outsourcing of unskilled-labour-intensive products to the Arab countries with considerably low wages[39] is likely to have a positive impact on employment in those countries. However, this expectation should be taken with due caution, since the outsourcing of production to the Arab countries (and to the Third World countries in general) is limited. This is because a small portion of the world FDI is channeled to the Third World countries, and a tiny fraction of this small amount is heading towards the Arab countries. As shown above, significantly less than 3% of the total FDI flows to the developing countries were attracted to the Arab countries.

D. Generally speaking, by lowering the tariff levels and phasing out other trade restrictions, trade liberalization helps expand markets. This will increase production and, hence, will create more employment opportunities in the producer countries. However, such implied benefits of trade liberalization on employment will not be equally shared by all countries. The lion's share of these trade benefits will be received by the manufacturing-producing countries, while the smallest share will be going

to the agricultural-producing countries. This is because the Agricultural Agreement in GATT 1994 will not liberalize the trade in agricultural goods to the same extent as the trade in manufacturing products, even after its full implementation. According to this Agreement, all tariffs will be reduced on average by 36% (with a minimum of 15% per each tariff line) as compared to the base period 1986-88. Also, where export subsidies are used, expenditure on subsidies are to be reduced by 36% and the volume of subsidized exports is to be decreased by 21% from the base period 1986-90[40] (Tanner and Swinbank, 1996; Safadi and Laird, 1996). The Agricultural Agreement will be fully implemented by the developed countries in the year 2001, and by the developing ones at 2005[41].

As is frequently the case in the Third World, the Arab countries are mainly producers of agricultural products. A large percentage of the labour force in the Arab countries in Group 2 work in the agricultural sector. With the exception of Lebanon and Jordan, the percentage of labour force working in agriculture in Group 2 countries range from 27% in Syria to 60% in Sudan; only Oman and Algeria of the Group 1 countries have a higher percentage of the labour force in the agriculture sector[42] (see Table 1). Thus, the impact of trade liberalization on growth and employment creation in the Arab countries (and most of the developing countries) will be less than in the case of developed economies that are mainly manufacturing-producers.

E. Lowering tariffs under trade liberalization threatens the production of manufactured goods in most of the Third World countries, including the Arab countries. Being unable to compete with the foreign-produced products in the domestic and international markets, many of the manufacturing industries in those countries will most likely be phased out. The result will be a fall in the demand for labour in the manufacturing sector in the Third World which may not be compensated for by the outsourcing of production from the advanced economies. This is because outsourcing helps very few developing countries, as implied by the skewed pattern of FDI distribution to this part of the world. As mentioned in Part II above, two-thirds of the FDI flowing to the developing countries are allocated to ten countries only. Although Egypt is one of the ten privileged countries, and one may also add to this group Morocco and Tunisia as major recipients of FDI in Arab region, still most of the Arab countries fall in the non-privileged group of developing countries which are marginal recipients of FDI. Even in Egypt and Tunisia, the percentage of FDI to total investment was below 7%, as shown above. Thus, the majority of the Arab

countries are likely to experience falling production and increasing unemployment in the manufacturing sector, being unable to compete with low-priced foreign manufactured goods after trade liberalization.

However, a study on Morocco carried out in 1983 on employment in manufacturing arrived at a different conclusion regarding the effect of trade liberalization[43]. Based on a certain model, the study concluded that employment in the average private sector manufacturing firm was unaffected. Many firms adjusted by cutting profit margins and raising productivity rather than reducing employment. However, there were considerable employment losses to exporters, and publicly-owned firms adjusted by hiring low-paid temporary workers (Currie and Harrison, 1997). On the other hand, the outcome of other studies reviewed by Boughzala (1997) on the likely impact of the free trade area (FTA) with the EU on employment in Morocco and Tunisia confirmed that the effect of the FTA on new employment in the two countries may be marginal or even negative, and that unemployment may worsen and exceed the high rates already prevailing in the two economies. Boughzala (1997) criticized these findings on the basis that they are based on static models[44]. Alternatively, he used a model with a dynamic framework based on what ought to be[45], and not what exists already. His conclusion was that the loss of employment can be compensated for if there will be an annual flow of $1 billion in Tunisia and $2-3 billion in Morocco into low-skilled manufacturing. Given the level of FDI flows to Morocco and Tunisia, this implies a tripling of the current level of capital flows to the two countries to compensate for the expected loss in employment due to globalization (see Table 7).

F. The labour clause, which the developed economies are pushing hard to enforce through the WTO (despite the strong resistance of the developing countries), will have a negative impact on economic growth and employment in much of the Third World, including the Arab countries. According to the labour clause, no imports will be allowed from countries where child labour exists and where working conditions do not abide by human rights requirements (Castle *et al.*, 1998). This labour clause, if applied, will have detrimental effects on the Arab countries and many other developing countries where child labour prevails and where working conditions (like wage level, work environment, unionization) do not fulfill human rights requirements[46]. If the developed countries succeed in enforcing the application of this clause by the WTO[47], this implies putting

trade restrictions on goods produced by the Arab countries which have child labour and unfavorable working conditions. In particular this factor may be important for Mauritania, Yemen and Egypt, where child labour represented 23%, 20% and 10%, respectively, of the population in the child age-bracket (10-14 years) (Arab League *et al.*, 1999, p.23). The impact of this act will be a reduction in economic growth and an increase in unemployment in the countries, most of whom suffer already from low growth and high unemployment rates, as previously shown.

G. As expressed by one study, we might be on the verge of a major revolution in productivity through advances in robotics and information technology, making possible the widespread replacement of human labour (Hirst and Thompson, 1996). In this case, the demand for unskilled labour will be reduced in all countries, developed and developing. But the latter group is the one which is more likely to be hurt most because of the biased structure of its labour force is towards unskilled labour. This is another potential source for the negative impact of globalization on unemployment in the Arab region.

H. Institutionalization of the market-economy, which is one dimension of globalization, will raise unemployment in the economy. This is because one of the important components of the SAP advocated by the IMF and the World Bank is the privatization of publicly-owned enterprises. The Arab countries have substantial public-sector employment as compared to developing and developed countries. Public employment in the Arab countries was, on average, 37% of total employment in the period 1987-92, as compared to an average of 10% for developing countries and 18% for OECD countries (UNESCWA, 1997a, Table II.1 and p.86).

In the Arab region, public-sector employment is highest in the GCC countries, thanks to the practice of providing well-paid jobs to the national labour force, and also because of the states' commitment to providing extensive social services to the population. In the early nineties, public-sector employment in Kuwait and Bahrain was 23% of total employment[48]. Public sector employment is also high in the Arab countries in Group 2; it was 45% of total employment in Jordan in 1987, and was 34% and 33% in Egypt and Syria respectively (UNESCWA, 1997a, Table II.I).

This large public-sector employment makes the price of the institutionalization of the market economy, which is one dimension of globalization, high in terms of job losses. Quite a few of the Arab countries

are adopting structural adjustment programmes. Algeria (1994), Egypt (1991), Jordan (1992), Morocco (1983), Tunisia (1986) and Mauritania (1985) have been applying structural adjustment programmes in cooperation with the IMF and the World Bank[49] (Arab League *et al.*, 1994). One of the important features of these programmes is the privatization of publicly-owned enterprises. Other Arab countries have independently implemented structural adjustment programmes by privatizing the public sector (UNESCWA, 1997a). This implies an increase in unemployment since privatization is accompanied usually by a reduction in the demand for labour. Moreover, the public sector has always served as employer-of-last-resort in the Arab countries[50] and, hence, the reduction of its size implies the elimination of this role[51].

V.2. Implications for Poverty

Poverty estimates in the Arab region are available only for some countries. Comparison of such estimates cannot be safely made because of differences in the methods used in poverty measurement. To minimize this problem, we shall depend on one source for reviewing poverty estimates in the Arab region, the Human Development Report (UNDP, 1995, 1999). But even in this source, poverty data reported for the same country may differ widely because of the difference in the estimation methodology used (see Table 10). It should be noted that the figures in Table 10 are not the only poverty estimates for countries included[52] and, also, the Arab countries that are not included in the Table do not necessarily lack poverty estimates[53]. Thus, the estimates in Table 10 should be taken with due caution; they just give an idea of the state of poverty in some countries in the Arab region. The Table shows that in six out of the eight Arab countries for which data are reported, the poor in the nineties included 30% or more of the population at the urban and/or rural and/or national level. Those countries are: Egypt, Morocco, Syria, Tunisia, Yemen, and Mauritania, according to the estimates in the two Human Development Reports (1995 and 1999).

Globalization affects poverty through its impact on a number of factors: labour earnings, prices of basic commodities and services, and on the scope and intensity of the social safety net provided to low-income people. One may point out the following likely impacts of globalization on the Arab countries, as part of the Third World:

A. Globalization is likely to have contradictory impacts on labour earnings: First with financial liberalization, capital becomes highly mobile to move from one country to another, leaving the countries with high taxes for those with lower ones. Thus, in order to attract more capital—especially FDI—countries compete with each other to lower the tax rates on capital. This is true in all developed and developing countries, but it is of special importance to the latter group of countries which try to attract as much FDI as possible to raise investment and production, despite their low domestic savings. In comparison to capital, labour is less mobile and hence less able to resist higher tax rates. Consequently, it is found that governments are imposing relatively high tax rates on labour as compared to capital. Moreover, taxes on wages would by necessity have to be high enough to compensate for the reduction in government revenue due to the lower taxes on capital (Obstfeld, 1998; Feenstra, 1998).

Thus, financial liberalization, which is one dimension of globalization, is likely to result in a fall in the net income received by workers, who represent the low- and middle-income strata in any society. This implies a deterioration in the income distribution pattern since the government, by applying this discriminatory tax policy against labour, redistributes income in favor of the high-income earners in the society—the capital owners—and against the low-income group, the wage earners. This negative impact of globalization on wages is likely to be greater in the developing countries, including the Arab countries, when compared to developed ones. The former lack strong labour unions and democratic political systems, which provide appropriate forums for the different groups in the society, workers and others, to express themselves freely and defend their interests.

Second**,** labour unions are either lacking or weak in the Arab countries, and commonly in the Third World. Strong labour unions have positive impacts on the standard of living of the workers by raising wages and improving working conditions. Globalization is likely to have two contradictory impacts on labour unions in the developing countries and the Arab countries as part of this group. Institutionalization of the market-economy, which is one dimension of globalization, implies a stronger role for labour unions in the economy. This is supposed to have positive impacts on the standard of living and the quality of life of the labour force in the developing countries. On the other hand, outsourcing of production, another dimension of globalization, is likely to weaken labour unions. This is attributed to the severe competition among countries to keep the production costs as low as possible to attract foreign direct investments and

boost production. Accordingly, labour unions become more reluctant to ask for higher wages in order not to source out production to other countries with lower wages and, hence, lost jobs. Considering these two contradictory implications of globalization on the labour unions, the final outcome of the institutionalization of the market economy in the Arab region may not be as beneficial as one might have expected with respect to its impact on employment and wages. As some writers put it, globalization implies a "race to the bottom" with respect to wages (Lee, 1996).

B. As shown in Table 2, the share of agriculture in GDP is high in most of the Arab countries in Group 2, and in Iraq in Group 1. The impact of globalization on farmers' income in those countries is likely to be positive, but the effect on poor farmers can be considerably less. According to the Agricultural Agreement, the tariffs and subsidies on agricultural products in the developed countries each will be reduced by 36% over a six-years period which started in 1995. The reduction of the subsidies will raise prices of the currently subsidized agricultural products[54] in international markets, while the reduction of tariffs will open the markets of the developed countries for the agricultural products produced in the developing ones. The positive impact on the farmers' income in developing countries, and hence on the Arab countries, will be through the rise in prices of the agricultural products and the increase in exports. However, surveys from several countries indicate that internationally-traded commodities account for the minority of the income of the poor farmers. This reduces the positive impact of trade liberalization on this group. On the other hand, there can be indirect benefit to the rural poor as farm labourers, derived from the increase in income of better-off farmers. With trade liberalization, this latter group will probably increase their demand for labour to produce more export crops (Weeks, 1997).

C. The impact of globalization on the prices of basic consumer goods—which are our main concern when dealing with poverty—is contradictory. Reducing the subsidy on agricultural products in the developed countries, according to the Agricultural Agreements, will raise the prices of basic agricultural goods (like wheat, corn, and sugar) in the international markets. This will raise the cost of living for the consumers, especially hitting the poor and the low-income citizens, since they spend a larger proportion of their budget on food.

However, to assess the impact of the likely rise in the prices of agricultural products on poverty, we should differentiate between the exporting and the importing countries. In the exporting countries, the

impact will be a rise in the cost of living of the urban consumers, while for the rural consumers, specifically the farmers, the net impact is disputable. This is because they will gain from the rise in agricultural prices as producers, but they will lose as consumers[55]. The impact of the rise in agricultural prices on the importing countries is negative. The cost of living will be increased for both urban and rural consumers, with the pinch to be felt most by the poor and the low-income people. However, since countries are usually exporters and importers at the same time, the impact is not that clear-cut when we consider net exporters and net importers of agricultural products. One may say, though, that in the net-exporting countries the positive impact of the rise in agricultural prices on farmers' income as producers may exceed the negative impact on raising their cost of living as consumers, while the reverse is true in the net-importing countries.

Within the Arab world, all countries except Sudan, Syria and Somalia, are net importers of agricultural products according to the 1997 data (see Table 4)[56]. They differ considerably, though, with respect to the export-import gap of agricultural products per individual. As shown in Table 4, the average net import of agriculture products per individual in 1997 is considerably higher in the GCC countries and Libya than to the Arab countries in Group 2, with the exception of Lebanon. In the major oil-exporting countries (Group 1), with the exception of Iraq and Algeria, the average net import of agricultural products per individual in 1997 was above $200 (and was as high as $550 in Kuwait), as compared to an average of less than $70 in Group 2 countries, with the exception of Lebanon, Jordan and Djibouti. Syria and Sudan had a net export of agricultural product per individual amounting to $20 and $7 respectively.

The low average net import of agriculture products per individual in most of the Arab countries in Group 2 has positive implications for the Arab region. It will reduce the likely impact of the expected rise in prices of agricultural products on increasing poverty in the region, since most of the large net importers of agricultural products are the countries with relatively high income per capita (see Table 2). Given the relatively low income per capita level in Group 2, the Arab countries that are likely to be hurt most by the rise in agricultural prices are Lebanon, Jordan and Djibouti, judging by the average net import of agricultural products per individual, which was $312, $139 and $121 respectively in 1997 (see Table 4).

On the other hand, the prices of the manufactured products, including the basic ones (like clothing), will likely be reduced due to trade

liberalization. All the Arab countries are major importers of manufactured products. Given the likely increase in the prices of agricultural products and the likely fall in the prices of the manufactured goods, the net effect on the cost of living of the population in the Arab region is not entirely clear. For the poor, it is more likely that their cost of living will be increased, because of the high share spent on food in their budget. However, the percentage rise in their cost of living is expected to be less than the rise in the prices of agricultural products, because part of the increase in the prices of food will be compensated for by the fall in the prices of basic manufactured products.

D. The extension of protection for inventions may promote monopoly and raise the cost of basic goods, which will hurt the population of the Arab countries (and Third World countries in general), especially those with low-incomes. The majority of patents are located in the advanced economies. It is estimated by one study that only 1% of the patents in the world are owned by the Third World countries, and some 84% of all patents are owned by MNCs from the five richest countries (Schaeffer, 1997).

One of the serious impacts of the TRIPS agreement is the raising of the prices of drugs and food, which are basic commodities. Canada, for example, protects drug patents for only seven to ten years, about half the duration of US patents. This has resulted in keeping the drug prices in Canada at a level 32% lower than the drug prices in the US (Schaeffer, 1997 p.204). In addition to drugs, there is a proposal to extend patent protection to seed and agricultural chemical companies[57]. Extending patent protection to this area means that farmers pay royalties on seeds saved from the previous harvest which will raise the cost of food production. Seed companies claim that they need patent protection to protect costly inventions. The irony of this situation is that much of the raw material for new drugs, seeds and chemicals come from rain forests and the farms and gardens of poor people in the Third World, without even being paid for, in many cases[58] (Schaeffer, 1997). Thus, by extending patent protection to drugs and seeds, prices of essential goods (drugs and food) will rise in the Arab countries as well as in other parts of the world. This will hurt consumers everywhere, but most particularly the poor. In the Arab region, the harm will be greater for Group 2 countries, where the income per capita is relatively low and the level of poverty is high when compared to that of the major oil-exporting countries (Group 1).

Moreover, extending protection for inventions will likely raise prices on high-tech commodities, which may become beyond the reach of

increasing numbers of the inhabitants in the low- and lower middle-income Arab countries (Group 2); this applies also to many other developing countries. The likely result is a widening of the technological and income gaps between the Arab countries (and the developing countries in general) and the advanced industrial countries. The expectation that globalization will narrow the already wide gap between the developed and developing countries[59] by creating a "borderless world" is likely to be a myth.

E. Another negative impact of globalization on prices will be through the GATT ban on export restrictions. This will have negative effects on the economies and people in the developed and developing countries; but its negative impact could be devastating for the developing countries (Schaeffer, 1997). Countries may limit the export of raw material in order to reduce the total supply of the commodity in the international markets and raise the price accordingly. Banning these export restrictions through GATT will have a favorable impact on consumers everywhere, because they will be able to get those commodities at low prices. But this will have an unfavorable impact on the exporting countries because it forces a deterioration in their terms of trade. Lower prices for their main exports will make it more difficult for those countries—especially the developing ones—to pay for their imports, repay debts, and invest their earnings in domestic development projects, thus creating more employment opportunities and raising the standard of living of their inhabitants. In the case of food, prohibiting export restrictions could be devastating for the agricultural Arab countries, especially the low-income ones such as Sudan, Mauritania and Yemen, where GNP per capita is below $400 a year (Table 2). If a country had a bad harvest, and its government could not restrict the export of its food crop according to GATT, domestic food supplies could fall and prices rise, which will hurt mostly the poor people in the society. This ban on restricting exports is also potentially relevant for the Arab countries in the case of oil and gas, but it may not have as strong an impact on poverty.

F. A social safety net is among the most important and effective means of reducing poverty. Subsidizing basic consumer goods and social services (education and health) by the government provides a social safety net for the low-income people in the society. This group of people includes all those whose incomes fall below the poverty line (like the receivers of pensions, social insurance, and transfer payments). The governments in the Arab countries provide a social safety net, in one form or another, to protect the vulnerable groups in the society. One of the social safety net indicators is public expenditure on education. The share of the average expenditure on

education in total government expenditure in the Arab countries in the mid-nineties amounted to 15.8% as compared to an average ratio of 14.8% for the developing countries, and a ratio of 12.3% for the industrialized countries (UNDP, 1999, Table 10). According to the most recent data (1998), the highest ratio was in the low- and middle-income Arab countries (Group 2); this ratio was 24.9% in Morocco, 20.8% in Yemen and 19.8% in Jordan. In the major oil-exporting countries, the highest public education expenditure ratio is in Oman (17.8%), Saudi Arabia (17.0%), UAE (16.7%) and Algeria (16.4%) (see Table 3).

Another indicator for the social safety net is the ratio of government social expenditure to total expenditure. On average, government social expenditure is one-quarter of the total expenditure in the Arab countries in 1998. At the country level, the percentage of government social expenditure in total expenditure in all the major oil-exporting countries (Group 1) was 20% and more in the GCC countries, with the exception of UAE, and was as high as 42.8% and 57.6% in Algeria and Libya respectively (Table 3). In Group 2 countries, out of the eight countries for which data were available, the ratio was about one-quarter and more in five countries: Tunisia (38%), Jordan (44.3%), Yemen (27.1%), Morocco (26.2%) and Egypt (23.5%).

What is the likely effect of globalization on the social safety nets that protect the poor economically and socially in the Arab countries? Institutionalization of the market-economy system in those countries by means of IMF-WB SAPs implies phasing out subsidies on basic goods and services to reduce the deficit in the government budget. Moreover, globalization in itself is likely to have negative impacts on social safety nets in all countries, advanced and developing, because of the implied reduction in government revenue. This is due to the cuts in customs tariffs and taxes on capital as mentioned above[60], and also due to the weakening of the sovereignty of the state which reduces a government's ability to raise revenue (Lee, 1996). The fall in government revenues due to the mentioned factors reduces government's ability to spend on social services and to provide the necessary funding to cover the cost of the social safety net. The likely weakening of the social safety net in the Arab countries due to these factors implies raising the cost of living of the low-income citizens in the Arab region[61].

VI. Suggested Policies to Enable Arab Countries to Deal with Globalization More Effectively[62]

The likely negative impacts of globalization on Third World countries in general and the Arab countries in particular may exceed the positive impacts. As pointed out by one study (Mittelman, 1997), the social structure of the world is shaped by globalization in the form of a three-part hierarchy that prevails both among and within countries. At the top are people who are integrated into the global economy, including everyone from the managers down to the relatively privileged workers who serve global production and finance in reasonably stable jobs. The middle level in the hierarchy includes those who serve the global economy in more insecure jobs; this comprises an expanding group segmented by race, religion and sex as a result of the global restructuring of production. The bottom level consists of those who are excluded from the global economy and serve it only as a potentially destabilizing force. The whole region of Africa is classified by Mittelman (1997) as belonging to the bottom level[63]. We should add that the Arab countries and all the developing countries, including the NICs, belong to the second and third categories[64]. However, despite the likely negative impacts of globalization on the developing countries, no one country could afford, we believe, to opt out of this process; the price it will pay in this case is likely to be much higher than the benefit. This is much more so for the Arab countries in view of the small size of their economies; none of them belong to the league of the 30 largest economies according to the size of GNP (for 1998).

Consequently, the question that should be raised with respect to the Arab countries is: which policies can be applied at the national, regional and international levels to minimize the negative implications of globalization and to maximize its positive impacts on their economies? We shall attempt to answer this question with respect to policies relevant to the economic and social impacts of globalization, with particular attention to growth and sectoral structure, vulnerability, employment and poverty. It should be emphasized, though, that this question is too important to be tackled in just one study. Thorough and detailed studies should be made by competent professionals in order to provide a consistent package of policies that address the likely negative impacts of globalization at all levels: economically, socially, educationally, politically, etc. The gloomy future that most of the Arab countries are likely to face soon, especially when the concessions periods given by the GATT 1994 are over, necessitates urgent policy action.

VI.1. At the National Level

A. The governments in the Arab countries should focus on accelerating growth. Economic growth is the engine for employment creation and poverty reduction, if coupled with appropriate policy measures for income redistribution in favor of the low-income strata in the society. Not only the rate of growth, but also the sectoral structure is of vital importance, because of its implications for employment and income distribution. For the densely-populated countries (like Egypt), and also for the countries with high unemployment rates (like most of the Arab countries), greater emphasis should be placed on labour-intensive methods of production. Accepting some trade-off between productivity and employment may be necessary, as the Arab countries should strike a balance between their needs and the latest technology available in the global arena[65].

Giving more consideration to the labour inputs and the technique chosen in production will not only create more jobs in the economy, but the share of wages in national income may be raised too. This implies that the pattern of income distribution generated by economic growth will favour the low- and middle-income groups in the society.

However, in view of the increasing role of FDI within globalization, this kind of technological choice is not open to the Arab countries on an individual basis. Survival in globalization implies that production is likely to be led by the MNCs and strong foreign investors who usually apply the latest technology available. Only when the Arab countries cooperate effectively to establish a regional bloc, might this kind of technological choice be feasible to consider. The success of GAFTA[66] will ultimately strengthen the negotiating position of individual Arab countries *vis-à-vis* MNCs regarding appropriate technology.

B. The shift from a state-managed economy to a market-economy, which is part of globalization, does not appear favorable to employment in the Arab countries. An increase in unemployment has been a common outcome of privatization and the strong contractionary fiscal and monetary policies applied to achieve financial stability, which are innate features of the IMF-WB SAPs implemented by the countries. Thus, the Arab countries are embarking on globalization with rising supply of and low demand for labour, which will likely magnify the negative social impacts of globalization in these countries. Consequently, much emphasis should be

placed on raising the overall rate of capital accumulation by mobilizing investments from all sources: private and governmental, domestic and foreign.

Privatization should not mean the complete withdrawal of the government from investment. Part of the returns from the sale of public enterprises should be directed to building new enterprises, especially in the manufacturing sector, and to creating more employment opportunities. This does not necessarily imply downplaying the private sector and the shift to a market economy. The relative weight of the private sector will continue to increase as long as the private sector grows at a rate higher than the public sector, which is one of the policy targets in the SAPs. Besides, ownership and management could be separated; i.e., government invests and owns projects, but the management could be left to the private sector. Leaving the main responsibility of economic growth and employment creation in the Arab countries entirely to the private sector is almost impossible, especially under GATT/ WTO rules. In many Arab countries, the private sector is still nascent, and the challenges of globalization are too tough to be handled. Despite the current crisis in the NICs, the lessons of their development experience cannot be disregarded. They clearly show the importance of the government's role in accelerating growth, if properly designed. Although some important instruments for government intervention are prohibited under GATT 1994, there is still some room to maneouvre: support for research and development, infant industries, regional development and the environment. The potential here remains to be tapped.

C. A high rate of investment is a precondition for fast growth. For a high rate of investment to be sustainable, it should be consistent with macroeconomic stability. Large external borrowing and/or expansionary fiscal and monetary policies should be avoided. Excessive dependence on foreign investment is more likely to render the economy vulnerable to external factors (as in the Latin American countries) (Hirst and Thompson, 1996; Khan and Muqtada, 1997). Achieving and sustaining a high rate of investment requires a high rate of domestic saving. Country experiences have shown that steady growth is the result of investments that are financed primarily by domestic savings (as in the case of East- and South-East Asian countries), Thus, raising domestic savings should be one of the primary concerns of the Arab countries if steady economic growth is opted for. In particular, authorities should avoid the easy but dangerous option of smoothing expenditure over the course of oil cycles at the expense of saving.

D. In the Arab countries, more effort and resources should be directed toward catching up with the fast technological progress that is taking place in the advanced economies. There is a dire need for providing the scientific infrastructure and research environment that are capable of producing competent professionals in the different fields of social and hard sciences[67]. Furthermore, lack of attention to the research activity by production firms is common in the Third World countries. Despite the importance of R&D in raising productivity and accelerating economic growth, it is felt that national research institutions have not earned sufficient credibility to justify extending the necessary support to them. For example, industrialists in the African countries are seeking answers to their technological problems abroad (UNESCO, 1998). This applies as well to the Arab countries.

Increasing the private sector's demand for R&D in the Arab countries is necessary, especially in manufacturing, because of the strong correlation between technology developments and production growth. Policies should be applied to provide the necessary scientific infrastructure, competent professionals and research institutes, to produce serious research. This means overhauling the education system at all levels in the Arab countries. Having competent scientists and professionals, especially in basic sciences, is a must for the Arab countries to reap the benefit of globalization, e.g., competent scientists can adapt technological innovations to the needs of the Arab economies to fit the relative abundance of human resources and relative scarcity of capital in those countries. This is one important way to reduce the present marginalization of the Arab countries in the world economy.

Contrary to what some may believe, the financial constraint is not the binding one for such an objective. To improve the quality of research produced in the Arab countries, it takes much more than just funding[68]. The quality of research is a function of both the scientific background and training of researchers and the research environment. A coherent national policy for science and technology is needed to address national priorities in this vital area.

E. The Arab countries cannot continue to rely for their comparative advantage on low-cost unskilled labour and natural resources, since both factors represent a diminishing share in the value added in virtually all products, thanks to the advances in technology[69]. This implies that the Arab countries have to acquire new bases for comparative advantage to be able to attract foreign investments and create new jobs. For example, the

Arab countries with a high population growth rate might be able to substitute the comparative advantage in cheap unskilled labour by a new comparative advantage in low-cost semi-skilled and skilled labour, if they succeed in restructuring their education system and build a scientific infrastructure suitable to accelerating technological change that accompany the globalization process.

F. A high population growth rate is an important factor that the Arab countries should take care of to reduce the negative social impacts of globalization. High population growth means a large increase in the supply of labour, which intensifies the unemployment problem in these countries. Thus, reducing the population growth rate should be one of the important policy targets in these countries.

G. In view of the potentially destabilizing effect of foreign portfolio investment (FPI), small, open economies such as those of the Arab countries need to put in place some controls on the convertibility of the capital account[70]. This has often been referred to in the literature as the 'sand in the wheel' policy. The local banking system has to be monitored carefully to avoid accumulation of short-term debt denominated in foreign currency.

Among the Arab countries, the GCC countries, Egypt and Lebanon all have full capital mobility, while Jordan, Morocco and Tunisia have partially liberalized their capital account (Arab League *et al.*, 1996, Ch. 7). The increase in foreign syndicated bank loans and banking facilities to the Arab countries in 1998 represented the main component of the growth of long-term net capital inflows to these countries. An increasing number of Arab banks, particularly in Egypt and the GCC, continued their practice of co-participation with foreign banks to mobilize funds for development projects, mainly in the energy sector, through syndicated loans (The Arab League *et al.*, 1999, 97). The practice in Chile and Colombia of imposing extra reserve requirements on such claims proved successful, whereas uncontrolled short-term private bank debt in foreign currencies, was fatal to the Indonesian and Korean currencies in 1997 (Tobin, 1998)[71]. Denominating a large amount of debt, especially short-term debt in foreign currencies should be avoided. In 1997, the overall ratio of short-term debt to total foreign debt for the Arab countries averaged 12%. But it was significantly higher for several countries: the Sudan (43%), Syria (23%), Oman (21%), Yemen (16%) and Tunisia (14%) (Arab League *et al.,* 1999, Appendix Table 9/8). This is the hard lesson of the Mexican peso crisis of

1994-95 (Mishkin, 1996). There are many disturbing parallels between some Arab countries now, notably Egypt, and Mexico before 1994 (Abdel-Khalek, 1998).

H. Pegged or fixed exchange rates should be avoided, as experience in Mexico and East Asian countries proved that pegged currency can be an easy target for speculative attacks. The danger is much more grave when the banking system is fragile, as it is the case in the Arab countries[72]. We have shown that although the number of countries having a floating exchange rate increased from 6 to 8 between 1995 and 1998, 12 countries still apply a peg of some sort. Having a pegged exchange rate regime combined with the features mentioned in G. above, amounts to "putting the economy on a knife's edge: one slip and the economy comes crashing down"(Mishkin, 1996, p.59). It is therefore prudent policy to restructure exchange regimes in the Arab countries away from the peg.

VI.2. At the Regional Level

A. In terms of economic size (measured by the level of GDP), all the Arab countries are small, some really tiny; none of them belongs to the list of the 30 largest economies. In fact, their combined GDP in 1998 is less than that of Canada, only 40% of that of France and just 7% of that of the USA. For theses countries, they can only face the challenges of globalization if they form a solid regional bloc. Ironically, the countries that have joined successful regional blocs are the advanced economies, which have already "smooth" integration in globalization; the two largest regional blocks, the EU and NAFTA[73], consist mainly of developed countries.

Of particular interest from the vantage point of the Arab countries is the modest step already taken by establishing GAFTA, to be completed in the year 2007. The Arab countries need to accelerate the process of integration and quickly establish a customs union. Only by creating their own autonomous customs territory can the Arab countries collectively maximize their development potential within the global economy.

Becoming a member of a sub-regional grouping is vital for the Arab countries. Several types of dynamic benefits may be pointed out in this respect[74].

1. Competition among the firms producing homogeneous products within the regional bloc will end up in phasing out the least efficient firms in the

Arab region and strengthening the more efficient ones, since the enlarged market resulting from economic integration allows economies of scale in production and specialization. This may also create specialization in differentiated products, which will lead to intra-industry trade, as it has been the case in the EU. Increased competition in the regional bloc may be looked at as an introductory phase that prepares the Arab firms to reach a wider market outside the region, and getting integrated smoothly into the global market. The manufacturing firms that survive the competition in the region will more likely reach a standard of production that will enable them to compete in the global market. These firms would not be able to survive in the region if they do not succeed in competing in quality with similar products of the non-member countries, since the member countries have the choice to import from outside the region at low tariffs according to the GATT, if they are not satisfied with the product of the regional firms.

2. Regionalization may lead to an increase in production in the commodity sectors (manufacturing and agriculture) by the division of production activities among the Arab countries in a complementary way, taking into consideration the capabilities and potential of the countries in the region. In the cases where similarity in comparative advantage in the Arab countries exists, some kind of agreement can take place to compensate for the loss that a member country may experience if it has to close certain lines of production. In short, the regional bloc represents a kind of smaller global economy in which the member countries are the main players and can then put in place the appropriate rules and regulations that fit their conditions.

This does not mean, though, that the Arab countries are completely free in designing and implementing their production and trade policies, since the GATT rules are binding constraints to them. But despite that, they have room to move and maneuver by isolating themselves as a group with preferential rules which they can apply to the member countries, and which are allowed by the GATT[75]. These preferential rules give each member country an edge over the non-member countries within the regional bloc, which should have a positive impact on the trade and production of the member countries in GAFTA, and could present a transitory phase for them to be introduced to the globalization process in a smoother way.

3. By reducing tariffs among member countries to a level lower than with the non-members, and eventually eliminating them completely, the intra-trade within the Arab region will increase, substituting part of the trade which is taking place between non-members and member countries for

similar products. Moreover, the creation of intra-industry trade, as the result of specialization in heterogeneous products, is an additional factor that will enhance intra-trade within the regional bloc.

4. The regional bloc may lead to increased foreign investment in the Arab countries as non-member countries build plants inside the bloc in order to avoid the tariff barriers. For example, the USA increased its investments in Europe following the creation of the European Economic Community.

5. Since regional trading blocs involve few countries, it becomes more feasible to agree among them on ways to reduce the transactions costs of international trade through harmonization of standards, dissemination of information leading to a reduction in risk, removal of bureaucratic controls, etc. Moreover, the Arab countries become more capable, as a regional bloc, to persuade large non-member countries or other trading blocs, to engage in reciprocal tariff reductions. The outcome will be an increase in intra-trade and production in the Arab region. As pointed out by Mittelman (1997), many Asian countries and firms look to improve regional cooperation for access to regional markets and as a sound base for sharing in globalization.

We may underscore two factors in this respect: first, working as a group in the division of production within the member countries of the Arab region means that the regional pattern of production will be supported by the resources (human and financial) of the whole region and not by the resources of one country only, which may relatively be too small to stand the competition in the global market. Second, the sovereignty of the state is maintained within regionalization, which makes room for the governments of the Arab countries to play effective roles in supporting the economic activities in the region by appropriate policies. A common element that is found among the different regional blocs is that the state is increasingly a mechanism in the globalization process and, hence, intervenes directly in the economy to promote capital accumulation (Mittelman, 1997). Thus, cooperation in regional blocs is an extremely important step that should be accelerated by the Arab countries.

B. The Arab countries may benefit considerably by setting up a facility for common strategic food reserves. As pointed out, most of them are net food importers. Their food security may be greatly enhanced if they establish such a facility. Details could easily be worked out; the point here is to draw attention to this neglected problem.

VI.3. At the International Level

A. The Arab countries need to join forces with other developing countries, perhaps with Group of 15, to redress the imbalances and injustices in the globalized economic environment. Special attention has to be given to GATT/WTO, and its relation to UNCTAD. The basic difference between the two is which comes first, trade or development? Under GATT/WTO, trade is first and foremost, then development. If there is any conflict between the two, trade should prevail. Under UNCTAD, development is first, and trade follows. From the point of view of the developing countries, the Uruguay Round must be seen as a setback. The Arab countries, as part of the Third World, should push for an assessment of the results of the Uruguay Round before moving forward to the Millenium round. The Uruguay Round was advocated in terms of efficiency, competition and a level-playing field. In reality, it is economic Darwinism in disguise.

B. The Agreement on Agriculture in GATT 1994 stipulates liberalization of agricultural trade, the consequence of which is to raise the prices of many temperate products. Simulations produce a wide range of predictions for the rise in prices. Of particular interest to the Arab countries are cereals, dairy products, meat and sugar. For these products, price increases as a result of the Uruguay round (based on general equilibrium models) range as follows: 15-18% for wheat, 10-18% for meat, 14-1% for dairy and 57% for sugar (Laird and McDonald, 1996, Table VI). UNCTAD estimated annual losses from higher food prices and the erosion of preferences for the Least Developed Countries (LDCs) at $300-$600 million. Article 16(2) of the Agreement on Agriculture established a Committee on Agriculture within the WTO with the mandate of monitoring the follow–up to the "Decision on Measures Concerning the Possible Negative Effects of the Reform Programme on Least-Developed countries (LDCs) and Net Food-Importing Developing Countries (NFIDCs)". But very little has been achieved. The Arab countries, led by Saudi Arabia (when it joins WTO) and Egypt as the largest net food-importing countries in the region (Table 4), should press for the establishment of a Food Import Facility (FIF) through the WTO, not through the IMF. The justification of having a FIF within WTO instead of the Compensatory and Contingency Financing Facility (CCFF) within the IMF is that the latter involves strong conditionality (Abdel-Khalek, 1996, Ch. 10). The FIF should operate as a commercial insurance scheme without conditionality, like the Stabex scheme[76] in Lome I (Raffer, 1997).

C. While the Arab countries and the developing countries should concentrate their efforts on raising their savings rate to guarantee steady investments and growth, they must be helped by international action. Measures needed include debt reduction and an increase in the share of grants in capital flow, in order to increase the inflow of foreign savings without the danger of increased indebtedness (Khan and Muqtada, 1997). This endeavour is highly important for the Arab countries since 15 of them are indebted and four are severely indebted countries according to the World Bank classification[77].

D. One of the issues that needs to be addressed by the international community, and which has not been tackled by the tariffs reduction agreements in the GATT, is the escalated tariffs used by the developed countries to discriminate against manufactured products in the developing countries. The developed countries typically levy low tariffs on raw material imported from developing countries, but high tariffs on their manufactured goods to discourage them from making goods that might compete with the developed countries' producers[78]. Across-the-board tariff reduction might benefit consumers, but it would leave in place the discriminatory tariff structures that hurt the developing countries (Schaeffer, 1997). Thus, before moving toward any further trade liberalization under the Millenium Round, the structure of tariffs, and not only the level of tariffs, should be discussed and revised to eliminate the discrimination that exists against some products of the developing countries, like the manufactured goods.

E. Other issues in the GATT may have similar discriminatory impacts against the developing countries, which means that the Arab countries in the broader context of the Third World, assisted by the international community as a whole, should be concerned with investigating and revising GATT's regulations to eliminate other discrimination that may exist in the agreement. In view of the paramount importance of oil for the Arab countries, it qualifies for the status of a sensitive commodity which should be subject only gradually to the free market discipline of GATT. Some analysts even extend that to petrochemicals (Al Sahlawi, 2000).

F. To avoid the expected marginalization of the South, a different perception by advanced countries and international organizations is needed with respect to the role that the developing countries could play in globalization. Despite the heterogeneity of the developing economies, they still have common problems that need to be addressed by the international community, and should be considered in designing the regulations and rules of globalization as reflected in GATT. Otherwise, these countries will largely be excluded, *ipso-facto*, from the benefits of globalization, which will sooner or later have its unfavorable impacts on the advanced economies. It is unrealistic to assume that the marginalization of the Third World countries is irrelevant to the benefits of globalization that will accrue to the advanced economies. Poverty and prosperity cannot coexist for long in the "borderless" world of globalization. The nascent Group of 20 (established in 1999 and including the seven industrialized countries, 11 other countries that represent the newly emerging markets[79], and the representatives of two international organizations), may reflect this changing perception. The objective of this Group is to support and enhance world cooperation on various economic issues, and to coordinate among the other country groups, like the Group of 7, the Group of 10 and the Group of 24[80].

Although the establishment of this Group of 20 is one step in the right direction, the countries included do not provide a fair representation of the Third World. The developing countries in Africa and in the Arab region are largely neglected. Africa is presented by one country only, South Africa, which by several criteria is considered a developed economy; the Arab region is presented only by Saudi Arabia. The choice of the member countries in the Group of 20 is heavily biased towards the developing countries in Asia (China, India, South Korea, and Turkey) and in Latin America (Argentine, Brazil, and Mexico); also, the low-income countries are poorly represented. To have an operationally effective mechanism for cooperation between the North and the South, the member countries in the Group of 20 can be increased to provide a better representation of the Third World, or another Group could be formed which should include low-income developing countries along with the medium-income countries and the newly emerging markets.

In conclusion, two points may be emphasized: First, the economic and social problems of the Arab countries and the developing countries in general are more likely to be increased than reduced by globalization. Finding solutions to overcome the current economic and social difficulties in the developing economies is beyond these countries' means; close cooperation with advanced economies and international organizations is needed for this purpose[81]. Second, without the cooperation between the South (with its heterogeneous economic and social characteristics) and the North, the full potential of globalization cannot be achieved, and the losers will not only be the developing economies—Arab and others—but the advanced economies will suffer as well.

Notes

[1] Gouda Abdel-Khalek is Professor of Economics, Faculty of Economics, Cairo University; and Karima Korayem is Professor of Economics, Faculty of Commerce (Girls), Al-Azhar University, Cairo. Email (joint) nile@intouch.com

[2] This part draws heavily on Korayem (2000).

[3] We prefer to call them MNCs and not transnational corporations (TNCs), since most of them are nationally based and they largely abide by the regulations and policies of the mother country. The TNCs are footloose entities without specific national identity and they are not controlled, or even constrained, by the regulations and policies of any particular nation state. The TNCs working in the world at present appear to be relatively rare (Hirst and Thompson, 1996).

[4] Including intra-EU trade.

[5] Those countries are: Singapore, Mexico, China, Brazil, Malaysia, Hong Kong, Argentina, Thailand, Egypt and Taiwan (Hirst and Thompson, 1996; Table 3.2).

[6] According to GDP distribution figures, the relative share of the developed countries in the total was 69.6% during the seventies and eighties, i.e. from 1970 to 1989 (Hirst and Thompson, 1996; Table 3.4).

[7] Krugman stated that the entire net flow of investment since 1990 has reduced the advanced countries' capital stock by only 0.5% (cited in Hirst and Thompson, 1996, p. 117).

[8] The dependency ratio, which is also referred to as the support burden ratio, indicates how many people are financially supported by one worker, on average. The high ratio in the Arab countries means that each worker in those countries has to support three or four persons on average, while each worker in the developed countries and the NICs —where income is considerably higher— has to support, on average, two persons only (Korayem, 1998, p.41).

[9] The non-Arab countries included in this group of countries are Iran, Israel and Malta; and the Arab countries excluded from the MENA group and classified as part of Sub-Saharan Africa are Djibouti, Mauritania, Somalia and Sudan (see the classification of economies by income and region, 1999 in World Bank (2000a, p.290).

[10] Calculated from World Bank (2000a, Table 3) as equal to: [1 – (population aged 15-64 / total population)]*100.

[11] In Group 1 countries, there has been a fall in the GNP per capita in the GCC countries (with the exception of Bahrain and Oman) and in Libya in 1998 as compared to 1993; while the GNP per capita in the more diversified Arab economies (Group 2 countries) has increased over the period, with the exception of Mauritania, Sudan and Yemen. For the 1993 figures, see Korayem (1996; Table 1).

[12] For the 1993 ratios, see Korayem (1996, Table 1).

[13] Sachs (1998) invokes yet another distinction: that between tropical *versus* temperate zone countries. He argues that the first may suffer the burden of poor agricultural conditions and infectious disease.

[14] Sachs acknowledges the existence of two exceptions. The first is based on geography, as when the economy is isolated from the world market. The second is based on climate, such as the case of tropical countries which suffer from infections diseases and poor agricultural conditions.

[15] For more detailed data and analysis of demographic and labour force trends over the period 1960–1990, see Sirageldin and Al-Khaled (1997) and Karshenas (1997).

[16] The price of crude oil jumped from $3.1 per barrel in 1973 to $10.4 per barrel in 1974, and from $12.9 per barrel in 1978 to $29.2 per barrel in 1979 and further to $36.0 in 1980. Deflated by the index of industrial countries' manufacturing exports unit value (MUV), the real price of oil hit a record high in 1980. See Appendix 5/4 of the Arab League *et al.*, 1999.

[17] Calculated from: Arab League and others, 1999; Appendix Table 5/6.

[18] For the 1998 figure, see Table 2 in the text; for the 1993 figure, see the Arab League *et al.*, 1994, Appendix Table 2/5.

[19] For an extensive discussion of the oil-remittance nexus and its impact on the labour market in the case of Egypt, see Karshenas, 1997.

[20] Mainly for these reasons, the World Bank has revised downward its long-term (2002-2008) forecasts for growth in developing countries from 5.2% per annum in the *Global Economic Prospects (World Bank, 1998/99)* to 4.9% in the *Global Economic Prospects (World Bank, 2000b).*

[21] In 1997, global foreign exchange transactions amounted to the equivalent of $1.5 trillion per day, compared to $82 billion GDP per day and world exports of $16 billion per day (Naggar, 2000).

[22] The corresponding shares in world production are 28% and 14% for oil and gas production respectively, according to the 1998 figures. See Arab League *et al.*, Annexes 5/12 and 5/13.

[23] Iraq had 100 billion barrels of proven reserves, second only to Saudi Arabia. It also has some underdeveloped super giant and giant fields that, when fully developed, could raise Iraq's proven reserves by at least 50%. Prior to the Gulf war, Iraq was producing more that 3 million barrels per day and exporting 2.8 million barrels per day. For more details, see Sullivan (1998).

[24] See footnote 9 in the text.

[25] To use imagery borrowed from the Arab environment, portfolio flows may be compared with swarms of locusts from the desert invading the green fields.

[26] In fact, the share of extractive industries was especially low in 1998 because of the oil bust. Allowing for this, the share of extractive industries in GDP is really higher than revealed by Table 2. By definition, the shares of the other sectors are lower.

[27] Engel's Law stipulates that as income rises, a lower proportion thereof will be spent on necessities. Agriculture is generally where necessities are produced, and services are less necessary than agriculture products. Hence the Law.

[28] Unfortunately, solid data are conspicuously lacking; one has to rely on circumstantial evidence. Investments in petrochemicals rose significantly in the 1980's, resulting in more than 9.0 million tonnes increase of productive capacity; 60% of the increase was in basic chemicals in Saudi Arabia (Abdel-Khalek, 1987b, p. 84). Planned production capacity in Saudi Arabia, which is to go on stream in the year 2000, totalled 1.738 million tones of Ethylene, Polyethylene and Propylene (Arab League *et al.*, 1999).

[29]It should be noted that efforts for regional cooperation predate the above-mentioned ones, particularly the Gulf Cooperation Council (GCC) and the Arab Maghreb Union in the 1980's. In addition to these efforts at regionalism, a number of bilateral free trade areas (FTAs) has emerged, mainly to counter some of the effects of the Euro-Mediterranean Association Agreement (EMAAs). Egypt signed bilateral agreements with Jordan, Lebanon, Morocco and Tunisia; Morocco signed bilateral agreements with Tunisia and Jordan. Tunisia signed an agreement with Jordan. Syria and Lebanon signed an agreement also (Zarrouk and Zallio, 2000).

[30] This is because until the 1997 *World Development Report*, remittances were recorded separately. Starting with the 1998/99 *Report*, they were included partly in item called "net income" and partly in the item called "net current transfers". See Technical Notes to the 1997 and 1998/99 *Reports* for details.

[31] For measures 1 and 2 in 1993, see Korayem (1996).

[32] See the roundtable discussion in Sabri, 1999, pp. 233–78.

[33] For more details on the subject, see Lall (1995).

[34] Calculated from Table 7.

[35] In 1997, total investment was $6914 million in Morocco, $15300 million in Egypt and $5075 million in Tunisia (The Arab League *et al.*, 1999, Appendix Table 2/6).

[36] Total investment in Yemen was $1605 million in 1997 (The Arab League *et al.*, 1999; Appendix Table 2/6).

[37] It consists of the Russian Federation, Turkey, and Poland.

[38] For other views on the negative impacts on the developing countries, see Thomas and Wilkin (1997)

[39] For example, average annual labour cost in manufacturing in Tunisia in 1993 was 10.5% and 8.6% of the comparable labour cost in France and Germany respectively (Boughzala, 1997). In Indonesia, the wage is 2% of the wage in Germany; it is $0.5 an hour in the former as compared to $25 an hour in the latter (Hirst and Thompson, 1996, p. 117).

[40] It is argued also that the actual extent of liberalization of agricultural markets resulting from the 36% reduction in tariffs by developed countries at the end of the implementation period is likely to be "far less" than what the figure suggests. One of the reasons brought up in this regard is that the tariff rates in the base period 1986-88 were relatively high compared to more representative periods because of the considerably low prices of agricultural goods in these years. Consequently, the tariff rate applied on agricultural products after the 36%

reduction will be higher than what it would have been if the base period was more representative of the average tariff level (Tanner and Swinbank, 1996).

[41] The Agricultural Agreement came in effect in 1995 (Tanner and Swinbank, 1996, p. 629).

[42] The large employment in the agriculture sector in Oman could be explained by the heavy direct and indirect subsidies provided to agriculture activities, including fisheries (UNESCWA, 1997, p.74).

[43] In 1983, as a result of payments crisis, Morocco virtually eliminated quantitative restrictions on imports and reduced the maximum tariff from 165% to 45% over a six year period (Currie and Harrison, 1997).

[44] Those models assumed that all basic parameters —import and export elasticities, technology and the structure of preferences— remain unchanged when the trade barriers are completely dismantled (Boughzala, 1997).

[45] It is assumed that Morocco and Tunisia are moving up to the grade of a medium-skill country, and they will have the capacity to develop and export more advanced products. It is assumed also that firms will behave more efficiently and adopt international requirements when protection is lifted and the FTA with the EU will increase foreign direct investment (Boughzala, 1997).

[46] Although on moral grounds child labour is rejected, it is argued that eliminating market access to goods produced by child labour may hurt the children themselves whom the labour regulations are supposed to help, because of the socioeconomic realities in the developing countries. For more details on this argument, see Hasnat (1995).

[47]They have already made some success in this direction in the successive meetings of the Uruguay round. In Singapore in December 1996, the members of the WTO agreed to respect social labour standards, but leaving the responsibility for monitoring the implementation of those standards to the International Labour Organization (ILO) rather than the WTO (Windfuhr, 1997; Castle *et al.*, 1998).

[48] The public sector employment as a percentage of total national labour force is much higher; e.g., in Kuwait, 91% of the nationals were employed by the public sector, which pays two to three times more than market wages (UNESCWA, 1997a).

[49] The year in brackets indicates the starting date of the programme.

[50] In Egypt, for example, 44.4% of the new entrants in the labour market were absorbed in the public sector over the period 1976-1986 (UNESCWA, 1997a, p. 87).

[51] For example, in Jordan, the public sector employment decreased from 50% (and 45% in some estimates) in 1987 to 33.7% in 1993 (UNESCWA, 1997a, p.79).

[52] For Egypt, for example, see the estimates of the Institute of National Planning (1994) and Korayem (1994); and for Jordan and Yemen, see the estimates in UNESCWA (1997b).

[53] For example, there are individual studies that estimated poverty in Bahrain (Abdel-Khalek, 1987a) and in Sudan (Abdel-Kader, 1994).

[54] This includes main food grains, like wheat, coarse grains and rice.

[55] However, the rise in their cost of living as consumers will probably be less than in the case of the urban population, since part of their exportable crops can be used for own-consumption. In addition, they can also cultivate different food products on a small scale for their own consumption and thus avoid some of the food price increases due to globalization.

[56] For Somalia, see the Arab League *et al.*, 1999, Appendix Table 8/3.

[57] On 3 March 1993, two hundred thousand Indian farmers rallied in Delhi to protest GATT proposals to extend patent protection to seed and agricultural chemical companies (Schaeffer, 1997).

[58] For example, a variety of Turkish barley was donated to US farmers to combat a yellow dwarf virus, saving US farmers $150 million a year in crop losses (Schaeffer, 1997, p. 205).

[59] With the exception of the East and East-South Asian countries, the income gap between developed and developing countries is wide and getting wider. For example, the average per capita income of the Group of Seven Industrialized countries (G-7) was 20 times that of the world's poorest seven countries in 1965, and became 39 times as much in 1995. In Africa, the average per capita income is only 7% of that of the industrial countries. In Latin America, average per capita income has fallen from over one- third of the level in the industrial countries in the late 1970's to one-quarter in the nineties (Ricupero, 1997).

[60] For example, by reducing tariffs to zero, NAFTA will cut US revenues by about $4 billion a year, and cut tax revenues for Canada and Mexico by about $3 billion (Schaeffer, 1997).

[61] The weakening of the social safety net at the national level is taking place in the developed countries also, where social services provided to the poor and the elderly have deteriorated over the last decade.

[62] This section is partly based on Korayem (2000).

[63] It is also mentioned that most of the former Soviet block are joining this bottom level category (Mittelman, 1997).

[64] The severe crisis that the NICs in South East Asia and Latin America have experienced showed how vulnerable those countries are economically and socially, despite their successful integration into the global economy, as frequently referred to in the literature.

[65] Choosing the appropriate technology for the developing countries, which is not necessarily the latest technology, is advocated by other economists; e.g., Lall (1995).

[66] This is also referred to as Pan Arab Free Trade Area (PAFTA) in some sources.

[67] As an example of the deficiencies in the research environment that exists in the Third World countries, see the study on The Research Environment in Egypt (Korayem, 1999).

[68] For example, it is not a coincidence that countries like India and Pakistan, despite their meager resources and large population, have been able to produce scientists who have successfully built the atomic bomb. Despite our condemnation of the production of atomic bombs or any other weapons of mass destruction, one cannot disregard the implied scientific achievement of this act. There are also considerable achievements in social sciences (such as in economics), as revealed by the respectable publications of Indian and Pakistani scholars. This respectable performance in both hard and social sciences is an indicator for the competitive education infrastructure that the two countries have built successfully despite financial constraints.

[69] On this point, see Cardoso (1996).

[70] Yamazawa (2000) makes a similar suggestion for the East Asian economies to meet the challenges of a changing global environment. But Calvo et al (1996) advocate liberalizing outflows and controlling inflows.

[71] Tobin suggests that the People's Republic of China proved immune to the 'Asian flu' because it restricts the convertibility of its currency. The right to convert renminbi funds into foreign currency is strictly given only to foreigners who have earned them through commercial transactions. However, China continues to top the list of countries attracting FDI.

[72] See Arab League *et al.* (1996 and 1999; Ch.7) for details.

[73] It consists of the USA, Canada and Mexico.

[74] Many of the cited benefits are derived from Rodgers (1998).

[75] Regional trading blocs conflict with the Most Favored Nations (MFN) Principle of the GATT. However, Article XXIV of the GATT makes an exception for preferential trading arrangements provided: (a) the agreement eliminates tariffs and other restrictions on 'substantially all the trade' among the member countries of the trading bloc within 'a reasonable period of time', and (b) the remaining barriers to trade with non-members of the bloc are no more restrictive 'on average' than barriers in place prior to the bloc's formation. The aim of these conditions is to ensure that trade creation exceeds trade diversion (Rodgers, 1998, p. 213).

[76]This is a scheme for the STABilization of EXport earnings established under the Lome Treaty.

[77] The severely indebted countries are: Iraq, Jordan, Mauritania and Syria (World Bank, 2000b). To these, one should add Somalia as a member of the League of Arab States.

[78]For example, the industrialized countries place a 0.1% tariff on raw rubber from the developing countries, but a 16.5% tariff on rubber footwear (Schaeffer, 1997, p. 200).

[79] Those countries are: Argentina, Australia, Brazil, China, India, Mexico, Russia, Saudi Arabia, South Africa, South Korea and Turkey.

[80] The daily newspaper Al-Ahram, September 27 1999, Cairo (in Arabic).

[81] See the statement of Ambassador Betty King, the US Representative on the United Nations Economic and Social Council (King, 1999).

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