

Can Mediterranean Value Chains Offer a Path of Development to the South?

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The links between Europe and the southern and eastern Mediterranean have for centuries been crucial to both parts of the world. Throughout history, different empires have emerged and expanded in this region creating links of trade and migration and deep connections between the different people there. In recent decades, this space has become a microcosm of a broader world. A prosperous North adjacent to a much poorer South, often with colonial or post-colonial linkages shaping the relationship between the two parts. Increasingly, the North has been moving towards stronger political integration, further expanding the power imbalances in the relationship between a large integrated prosperous North and a fragmented poorer South.

A Garden and a Jungle?

The region has also become a microcosm for another political and economic debate in today's world. Can prosperity in one part of the world be protected by political and physical walls? Or does prosperity in an interconnected world require a degree of prosperity in other parts of the world? Before subsequently apologizing, the EU's foreign policy chief Josep Borrell told an audience in Bruges in Belgium last year:

Europe is a garden. We have built a garden. Everything works. It is the best combination of political freedom, economic prosperity and social cohesion that humankind has been able to

build – the three things together... The rest of the world is not exactly a garden. Most of the rest of the world is a jungle, and the jungle could invade the garden

While the framing of the garden and the jungle was rightly criticized, at a deeper level this quote shows the struggle within Europe of what vision it has for its relationship with the southern and eastern Mediterranean. Almost thirty years earlier, in his closing speech of the first Euro-Mediterranean conference in Barcelona, former Spanish Prime Minister Felipe Gonzalez expressed a different vision to that of "Fortress Europe" by highlighting to attendees from the EU and the southern and eastern Mediterranean the interdependencies between the two regions:

We are deeply interdependent in agriculture, migratory flows, trade patterns and industrial production, as well as in the resolution of problems of environmental deterioration, water shortages, pockets of poverty, drugs or ethnic tensions.

The focus on interdependencies and working together by Gonzales was, it has to be said, in a very different political moment both internationally and in the southern and eastern Mediterranean. At a global level, this came after the end of the Cold War and the optimism that this end would usher in a new era of globalization and global cooperation. Regionally, it came at a time of optimism that solutions to long-standing issues in the southern and eastern Mediterranean, such as the Arab-Israeli conflict, would be reached providing a path to deeper regional integration within the region and with Europe. Initiatives such as the Euro-Mediterranean Partnership and the later proposal by France for a Mediterranean Union reflected such ideas. Thirty years on, Josep Borrell

was speaking at a time when many countries in the southern and eastern Mediterranean have descended into a range of political and economic crises and some into military conflicts. In the eastern Mediterranean, the regional and political repercussions of the Syrian conflict have reshaped political and economic trajectories in the region and reduced the priority of issues such as economic development. In the southern Mediterranean, while countries such as Morocco have continued to develop their economic linkages with Europe, others such as Libya have entered periods of conflict, and others, such as Egypt, have been embroiled in economic crises. Instead of the hope of the 1990s for a peaceful resolution to long-standing conflicts, particularly the Arab-Israeli one, recent shifts have diminished such hopes. Rather than the Mediterranean becoming a space for cooperation and dialogue, it has become a space in which thousands die every year as they try to escape these conflicts and reach the safety of Europe.

Mediterranean Value Chains and the Hope of Development

This tension between cooperation and development on the one hand, and security and protection on the other, reflects the strain on the international political economy. Firstly, states are sovereign entities with, in principle, full autonomy to adopt and implement different policies in multiple arenas. Those states, however, are also interdependent in the sense that their political, economic and security policies have multiple implications for neighbouring countries and for countries further away. In recent decades, globalization has intensified these interdependencies by increasing the links between states and creating multiple channels through which the policies of one state affect other countries. In the economic sphere, one of the important shifts intensifying those channels of interdependencies is the fragmentation of global production and the emergence and expansion of what became known as global value chains or global production networks. While production has always been globalized to an extent, shifts in recent decades have enabled a new type of joint production, through which different parts of the world not only exchange goods and services but also jointly produce those goods and services. The shifts enabling this transfor-

mation included changes at the more structural level of the global economy with advancements in shipping and communication, allowing faster movement of goods and better tools to communicate between different parts of the world. These shifts also included broader political changes through the reduction in trade and investment barriers and the adoption of more liberal trade policies by many countries. In particular, the institutionalization of these shifts through free trade agreements and multilateral organizations such as the World Trade Organization (WTO) gave businesses a sense of certainty and predictability about conducting cross-country production. Globalization, it was believed, was inevitable and irreversible and any change will only be towards deeper global integration. For developing countries, the emerging international division of labour appeared to offer a new path to development. Rather than exporting primary goods to the advanced economies and importing manufactured goods, developing countries can industrialize through exploiting their lower labour costs and integrate into global value chains to achieve growth and job creation. The fragmentation of production seemed to offer a path to boost industrialization without the need to localize the full supply chain, as countries could aim to first attract labour-intensive segments of production, before upgrading to more capital-intensive activities.

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This new international division of labour was reflected in the Mediterranean region. A few countries, mostly south of the Mediterranean, particularly Morocco, Tunisia and Egypt, adopted a set of policies that aimed to boost their integration in the global economy and attract investments from the European Union. These three countries entered free trade agreements with the European Union, facilitating growth in trade and investments. Furthermore, across the three countries, export-oriented industrial zones, often close to their Mediterranean ports, were set up with favourable

rules and regulations with regards to investments and exports. In Tunisia, for example, the “offshore regime,” which was put in place as early as 1972, provided exporting firms with tax exemptions from company tax, tariffs on imported inputs and machinery, lower income tax for foreign staff employed in these companies and no restrictions on the repatriation of profits. These zones offered significantly lower costs of production to European firms and preferential market access to the European market, in addition to tax incentives. One of the early manifestations of these economic shifts in the Mediterranean region was the system of outward processing, linking European textile and apparel firms to those in North Africa. Faced with growing competition from Asia, European producers sought to lower their production costs by tapping into lower-cost pools of labour for the labour-intensive apparel stage of production. As a result, trade in textile and apparel was structured to allow North African producers to perform apparel production, but mostly using European fabrics and inputs. Proximity to Europe meant that fabrics and inputs could be quickly shipped to North Africa where they could be processed and then sent back to Europe. Tunisia and Morocco, in particular, became important outward-processing locations for European textiles by offering incentives to apparel factories facilitating European imports of fabric and inputs. While German and French firms were the first European firms to use this system in the late 1970s and 1980s, firms from other countries followed suit in subsequent years. As a result, Tunisian and Moroccan exports of apparel to the EU increased rapidly, while imports of fabrics and other inputs in the other direction increased simultaneously. In subsequent decades, this pattern of production expanded in industries such as electronics, automotive parts and components, amongst others, in addition to service sectors such as call centres and IT support. In sectors such as automotives, Tunisia and Morocco have become important players in European value chains through the relocation of labour-intensive activities to firms in those countries. As a result, manufactured exports from some countries in North Africa increased rapidly over the last few decades. In the case of Morocco, the share of manufactured exports from total merchandise exports in-

creased from around 20% in the late seventies and early eighties to 72% in 2021.¹ Similarly, the corresponding share for Tunisia increased from 36% in 1980 to 80% in 2021. This is significantly higher than the overall share for the Middle East & North Africa (MENA) region where the share stands at 24%. Such shifts have also enabled those economies to create jobs in these sectors, with industries such as apparel, electronics and automotives absorbing a high share of the labour force. One of the largest employers in Tunisia, for example, is the German automotive parts firm Leoni, which employs around 23,000 workers in four factories in the country.

The reliance on low-cost labour and the dependency on the EU in terms of market access has placed Mediterranean partners in a highly dependent position

While integration in EU-centred global production networks has enabled a few countries in the Mediterranean region to achieve a degree of industrialization and to deal with challenges such as job creation, it has also created a high degree of dependency of these economies on the European economy. To a degree, this is predictable as many of those economies are relatively small countries bordering one of the largest consumer markets in the world. Nonetheless, this model of development has not succeeded in creating dynamic economies capable of producing sustainable economic and social development. The reliance on low-cost labour as the main comparative advantage and the dependency on the EU in terms of market access, technological capabilities, capital and value chain capabilities has placed those Mediterranean partners in a fragile position in terms of their future development, and in a highly dependent position with regards to shifts in the policies of European states or shifts in the strategies of European firms. I highlight two issues as an example: shifts in trade policy and technological change.

¹ Data from the World Bank.

Shifts in Trade: Not that Special Anymore?

Throughout their history with the EU, Mediterranean partners have been situated in what some scholars have called a position of “on the outside looking in” (White, 2001). This has placed those economies in a position of having to react to shifts in European policy with regards to two major issues: EU enlargement and EU trade policy. Each of these issues has had direct implications on the economic position of Mediterranean partners and their prospects for industrial and economic development.

In terms of EU enlargement, the integration of former socialist eastern European economies into the EU, starting in the 1990s, had important implications for the position of Mediterranean countries in Europe-centred production networks as it opened up new low-cost spaces for western European firms to invest in or outsource to. Countries such as Poland, the Czech Republic and Slovakia became attractive locations for production in the 1990s and the 2000s due to multiple factors. German firms, in particular, shifted some of their production to those countries in industries such as the automotive sector, which hindered growth in the Mediterranean region. For example, German imports of automotive parts from the EU's 2004 enlargement countries² increased significantly in the 1990s and 2000s contrary to much slower growth for those imports from Mediterranean partners. These shifts, however, were not permanent as the increase in production costs in eastern Europe, as a result of gradual convergence of their wages to the rest of the EU, partially due to free movement of labour, made locations such as Morocco and Tunisia more attractive, driving a growth in investments and exports in the 2010s. Overall, however, countries in the southern and eastern Mediterranean that are integrated in the European economy often see their position changed on issues such as trade and investments as a result of EU decisions related to enlargement.

Similarly, the economies of the Mediterranean region have been shaped by the trade policies of the European Union, not only regarding direct trade with them, but also in terms of trade with third countries. In the early years of expansion of the Europe-centred pro-

duction in North Africa, predictability of market access was an issue for producers in the region. In 1977, for instance, Egypt, Morocco and Tunisia all faced quantitative restrictions on their textile exports to the EU (Pomfret, 1982). Subsequently, the three countries signed free trade agreements with the EU, which made their access to the European market more predictable. Nonetheless, this privileged position of the Mediterranean partners in the EU market was gradually eroded as the EU signed further free trade agreements with third countries and offered preferential access to developed economies. This expansion of preferential access to the European market by third countries has led to growing competition in this market and to an erosion of the privileges enjoyed by the Mediterranean partners, relative to third countries. In some industries, this has provided third countries with a more advantageous position, at least from the perspective of firms in the Mediterranean region. In the textile industry, for example, producers in some Mediterranean partners often complain that producers in countries such as Bangladesh enjoy more preferential access to the EU market due to their ability to source fabrics from low-cost producers, while firms in the Mediterranean region have to comply with rules of origin (RoOs) that mandate certain input sources.

Shifts in Technology: Who Needs Workers?

The integration of some countries in the southern and eastern Mediterranean into EU-centred value chains was largely based on the low labour costs those countries can offer to European firms. As such, industries that are labour-intensive and where labour cost is an important competitive factor have moved to locations within those countries. Today, however, we are experiencing a technological push in some of those industries towards a higher degree of automation and lower use of manual labour. While some industries such as apparel might still need some time to reach this stage, this push is stronger in some other industries. In automotive parts, for example, North Africa is a major producer of wiring harnesses, the sector employing around one hundred thousand workers in the region. European firms, however, are today

² Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia.

pushing for the automation and relocation of some of those activities to Europe. This push is driven by a number of factors. First, shifts in the international political economy have raised renewed concerns about the once-inevitable path of global integration. Events such as Brexit, the trade policies of the United States in recent years, and the growing trade tensions between the United States and China have alerted firms to the impact of growing uncertainties on their business. Second, the emergence of crises, including military conflicts, across the region and in other parts of the world have alerted businesses to the risks of dispersed production. In some industries, such as automotive parts, the Russian invasion of Ukraine was particularly alarming considering some of those firms have been relocating production to Ukraine. Similarly, political instabilities in the southern and eastern Mediterranean have contributed to these concerns. Third, technological shifts are imposing a rethink on how production is structured in some industries. In the automotive sector, for example, the expansion of electric and self-driving technologies is demanding new requirements with regards to traceability and safety, the importance of digital infrastructure and skills and collaborations across value chains (AzmeH et al., 2022). Finally, the Covid pandemic and its impacts on cross-border production in terms of travel restrictions and border closures has contributed to concerns over dispersed production. These different factors are driving a push for the reorganization of global production. This does not necessarily mean a move to what is referred to as reshoring (i.e., shifting production to Europe), but it does mean that we might be entering an era of production restructuring, which will have major implications for the developmental model of the southern and eastern Mediterranean and their connections to Europe. Some countries in the region, such as Morocco, are making advances to gain from such restructuring processes, while others might face more difficult prospects.

A Walled Garden or Deeper Cooperation?

In a world with growing political and economic crises, the vision of the European walled garden might

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be tempting to some. Why can't Europe rebuild its industrial sector using new production and energy technologies, reduce its links with surrounding regions, and build barriers to limit how crises in neighbouring regions affect Europe? While possibly tempting to some, this vision is highly unrealistic. Even prior to deeper integration through globalization, the interdependencies between different states were crucial in shaping their joint economic and social prosperity. If anything, the last decade or so of crises in the southern and eastern Mediterranean shows how hard it is, especially in a world of globalization, for one part of the world to maintain prosperity and to limit the implications of crises in other parts of the world. The question, thus, is what is the alternative? And can a new vision of Euro-Mediterranean cooperation be launched to promote sustainable social and economic development in the southern and eastern Mediterranean and to help address the political, socioeconomic and environmental challenges facing Europe and the Mediterranean region in an increasingly complex world?

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