Euro-Mediterranean Financial Integration and Reform of Maghreb Banking Systems

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Although European businesses have demonstrated a clear interest in the Maghreb (particularly in 2006), no major developments have taken place, and the region continues to attract considerably less investment from Europe than from other areas (Asia, Eastern Europe, etc.).

The question of the economic development of the Maghreb region has frequently been posed in social terms, given the integration difficulties experienced by immigrants in Europe, particularly in France.

Attention has now focused on the large remittances sent from Europe to the Maghreb. The fact is that this attention is long overdue, as the amount involved—equivalent to an annual Marshall Plan—is some 8,000-10,000 million euros a year, which is more than the amount received in international aid by Maghreb countries. Most of the money flows through informal channels because of the lack of suitable banking systems in both the host and destination countries (with the exception of Morocco).

A report entitled *Study on improving the efficiency of workers' remittances in Mediterranean countries*, published by the Facility for Euro-Mediterranean Investment and Partnership (FEMIP), clearly drew attention to the issues at stake in regard to these flows. Two other reports from France—one published by the Caisses d'Epargne (*L'intégration économique des migrants et la valorisation de leur épargne*) in September 2006 and the other published by the Institut de Prospective Economique du Monde Méditerranéen (*L'espace financier euro-méditerranéen*) in July 2006—proposed a number of strategies for facilitating these flows in a context of Euro-Mediterranean integration.

Three inseparable integration phenomena are currently at work on both sides of the Mediterranean: a) economic integration driven by European investment; b) population integration driven by regular remittances of large sums of money; and c) integration of the Maghreb in a globalised economy. Meanwhile, heads of state will be making every effort in 2007 to give a new impetus to the Barcelona Process.

We would like to demonstrate how commercial banks can play a crucial role in the intersection between these three dimensions.

Algeria's current drive to modernise its banking system in order to catch up with neighbouring Morocco is undoubtedly driven by this perspective. The capital of at least one of Algeria's main public banks, which put new payment systems in place in 2006, will be opened up to foreign investors.

In Search of New Channels for European Aid to Maghreb Countries

Growth is not as good as it could (or should) be in any of the three Maghreb countries, largely due to difficult-to-manage demographic and urban growth rates, an alarming unemployment rate among young people (particularly among qualified young people), and generally degraded public infrastructures.

There has been no shortage of aid from the international community—particularly from Europe. The Euro-Mediterranean Partnership's MEDA programme, for example, represented a cash injection of €5.35 billion between 2000 and 2006. This aid, however, has not been sufficient to trigger a sufficiently strong development environment capable of attracting high amounts of sustained investment.

Given the current trend towards the restriction of public budgets in Europe, a search is underway for new ways of providing aid to northern African countries, such as direct or indirect intervention in investment capital or the promotion of more targeted local initiatives (e.g., business creation, micro-credits, etc.). Although such interventions are eminently desirable, they still require considerable funds if deployed on a large scale; moreover, it is difficult to control aspects such as employment outcomes and impact.

Sight must not be lost of the important potential role that can be played by commercial banks at the grassroots level in terms of selecting projects and controlling methods of payment. Although the countries in the Maghreb region have sufficient resources and means for facilitating development, current banking practices are strangling development by blocking the transformation of large injections of cash into investment. Small and medium-sized enterprises (SMEs) in the Maghreb represent the bulk of companies and employment. However, a determining factor for these companies—which are a means for channelling savings into more productive uses—is the leveraging role of the banking system and the multiplier effect of credit.

Maghreb Banking Systems Are Ill-Suited to Fostering Development

Large borrowers (typically public companies and the state) absorb the majority of readily available resources. Banks, however, are obliged to take serious credit risks on board, as a consequence of a volatile economic environment and a legal system that does not adequately defend the rights of creditors.

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Banks, in a sense, bear the brunt of this reality, which has repercussions for all economic agents. Credit is rationed by economic agents—in particular as far as SMEs are concerned—yet banks are excessively liquid. This is why very few private individuals have a bank account (20% of Moroccans).

Given high loan delinquency and default rates and bank vulnerability in terms of collecting outstanding debt, credit supply in the Maghreb tends to be limited in terms of the number of loans (many companies have no access to credit), the quality of loans (few medium- or long-term commitments are undertaken), and lending conditions (asset-based guarantees and cash collateral for international trade operations are required). Credit in the Maghreb, in sum, is both difficult to obtain and expensive.

Major Change Is a Matter of Urgency

In the three Maghreb countries, the market of the banks—which preserve value above all else—is limited to a restricted group of privileged individuals and companies. In such a context, credit does not act as a leverage mechanism for the creation of wealth; it is, rather, circumscribed by the prior possession of wealth. The banking system, consequently, has developed no project-funding culture as banks are not willing to assume the risk.

Rather than being typical of the Maghreb region, this stance is a feature of nearly all developing countries. Morocco, Tunisia and Algeria are far from the bottom of the list, nonetheless, with banking cultures comparable to those of Turkey, India or Brazil.

The Maghreb region, however, does not attract the same interest as these other countries; black Africa aside, the Maghreb has undoubtedly attracted remarkably low levels of foreign direct investment in recent years—even from European neighbours. Their level of participation in international trade, furthermore, means that they fail to report the growth rates of 6% to 8% that distinguish today's emerging economies.

The growth evident in the Tunisian economy or the modern and dynamic Moroccan banking system should not be overlooked, however. Furthermore, the fact that Algeria is currently lagging behind is partly a consequence of a recent crisis that should soon be resolved.

Although the overall picture is to some extent reassuring, the fact remains that banking systems in the Maghreb countries—all very similar—are ill-suited to supporting emerging economies

Although there is no question of denying the development potential of the Maghreb economies, it should be stressed that, from a banking perspective, major changes are required which need to be tackled in the framework of a global strategy—in other words, more from a Mediterranean than a local perspective.

The Issues at Stake Regarding Remittances by Emigrants

The economic development of the Maghreb does not depend exclusively on financial aid from Europe.

Nonetheless, available cash needs to be pooled for allocation to productive uses. From this perspective, a logical starting point is mobilisation of the remittances of migrants located in Europe. It should be mentioned in passing that these have continued to increase over the years, despite a generalised opinion that they would eventually taper off as migrants settled down in their host countries.
The issues at stake are such that they need be taken on board by a multilateral body. For example, the creation of a Euro-Mediterranean institution would seem to be a logical step, given the shared growth process participated in by the two sides of the Mediterranean.
The role to be played by transfers from migrants is likely to change: no longer will transfers be viewed as exclusively providing financial support to families, but also as generating opportunities for investment and savings. Integration in the host country leads to increased incomes and to a desire to benefit from the different purchasing powers on the two sides of the Mediterranean. This, in turn, leads to a desire for savings that are convertible—and convertible savings represent a potentially powerful tool for leveraging co-development.
The fact that remittances have long been overlooked is barely credible, given the amounts involved: in Morocco, for example, remittances from abroad are not only equivalent to 25% of the country's balance of payments, but are Morocco's most important source of foreign currency.
Bearing in mind the geographic and cultural proximity of the Maghreb to Europe—and particularly to France—the reality is such that the 'middle classes' of Morocco, Tunisia or Algeria are generally to be found beyond the borders of the respective countries. This situation will lead to new formulae for integrating migrant populations and particularly those born in Europe—who, in all likelihood, will not fully integrate in either the host country or country of origin, but will hover somewhere in between the two cultures. This circumstance would imply powerful potential for leveraging growth in the entire region, and again, this situation applies equally to each of the three countries in the Maghreb region.

The Maghreb Will be Forced to Exist!

The return of political stability to Algeria has indisputably led to the Maghreb region–as a whole, rather than in terms of individual countries—acting as a pole of attraction for European companies.
The three countries of the Maghreb, however, do not represent a single economic area, and a common political initiative to create such an area is unlikely to be embarked on in the medium term. It is, however, important to bear in mind a possible external impetus to this development, and to start thinking in terms of a Euro-Mediterranean co-development zone, featured by steady growth in flows of people, business, and capital. This would undoubtedly make the region more homogenous—although nationalistic sentiments will undoubtedly continue to exist as an irrefutable potential destabilisation factor.
Although business exchanges with the European Union and beyond (the USA and China, for example) will undoubtedly continue to develop, the three countries will need to cooperate further, given that none of them has the critical mass necessary to function alone at the international level.
International investors are likely to design common strategies for the area and will tend to favour investment in projects that embrace the entire region. We can therefore anticipate the development of an increasingly uniform Maghreb market, even if not accompanied by the creation of a free trade area (which is possible despite the developments underway) or of a political association (which is probable).

Perspectives for Euro-Mediterranean Co-Development

One can speculate as to the existence, within a period of ten years, of a Mediterranean region, which—even if politically diverse—will raise few barriers to financial flows. Although, at present, these flows are essentially in the north-south direction, in the future, financial flows between countries in the broader region are likely to increase. In 2006, for example, a million Algerian tourists visited Tunisia, and Egypt is already investing more than France in the region, particularly in the telecommunications field.
Flows, in general, are currently dissymmetric—typically, raw materials and agricultural products exchanged for almost everything else. That said, the Maghreb could well develop into the EU's industrial hinterland in the near future—i.e. a platform for delocalisation. This trend is already evident: Morocco is the leading African destination for the establishment of call centres (with 150 call centres and 15,000 positions employing

20,000 employees). This could eventually lead to the emergence of economic champions in the Maghreb. Given the constraints on subcontracting (in the purest sense) highlighted by problems in the Moroccan and Tunisian textile sectors (in a context of wage-cutting across the globe), the future is likely to be marked by co-subcontracting on the basis of delocalised platforms that prove capable of producing value-added finished goods and services (Renault, for example, had parts of its Logan manufactured in Morocco).

Other sectors providing services to private individuals could also emerge, including health tourism, as is currently the case in Tunisia, or services for resident European pensioners.

Although little acknowledged, there is an increasing alignment of social trends on both sides of the Mediterranean. Similarities in terms of demographic growth are particularly striking: the population growth rate in Morocco, for example, has fallen from 2.1% for the 1982-1994 period to a current rate of 1.4%, and the birth rate has dropped from 5.5 children per couple in 1982 to 2.5 in 2002.

Cultural and national particularities aside, what is clear is the gradual emergence of a Mediterranean economic area, marked by enhanced economic (and cultural) flows, and despite the fact that each side is featured by clearly different levels of development.

From a macroeconomic point of view, these differences in development are likely to respond largely to demographic inequalities:

1. The relative ageing of Europe's population is likely to result in a flow of savings from north to south.
2. The lower standards of living and relative youth of the Maghreb populations is likely to trigger a desire for consumption which will lead to a level of growth that is not likely to occur in Europe.

Given these two circumstances, the money sent home to the Maghreb by immigrants in Europe is likely to represent an important link between the two sides of the Mediterranean. Although remittances from Europe mainly take the form of cash, it would be advisable to convert them into savings flows.

The interlinked savings and credit issue, which is key to the development of the Maghreb region, requires a global—or rather Mediterranean—solution, which is not possible without a properly functioning banking system.

THE SECOND EUROMED ECOFIN MINISTERIAL MEETING 25-26 JUNE 2006, TUNIS

Building on the successful outcome of the joint Euromed ECOFIN/FEMIP Ministerial Meeting held in Morocco in 2005, this meeting took place in Tunis on 25th and 26th June 2006 under the Austrian Presidency of the European Union and hosted by Tunisian Authorities.

High level participants included the Finance Ministers of the 25 EU Member States and the ten Mediterranean Partner Countries, as well as representatives of the European Commission and leading European and international Institutions active in the region on financial and economic matters.

Ministers reiterated the importance of the Euro-Mediterranean Partnership and the European Neighbourhood Policy (ENP). They recognised the high unemployment rate as the main challenge for Mediterranean countries and underlined that the strategies to reform are common in the region and concerned raising competitiveness, improving the investment climate to attract foreign investment and greater trade openness.

Ministers reaffirmed their support to the four inter-related priority areas for reform:

▪ Improving the business climate to enable firms to invest, create jobs and expand. Ministers welcomed the progress achieved by Mediterranean countries in improving the business climate by easing the business environment. This will pay in terms of increased investment flows, lower unemployment rates, better standards of living for workers and higher government revenues.

▪ Further liberalising trade and opening the economy to increase competitiveness, efficiency and productivity. Ministers recognized that trade reforms have advanced strongly in the region through the implementation of the association agreements and the ENP Action Plans. Ministers attached great importance to the rapid progress towards completing the process of liberalisation of trade in services and investments and in agricultural products by 2010. Ministers also restated the importance of deepening regional economic integration among Mediterranean Countries.

▪ Upgrading public institutions and governance systems. Ministers noted that in the area of governance, Mediterranean countries continued improving public sector accountability and the quality of Administration.

▪ Consolidating macroeconomic stability. Ministers welcomed greater macroeconomic stability in the region but noted that it remains vulnerable to external shocks.

EU Ministers reiterated their willingness to continue supporting Mediterranean partners' efforts to improve their public finances through technical assistance and training projects with the EU public finance administrations.

Ministers took note of the recently approved 2007-2013 Financial Perspectives for the EU, which provides for a significant increase of financial support to its neighbours through the European Neighbourhood Partnership Instrument (ENPI).

For further information:

Background: http://ec.europa.eu/comm/external_relations/euromed/ecofin/2006/background.pdf:

Conclusions of the Conference: http://ec.europa.eu/comm/external_relations/euromed/ecofin/2006/index.htm