THE EURO-MEDITERRANEAN PARTNERSHIP AND INWARD FDI IN MAGHREB COUNTRIES

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SUMMARY

ABSTRACT

Inward FDI in developing Mediterranean countries is supposedly expected to soar as a result of the Euro-Mediterranean Partnership (EURO-MED) between the European Union and twelve Southern and Eastern Mediterranean countries that emerged from the 1995 Barcelona Conference. This is especially true in the case of the Maghreb countries, which have strong economic links to Europe. This investment boom, however, is far from certain, and the early evidence available so far does not support it. Indeed, the Barcelona framework contains no specific provision for investment. Nor is it clear how the Euro-Mediterranean Free-Trade Area (EMFTA) might affect incentives or reduce perceived risks in the region, since such risks are mainly political and structural in nature. In fact, the liberalization of Southern Mediterranean imports inherent in EMFTA will cause European investors to lose some of the incentives they already had to invest in the region (in order to side-step the high tariffs levied in some industries), especially since manufactured exports from these countries have long enjoyed free access to European markets. This could give raise to a “foreign investment diversion” effect.
Besides that, any effective increase in FDI would most likely concentrate in certain areas within specific countries in each South Mediterranean sub-region (so-called investment hubs), and might, therefore, be detrimental to others as a result of agglomeration economies.

This paper reviews the available evidence and literature on the determinants of FDI in the three central Maghreb countries: Algeria, Morocco and Tunisia. It then explores the possible future development of inward FDI in these countries within the framework of EURO-MED. Finally, the paper identifies possible future scenarios in which inward FDI in this sub-region might be positively affected, both through national economic policies and through the implementation of the Association Agreements with the European Union. As a conclusion, it argues that only the creation of a horizontal free-trade area between the three Maghreb countries -as opposed to the creation of parallel bilateral

free-trade agreements between each individual country and the EU, as has been done so far- could boost FDI levels within the region.

Introduction[*]

Sustaining a high rate of economic growth is the main development policy challenge for all countries of the Middle East and North Africa (MENA). This is needed to improve living standards, reduce poverty and generate employment opportunities for the growing number of entrants into the labor force. To face this challenge, MENA countries cannot rely on their own forces alone: they need to deepen integration into the world economy and to become attractive destinations for foreign direct investment (FDI) as a means of receiving the resources for development they cannot generate on their own.

However, in 1995 the World Bank stated that the MENA countries were the region in the world (but for Sub-Saharan Africa) which had made a lesser use of the globalization process as an engine of growth, and there is a wide consensus on the fact that the Southern and Eastern Mediterranean countries have missed the expansion of private investment flows to developing countries registered in the last decade, despite their proximity to Europe and despite the favourable access conditions to the European markets for their manufactures. This picture did not change after the signing of the Euro-Mediterranean Partnership in 1995, which did not produce the expected anticipation effect. The same is particularly true for Maghreb countries (Algeria, Morocco and Tunisia)[1], even if there is no doubt about the fact that at least the two

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[1] Although in geographical terms the Maghreb region includes

latter are among the countries in the region with a better record of policy performance in the late 1980s and the 1990s (and, together with Egypt and Turkey, they account for 95% of inward FDI into the whole MENA region, which in turn in 1995 accounted only for 4.3% of total world FDI into developing countries and 2% of EU outward world investment).

If we consider the economic developments and prospects in the MENA region, the last four years have been dominated by the lights and shadows cast by the Euro-Mediterranean Partnership (EUROMED) agreed between 12 Southern and Eastern Mediterranean countries and the 15 Member States of the European Union at the Barcelona Conference which took place in November 1995. Adopting a multi-dimensional approach (which included a political and security basket, a social, cultural and human affairs basket and an economic and financial basket), the Euro-Mediterranean Partnership will trigger a deep upheaval in MENA economies, notably through the creation of an Euro-Mediterranean Free Trade Area (EMFTA) after a relatively short transition period (of twelve years, i.e. until 2010). The implementation of the Euro-Mediterranean Partnership was to be agreed through bilateral Association Agreements between the EU and every Southern and Eastern Mediterranean country[2].

Revealingly, the Barcelona Declaration devoted only one sentence to foreign direct investment, acknowledging its role, together with internal savings, as a basis for economic development and calling for the creation of "an environment conducive to investment, in particular by

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Libya and Mauritania as well, in this paper I will refer to the Maghreb as including only the three central Maghreb countries - Algeria, Morocco and Tunisia.

[2] Besides the Interim Association Agreement with the Palestinian Authority, the only Association Agreements which have entered into force so far are those with Tunisia (March 1, 1998), Morocco (March 1, 2000) and Israel (June 1, 2000). The Association Agreement with Jordan has already been concluded and is pending ratification.

the progressive elimination of obstacles to such investment and increased production and exports".

In the *Ad Hoc* Ministerial Meeting held in Palermo in June 1998, the EU Presidency issued a declaration whose point 9 acknowledged that the creation of a shared prosperity area -the stated goal of the whole Euro-Mediterranean Partnership- entailed three main elements: the establishment of free trade, reforms promoting economic transition and promotion of private investment. But in spite of devoting point 12 to FDI, no specific co-operation endeavor was ever undertaken in this field.

Instead the co-operation framework established in the Barcelona Conference seems to rely exclusively in growth induced by trade development -and particularly by the foreseeable competitive shock caused in Southern and Eastern Mediterranean economies by the removal of trade barriers, typically amounting to between 20 and 30%, with much higher tariff peaks for certain sectors-[3] rather than a deliberate policy of FDI stimulation. Notwithstanding this choice[4], there are many hints that at least for some Southern and Eastern Mediterranean countries the main goal in entering into these Agreements -besides having access to the flow of financial cooperation resources made available by the EU in exchange for the implementation of the EMFTA- was to stimulate inward FDI rather than expanding commercial

[3] The way in which economic theory predicts that an increase in imports will bring about development is through the reduction of input prices for potentially competitive industries, increased competition for local firms and a transfer of technology leading to an increase in productivity. But this presupposes a massive reallocation of productive resources between different industries within the economy, which can only happen at a cost (so-called adjustment costs).

[4] Basically an European choice. The Euro-Mediterranean Partnership was a project negotiated and designed within the European Union which subsequently was submitted on a "take it or leave it" basis to the Southern and Eastern Mediterranean partners "invited" to the Barcelona Conference.

exchanges as such[5]. This seems a realistic assumption taking into account the unilateral nature of the trade liberalization agreed (the European markets were already largely open to manufactures from the Southern and Eastern Mediterranean and the agricultural sector in which many Southern and Eastern Mediterranean countries have a comparative advantage was excluded altogether from the liberalization).

1. FDI IN MAGHREB COUNTRIES

All three Maghreb countries are lower-middle income countries (between $1,250 per capita income for Morocco and $2,050 for Tunisia), are moderately indebted and have strong economic ties to the European Union countries (between 55% in Morocco and 70% in Tunisia of their foreign trade flows take place with EU countries, and all three countries have large communities of migrant workers in Europe) and a shared history of colonialism up to their independence in the late 1950s and early 1960s. Up to two thirds of the inward FDI they receive does typically come from EU investors.

1.1 The pattern of FDI in Maghreb countries

Maghreb countries took some time after their independence to accept the key role of foreign investment in their development. At the time, there was heavy reluctance to the preference of foreign investors for light industries, the equipment imports they usually entailed (and the subsequent technological dependency) and the repatriations of profits, all of them with a negative impact on the balance of payments[6].

[5] See Michalet (1997, p. 44).

[6] See, for instance, Souleyman (1978). I will not discuss here the causality link between FDI and economic growth in developing countries (for a critic of the "extravagant claims of the positive spillover" of FDI made in the literature, see Rodrik 1999, p. 37). So I will take for granted the high desirability of FDI, as it is currently perceived by the policy makers in developing countries themselves.

Only in the 1980s it became clear that FDI could be both a means to modernize the industrial sector of their economies and a necessity in macroeconomic terms to counterbalance the endemic current account deficit (due to a recurrent trade balance deficit and increasingly to the impact of external debt service). Although the investment codes in all three countries took some time to reflect this change in views[7], ever since the trend has been to ease conditions for foreign investors, e.g. allowing dividend repatriation, granting tax incentives and legal guarantees against any kind of expropriation, etc. In fact, in the last ten years all the Governments in the region have implemented strategies designed to attract FDI[8].

This resulted in a clear increase of inward FDI (see Table 1): in Morocco, FDI increased from an average $82,8 millions a year in 1985-90 to $445 million a year in 1991-94, to fall again in 1995-96 and surge in 1997 due to exceptional circumstances linked to the privatization of state companies and the concession of a new telephone license. In Tunisia, it quadrupled between 1985-1990 and 1991-94, reaching a level consistently over $400 million to fall again to an average of $272 million in 1995-97. This means Maghreb economies did benefit from the surge of private finance flows registered in the early years of the 1990s in the first place, but failed to keep pace with the development of world FDI into developing countries (it more than doubled from 1989 to

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[7] In Morocco, the 1973 Law on *marocanisation* of companies, for instance, precluded foreign interests to own more than 50% of any company's equity, a restriction abolished only with the new Investment Charter adopted in October 1995. In Algeria, foreign investments were only assimilated to national ones in the Investment Code 1995, save for some strategic sectors. The Tunisian Investment Code dates from 1994 and excluded distribution, mining, energy and finance, but granted very generous tax and tariffs exemptions in other sectors, notably for outward oriented FDI (more of 80% of production exported).

[8] In all three countries investment promotion agencies were created: for example, the *Agence de Promotion, de Soutien et de Suivi des Investissements* in Algeria.

1992 -from 22,4 to 45,37 billion dollars- and again from 1992 to 1995 - to 103,6 billion dollars-, reaching 160,6 billion dollar en 1997). Thus, notwithstanding the alleged announcement effect of the EURO-MED Partnership inward FDI stagnated in Maghreb countries after 1995 and therefore the share of the region in world private capital flows to developing countries has declined ever since.

Table 1. Foreign Direct Investment into Maghreb countries. 1989-1997 (millions $)

¡Error! Marcador no definido.	1989	1990	1991	1992	1993	1994	1995	1996	1997
Algeria	12.1	0	12	12	15	18	5	4	7
Morocco	167.1	165	317	422	491	551	290	311	1,200
Tunisia	79	76	126	526	562	432	264	238	316
Total Maghreb	258.2	241	455	960	1,068	1,001	559	553	1,523

Source: World Development Indicators (1999)[9]

According to available data, in 1998 ($400 million for Morocco) and 1999 there was a sharp decline of foreign direct investment well below the exceptional inflows of 1997.

The first thing to explain in this data are the almost insignificant levels of inward FDI in Algeria. On the one hand, this is partly due to the fact that this country was the last in the region to lift heavy restrictions on FDI. Also, one of the major internationally financed projects undertaken

[9] The data are calculated in terms of net inflows in current dollars. The definition of FDI used is net inflows of investment to acquire a lasting management interest (10% or more) of voting stock in an enterprise operating in an economy other than that of the investor. It is the sum of equity capital, reinvestment of earnings, other long-term capital, and short-term capital as shown in the balance of payments.

in the present decade in Algeria (the Europe-Maghreb gas pipeline) was built on a credit granted by the European Investment Bank amounting to 638 million ECU. On the other hand, the US Department of State claims that American companies have invested around 3 billion dollars in the oil and gas sector in Algeria in the last few years, British Petroleum has allegedly invested 3.5 billion dollars in the same sector[10] and the Bank of Algeria itself reports FDI to have been 500 million dollars in 1998, 270 million dollars in 1997 and 260 million dollars in 1996. Since all relevant international statistics (World Bank Development Indicators, UNCTAD's World Investment Report, Eurostat's Euro-Mediterranean Statistics) largely coincide in reporting irrelevant levels of FDI in Algeria there must be some statistical distortion explaining this (maybe this is due to the fact that the investments by foreign oil companies confer them exploitation rights granted by Sonatrach, the Algerian State monopoly company in the sector, but no ownership interest; but this would not explain why there is no hint in FDI statistics of the establishment of four foreign banks: Citybank, Arab Banking Corporation and two French banks).

Throughout this period, the share of Morocco in total investment in Maghreb countries has been consistently higher than 50%. This is due both to the more diversified nature of its economy and the relatively big size of its market (28 million inhabitants; Tunisia has a more modern economy, but only 9,8 million inhabitants, whereas Algeria has 29 million inhabitants, but its economy turns around the oil and gas sector and its political situation is much more uncertain).

In any case, the volume of FDI is relatively small in all Maghreb countries: in Algeria it has never exceeded 0,1% of GNP or Gross Domestic Investment, and in Tunisia it reached a maximum of 3,8% of GNP in 1993 (13,1% of Gross Domestic Investment) to fall again and stabilize around 1,5% of GNP (4,2% of GDI). In Morocco, letting aside

[10] The Algerian oil and gas sector was opened up to foreign investment in 1991, maintaining the monopoly of the state company Sonatrach. Since then, 24 foreign companies have signed 45 contracts: 23 exploitation contracts for 5 to 25 years, 17 exploration contracts and 5 development contracts.

the exceptional year of 1997 (3,6% of GNP and 17,4% of GDI), it has never exceeded 1,8% of GNP (see Table 2). Still worse, FDI levels are quite erratic, reflecting the impact of big investment projects in specific years, rather than a steady flow of foreign resources, and FDI continues to flow overwhelmingly into traditional sectors: mainly energy and primary sector, textile and clothing and to a lesser extent tourism. Overall, the behavior of FDI seems to respond largely to the "one time attraction of privatization programs rather than an on-going commitment" to those economies.[11]

Table 2. Foreign Direct Investment into Maghreb countries as a percentage of Gross Domestic Product (GDP) and Gross Domestic Investment (GDI). 1989-1997

¡Error! Marcador no definido.		1989	1990	1991	1992	1993	1994	1995	1996	1997	Average 1989-97
Algeria	GDP	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	GDI	0.1	0.0	0.1	0.1	0.1	0.1	0.0	0.0	0.1	0.1
Morocco	GDP	0.7	0.6	1.1	1.5	1.8	1.8	0.9	0.8	3.6	1.4
	GDI	3.1	2.5	5.0	6.4	8.2	8.5	4.2	4.3	17.4	6.6
Tunisia	GDP	0.8	0.6	1.0	3.4	3.8	2.8	1.5	1.2	1.7	1.9
	GDI	3.3	2.3	3.7	11.6	13.1	11.3	5.9	4.8	6.3	6.9

Source: World Development Indicators (1999)

On the other hand, all three countries need a flow of external resources to finance their development, since their internal savings rate is too low to finance the level of investments they require, the government deficit (the level of public expenditure should increase in the coming years in order to cope with the so-called "social debt", the negative social impact of EMFTA and the population growth) and the recurrent current account deficit (all three countries are heavily dependent on food imports, although all three receive as well sizeable transfers of workers

[11] Joffe (1999).

remittances from their nationals abroad). The high level of external debt (in Algeria, in 1997 it amounted to 65% of GDP, in Morocco 53% and in Tunisia 58%) precludes them from turning again to the international capital markets to bridge their finance gap, and the debt service puts a further strain in their current account (it amounts to around 40% of exports in Algeria, 25% of exports in Morocco and 17% in Tunisia).

Foreign investment can act also as a catalizer of modernization of the economy (the "mise-à-niveau" is the buzzword for their economic reform programs), a key agent of structural transformations (a pre-condition for development) and a fundamental source of technology transfer. Thus, it is a crucial link to achieve the massive reallocation of productive resources the EMFTA is going to make necessary: in the case of Tunisia, for example, it is reckoned that 60% of its industrial production is threatened by the tariff suppression, and only half of it corresponds to competitive industries, what means that around a third of the industrial activities will be to be reallocated to competitive industries, provided the latter remain competitive. In Tunisia and Morocco, in particular, competitive industries are to be found basically in the textiles and clothing sector, and their competitive edge depends to a large extent on preferential access to European markets, but this preferences will disappear as a consequence of the dismantling of the Multi-Fiber Arrangement agreed in the framework of the Uruguay Round. So there will be an acute need of modernization and productivity enhancement even in the currently competitive industries, as well as the creation of competitive advantage in new sectors. Once again FDI will be vital in this process.

Admittedly, taking into account the efforts made by these countries to implement structural reforms in the last years, their low level of relative development and their geo-strategic importance, particularly for European countries, the aforementioned figures show that FDI is lagging behind (they consistently receive a lower volume of FDI than other regions with similar population and economic potential[12]), and the

[12] For econometric evidence on this issue, see Petri (1997), where a regression model is estimated using determinants like

EUROMED does not seem to have made a difference so far. The reasons and the prospects for the future are discussed in the following sections.

1.2 Determinants of FDI in Maghreb countries

According to the literature the three main economic motivations for inward FDI are resource-seeking, market-seeking (size and growth of the market) and efficiency-seeking. As for aggregate FDI inflows, macroeconomic factors, business environment and political risk considerations appear to play a dominant role over microeconomic considerations like the return of capital[13].

In order to capture in a simple conceptual framework the overall impact of changes in this determinants over time, we have adapted the organizational template first used by Blomström and Kokko (1997, p. 11) to study the impact on FDI of regional integration agreements. The attribute "locational advantages" is redefined as summarizing all factors directly affecting the profitability of investment projects: natural resources availability, market size and growth, availability and cost of factors of production and geographical location with respect to consumer markets, as well as the performance of alternative investment locations. Under "environmental change" we include all factors affecting the (perceived) risk incurred by FDI and the context in which it operates, i.e., business environment, political stability, macroeconomic policy and performance, public policies, etc. The resulting FDI-attractiveness change matrix can be represented as in Figure 1.

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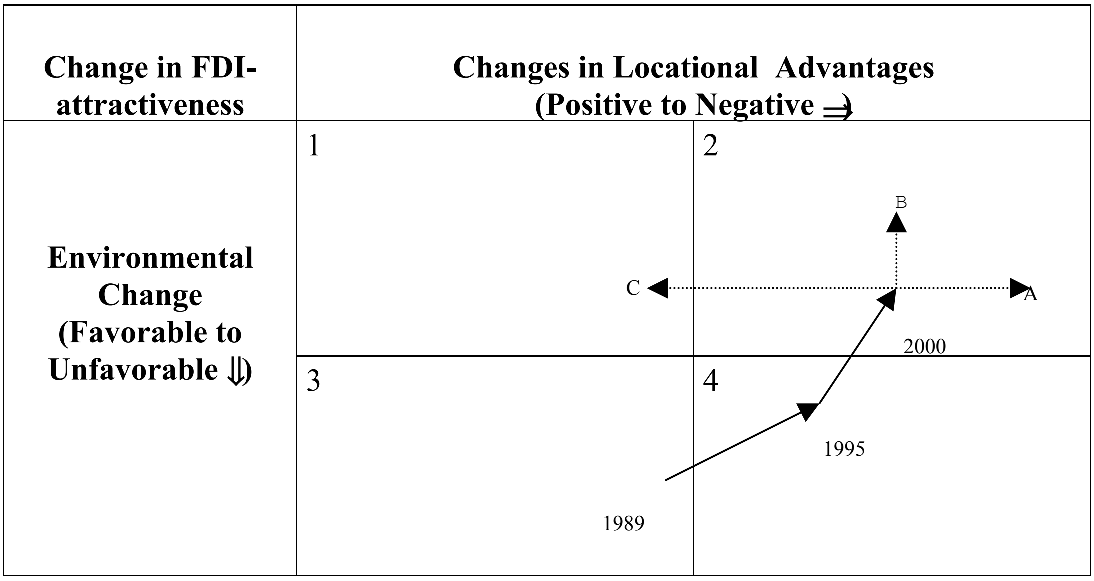
economic size, level of development, human capital endowment, resources endowment and macroeconomic stability, as well as a measure of political risk.

[13] See UNCTAD (1998, pp. 106-108). See also the review of the literature of determinants of FDI in Deardorff et al. (1996), Section III.

Figure 1. FDI-attractiveness change matrix



Although this analytical framework cannot explain FDI *levels* in a particular country, it does capture the main drivers of FDI-attractiveness, so any change in the relative position in Figure 1 would be expected to correlate with corresponding changes in FDI flows. So any movement upwards (an improvement in FDI environment) and leftwards (an increase in locational advantages) in Figure 1 will be expected to have a positive incidence on FDI flows, and vice versa. Accordingly, the framework can be used to understand changes in FDI-attractiveness of specific industries, areas or entire countries over time.

Taking the Maghreb region as a whole, during the 1970s and the 1980s it benefited from its relative geographical proximity to major European markets and its cheap labor supply, as well as the tariff-free access to European markets for manufactures granted under the Cooperation Agreements in force since 1976; on the other hand, the business environment for FDI could hardly be worse, with strong State intervention, lack of any legal guarantee, high levels of inflation and exchange risk and even an outright political bias against FDI .

This situation deteriorated in the early 1990s as the Eastern European countries opened up their economies and entered a transition process which should bring some of them into the European Union in the medium term: the highly educated, cheap labor force (the average hourly wage of a Polish skilled worker was in 1993 around half that of a Moroccan's and a third of a Tunisian's, according to calculations made by the World Bank) and the extensive industrial tissue in those countries, as well as the prospects for full market integration with Europe became a decisive attraction factor for European FDI, detracting from the FDI-attractiveness of Southern Mediterranean countries. This is reflected in our framework by a shift rightwards, from cells 3 to cell 4, as relative locational advantages of Maghreb countries deteriorated.

Simultaneously, in the early 1990s all three countries in the region undertook far-reaching structural adjustment and liberalization programs which led to a dramatic improvement of their macroeconomic condition and business environment (move from cell 4 into cell 2). Since this improvement seemed to prevail above the aforementioned deterioration of locational advantages (and since world FDI flows experienced a boom), they managed to attract increased flows of FDI (see again Table 1). This can be explained by the first wave of investments by foreign companies -to a large extent multinational companies with a global marketing presence looking to position themselves in each and every market, however small or adverse it is- following any opening of the market in formerly closed countries, regardless of locational advantages as such.

As discussed below (section 2.3) the signing of the Euro-Mediterranean Partnership in 1995 reinforced the commitment of Maghreb countries to sound macroeconomic policies and economic reforms and further improved the environment for FDI, but at the same time it has contributed to the deterioration of the forward-looking locational advantages as a consequence of the elimination of trade protection vis-a-vis the European manufactures provided for (see Section 2.3). Once the first wave of FDI exhausted, it was this worsening of locational advantages which prevailed, explaining the stagnation or decline of FDI flows in the subsequent period (1995-1997).

There is another factor which probably contributed to this poor FDI performance: the surge of radical islamism (particularly in Algeria, but not only), a phenomenon which might have offset all the gains in environment conditions for foreign investment derived from macroeconomic streamlining and apt to scare many foreign investors altogether (so the Maghreb countries could actually find themselves deadlocked in cell 4). A, B and C depict possible future scenarios for FDI attractiveness in Maghreb countries and will we discussed later in this paper.

At a country level, the pursuit of natural resources plays the key role in inward FDI in Algeria, where the bulk of FDI has gone into the oil and gas sectors. The relative isolation of the oil-producing areas have permitted this investments to go on in spite of the adverse security conditions in the country since 1992, but the uncertainty about the political and social stability in the future and the deterioration of the Algerian industrial tissue leaves little room for optimism about the development of FDI in other sectors of the economy (there may be some exceptions linked to the privatization of large state companies, the concession of telecommunications and utilities licenses and public works).

The relatively small size of the Tunisian market (Gross National Product of 19,2 billion dollars) lets Morocco as the only country in the area where there has been significant "market-seeking" foreign direct investments (apart from the “positioning investments” by multinational companies referred to above). However, the narrowness of the Moroccan market itself (GNP of 34,8 billion dollars) makes it necessary to have access to other regional markets as well in order to achieve efficient production scales even for relatively simple products like house electrical appliances (the combined GNP of the three Maghreb countries -100, 5 billion dollars for 66 million people- is smaller than that of Portugal -106,4 billion dollars with only 10 millions inhabitants, and the second poorest country in the EU- or around two thirds that of Poland).

And this is something which has not happened so far: the failure to implement the Arab Maghreb Union has deterred many investors from opening plants in the region to serve this whole regional market and is a permanent source of frustration for those who have done it[14].

As for the efficiency-seeking FDI, it is the phenomenon which is reshaping the industrial map across the world, but a region which has only a large supply of cheap unskilled labor to offer is deemed to remain largely ignored. In the Maghreb, it has involved mainly German, French, Belgian and Spanish firms investing in low value added processes in Tunisia and Morocco, particularly in the textiles and clothing industry and footwear (the so-called "delocalisation"), very often in export-processing zones specifically created for this purpose. But the links of these off-shore export processing zones to the domestic economy are very weak, they do not increase competition for local firms in the local markets, their contribution to tax revenue of the Government is low (since they are mostly exempt from taxes and import duties) and they create little value-added.

Ultimately, the Maghreb countries have lacked so far of production-oriented foreign investors which could help those countries to integrate into the international production chains, as well as of investors from countries with factors proportions relatively close to those of the region itself and therefore in a better situation to transfer the appropriate technologies.[15]

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[14] See section 3.1.

[15] Most of the academic and policy discussion on determinants and flows of FDI is based on figures and case-studies referring to multinational companies, since those are the data collected and researched by international agencies, particularly UNCTAD. However, the biggest positive spillovers from FDI in most developing countries, and notably in the Maghreb, are to be expected from medium-sized companies from other larger developing countries (South Korean companies have made some major investments in this region, like the Daewoo plant in Morocco) or from emergent developed countries (i.e., Spain, Portugal or Italy).

On the other hand, the specific investment decisions of foreign companies are affected mainly by economic stability (including an stable, transparent and reliable legal and regulatory framework and an effective and independent judiciary to guarantee its respect) and market size of the host country[16]. This may explain why FDI has not realized the full potential offered in Maghreb countries by the market access these countries enjoy to European markets since the mid-1970s[17].

It is true that the three central Maghreb economies have been subject to stringent structural adjustment programs for the biggest part of the 1990s. However, the positive impact this should have had on FDI has been offset by persistence of red tape, bureaucratic inefficiency and outright corruption in the public sector and the judiciary[18], on the one hand, and social and political instability, on the other[19]. The increased competition for a limited volume of available FDI resources exerted by Eastern Europe countries, with a more qualified workforce and a closer geo-strategic position to the central European countries (including the prospect to join the EU themselves one day) has also played a part.

Finally the high external indebtedness of all three countries has been another deterrent for foreign investors, even if in the last three years - following a decision by the Paris Club to lift the swap ceiling from 20 to 30%- Morocco has benefited from debt-for-investments swap schemes (at a discount) granted by France (almost $100 million in sovereign debt in November 1999, bringing the total to $485 million), Spain ($40

[16] See the results of the survey on FDI attraction factors conducted by the Foreign Investment Advisory Service (FIAS) reported in Michalet (1997, pp. 46-47).

[17] The first wave of Trade and Co-operation Agreements between Maghreb countries and the EEC were signed in 1976.

[18] In the case of Morocco, some problems, like the customs clearance procedures and the commercial jurisdiction have only began to be fixed in the last two years.

[19] For a discussion of the Algerian case, see Martín (1998).

million) and Italy ($100 million)[20].

More recently, a new kind of market-access FDI is emerging in the region induced by deregulation of major non-tradable service industries (like telecommunications and some utilities). This has been the main determinant of FDI in the last couple of years both in Morocco and Tunisia.

2. CHANGES IN CONDITIONS FOR FDI AS A CONSEQUENCE OF THE EURO-MEDITERRANEAN PARTNERSHIP

2.1 Overall economic impact of the Euro-Mediterranean Free Trade Area

The relatively few quantitative studies on the effects of EMFTA on Maghreb economies[21] arrive to similar conclusions. According to them, the impact on welfare would fluctuate, depending on assumptions, between 2.2 and -0.2% of GNP in Tapinos et al. (1994), 2.3 and 1.2% in

[20] These programs usually entail some concessions for the would-be investors. In the case of France, for instance, this amounts to a subsidy of around 10% for French investors. For the Spanish swap scheme, see Montalvo (1998, pp. 109-115).

[21] See Tapinos, Cogneau, Lacroix and De Rugy (1994), Rutheford, Rutström and Tarr (1995), Kébabjian (1995), Deardorff, Brown and Stern (1996), and Tovias (1999). All five refer to the Morocco and/or the Tunisia economies (the latter includes Algeria as well).

Rutheford et al. (1995), around 0.7% of GNP in Kébabjian (1995), between –0.2% and 3.3% in Deardorff et al (1996) and between –0,2% and –1,5% of GNP in Tovias (1999). However, these studies have only a limited value, since they are not able to capture the dynamic effects of integration and they are based in very questionable assumptions (for instance, on the values of sectoral import and export elasticities) due to the lack of reliable data[22].

In the short term, it is widely agreed that the EMFTA will induce a deterioration of the trade balance in all three countries and a net loss of jobs (particularly as the implementation of EUROMED goes hand in hand with deeper structural adjustment and privatization programs, reducing the size of the public sector and so contributing to unemployment).

Both issues remit to FDI as a possible solution. In any case, it is interesting to note that in some of the studies the slightly positive impact of EMFTA on growth improves dramatically when a considerable increase in FDI is assumed[23]. In fact, the increased flow of FDI is one of the elements mentioned in most studies as an expected dynamic benefit of the EMFTA for the Maghreb economies. This expectations are explained calling upon the experience of Spain and Portugal's accession to the EU in the late 1980s and Mexico integration into NAFTA in the second half of the 1990s[24]. But they oversee the essential differences between the "deep" federalist model of integration of the EU (with common policies and institutions, legal harmonization, a real single

[22] The evaluation of those studies and the quantitative methods for determining the impact of EMFTA in Maghreb countries will be dealt in a separate paper.

[23] For instance, in Kébabjian (1995) a doubling of FDI translates into a positive impact on GDP of 7%. However, Deardorff et al. (1996, p. 30), after admitting the low forecasting value of their estimation methods, come to the opposite conclusion: even a doubling of FDI inflow to Tunisia would be unlikely to make any significant difference for Tunisia welfare.

[24] For a discussion of those cases, see Blomström and Kokko (1997, Section 3).

market, structural funds at a much bigger scale that the co-operation funds provided for in the framework of EUROMED and up to an economic and monetary union) and the “free-tradist” model imposed by the EU countries upon their Southern and Eastern Mediterranean partners in the first case, and the fact that NAFTA did actually improve dramatically the locational advantages of Mexico, since it opened up a huge nearby market closed so far, what is not the case in EMFTA.

Indeed, the relevance of this expectations is not warranted by the particular features of the EMFTA, which actually does not open any truly new economic opportunities for Maghreb countries in comparison with the Trade and Cooperation Agreements in force since 1976, but impose on them a deep and brisk economic transition loaded with uncertainties (a very investment-discouraging word, by the way). It does not give access to new markets nor introduce new fiscal or financial incentives. As formerly discussed (Section 1.2), at the most the signature of the EUROMED Association Agreements by Maghreb countries confirms their permanent commitment to the adjustment and liberalization policies they have been pursuing since the mid-1980s, "locking in" certain structural market reforms that should give foreign investors a higher degree of security. In this way, it reinforces the credibility of their economic policies for the outer world, reducing the country risk premium for foreign investors (but not necessarily enhancing the profitability of investments in itself: see Section 2.3)

2.2 Impact on the need for FDI

For developing economies in general, prosperity in the future will depend at a large extent on their ability to mobilize foreign savings: in the Mediterranean context, this means establishing mechanisms for transferring the savings from the aged populations in the North to emergent economies in the South (and not only transferring workers from the young populations in the South to the welfare economies in the North). But so far the Southern and Eastern Mediterranean countries are still facing their external financial needs mainly through official sources of long and medium-term finance and migrant workers remittances. So one of the major challenges for the economic transition process under way in those countries consists in attracting an steady flow of private foreign investments. In fact, many authors make the increase in FDI flows one of the keystones for the EMFTA to succeed[25]. Thus according to Kébabjian (1995) a precondition for the economic success of the liberalization strategy is "a true big bang in the behavior of foreign investors" leading to a massive injection of financial resources in the economy, while Ghesquiere (1998, p. 22) takes for granted that "ultimately, the success of the [Association] agreements hinges on their ability to generate a critical mass of foreign investment in labor intensive export-oriented sectors".

Indeed whereas the adjustment costs induced by the free trade area are certain, the benefits are heavily conditional on the behavior of FDI:

- in macroeconomic terms, FDI will be vital to offset the expected worsening of the trade balance in the short term as a consequence of liberalization and to widen the tax basis to compensate for customs revenue losses for the Government;

- in political terms, FDI has a very important role to play as well in order to make the EUROMED politically feasible, as a means to stimulate job-creation and the modernization of the Southern and Eastern Mediterranean economies.

2.3 Impact on the determinants of FDI

The opening up of Maghreb manufactures markets within a relatively short period (twelve years at the most, to conform to the rules of the World Trade Organization) will mean the end of "tariff-jumping" FDI looking for access to local markets (however small it was so far). In fact, despite the significant improvements in the regulatory and institutional

[25] Mahjoub and Zafrane (1999, p. 4).

environment experienced in the last years the opening up of trade with the EU may result in greater competition from imports from European countries as an alternative to potential new investments. Actually, as a consequence of the reduction of prices in most sectors after implementation of EMFTA the nominal return to capital might (as it actually does in some estimations) fall over the short run, theoretically leading (if market signals are to be followed and the perceived political risk does not change significantly) to an outflow, not an inflow of FDI. Indeed, according to the standard international trade theory, and particularly to the Stolper-Samuelson theorem, the removal of trade barriers increases the real return of a country's relatively abundant factor -i.e., labor in the case of Maghreb- and reduces the real return of the scarce factor -i.e. capital). This is the "EMFTA only" scenario depicted in Figure 1 as A, where the locational advantages of Maghreb countries deteriorate further as a consequence of implementation of the Free Trade Area in manufactures (giving raise to a "foreign investment diversion" effect).

At the same time, at least over the short run the implementation of EMFTA is expected to bring about a serious deterioration of the trade balance, a macroeconomic imbalance that might put pressure on the exchange rate policy and usually scares foreign investors (this would pull the FDI-attractiveness downwards in Figure 1, due to the deterioration of the investment environment). In either case, the macroeconomic and political sustainability of EUROMED may suffer and the liberalization process might be frozen by political pressure at some stage. This would increase the perceived risk of investing into the Maghreb, consolidating a pattern which might explain the lackluster FDI performance of these countries in recent years: however impressive the real improvements in macroeconomic policy and business environment, any positive impact on FDI has been overshadowed by the perceived political risk due to social and cultural developments.

3. PROACTIVE SCENARIOS FOR INCREASING INWARD FDI FLOWS IN THE MAGHREB

In this section, two alternative scenarios within our FDI-attractiveness framework will be analyzed, where national authorities take proactive measures to render their countries more attractive through horizontal economic integration between Maghreb countries (increasing in this way their locational advantages, represented in Figure 1 by scenario C) and where complementary measures are taken at national level and in the context of he Euro-Mediterranean Partnership in order to render those countries more attractive for foreign investment (scenario B, reflecting an improvement of environment conditions). Either one of those scenarios or a combination of both would lead to a "foreign investment creation" effect of EMFTA.

In Section 3.3 a little studied by-effect of increased FDI into the region (provided it does come forward) is raised, namely the trend of foreign investors to concentrate in some particular areas of a country or (more probably in the Maghreb) of a whole region, what could be detrimental to other areas. Finally, Section 3.4 reviews the possible specialization of every Maghreb country in different FDI tiers according to their main economic features.

3.1 Sub-regional integration as a necessary complement of the Euro-Mediterranean Partnership

As it has been reiterated in the literature, as it stands the EMFTA is poised to give raise to a "hub and spokes" system[26] in the economic relations of the Southern and Eastern Mediterranean countries with the EU which could have very negative effects for FDI. This is defined by the fact that companies have incentives to locate in the "hub" (in this case, EU countries, where they enjoy unrestricted free movement of goods, services, capitals and workers without any significant political

[26] Kowalczyk and Wonnacott (1992) were the first to develop an economic model of the dynamics of a "hub and spokes" system for the North American Free Trade Area.

risk), as this gives them access to a series of "spokes" (i.e., the different countries in the Southern and Eastern Mediterranean signing one-to-one Association Agreements with the EU as a whole, but economically isolated from each other, as well as all other countries with which the EU has negotiated free trade areas). All other things equal this creates incentives against inward foreign direct investment by EU-based firms (as far as the protection rates on imports from the EU remain lower that the protection rates on imports from other Southern and Eastern Mediterranean countries) and third countries companies alike (which will be forced to establish within the FTA in order to avoid the trade diversion induced by the discriminatory tariff liberalization in Southern and Eastern Mediterranean countries, but will prefer to do it in EU countries to have access simultaneously to all Southern and Eastern Mediterranean countries).

So one vital complementary measure to the Euro-Mediterranean Agreements between Maghreb countries and the EU is the actual implementation of the so-called horizontal (or South-South) integration, be it through the reactivation of the Arab Maghreb Union or through other *ad hoc* measures. This is a pre-condition for taking full advantage of the opportunities offered by the free access of manufactured imports from the region to the EU and for developing intra-industry trade within the region[27], particularly since the EU has eased the way by granting the cumulation for rules of origin purposes across all three countries in the region[28]. This would allow to restore some of the locational advantages of Maghreb countries for FDI in terms of market size and move towards the C scenario in Figure 1.

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[27] Given the competitive rather than complementary nature of their industrial patterns, it is in intra-industry trade where the major scope for expanding intra-regional trade lies.

[28] In the Association Agreements with Tunisia and Morocco, it allows cumulation for products produced in all three central Maghreb countries and the EU itself, and in all other EUROMED countries with which they may sign free trade agreements, but it stops short from granting cumulation outright for all other Medite-rranean countries.

This is particularly true of more technology intensive industries, which tend to be those where the economies of scale and the minimum efficient scale are bigger and can hardly consider any plant investment into the region at all if its already small market remains fragmented. Arguably those industries are also the ones where positive spillovers from FDI are the biggest.

However, so far horizontal integration has met insurmountable obstacles (mainly political in nature) and has reached few concrete achievements[29]. This failure is best reflected by the low level of intra-regional trade in the overall trade flows of the countries belonging to the Maghreb region: less than 3% (of course, without taking into account the smuggling flows across the borders, which might be relevant in some sectors), a figure that has stagnated over the last 30 years. Although a trade intensity analysis may suggest that the intra-regional trade is close to its theoretical potential (i.e., to the relative weight of every country in international trade) and some authors have interpreted this as a lack of room for a significant increase in intra-Maghreb trade[30], the current levels are by no means consistent with an important increase in FDI flows into the region, which, as indicated, is a crucial success factor for the whole EMFTA project. Besides that, the use of historical data is not very helpful for assessing the prospects and policy challenges associated with a project that is going to shake the whole economic structure of the participant countries, as is the case of the EMFTA for the Southern and Eastern Mediterranean countries.

But in order to give impetus to the sub-regional economic dynamics needed to take advantage of the new environment created by EMFTA, the current obstacles to intra-regional trade should be eliminated. Besides political and trade policy obstacles (which prevent a "normalization" of trade), a relevant restraint to the development of

[29] See Martín (1999, pp. 34-36).

[30] See Escribano and Jordán (1999, pp. 108-111).

intra-regional trade are the logistical shortcomings (notably transportation and communications facilities), a field in which the MEDA funds could play a very important role.

3.2 A Partnership for investment

A second possible line of action would be to turn the EUROMED into a true Partnership for investment, taking concrete measures to foster FDI in the Southern and Eastern Mediterranean countries. So far this has not been the case. Although the Euro-Mediterranean Agreements refer to the right of establishment (i.e., freedom to engage in FDI) of companies in general terms there is no specific commitment or deadline in this respect (actually this is a matter to be decided by the bilateral Association Councils yet to be established). Along the same line, the EUROMED Agreements do not provide for national treatment of foreign investors either[31]. This means that no further improvement of the investment environment is to be expected from the EUROMED as such over and above the "locking-in" of economic reforms already referred to (whose effects have largely already been exhausted).

To make up for this shortcoming a new approach to the question of investment promotion in the context of EUROMED is required. Something is already being done in the context of MEDA programs (see, for instance, the London Conference on Investment in March 1997, the London Conference in Capital Markets in March 1998 and the Lisbon Euro-Mediterranean Conference on Investment in March 2000) , but on a rather *ad hoc* basis, when what is needed are structural measures which render FDI in Maghreb countries overall more attractive.

[31] As Hoekman and Djankov (1995, pp. 20-21) point out, both are central features of the European Agreements between the EU and Central and Eastern European Countries, what makes a big difference. NAFTA also provided for a "comprehensive system of rules and obligations dealing with foreign investment" (Lahouel 1999, p. 17).

Possible concrete actions which would certainly help to promote Maghreb countries as an attractive FDI destination and facilitate an effective mobilization of FDI would be:

- trust: to build on the political and security basket of EUROMED as a means to foster political stability, increase transparency and strengthen independence of the judiciary in Southern and Easter Mediterranean countries;

- finance: the establishment of an Euro-Mediterranean Development Bank (along the lines of the European Bank for Reconstruction and Development) which would finance venture capital projects, act as information clearing house and endorse investors endeavors (this was already considered when the EUROMED was being negotiated);

- information and facilitation: the organization of an annual Maghreb-specific investment conference under the auspices of the EU and optimization of the investment information databases already in place;

- guarantee: the creation of a Euro-Maghreb Investment Guarantee Agency covering non-commercial risks for European investors in the region [32];

- planning: to draw up a checklist of hurdles to FDI and actions to be taken by Maghreb partner countries in this field (a kind of "road map" similar to the one designed for EU accession candidate countries) with deadlines and periodic reviews.

No doubt, these measures would bring about an improvement of the FDI environment in Maghreb countries which would move FDI-

[32] See Sabkani (1998, pp. 22) for details on a proposed Euro-Arab Investment Guarantee Agency and other measures to create an Euro-Mediterranean financial space.

attractiveness towards scenario B in Figure 1.

3.3 The role of agglomeration economies

Assuming inward FDI into the Maghreb actually increases (a big if), a further important issue arises as for the geographical distribution of this FDI across the region. Particularly if the creation of a FTA between every Maghreb country and the EU is complemented by a sub-regional integration agreement (be it AMU or any other scheme), the dynamics of integration might lead to a concentration of economic activities (and particularly FDI) in clusters around "investments hubs" where foreign companies could benefit from positive externalities. This will cause a spatial polarization of production factors and income, and therefore an uneven distribution across the region of benefits and costs of the EMFTA.

This is due to the operation of so-called “agglomeration economies”. These may prevent real convergence of different regions in an integrated economy through a self-reinforcing process of accumulation of wealth in human and technological capital poles which already enjoy the highest stocks of capital and where investors benefit from externalities or spillovers from existing capacities (in developing countries other sources of increased productivity may contribute to the agglomeration economies, like the substantial reduction of services and transaction costs in areas where there is already a minimum industrial tissue and infrastructures in place). Agglomeration economies have been subject to extensive analysis in the case of the European single market and the United States under the light of the new theories of international trade under imperfect competition and endogenous growth models[33], but have been neglected so far in the economic analysis of EMFTA and possible horizontal economic integration projects in the Maghreb.

[33] See Krugman (1991). The debate seems still open as whether the trade adjustments prompted by economic integration processes as such foster real convergence between member regions or they contribute to exacerbate economic differences between regions.

The localization of this investment hubs is determined by geographical proximity to markets (i.e., transportation costs), availability of human capital, physical and business support infrastructure and, last but not least, regulation and legal security (contract enforcement arrangements and property rights). Given the market size, relative development and growth prospects of the three Maghreb countries considered, it is highly unlikely that the region can accommodate more than one of these investment hubs.

Taking into account a) the market size and b) the inherent fear of investors to the reversibility of any integration process between the three countries (combined, this two considerations all but exclude Tunisia as possible regional investment hub, in spite of it being the most modern economy in the region), c) the advancement of negotiations to conclude Association Agreements with the EU (the Tunisian one is in force since two years ago, the Moroccan one has just entered into force and the Algerian one is still stacked in a difficult negotiation process), d) the progress in regulatory reform and structural adjustment (Tunisia and Morocco are well ahead of Algeria in this respect) and e) the political, social and economic prospects (only Tunisia seems to offer a future without major uncertainties, but Morocco is improving fast its investment environment), the chances are for Morocco to become the country where the eventual investment hub for the region will be located.

In particular, the Atlantic economic axis Kenitra-Rabat-Casablanca[34], with two major ports (Kenitra and Mohammedia), an important financial center (Casablanca), a certain industrial tissue already in place (Casablanca alone concentrates 40% of Moroccan manufacturing plants) and the implementation of the project to build a new coastal Mediterranean highway across the Northern provinces (from Tangiers to Uxda, on the Algerian border) connecting it to the other two countries in the region with the contribution of European funds (45% of the budget), seems to rank first among the possible candidates. Of course this

[34] See Martín (2000, p. 96).

preliminary assessment is no substitute for detailed research on the possible patterns of FDI spatial distribution within an eventual Arab Maghreb Union free trade area.

3.4 Competition for foreign investment and specialization

In any case, the logic of the current EUROMED process leads to an increased competition to attract foreign investment between the three Maghreb countries through the offering of locational advantages (tax exemptions, customs concessions, free transfer abroad of dividends and foreign currency, cheap energy, labor laws flexibilization). In this context, in the foreseeable future only Tunisia in the region seems able to offer a competitive combination of secure legal environment (i.e., low risk), appropriate levels of wages, skills and productivity (i.e., high profitability) with the potential to move on to a better quality FDI in higher value-added, medium-skills but still labor-intensive industries which would eventually lead to a sustained process of industrialization and its integration into multinational companies value chains. In fact, according to official data foreign companies account already for one third of Tunisian exports.

Algeria, in turn, does not seem able in present circumstances to attract much foreign investment, letting aside the exploitation of the largely untapped opportunities in the oil and gas sector.

This would lead to an investment landscape in the Maghreb where Algeria would consolidate as energy powerhouse of the region (and of Southern West Europe as well), Morocco would take all chances to become the investment hub for market-seeking FDI in the region (provided there is a liberalization of trade between the three countries) and Tunisia would have to upgrade its FDI-attracting capabilities to try to become a localization of choice for efficiency-seeking FDI by companies in search of cheap and relatively skilled workforce in the Southern and Eastern Mediterranean to integrate into their world-wide (or at least European-wide) supply chains. This profile seems to be supported by the Report on Africa Competitiveness (2000), revealing Tunisia as the most competitive country in the continent, Morocco in a promising fifth place (and leading the ranking as far as the improvement index 1996-1999 is concerned) and discreetly leaving Algeria out of the report altogether.

4. POLICY IMPLICATIONS

4.1 At country level

Taking into account what has been said on the determinants of FDI, the first recommendation for any Maghreb country is to invest in FDI-attracting resources, i.e. human capital (in particular, the low education level of Moroccan work-force[35] is a major threat to its prospects to become a regional investment hub, and Tunisia has to focus on the skills of its work-force if it wants to upgrade its industrial structure and compete in higher value-added goods) and infrastructure (in particular, transportation and telecommunications). Equally important is to pursue the sound macroeconomic policies implemented since the late 1980s and to complete the modernization of the legal and regulatory environment (in order to render it more investment-friendly). The key in this respect is the independence of the legal system from the political ups and downs.

Political stability is another key factor as far as FDI is concerned (and, in the case of Algeria it is probably what explains its FDI underperformance save for the oil and gas sector), but this is a variable more difficult to control by national authorities. In any case, one obvious recommendation is to strengthen social security networks and prioritize the fight against poverty, since this would undermine the social and political predicament of radical islamist groups and ease the expected negative social consequences of EMFTA (including possible

[35] Illiteracy affects 57% of adult population (World Bank 1999b).

agglomeration economies), contributing to its political feasibility.

Finally, since the low levels of foreign investment have coexisted with substantial flows of capital flight (particularly in Morocco and Algeria), another sensible policy would be to promote the repatriation of national capitals located abroad: the World Bank has estimated that accumulated capital flight amounts to $11 billion for the Maghreb as a whole[36]. They could make a very important contribution to filling the financial gap all countries in the region suffer.

4.2 At regional level

Maghreb countries should make their best to promote regional integration in order to avoid the consolidation of a "hub and spokes" system and reach the necessary scale to attract market-seeking FDI and take advantage of the possibility to cumulate value added for rules of origin purposes across them. However, this might give rise to agglomeration economies that would favor one specific country in the region in detriment of all others. This together with the political hurdles regional economic integration has encountered so far suggests that maybe it is more feasible to begin by establishing a network of bilateral/sectoral co-operation and integration agreements/programs (when possible, establishing bilateral/sectoral free-trade areas) which guarantee a fast approaching among Southern and Eastern Mediterranean countries to the levels of protection prevailing vis-a-vis the EU as a first step towards real regional integration. In any case, the removal of barriers of every kind to intra-regional trade -be it bilateral, regional or multilateral under the most favored nation clause- will be crucial for every country in the region to be able to fully develop their comparative advantages.

[36] However, some other estimates point to much more substantial volumes: $37 billion in Algeria according to some official records, and more than $50 billion in Morocco according to the political opposition, higher that its GDP.

Finally, as one important aspect of any process of economic integration is the development of compatible (let alone common) technical regulations and standards, Maghreb countries do not seem to have any other real choice at this stage that conforming to EU regulations in this field, however inappropriate they might be in some cases to their level of development. So they would make a capital step forward if they decide to adopt them explicitly and arrange for MEDA programs to support this effort.

4.3 Within the EURO-MED framework

So far, the record of the Euro-Mediterranean Partnership in the field of promotion of foreign investment into the Maghreb countries has been rather poor. Now, as FDI is deemed to become a key factor of success for the whole Partnership, it is necessary to give it a central role in its implementation. Some possible steps in this direction are quite outright.

The volume of external debt in all three central Maghreb countries has become one of the major constraints for their development, absorbing far too many financial resources. At the same time, the weight of the external debt service on their balance of payments is an important deterrent for foreign investors. The recent experience in Morocco shows how debt alleviation schemes may be instrumental to channel FDI towards certain sectors, facilitating the arrival of new foreign investors. This experience should be expanded and replicated in other countries.

To avoid a damaging investment incentives competition run, a certain degree of incentive co-ordination should be implemented across the three Maghreb countries, establishing maximum thresholds (if relevant, modulated for various kinds of incentives and development levels, like the ones applicable at EU level). This would benefit all participant countries, reducing the cost of attracting the much needed FDI for individual countries.

There is also much to do in the field of institutional co-operation of all participants in EUROMED as regards investment promotion, e.g. to ensure the establishment of a regional Investment Guarantee Agency, to implement a better investment information system for all Maghreb countries and a better gearing of the co-operation funds provided for in the Barcelona Declaration towards FDI-enabling measures.

5. CONCLUSIONS

In the last years, inward FDI in Maghreb countries has been lagging behind in relation to their development level, their geo-strategic relevance for the European Union countries and their efforts in structural adjustment and macroeconomic management. However, the increase in FDI flows will be a fundamental success factor for the whole Euro-Mediterranean Partnership, both as an agent for structural transformation, as a factor to offset the expected deterioration in the current account balance and thus to make the Euro-Mediterranean Free Trade Area politically feasible.

Contrasting with this important role of FDI, the Barcelona Declaration and the subsequent Associations Agreements do not provide for specific measures to foster European FDI into the region. And the economic analysis of the prospects for FDI leads to worrying results: inward FDI into the Maghreb could be reduced, not increased, as a consequence of the implementation of EMFTA ("foreign investment diversion" effect), and its geographical distribution might favour mainly one "investment hub" in the region, being detrimental to all other economic areas in the Maghreb. In either case, the macroeconomic and political sustainability of EUROMED might suffer.

To promote more promising scenarios (and a "foreign investment creation" effect of EMFTA) two required lines of action are the promotion of effective economic integration between the three countries in the region (leading at least to the elimination of trade barriers between them) and the adoption of proactive measures –both by the national authorities themselves and within the framework of EUROMED- to attract FDI.

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