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From Isolated Oases to
an Integrated Landscape
*The Continuing
Evolution of Middle
East Economies*



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EXECUTIVE SUMMARY

A steady expansion of economic integration is taking place across the Middle East and North Africa (MENA) region, giving rise to increasing optimism about the region's development. Reform-minded leaders have created much-needed investment, development, and trade opportunities by embracing new strategies and structural reforms. As a result, the isolated pockets of prosperity that characterized the old economic landscape are beginning to overlap. A new landscape is emerging, in which the economic fortunes of member countries are linked as never before by strategic cooperation. The benefits of regional integration are clear in five key areas:

Investment: Arab investors are putting more money than ever before into their countries. They are responding to investment opportunities, aided by reforms that provide for more efficient flow of capital, as well as a desire to hedge against uncertain environments in North America and Europe.

People: The number of Arab workers from Egypt, Jordan, Syria, and Lebanon who have moved to the oil-producing GCC countries¹ has risen substantially, distributing oil wealth to the Levant and North Africa through remittance flows.

Trade: Private monopolies, high tariffs, and bureaucratic import procedures

have been recognized as hindrances to regional trade, and progressive actions have helped cut tariffs, promote private-sector competition, and open doors for further trade opportunities.

Infrastructure: Regional projects in producing and sharing electricity, transporting oil and gas, and developing transportation links play important roles in economic integration.

Communications and Media: The proliferation of broadcast and broadband services has broken down national barriers and helped people in the region feel part of the larger pan-Arab community.

KEY HIGHLIGHTS

- Business, political, and social changes throughout the Middle East are creating a favorable climate for economic cooperation between neighboring countries.
- Structural reforms, global perspectives, and a strong united front now are seen as enhancements to the region's natural resources and as building blocks in a foundation for economic growth.
- Improved governance and accountability are critical to the process of economic integration, as removal of remaining barriers is to the movement of commodities and people.

STRENGTHENING TIES IN THE MENA REGION

Fifty meters below the calm surface of the Arabian Gulf, a safe distance from vulnerable coral formations, lies a 48-inch diameter pipeline that carries 2 billion standard cubic feet of natural gas each day. The Dolphin Gas Pipeline is the longest and largest subsea pipeline in the Middle East, a conduit for refined methane gas flowing from Qatar to the United Arab Emirates and, since 2008, on to Oman.

But the Dolphin Gas Pipeline is more than a way to move a product from one country to another. It's also a slender thread in the fabric of economic integration that continues to grow in texture, color, and richness throughout the GCC and in the wider MENA region. This fabric—spun from emerging

business, political, and social forces inside and outside the region—is creating a tapestry of pan-Arab collaboration and cooperation that is unprecedented in its momentum, and it has engendered a brighter outlook for the region.

Each time a new cross-border highway opens, each time a sovereign wealth fund invests in a Middle East venture, each time immigration laws are revised to allow the region's residents to settle more easily in a neighboring country, each time a new trade agreement is negotiated between Arab countries, the region's collective economy and the relationships between countries that drive it are strengthened. Further, thanks to the rapid spread and adoption of communications technology, economic integration is having the corollary effect of strengthening Arab culture itself. This confluence of planning, execution, and resources has brought the countries of the MENA region ever closer and ushered in a new phase of economic collaboration.

PERFECT TIMING

Efforts to create stronger economic integration in the region are not new, but the recent growth of intra-MENA investment is an indication of the broader economic integration evident in the region. It reflects a significant shift in Arab investor sentiment.

Witness the proliferation of regional trade agreements: At least 10 major regional, and an even higher number of bilateral, accords have been signed since the 1950s. Yet progress on this front had been slow until a few years ago. What, then, changed in the last decade to prompt a surge in investment, trade, and remittance flows between MENA countries?

A new generation of reform-minded leaders in the Middle East has led the way, liberalizing key sectors of their economies and implementing structural reforms, which have created investment and trade opportunities. Regional leaders have recognized both internal and external challenges facing their economies, such as demographic pressures and globalization. Their response has been to actively pursue strategies for economic development rather than simply rely on the natural endowment of their countries' resources.

A key outcome of these economic reform efforts, particularly in Egypt and the Levant countries, has been a dramatic improvement in the business climate, prompting greater investment from the Gulf states and facilitating cross-border business activity. Egypt stands out in this regard, having embarked on an ambitious reform and privatization program in 2004. As a result, Egypt has consistently been among the top reformers in the World Bank's annual *Doing Business* report, climbing 59 places in the ranking since 2006. Similarly, Jordan's trade reforms and privatization initiatives in strategic economic sectors have helped attract

GCC capital despite relatively slower reform of its business climate. Even among Gulf countries that are more conservative in their approach to reform, the pace of meaningful change in business climates has picked up, with Saudi Arabia leading the ranks of the most active reformers.

Another factor forging greater economic ties between MENA countries is the substantial economic growth of the GCC. Buoyed by rising oil prices since 2003 and flush with cash, Gulf states have sought new destinations for their money in addition to traditional investment opportunities in North America and Europe. Indeed, the change in the geopolitical environment after the 9/11 attacks, and subsequent repatriation of capital (especially by GCC private investors that had been active in the U.S. and Europe), completes the circle. This inflow of funds led to an increased supply of capital in the Gulf that was looking for a home. The timing could not have been better.

Underlying these events is a subtle shift in perception: a recognition that the region is stronger when it is united economically, which in turn provides an incentive to seek regional investment opportunities. The 2009 Arab Economic Summit in Kuwait affirmed this perspective by highlighting the need for further pan-Arab socioeconomic development. Fortunately, the timely social, economic, and even political changes that took hold in many MENA countries over the last decade have provided the right factors for strengthening regional integration, despite recent setbacks brought about by the global economic downturn. That integration is most clearly manifested in five areas: investment, people, trade, infrastructure, and communications and media.

INTEGRATED THROUGH INVESTMENT

Arab investors have been investing in their own neighbourhoods like never before, seeking opportunities within the MENA region by targeting strategic sectors with high potential for growth. Cultural similarities, a common language, and shared heritage, which in the past were overshadowed by political disagreements, have helped contribute to the attractiveness of intra-regional investments. Arab foreign direct investment (FDI) in the MENA region grew almost six-fold between 2004 and 2008,² reflecting a fundamental change in the region's economic climate and business environment.

Demographics have been an important factor in creating new opportunities for investment, both in the GCC and across the region. The rapidly growing population and

increased urbanization have boosted demand for water, sanitation, healthcare, housing, and education. With a population expected to grow by another 40 percent over the next 20 years,³ demand for these services—and the infrastructure that supports them—will remain strong. In 2007, Egypt's total capital expenditure on infrastructure projects was estimated at US\$13.2 billion. Within the GCC, the UAE, Saudi Arabia, Qatar, and Kuwait had an estimated \$242 billion of infrastructure investments for the same year.⁴

Investment has also increased over the last five years due to initiatives such as structural reforms, less-onerous restrictions on intraregional FDI and portfolio flows, tax cuts, privatizations, and measures to facilitate the development of

financial markets and expand the private sector. As a result, intraregional investment has increased significantly over the last decade, reaching over \$30 billion in 2008.⁵

Notably, Arab intraregional investments have been poured into strategic sectors (such as real estate and tourism infrastructure) that are long term by nature. Arab investors have become more comfortable investing in their own backyards, a strategy made more attractive by prospects for higher returns—thanks to a regional economy that offers stronger potential for investment than the U.S. or Europe, especially as those regions may face a long and sluggish economic recovery.

A significant portion of investment and financial flows in the Arab

world have been from wealthy GCC states to emerging markets in the Levant and Egypt. In 2008, the GCC accounted for 75 percent of all Arab funds invested within MENA, with the UAE being the largest single investor in the region. On the receiving end, Lebanon and Egypt have attracted most of the Gulf investments, accounting for about 20 percent of total Arab investment in MENA over the last few years.⁶ Real estate and services sectors, including banking and tourism, have been the big winners.

In real estate, UAE-based firms have led the way, investing in billion-dollar projects in Egypt, Jordan, and Lebanon. According to the IMF, about half of all GCC investment in Lebanon is in the real estate sector,⁷ which has been a key engine of

economic growth in that country over the last few years. Kuwait and Saudi Arabia have been important investors in real estate development in Syria; in fact, some of the largest real estate companies are enlarging their scope of investment. For example, investments in real estate across the MENA region by Dubai-based Emaar Properties have expanded to include financial stakes in education and healthcare.⁸

Lebanon's and Egypt's dominance in attracting Arab investment does not mean that other MENA countries have lost out. On the contrary, many other economies in the region have seen Arab investment surge in recent times despite the setbacks of 2008. In Jordan, for example, Arab investments over the course of the past five years have multiplied. From a low of

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approximately \$18 million in 2003, total investments reached highs of about \$960 million and \$816 million in 2006 and 2007, respectively, retreating to a still significant \$433

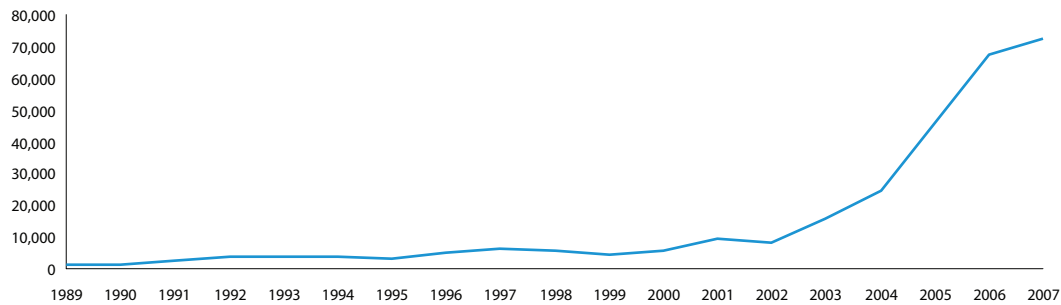
million in 2008.⁹ Other MENA countries showing substantial progress on economic reforms, such as Morocco and Tunisia, have also attracted capital from GCC nations

and are poised to receive additional future investments (see Exhibit 1).

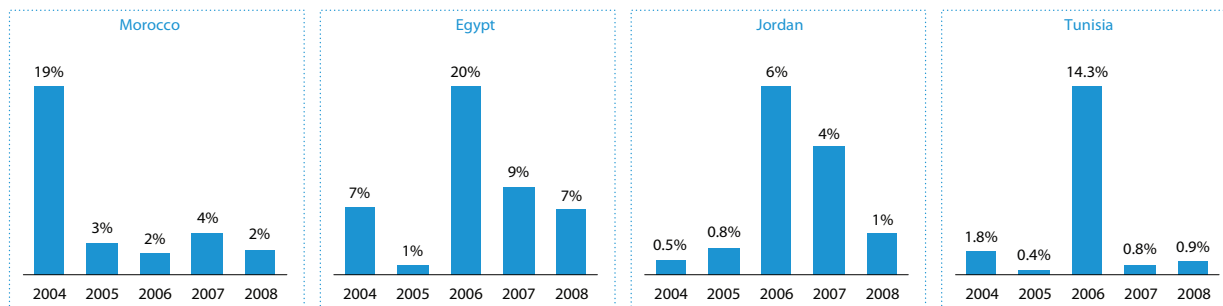
Although GCC investment flows to the Levant and Egypt have been

Exhibit 1
Regional FDI Has Shown Impressive Growth Over the Last Decade

TOTAL FDI INFLOWS IN MIDDLE EAST COUNTRIES¹
(in US\$ millions)



INTER-ARAB INVESTMENTS BY COUNTRY
(percentage of total investments)



1) Includes all Arab countries with the exception of Comoros.
Note: Numbers are rounded off.
Source: The Arab Investment and Export Credit Guarantee Corporation; Booz & Company Ideation Center analysis

an important trend over the last five years, GCC countries have also been on the receiving end of intra-Gulf investments, especially in the telecom sector. Saudi Telecom Company invested \$900 million in 2007 and \$230 million in 2009 in Kuwait's and Bahrain's telecom sectors, respectively. In 2007, Qatar Telecom acquired a controlling interest in Kuwait's second-largest mobile operator for \$3.8 billion. The UAE's Etisalat-led consortium invested \$3.25 billion to acquire the second mobile license in Saudi Arabia in 2004. Kuwait's Zain invested a record \$6.1 billion in 2007 to get a share of the Saudi mobile telecom market. Indeed, the Saudis have taken the lion's share of FDI across many economic sectors and especially the services sector. About 44 percent of all Arab investment over the last five years has gone to Saudi Arabia.¹⁰ Similarly, a large proportion of global

FDI coming into the region has also gone to Saudi Arabia, growing to \$23 billion in 2008 from just \$200 million in 2000.^{11,12} The sheer size of the Saudi economy, plus the acceleration of reforms since 2006, have drawn Arab investors from other GCC states to invest heavily in Saudi Arabia's infrastructure, energy, telecommunications, and utilities.

Sovereign wealth funds (SWFs) and private equity funds have been active investors in the region in recent years, hoping to capitalize on numerous opportunities created by the appealing combination of structural reforms, economic liberalization, and the need for more investment closer to home. SWFs have plowed some of their vast wealth back into the MENA region, with Egypt and Jordan among the countries that have benefitted from investment in their financial and industrial sectors,¹³

among others. Regional private equity funds have raised almost \$20 billion, mainly from private investors, of which about \$9 billion has been placed in the MENA region. One of the bellwether private equity deals was the 2007 buyout of Egyptian Fertilizers Company by Abraaj Capital, a Dubai-based private equity firm, worth \$1.4 billion.¹⁴

Both SWFs and private equity are likely to continue to be important agents of investment and integration in the region. On the private equity side, an estimated \$11 billion of capital—committed but not drawn upon because of the 2008–09 global economic downturn—could be invested over the next few years in stable sectors such as healthcare and education.

The development of capital markets in MENA is another contributor to

regional financial integration; the combined market capitalization of stock exchanges in MENA grew by 104 percent between 2004 and 2007. This trend is likely to continue despite setbacks brought about by the 2008 global financial crisis (see Exhibit 2). The flow of funds has been largely from the GCC countries to the Levant, with the Beirut, Amman, and Cairo stock markets

seeing a surge in Arab investment in their respective exchanges over the last five to 10 years.¹⁵

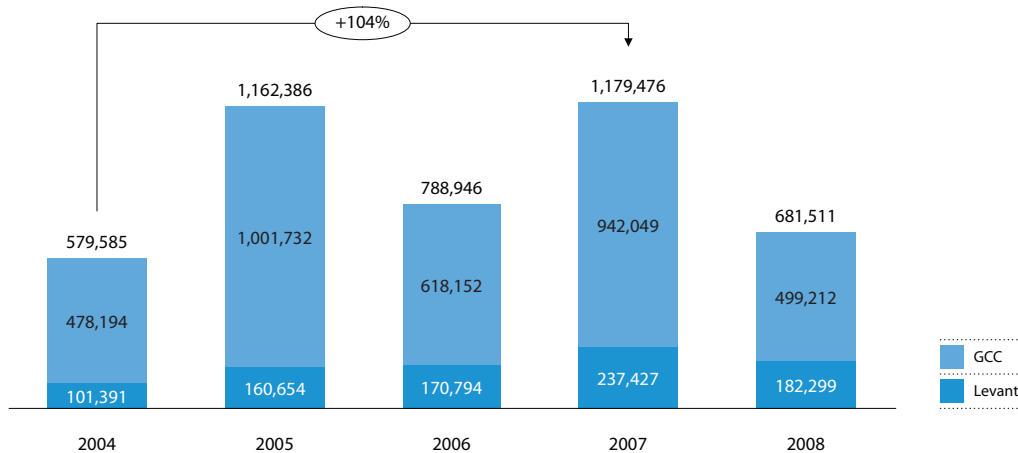
The emergence of regional stock exchanges in MENA countries, and in the GCC region in particular, reflects those countries' desire to diversify their economies, facilitate the flow of capital to the region, and become regional financial hubs.

Egypt's Smart Village Financial District, Jordan's National Financial Centre, and Saudi Arabia's King Abdullah Financial District, all under construction, will add new points of access to the region's capital markets and increase competition for foreign investors. At the same time, these financial centers could act as springboards to further integration.

Exhibit 2

Despite Setbacks Caused by the Global Economic Downturn, MENA Stock Exchanges Are Poised to Show Significant Growth

TOTAL MARKET CAPITALIZATION OF MIDDLE EAST REGION STOCK EXCHANGES
(in US\$ millions)



Note: Countries whose stock exchanges are included are Bahrain, Egypt, Iran, Iraq, Jordan, Kuwait, Lebanon, Oman, Palestine, Qatar, Saudi Arabia, and UAE.
Source: Grant Thornton, "Middle East Capital Market Guide 2009"; Booz & Company Ideation Center analysis

INTEGRATED THROUGH PEOPLE

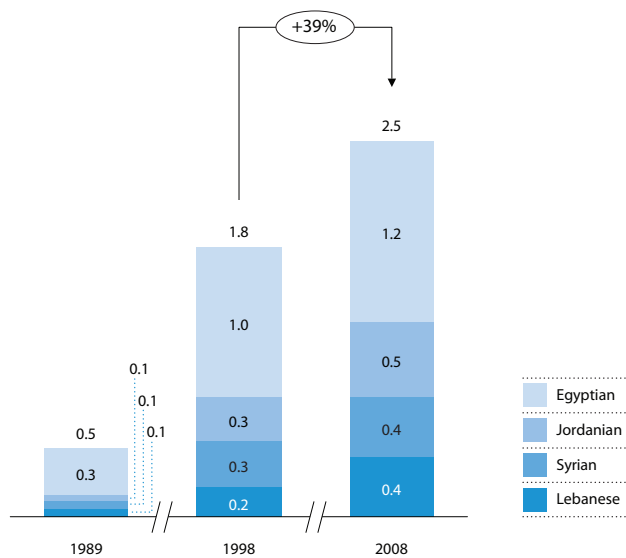
Visitors to Riyadh, Abu Dhabi, Doha, or Manama a decade ago might have remarked that many of the taxi drivers, shop assistants, hotel staff, and waiters they encountered were Arab nationals from outside the Gulf nations. Indeed, the migration of workers from resource-poor MENA countries to the GCC, and the remittance from these workers to their countries, was then the main—if not only—component of regional economic integration. Visitors today would note these jobs are overwhelmingly taken by immigrants from South and East Asia. Yet despite that shift in immigration trends over the past decade, the number of Arab migrant workers in the MENA region has increased even further.

The GCC’s strong economic growth over the last decade, accompanied by a surge in the demand for labor,

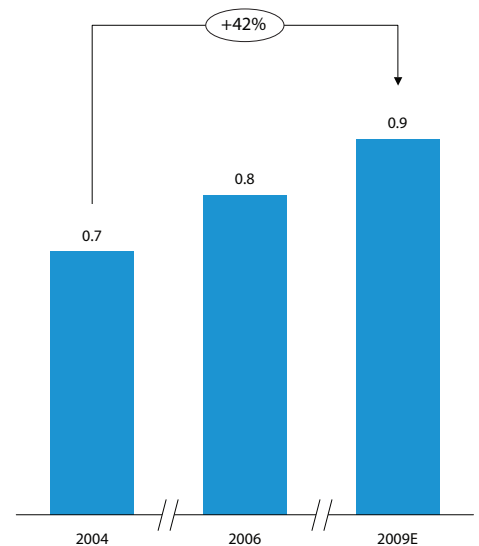
has sparked rising numbers of both Arab and Asian immigrant workers, especially at semi-skilled and professional levels. As a result, the number of Arab workers—mainly from Egypt but also from Jordan, Syria, and Lebanon—moving to the oil-producing GCC countries has risen substantially. Data for Saudi Arabia and the UAE suggests the number of Arab migrant workers has risen by about 40 percent over the last five to 10 years (*see Exhibit 3*). This number is expected to climb in the coming years as political initiatives are translated into economic programs. Recent “Arab reconciliation” initiatives by the Saudi monarch to realign political goals with other Arab countries (notably Syria) will serve to refocus efforts on economic issues that are likely to include increased migrant workers to the GCC region.

Exhibit 3
Arab Workers from North Africa and the Levant Seek Opportunity in the Gulf

LEVANT MIGRANT WORKERS IN SAUDI ARABIA, BY NATIONALITY
(millions of immigrants)



ARAB IMMIGRANTS TO UAE¹
(millions of immigrants)



1) Arab immigrants include immigrants from the following countries: Egypt, Lebanon, Syria, Jordan, Palestine, GCC countries, Iran, and Yemen.
Source: Kingdom of Saudi Arabia Central Department of Statistics and Information; UAE Ministry of Economy’s Central Statistics Department

The increase in intra-MENA labor migration has had an important role in distributing oil wealth to the Levant and North Africa through remittance flows. It has helped to chip away at high unemployment rates, alleviate poverty, and spur economic development in these regions. Remittances are a significant source of income for many MENA countries. Although data is scarce on intra-Arab remittances, a significant portion flows from GCC to MENA countries that are poor in resources but abundant in labor (see Exhibit 4). The recent oil windfall bolsters this conclusion. For example, gross remittances in MENA countries increased 17.6 percent when oil prices were at their height in 2007, after a 14 percent increase in the

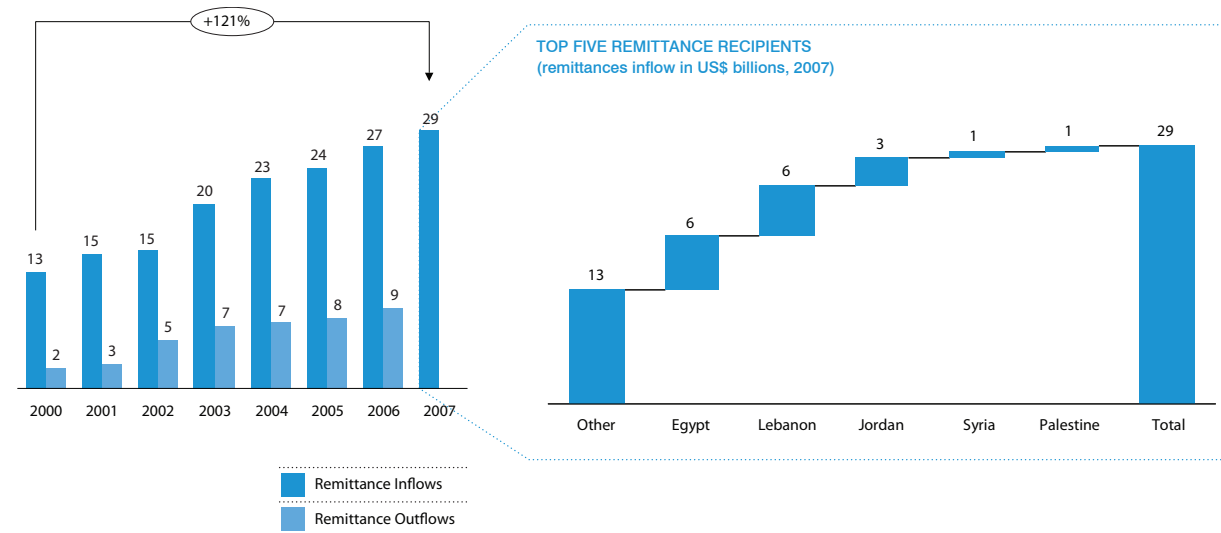
previous year.¹⁶ According to the IMF, workers' remittances in Middle Eastern oil-importing countries reached an estimated \$31 billion in 2008¹⁷—equivalent to total FDI inflows and more than double what they were in 2000. Investments from the GCC plus remittances sent by Arab residents in the GCC to their native countries in the Levant have had a strong impact on the economic growth of MENA countries. Thanks to these funds, demand for consumer goods and services has increased and more jobs have been created, underlining the importance of people to economic integration.¹⁸

Given their small populations and strong economic growth projections for the next decade, the GCC

countries will need more migrant workers of various skills. How this demand is met and by whom, however, is subject to contradictory developments at this juncture. On one hand, the shift continues toward the use of cheaper labor from South and East Asia, and economic growth in the labor-exporting countries of MENA (such as Egypt) is likely to provide greater job opportunities at home for job-seekers. On the other hand, recent political reconciliation—led by the Saudis—may result in a greater number of immigrants from other Arab countries and the continued integration of the region's labor force. Exactly what will happen as these conditions evolve is uncertain.

Exhibit 4
Remittances from the Gulf States Are Spreading Wealth to the Levant and North Africa

REMITTANCE INFLOWS AND OUTFLOWS IN ARAB COUNTRIES
(in US\$ billions)



Source: World Bank, *Migration and Remittances Factbook 2008*; Booz & Company Ideation Center analysis

INTEGRATED THROUGH TRADE

Over the past five decades, different circumstances within MENA countries have created obstacles to trade. Oil-producing countries, because of the dominance of that resource, have overlooked the development of trade in non-oil industries. For other countries in the region, the lack of a wide industrial base has limited the amount of tradable goods they can produce. Dominant and bureaucratic government sectors, as well as private monopolies, have contributed to trade barriers in the form of high tariffs and cumbersome import procedures. As a result, intra-regional trade in the MENA region as of 2007 (in terms of the share of regional trade flows, including oil) lagged behind that of other regions, averaging 19.1 percent compared with 71.2 percent and 57.4 percent in Europe and Asia, respectively.¹⁹

However, signs of progress in intra-regional MENA trade are beginning to appear. With policy focused on structural reforms, strengthened by World Trade Organization accession agreements, the steps taken to cut tariffs and promote regional trade are starting to bear fruit. The introduction of the GCC customs union agreement in 2003 and GAFTA in 2005 have helped reduce tariffs across the region: Average tariffs in the GCC and Lebanon came down from double digits to 5 percent.²⁰ As GAFTA develops into a wider, more comprehensive agreement, high tariffs, which have reached 20 percent in some North African countries, are likely to drop substantially in the coming years and spawn more trade activities in the region.

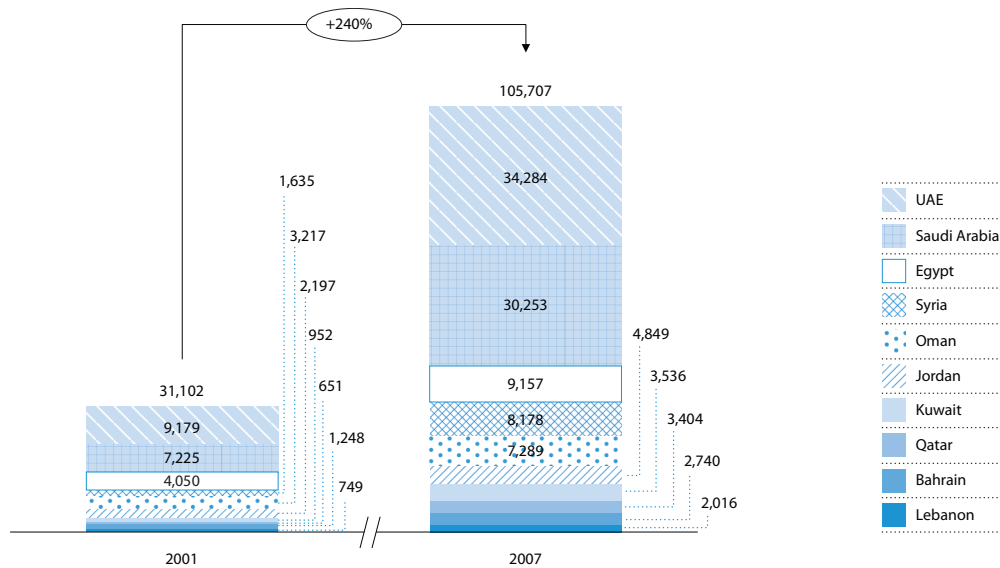
At the same time that countries have coordinated and implemented these structural reforms on trade policy, greater economic diversification in MENA economies has led to more trade within the region. Lower import tariffs on goods

produced in MENA countries such as Jordan, Egypt, and the GCC nations have helped boost trade activities between them. Jordan and Syria enjoy relatively high levels of intraregional trade with the GCC, which represents their main export

market; and Lebanon sends almost a quarter of its exports to GCC markets.²¹ Furthermore, the value of intraregional exports (excluding oil) increased significantly over the 2001–2007 period (see Exhibit 5).

Exhibit 5
The Value of Exports in the MENA Region Is on the Rise

TOTAL VALUE OF EXPORTS TO THE MIDDLE EAST REGION BY COUNTRY
 (excluding oil products; in US\$ millions)



Source: Trade Map, International Trade Center; Booz & Company Ideation Center analysis

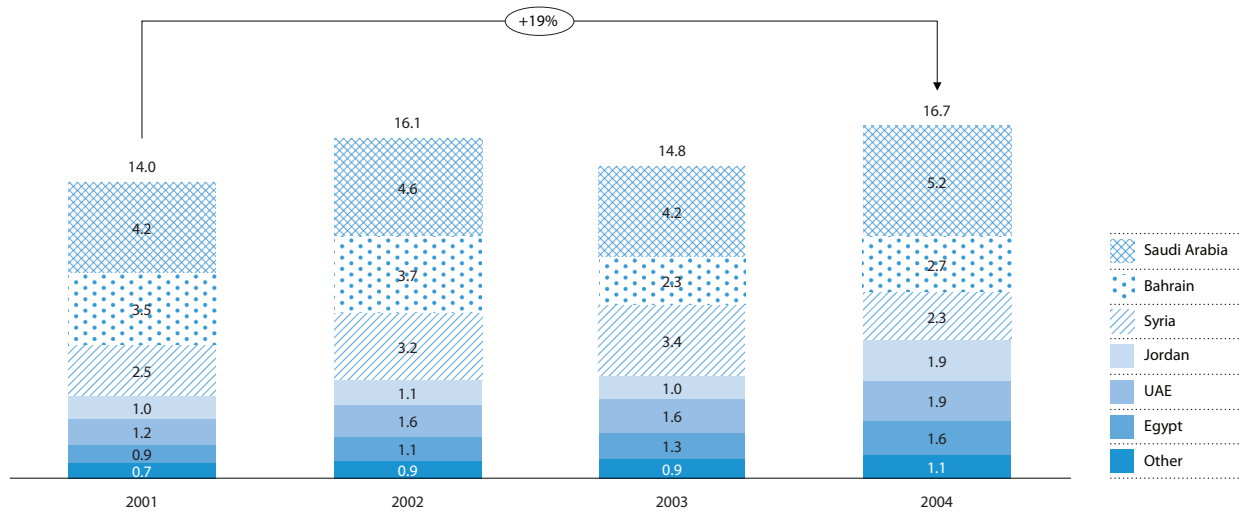
Growth in the regional trade of services has been even more noticeable, despite the recent damper placed on the region's economies by the global downturn. Aided by a growing volume of short-haul travel within the region, tourism in MENA

has seen measurable growth over the course of the past decade. From 2001 to 2004, for example, the number of Arab visitors to Saudi Arabia, Bahrain, Syria, Jordan, the UAE, and Egypt increased by about 19 percent from 14 million to almost 17 million

(see Exhibit 6).²² More recently, in 2008, the Middle East witnessed a rise of 11 percent in tourism as compared to 2 percent for the rest of the world—generated, in no small part, by Arab tourism. Indeed, Jordan and Lebanon are estimated to have

Exhibit 6
Popular Tourist Destinations for Arab Travelers Have Sprung Up around the Region

TOTAL NUMBER OF MIDDLE EAST TOURISTS BY COUNTRY
 (in millions)



Source: UN World Tourism Organization, *Tourism Market Trends 2004 Edition, Middle East*; Booz & Company Ideation Center analysis

received 2.4 million and 2 million Arab tourists, respectively, in 2009. Syria estimates that GCC visitors surged more than 23 percent from the first quarter of 2008 to the same period in 2009, although the actual numbers remain relatively low—from 94,157 tourists to 116,109.²³ More Arab travelers are choosing to vacation at tourist destinations closer to home, prompting investors and policymakers to capitalize on this sector and develop it further.

In Egypt, new cities have sprung up along the Red Sea and Mediterranean coasts to attract Arab travelers and investors alike. Sharm el-Sheikh, for example, a popular resort destination on the southern tip of the Sinai Peninsula, is typical of a developing tourism industry that has drawn the

attention of private investors in GCC countries as more and more Arab tourists flock to the region each year. Government officials in Tunisia have been promoting tourism and tourism investments in their country to Arabs via a series of recent visits to countries across the MENA region. Within the GCC, Dubai has achieved international fame over the past five years and attracted tourists and investors from across the Arab world. Tourists from MENA countries now account for about 45 percent of all tourist arrivals in the region,²⁴ with Egypt, Jordan, Syria, Bahrain, and Saudi Arabia all proving popular with MENA tourists.

Trade in telecommunications services has also experienced intraregional growth, thanks to the liberalization

of this sector across the region. MENA-based telecom service providers have expanded within the GCC as well as into North Africa, the Levant, and beyond. Etisalat is now one of the largest telecom providers in the regional market, connecting an estimated 100 million subscribers in the MENA, sub-Saharan Africa, and Southeast Asia regions. Saudi Telecom has also expanded regionally into Kuwait and Bahrain, with plans to extend its services to other Arab countries, in addition to its inroads in Turkey, South Africa, and Southeast Asia. In Egypt, Orascom telecom investments span other MENA countries like Tunisia, Algeria, and Lebanon; several countries in sub-Saharan Africa and Asia; and, more recently, Canada, through its subsidiary Globalive.

Growth in health-services exports has also been strong, driven by demographic trends. Life expectancies are rising in the region, and changing lifestyles are leading to higher demand for healthcare. Tunisia is a regional leader in providing health services (particularly to Libyans willing to travel to Tunisia), as are some GCC countries. Jordan is emerging as another healthcare destination for citizens from other Arab and non-Arab countries, with revenue from this sector exceeding \$1 billion in 2007. The number of foreign patients going to Jordan for medical treatment has grown an average of 10 percent a year since 2004, and the

World Bank expects continued strong growth over the next five years.²⁶ The health sector is likely to see strong investment and growth in coming years, driven by demand and the increasing liberalization of healthcare markets in the region. Private equity investments in the health sector almost doubled year-on-year in 2008, and as healthcare is generally considered a defensive play during economic slowdowns, this sector is expected to attract more investments over the next few years that will boost the potential for health-services exports within the MENA region. The growth in tourism, regional telecoms, and healthcare services has been a direct result not only of

structural reforms in the region, but also the strong economic expansion and tremendous liquidity that have financed key projects and infrastructure in these sectors. These investments have further positive economic implications that could quicken the pace of integration in MENA. For example, the rise in the number of competitors and the quality of telecom services contribute to economic efficiency and enhance consumer welfare. Similarly, a hike in traditional and healthcare tourism services, induced by competition, improves service quality and raises the standards of living in the MENA region.

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INTEGRATED THROUGH INFRASTRUC- TURE

The oil windfall in the GCC states, as well as higher FDI inflows to the region since 2003, have financed ambitious and much-needed infrastructure programs across the Middle East. Infrastructure projects scheduled over the next five years are estimated to range between several hundred billion dollars and more than one trillion dollars. Cross-border infrastructure initiatives, such as power grids, gas pipelines, transport links, and telecommunications networks, have become more common over the last decade.

Cross-border electricity projects were initiated in the past mainly to ensure backup power supplies rather than to become a major source of electricity. Today, the MENA region's leaders have found new ways of dealing with higher demand by developing enough energy capacity to facilitate economic and industrial growth and meet the needs of a growing population. New projects are focused on sharing power-generating capacity that allows greater flexibility and reliability and reduces cost.

An excellent example is the GCC's new \$1.4 billion electricity grid,

Interconnection Project, which links the power grids of Saudi Arabia, Bahrain, Qatar, and Kuwait. The first phase of this project was completed in July 2009, and the second phase will see the addition of the UAE and Oman to the grid. A critical element of the project is the sharing of power reserve capacities and the exchange of electricity between countries, which allows them to meet their growing electricity demands at a fraction of the cost each country would require to build its own generation plant. Elsewhere, recent investment in a relay power station in Lebanon—where electricity is in short supply—is part of an increasing Arab integration effort in infrastructure aimed at meeting demand and reducing cost. Egypt, Jordan, Syria, and Lebanon are expected to become part of a regional electric power grid that will connect eight MENA countries in the coming years.

Oil and gas sector infrastructure has also been a key beneficiary of increased investment in the region. A number of trans-country natural gas pipelines that have already been built, and others that are under construction, such as the Euro-Arab

Mashreq Gas pipeline that will link gas markets in Egypt, Jordan, Lebanon, and Syria, will further boost regional integration. The ultimate aim is for this regional gas market to link to its EU counterpart. The GCC gas pipelines, of which the \$10 billion Dolphin Gas Pipeline is a part, carry natural gas from Qatar to export markets in the UAE, Bahrain, and Kuwait. Along with boosting trade between Gulf states, GCC pipelines have helped alleviate the shortage of natural gas in the importing countries. These pipelines, together with the electricity interconnection project, have ensured that energy integration in the region is much deeper than it was a few years ago, and the supply of energy has increased to meet the demand in these rapidly growing economies.

The region's transportation systems are also more integrated now than just five years ago, particularly with respect to air transport. This is evidenced by Bahrain, Jordan, Lebanon, Morocco, Oman, Qatar, and the UAE taking steps to implement "open skies" agreements.

Other countries in the region are progressively eliminating restrictions in their markets in an effort to draw in more regional investments.²⁷ In the less-developed road and rail transportation systems, governments are making efforts to improve and upgrade road and rail links between MENA countries to facilitate trade. Saudi Arabia has fully implemented the 2001 UN Agreement on International Roads in the Arab Mashreq, and has invested heavily in widening and modernizing many sections of its road network. Egypt, Jordan, and Syria are also upgrading their major international routes.

In Saudi Arabia, the North-South Railway will play a major role in further integrating the GCC and other MENA countries. The railway will link the Al-Jalamid phosphate deposit in the far northwest region (close to Jordan and Iraq) to Ras al-Zour, near Kuwait, on the Gulf coast. It will provide more efficient means of transportation of goods, and its benefits in the longer term will be further regional integration through both goods trade and tourism.

Although there is widespread agreement on the need to improve rail links across the region, track gauge differences between countries mean that it has not been possible to simply connect national railway lines. The actual connectivity of railways in MENA will depend on construction of new railway lines as well as major upgrading of existing lines. The Agreement on International Railways in the Arab Mashreq (2005) sets out the technical specifications and timeline to develop an integrated railway system in the region, and calls for project completion by the end of 2020.²⁸

In the future, the development of an integrated physical infrastructure of roads, highways, railways, and airways will contribute to greater economic efficiencies within MENA when combined with updated information and communications technology. Better communication leads to faster and more standardized procedures, which in turn helps improve the flow of regional traffic.

The development of an integrated physical infrastructure of roads, highways, railways, and airways will contribute to greater economic efficiencies within the MENA region.

INTEGRATED THROUGH COM- MUNICATIONS AND MEDIA

The integration of telecommunications infrastructure over the last decade in the MENA region has been phenomenal. Telecom liberalization in many countries has followed international standards, opening the way for greater cross-border investment and the emergence of regional telecom providers. These operators have increased affordability and accessibility for consumers.

The MENA region's integration in communications is also visible in broadband, fiber-optic cable, and connectivity via satellite fiber-optic technology. Arabsat, the region's largest satellite services provider, offers the full spectrum of broadcast, telecom, and broadband services to more than 164 million people in 21 countries.²⁹ Without this shared ICT infrastructure, the phenomenal growth in the Arab broadcasting media industry over the last few years

would not have been possible. The number of pan-Arab and free-to-air GCC TV channels has grown by about 45 percent every year from 2003 to 2006.³⁰

Shared regional infrastructure has led not only to growth in media channels but to their continued integration. One example of a truly regional media company is the Maktoob Group, a leading Arab online community based in Jordan. It was backed first by Abraaj Capital and then by Wall Street hedge fund Tiger Global Management. Its subsidiary Maktoob.com was purchased by the U.S. Internet giant Yahoo—largely because of the site's extensive market penetration throughout the region. Maktoob serves as a model for what can happen when media companies reach beyond local audiences and find innovative ways to build regional reach.

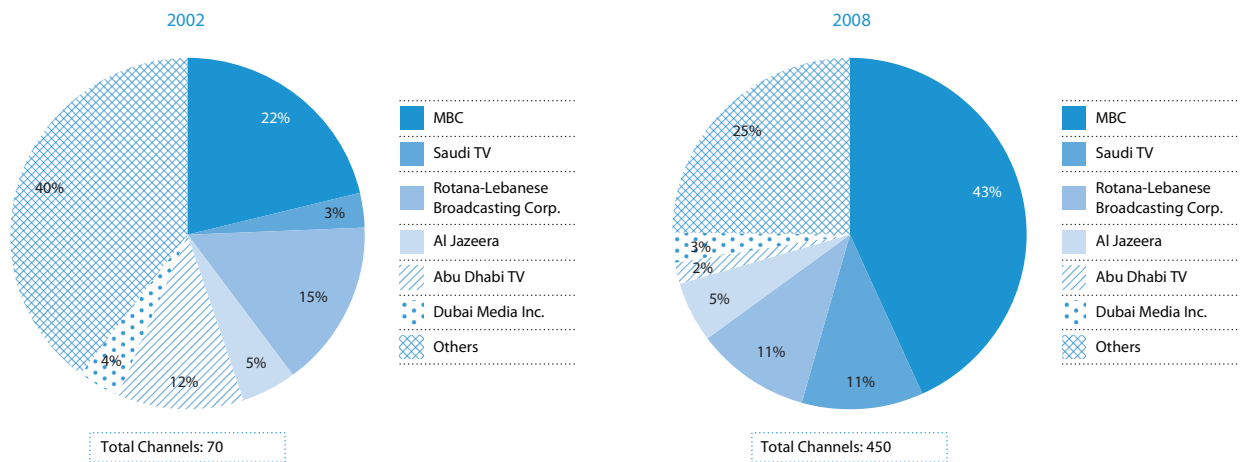
In broadcasting, the Middle East Broadcasting Corporation (MBC) is a leading international network of Arab origin—another strong indicator of the extent of regional integration on the media front. In fact, the industry structure has dramatically evolved since 2003 in

terms of the number of pan-Arab broadcasters (*see Exhibit 7*). This increase has been accompanied by a rise in related economic activity. For example, by the end of 2009, we estimate net advertising revenues will have reached about \$425 million—a 17 percent increase from

\$230 million in 2004. This increase reflects not only Arab audiences' viewership of TV programs of common interest, but also the rise in economic ties between Arab countries. In particular, firms that in the past pursued only local customers are now actively pursuing

Exhibit 7
There Has Been a Dramatic Increase in Pan-Arab Broadcasting

EVOLUTION OF PAN-ARAB BROADCAST SECTOR IN THE MIDDLE EAST
(market share)



Source: IPSOS, Booz & Company Ideation Center analysis

Arab consumers. Thanks to viewers' common cultural heritage, regional integration through the media is poised to increase even further.

The mushrooming capability and accessibility of broadcast and broadband services, aside from their obvious benefits to economic growth, have had the unintended consequence of promoting greater social interaction throughout the

region. Some believe that this unprecedented access to information appears to be changing the fabric of Arab culture itself. People now communicate with each other with greater convenience and frequency, breaking down barriers of time and distance. They watch the same television programming, hear the same news, and travel the same information highway in cyberspace no matter where they live. It is

evident that the media have united Arabs on certain topics while exposing their differences on others. Opinions aside, what's assured is that the proliferation of communications technology has helped Arabs be more informed and feel they are part of the larger pan-Arab community throughout the entire region, not just their local community.

The mushrooming capability and accessibility of broadcast and broadband services have had the unintended consequence of promoting greater social interaction throughout the region.

A MEANS TO AN END

It is unarguable that links between MENA countries have deepened, and the region is far more integrated on a number of levels today than it was at the turn of the 21st century. Although this is partly due to the wealth generated by rising oil prices for most of the last decade, policy-driven developments have been equally important: Without the structural and economic reforms in many countries and the efforts to diversify economies in the region, the oil wealth could have been invested outside the region. Yet business and political leaders in the Middle East have recognized the advantages that greater regional integration offers and have actively pursued this strategy.

Regional integration among MENA nations is not just an end in itself. Rather, it is a stepping stone to greater global integration for many countries in the region. It encourages greater competition in key sectors, but in a gradual and controlled way, giving domestic firms and industries a chance to adjust and become more competitive before taking on the global market. The World Bank argues that regional integration offers

policy-makers and business leaders a training ground of sorts, allowing them to hone their negotiating skills with their counterparts in neighbouring countries before tackling international trade agreements and policies.³¹ Finally, the rise in regional economic integration is an important step in fulfilling the aspirations of political harmony harbored by many in the Arab world. Indeed, as it moves forward with the standardization of rules relating to the flow of goods, services, and capital, the entire region will become a less risky, more attractive proposition for all MENA countries and the rest of the world.

Greater integration within MENA should make firms in the region more efficient, productive, and competitive, which will encourage greater investment in all countries and thus spur stronger economic growth. Reducing unemployment and alleviating poverty become easier to achieve in an economy that is growing in a sustained way from a diversified base, rather than stuck in a boom-bust cycle dictated by oil price movements.

THE WAY FORWARD

Despite making tremendous progress over the past years, there is still much room for improvement. Greater integration on the trade front, particularly through the reduction of non-tariff barriers to trade and improved transport infrastructure and logistical services, would yield significant economic benefits and help lock in the structural reforms that have been implemented so far. WTO membership and trade agreements that enhance economic development and cooperation between MENA countries and the rest of the world can also help anchor reform policies and boost competitiveness.

Improving the business environment in MENA is also likely to have a positive impact in terms of deepening integration in the region and encouraging further investment. Many countries have already made good progress on this front, and this has been one of the factors driving

intraregional investment flows over the last decade. The World Bank's *Doing Business 2010* report shows that reforms in MENA are keeping pace with those in central Europe and central Asia.³² Egypt, Jordan, and the UAE are among the most active in pursuing economic and business reforms with other countries in the region steadfastly implementing them. Saudi Arabia has significantly reduced the red tape involved in business procedures and jumped up to 13th place globally in 2010 for ease of doing business. The improvement in the business environment in these countries reflects reforms in a number of areas, including ease of starting a business and registering property, improved access to credit, greater investor protection, and faster cross-border trade.

Improved governance and accountability are critical for sustaining reforms. MENA countries, particularly resource-poor states such as Egypt,

Morocco, and Tunisia, have made a concerted effort to improve public service delivery and administration. In the wealthy GCC countries, too, governments have made remarkable efforts to improve the quality of public administration and introduce greater accountability: Bahrain and Kuwait are key examples of GCC countries that have moved toward greater public participation in the political process and freedom of the press. Persevering with political reforms and building capacity in public services and government can only improve the quality of reforms being implemented. Doing so will maximize their impact on the economy and MENA's competitiveness in the global context.

Notwithstanding the great strides that have been made in integrating the region's economies and

infrastructure, the full benefit of this integration can be achieved only by removing the remaining barriers to the movement of goods and people. Non-tariff barriers to trade—such as complicated customs procedures and red tape, the lack of logistical support, and visa requirements for non-GCC nationals—add to costs and make accessing GCC markets, education, and health facilities more difficult for businesses and individuals in the rest of the region. The development of integrated railway and road systems and efforts to create regional centers of excellence for health services (Jordan, Tunisia, and the UAE) and education (Saudi Arabia and Qatar) can be successful only if capital investment is complemented by legal and other procedural reforms, making it easier to do business, learn, and live in the MENA region.

Although there are still several areas where the MENA region's governments need to continue reforms to encourage further investment in their economies, there is no doubt that a significant shift has taken place that increases the momentum of change in these economies, particularly in the last five years. These structural improvements have had a number of positive consequences, including deeper regional integration, greater investment, and increased diversification of economies in the region. Provided the reform momentum is sustained, economies in the region will continue to attract the necessary capital to develop critical infrastructure, expand capacity, and build a solid foundation for sustainable growth.

Endnotes

- ¹ The GCC consists of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates.
- ² Arab Investment and Export Credit Guarantee Corporation (Dhaman) (<http://www.iaigc.net/>).
- ³ "Arabic Pressures," *The Economist*, July 23, 2009 (http://www.economist.com/specialreports/displaystory.cfm?story_id=14027674).
- ⁴ Booz & Company research.
- ⁵ Arab Investment and Export Credit Guarantee Corporation (Dhaman).
- ⁶ Ibid.
- ⁷ IMF Article IV report, April 2009
- ⁸ World Bank, "Middle East and North Africa Region 2008 Economic Developments and Prospects: Regional Integration for Global Competitiveness" (<http://web.worldbank.org/WBSITE/EXTERNAL/COUNTRIES/MENAEXT/0,,contentMDK:21822147~pagePK:146736~piPK:226340~theSitePK:256299,00.html>).
- ⁹ Arab Investment and Export Credit Guarantee Corporation (Dhaman).
- ¹⁰ Ibid.
- ¹¹ IMF Public Information Notice, 23 October 2007 (<http://www.imf.org/external/np/sec/pn/2007/pn07131.htm>).
- ¹² IMF Public Information Notice, 18 August 2009 (<http://www.imf.org/external/np/sec/pn/2009/pn09109.htm>).
- ¹³ SWF Institute (<http://www.swfinstitute.org/>).
- ¹⁴ Abraaj Capital (<http://www.abraaj.com/english/NewsDetail.aspx?nid=134>).
- ¹⁵ Arab Monetary Fund (www.amf.org); World Bank, "Middle East and North Africa Region 2008 Economic Developments and Prospects: Regional Integration for Global Competitiveness."
- ¹⁶ World Bank, "Middle East and North Africa Region 2008 Economic Developments and Prospects: Regional Integration for Global Competitiveness."
- ¹⁷ IMF, "Regional Economic Outlook: Middle East and Central Asia," May 2009 (<http://www.imf.org/external/pubs/ft/reo/2009/mcd/eng/mreo0509.htm>). Estimate refers to total workers' remittances in these countries, not just from the MENA region. This figure includes data for Pakistan.
- ¹⁸ Nadeem Ilahi and Riham Shendy, "Do the Gulf Oil-Producing Countries Influence Regional Growth? The Impact of Financial and Remittance Flows," IMF Working Paper 08/167, July 2008 (<http://www.imf.org/external/pubs/ft/wp/2008/wp08167.pdf>).
- ¹⁹ Dubai International Financial Centre, "Trade and the New Economic Geography of the Middle East," Economic Note No. 4, April 2009 ([http://www.difc.ae/press_centre/knowledge_centre/research_reports/files/Economic%20Note%204%20-%20FINAL%20\(April%202021\).pdf](http://www.difc.ae/press_centre/knowledge_centre/research_reports/files/Economic%20Note%204%20-%20FINAL%20(April%202021).pdf)).
- ²⁰ World Bank, "Middle East and North Africa Region 2008 Economic Developments and Prospects: Regional Integration for Global Competitiveness."
- ²¹ Ministry of Economy and Trade, Lebanon; calculation based on 2006 trade data.
- ²² World Tourism Organization (<http://www.unwto.org/index.php>).
- ²³ Tamara Walid, "Tourism within Arab states to grow in 2009: report," Reuters, July 21, 2009 (<http://www.reuters.com/article/lifestyleMolt/idUSTRE56K3CN20090721>); Travel and Tourism News Middle East, "Arab Tourism Sees Steady Growth Rate," vol. 27, no. 8, August 2009 (<http://www.ttnworldwide.com/arcarticles.aspx?id=1259&artid=9044&issueid=301>).
- ²⁴ World Bank, "Middle East and North Africa Region 2008 Economic Developments and Prospects: Regional Integration for Global Competitiveness."
- ²⁵ Ibid.
- ²⁶ Hani Hazaimah, "Jordan tops region as medical tourism hub," *The Jordan Times*, September 8, 2008 (<http://www.jordantimes.com/index.php?news=10589>).
- ²⁷ World Bank, "Middle East and North Africa Region 2008 Economic Developments and Prospects: Regional Integration for Global Competitiveness."
- ²⁸ Ibid.
- ²⁹ Ibid.
- ³⁰ Gabriel Chahine, "Trends in Middle Eastern Arabic Television Series Production: Opportunities for Broadcasters and Producers," Booz & Company white paper, 2008 (http://www.booz.com/media/file/TrendsInMiddleEasternArabicTelevision_FINAL2.pdf).
- ³¹ World Bank, "Middle East and North Africa Region 2008 Economic Developments and Prospects: Regional Integration for Global Competitiveness."
- ³² The World Bank, highlights from *Doing Business 2010* (<http://www.doingbusiness.org/>).

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