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Item 7 of the provisional agenda

Trade costs in the Arab region**Summary**

Trade costs encompass the various expenses associated with transferring goods from producers to consumers. Trade costs can be incurred either because of policy or lack of policy measures. Given that trade costs are a major determinant of competitiveness and integration in the regional and global economy, higher costs in the Arab region compared to other economies and comparable trading blocs, affects its competitiveness and leads to its weak integration into global economy. The costs are higher for intraregional trade than external trade. To overcome this hurdle a reform of trade channels is necessary.

The Committee on Transport and Logistics is invited to review the content of this preliminary analysis and provide comments thereon.

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Introduction

1. The cost of trade is an important determinant of competitiveness in international trade markets. It includes all costs incurred in the process of moving a product from producers to consumers, minus the cost of producing the product. As such, trade costs could be divided in two principal groups: 1) policy-made trade costs (such as tariffs, tariff equivalents and non-tariff measures such as quotas and licenses, etc.) and 2) and non-policy-made trade costs which mainly includes transport, insurance and customs procedures.

2. The sum of all these costs (whether policy-induced or not) have significant implications on the economic performance of countries and, if excessive, greatly undermine the gains. The negative impacts on nations' competitiveness hampers the development of trade at the regional and global levels. Some studies have investigated the impact of trade costs on economic welfare or on other macroeconomic aggregates. For example, Anderson and van Wincoop (2002)¹ argue that trade costs are often worth more than 10 per cent of national income while Obstfeld and Rogoff (2000)² have stated that all the major puzzles of international macroeconomics hang on trade costs. Another interesting study done by Bernard and others (2006)³ examined the response of American manufacturing industries and plants to changes in trade costs using a unique new dataset on industry-level tariff and transportation rates. They found that industries experiencing relatively large declines in trade costs exhibit equally strong productivity growth.

3. Ground-level evidence of the magnitude of trade costs for Arab countries explains their relative isolation from global value chains, apart from few exceptions related specifically to petroleum industries. Thus, computing these trade costs at the macroeconomic level for given sectors and periods could be a first step to understand the extent of the impact of high trade costs, which in turn could lead to an understanding of their composition to find a way to mitigate them and take advantage of hidden potential benefits.

4. In this respect, boosting trade among countries is increasingly linked to the non-policy dimension of trade costs rather than to policy instruments. For example, a product shipped from Morocco to the United States costs around three times its cost at the factory level. Keeping in mind that tariff and non-tariff measures represent between 10 and 50 per cent in average of the total trade costs and 270 per cent are due to non-policy instruments.

5. The present document provides a closer look at trade costs at national and sectoral level in the Arab region based on data obtained from global sources.

I. TRADE COSTS IN THE ARAB REGION

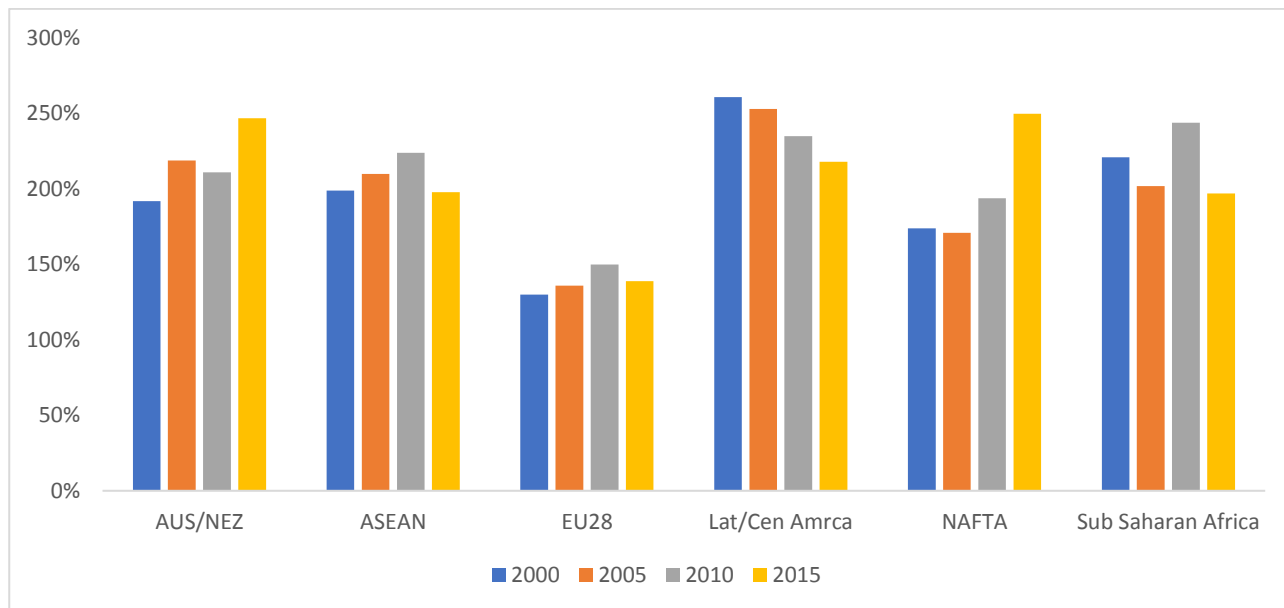
6. Trade costs in the Arab region appear to be becoming more balanced across all the subregions examined and have been declining over the years. Overall, the region's lowest trade costs are with the European Union (EU), although they slightly increased from 130 per cent in 2000 to 139 per cent in 2015. The highest trade cost for Arab exports is seen with Latin and Central America although it has fallen by around 20 per cent from 261 per cent in 2000 to 218 per cent in 2015. Trade costs with Sub-Saharan Africa are have also declined by around 10 per cent from 221 per cent in 2000 to 197 per cent in 2015. Export cost with the North American Free Trade Agreement (NAFTA) increased sharply from 174 per cent in 2000 to 250 per cent in 2015, an increase of 44 per cent the highest increase of export cost for Arab region's exports to any region.

¹ Anderson, James E. and Eric van Wincoop, "Borders, trade and welfare", in *Brookings Trade Forum 2001*, Susan Collins and Dani Rodrik, eds. (Washington, D.C., Brookings Institution, 2002), pp. 207-44.

² Maurice Obstfeld & Kenneth Rogoff, 2000. "The Six Major Puzzles in International Macroeconomics: Is There a Common Cause?" NBER/Macroeconomics Annual, vol 15, No. 1 (March 2001) pages 339-390.

³ Andrew B. Bernard, Bradford Jensen and Peter K. Schott, "Trade costs, firms and productivity," *Journal of Monetary Economics*, vol. 53, No. 5 (July 2006), pp. 917-937.

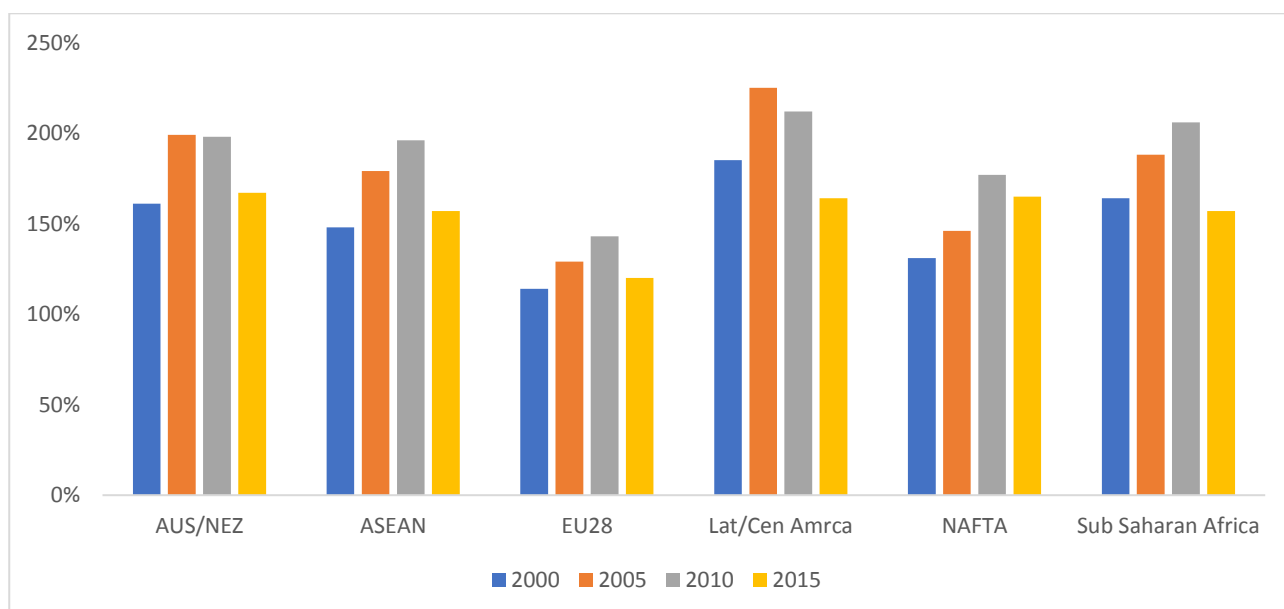
Figure 1. Export costs for Arab countries to selected regions



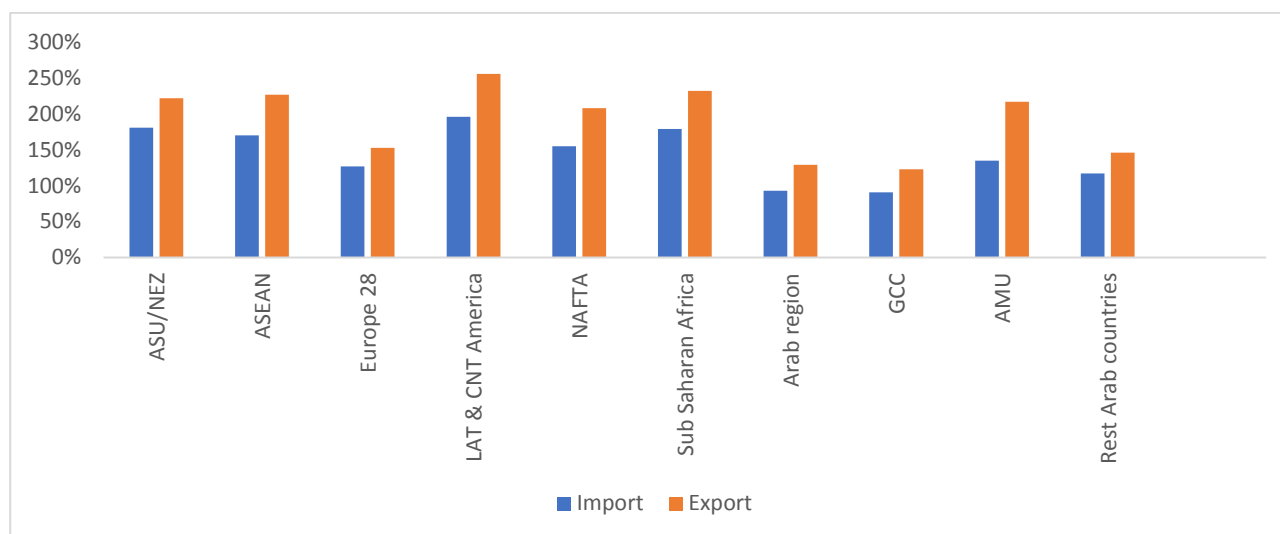
Source: ESCWA calculations based on ESCAP/World Bank database on trade costs and UN Comtrade database on trade flows.

7. Turning to imports of the Arab region, results show that the lowest import costs are for imports originating in the EU, with the overall cost ranging between 114 per cent in 2000 and 120 per cent in 2015. Interestingly, imports from the NAFTA region show low costs ranging from 131 per cent in 2000 and 165 per cent in 2015, the lowest cost among partners examined after the EU. Trade costs for imports from the Latin and Central America region to the Arab region remain high comparable to the export costs. Import costs from the Association of Southeast Asian Nations (ASEAN) to the Arab region remain high but are less than the cost of Arab exports to the region. Sub-Saharan Africa, Australia and New Zealand top the list in terms of import costs to the Arab region.

Figure 2. Import costs for Arab countries from selected regions



Source: ESCWA calculations based on ESCAP/WB database on trade costs and UN Comtrade database on trade flows

Figure 3. Average import and export cost for Arab countries, 2000-2015

Source: ESCWA calculations based on ESCAP/WB database on trade costs and UN Comtrade database on trade flows.

8. Taking a general look at both sides of the costs, figure 3 shows clearly that export cost is higher for the Arab region than import cost to all trade partners including the subregions of the Arab region. Results show that import and exports cost from the whole Arab region to the region is the lowest among all examined regions contrary to what is perceived to be the reason for low intra Arab trade. The cost of export is the highest with Arab Maghreb Union (AMU) at the regional level and Latin and Central America regions at the global level. Table 1 shows that overall trade cost of the Arab region is high with most regions when compared with that of the ASEAN block, Indonesia and Turkey.

TABLE 1. OVERALL TRADE COST OF THE ARAB REGION IN COMPARISON WITH CERTAIN REGIONS, 2015

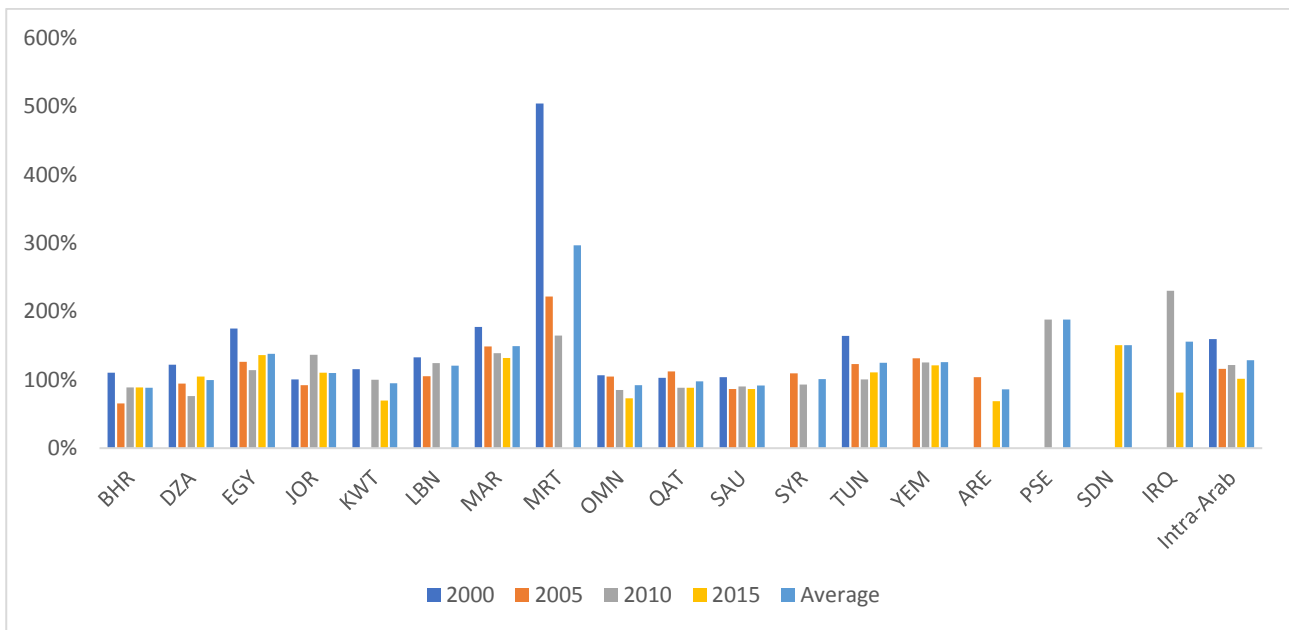
Region/country	Arab region %	ASEAN %	EU %	NAFTA %
Arab region	174	279	199	265
ASEAN	279	175	219	251
Indonesia	225	173	189	195
Turkey	134	230	117	180

Source: ESCWA calculations based on ESCAP/WB database on trade costs and UN Comtrade database on trade flows.

A. SUBREGIONAL FOCUS

9. The level of trade cost among Arab countries can be an important catalyst for trade growth. Over years, trade cost has been blamed for the low intraregional Arab trade. Intraregional Arab export cost averaged 129 per cent over the period 2000 to 2015 with a peak in the year 2000 at 160 per cent before it dropped to 102 per cent in 2015, marking a decrease of 36 per cent. The highest export cost with the Arab region of more than 500 per cent was recorded in Mauritania in 2000 before it dropped to 165 per cent in 2010. Averaging around 297 per cent for the whole period, it is still the highest among all Arab countries. Nearly all Arab countries have seen a decrease in export cost between 2000 and 2015, although modestly in most cases. Jordan, however, stands out with an increase of export costs by around 9 per cent between 2000 and 2015 (figure 4).

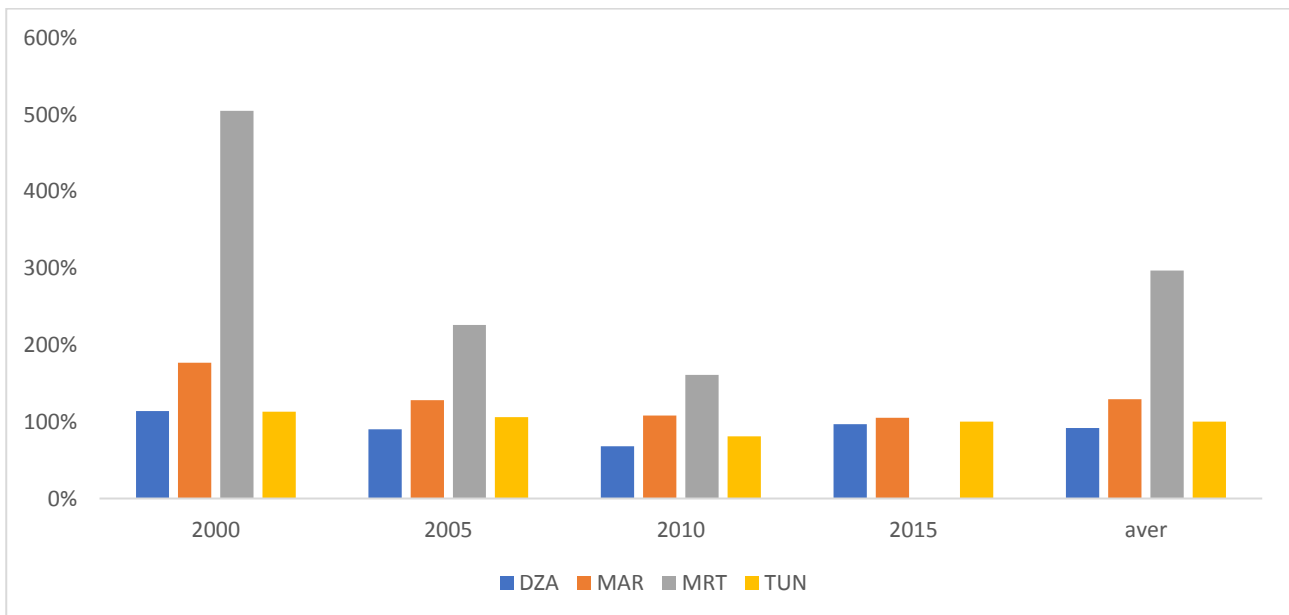
Figure 4. Intraregional Arab export cost



Source: ESCWA calculations based on ESCAP/WB database on trade costs and UN Comtrade database on trade flows.

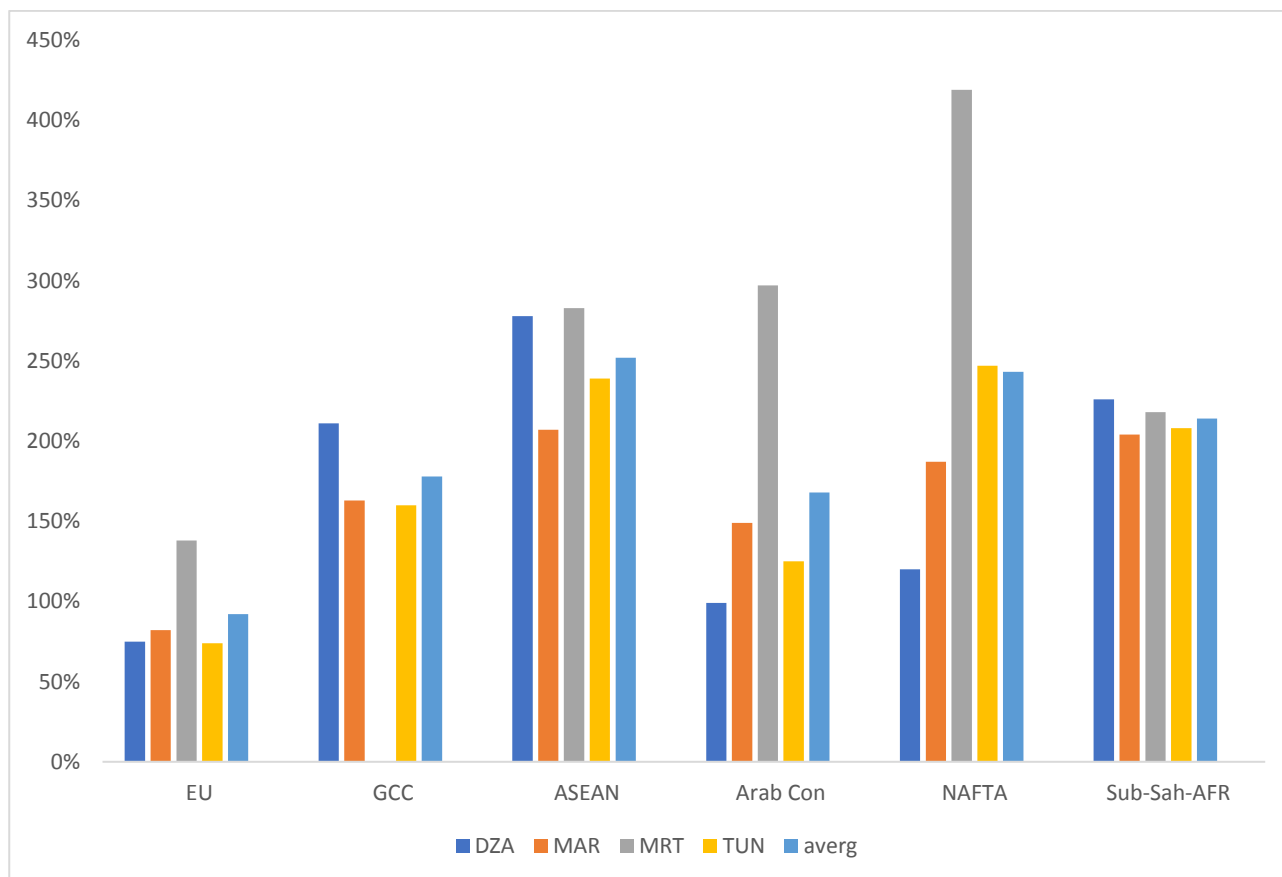
10. At the subregional level, the Maghreb countries exhibit the highest trade cost when exporting to each other. Algeria recorded the lowest export cost to the group followed by Tunisia and Morocco, while Mauritania recorded the highest export cost to the region (figure 5).

Figure 5. Intra-Arab Maghreb Union export cost



Source: ESCWA calculations based on ESCAP/WB database on trade costs and UN Comtrade database on trade flows.

11. The AMU region’s trade costs are lowest with the EU followed by the Gulf Cooperation council (GCC) countries and the Arab region as whole, while export cost with the ASEAN remains the highest followed by Sub-Saharan Africa and NAFTA (figure 6).

Figure 6. Export cost of Maghreb countries, average 2000-2015

Source: ESCWA calculations based on ESCAP/WB database on trade costs and UN Comtrade database on trade flows.

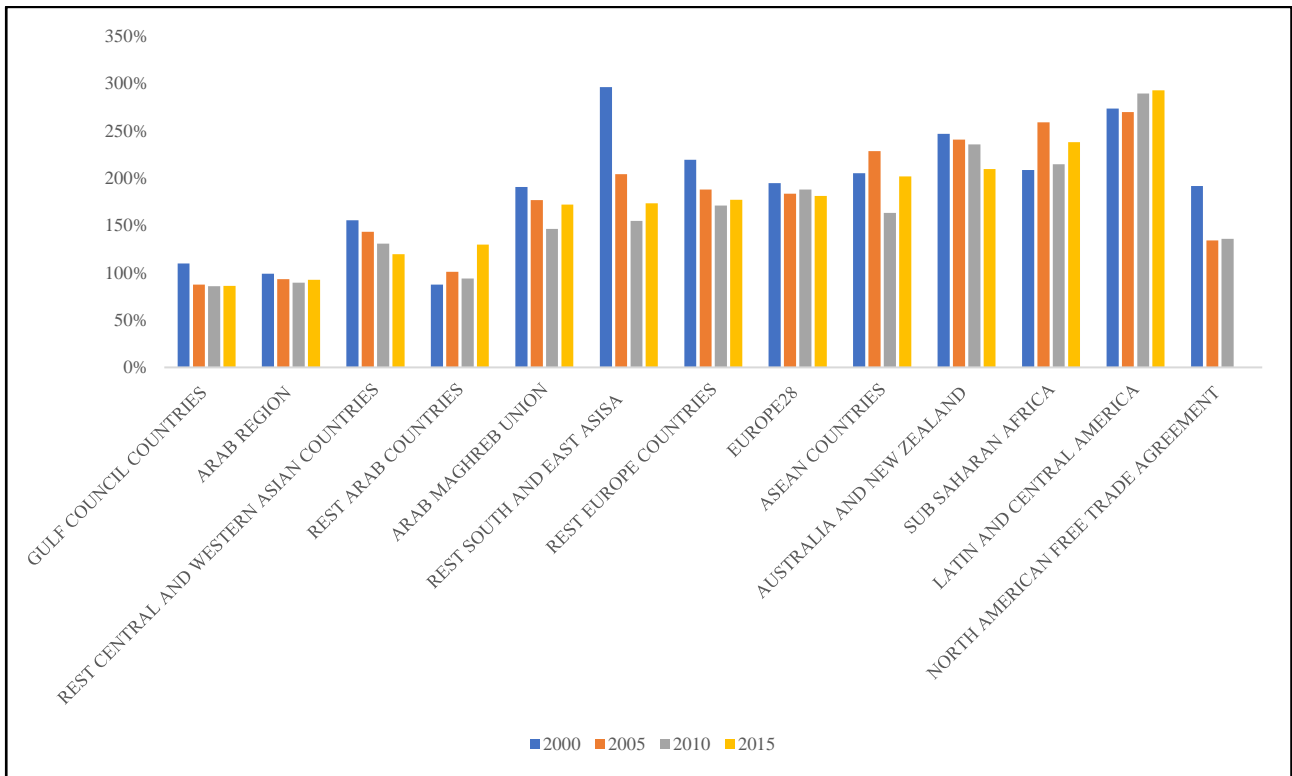
B. CASE STUDY: JORDAN

12. Jordan has the lowest costs on its imports from Arab region and the rest of Central and Western Asia. The more expensive products originate in Latin and Central America, Sub-Saharan Africa and Australia and New Zealand. There is evidence of some improvement in terms of lowering imports trade costs during the period 2000 to 2015, especially with the GCC countries, other Central and Western Asian countries, NAFTA, Europe and Southeast Asia.

13. Additionally, the high levels of trade cost with the 28 countries of Europe is remarkable given the relative geographical proximity between Jordan and the European bloc. The average cost with the EU is about 187 per cent, more than the double than what has been recorded with Tunisia.

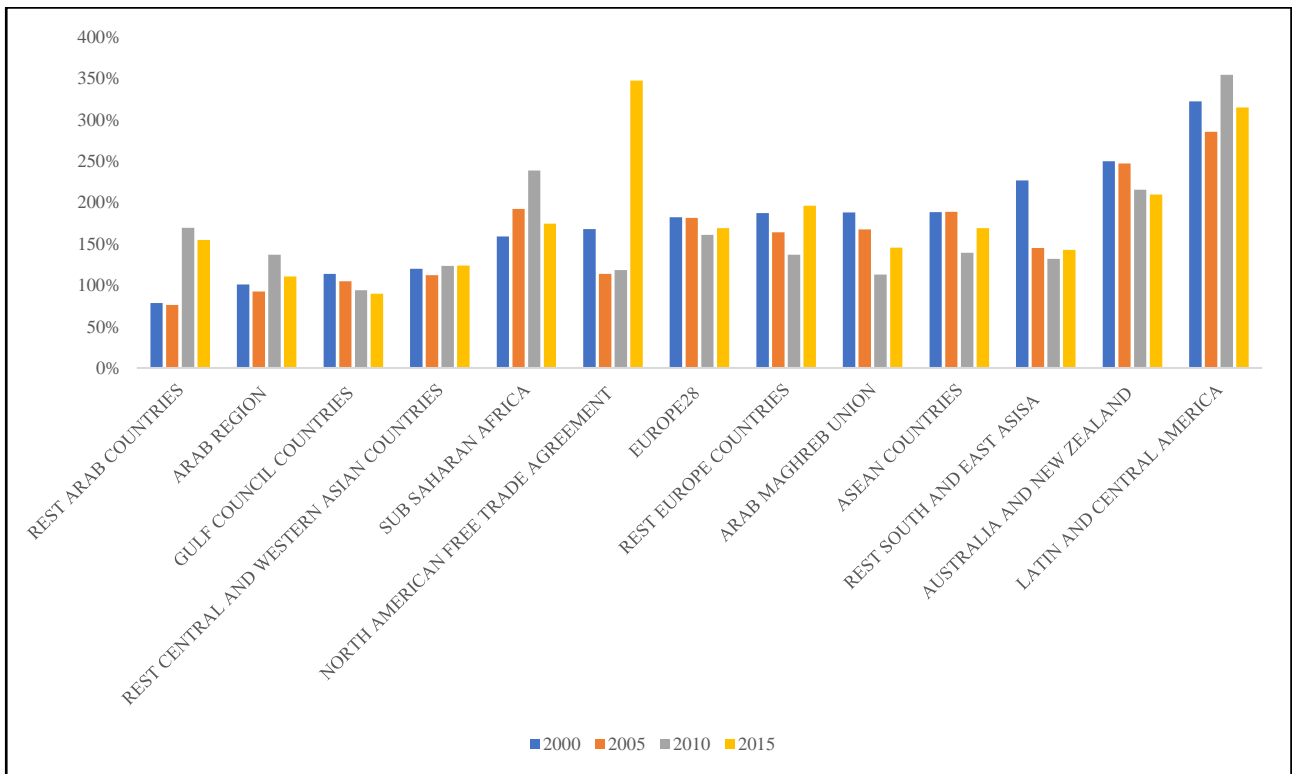
14. With regards exports, Arab blocs are by far the best partners in terms of trade cost for Jordanian exports. However, the sharp rise of the bars for the rest Arab countries in 2010 and 2015 in the graph in figure 7 deserves mention. The right part of the graphic is somehow less abrupt than the one related to Jordanian imports suggesting that Jordanian exports to non-traditional markets are faced with cheaper costs than the Jordanian imports from these same non-traditional markets. The same remarkable improvement for imports trade cost with NAFTA countries is observed for exports, apart from the value related to the year 2015 which should be considered as an outlier.

Figure 7. Jordanian exports costs



Source: ESCWA calculations based on ESCAP/WB database on trade costs and UN Comtrade database on trade flows.

Figure 8. Jordanian imports costs



Source: ESCWA calculations based on ESCAP/WB database on trade costs and UN Comtrade database on trade flows.

C. SECTORIAL ANALYSIS OF TRADE COSTS

15. Although overall trade cost analysis is useful to shed the light on a country's factors of competitiveness, it remains impeded by the generalities that prevent drawing a precise picture of the specific competitiveness of a country, due mainly to the difference between the cost factors of trading different goods. For instance, the cost of importing or exporting a container of biscuits is different from the cost of importing or exporting similar container of books and other paper products. Thus, taking the analysis down to sectoral level is essential for gauging the actual cost of trade for the respective sectors and dispensing policy advice to address the hurdles.

D. SECTORAL TRADE COSTS IN THE ARAB REGION: THE CASE OF JORDAN

16. Sectoral trade cost in the region varied greatly from one sector to another. Subregional estimates also show significant differences between different subregions.

TABLE 2. SECTORAL EXPORT AND IMPORT COST FOR JORDAN, AVERAGE

Sectors	Exports cost	Imports cost
Food and Bev	224	221
Leather	134	153
Wood	224	223
Paper	154	178
Printing	258	242
Refined petrol	350	372
Rubber	185	188
Non-metallic mineral	252	275
Basic Metals	134	144
Fabricated Metals	170	188
Machinery and Equipment	128	141
Electrical Machinery	118	176
Medical Precision	106	147
Motor Vehicles	95	159
Furniture	176	176

Source: ESCWA calculations based on the inverse gravity model.

17. Jordan's trade costs at the sectoral level reveal interesting conclusions. On the export side, refined petroleum products have the highest cost for export standing at 350 per cent, followed by printing at 258 per cent. The lowest export costs are seen with motor vehicles at 95 per cent followed by medical precision products at 106 per cent. On the import side, results are not very different: refined petroleum have the highest import cost at 372 per cent followed by non-metallic mineral at 275 per cent. The cheapest import costs are seen for machinery and equipment at 141 per cent, followed by basic metals at 144 per cent then medical precision products at 147 per cent.

II. CONCLUSION AND RECOMMENDATIONS

18. Most Arab countries maintain a high cost of trade which is affecting their ability to integrate further both at the global economic level and at the regional level. Various reasons contribute to this situation including several policy and non-policy realities that drive up trade costs. The types of causes of trade cost can change

according to the level of development of each country and other factors. Addressing trade cost causes requires that separate and independent analysis be carried out in each country to identify exact factors behind trade cost in the country and the required response to them be designed. It is widely acknowledged that addressing trade cost causes is essential to bring about positive changes that boost trade competitiveness, enable more integration in regional and global value chains, enable diversification of exports and markets and subsequently foster economic growth and job creation. It is worth mentioning that ESCWA is aiming to take the analysis further by dissecting trade cost to its basic elements. Such an exercise will allow the clear identification of the role of transport costs in trade cost and will subsequently enable drawing up policy advice for member countries as how to reform transport sectors toward lowering and rationalizing transport cost. Notwithstanding the particularity of each case, the following interventions are deemed necessary for overcoming the hurdles of high trade and transport costs in the Arab countries:

- Improvement of the quality of infrastructure at ports, with a focus on efficiency not size, is important target to enable the provision of efficient services which also requires the development of appropriate policies that ensure healthy competition to provide competitive services and prices;
- Enhancing connectivity to the global transport network is a prerequisite for lowering transport costs and trade costs. It requires the development of maritime networks, port efficiency and connectivity of hinterlands in order to smooth the transport of shipments from and to the country at competitive prices. Today's technological developments are also instrumental to increasing the efficiency of channelling tariffs through limited ports capacities;
- Full implementation of trade facilitation measures is a necessary action to reduce the delay at borders and thus lower the cost of clearing goods. To this end, full implementation of the trade facilitation agreement is a good start, but certainly not sufficient as other measures to improve logistics performance of services is crucial. Addressing the major causes of delays, as revealed by the analysis of the logistics performance index, is a necessary step to improving efficiency in ports and reducing costs;
- Improving transparency through digitization of processes and provision of necessary information via electronic means and portals can have a positive effect on trade cost;
- By the same token, the removal of unnecessary non-tariff measures can also lead to the substantial reduction of costs of trade. Thanks to advances in technologies, countries can now substitute time-consuming cumbersome procedures with electronic and remote processes that secure the interests of the country while minimizing the delays encountered and paid for by economic agents.
