ANALYSIS OF DIVERGENCE OF WESTERN ASIA IN TERMS OF ECONOMIC GLOBALIZATION, TRADE AND FOREIGN DIRECT INVESTMENT

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Abstract

The article is a part of a team serial political economy research on Western Asia. The purpose of this study is to configure the region of Western Asia in three economic categories: economic globalization, international trade and foreign direct investment.

Key words: *Western Asia, KOF globalization index, international trade, foreign direct investment flow inward/outward*

INTRODUCTION

The article dwells on the results of the team serial project, an objective of which is to configure the region of Western Asia in three political economy categories: economic globalization, trade as a GDP ratio and inward/outward flows of foreign direct investment. We use a comparative analysis technique: put the target region along the spectrum of the world countries and then analyze the degree of diversification within the region.

Western Asia is a target region. It includes Armenia, Azerbaijan, Bahrain, Georgia, Iraq, Israel, Jordan, Kuwait, Lebanon, Oman, Palestinian Territories, Qatar, Saudi Arabia, Syrian Arab Republic, Turkey, United Arab Emirates, Yemen and Bahrain. By the rules of the project, small states with a population less than 1.5million are excluded. Thus, Bahrain is not represented in the sample.

We have chosen countries of Western Asia as units of analysis for several reasons:

- The total population of Western Asia is about 300 million as of 2015 or about 4 % of world population, with projection to reach 370 million by 2030 (Maddison 2007). It corresponds to an annual growth rate of 1.4 %, which is above the world average annual growth rate of 0.9 % (Maddison 2003). Thus, the region is growing in population terms, which potentially affects the economic size of the countries and make the region attractive for development of international economic relations.
- The region significantly overlaps with the Middle East, the economic structure of which is highly diversified. While some countries are largely dependent on export of oil and oil-related products (Saudi Arabia, Kuwait, UAE), the economies of others are diverse (Turkey, Israel). While some countries are poor (Palestine, Yemen), others are extremely wealthy (UAE, Qatar). It makes the target region interesting for analysis in order to reveal factors of divergence. Overall, all countries in Western Asia are maintaining a positive growth (The World Factbook 2016).
- Since Western Asia is mostly represented by Arabic nation, which the author belongs to, it is of a particular interest to configure this region along the world spectrum and make comparisons within the region, so as to discover differences and similarities and reveal a potential for international relations and economic growth.

The technique of comparative analysis in study is as follows. We place a target region along the spectrum of the other countries in the world. We rank the data of all the world economies in ascending order and draw diagrams in order to see how our countries are located in the world. Then we describe whether the countries of Western Asia are at the top, middle, bottom or scattered randomly; whether they are similar or clustered, or diverge radically. Eventually, we suggest possible explanations for the observed results.

As units of analysis we have chosen three economic categories: economic globalization, trade and foreign direct investment (FDI).

The first set of data we will examine is economic globalization measured in economic globalization index with two components: international economic transactions (actual flows) and restrictions.

The second item we will examine is a national trade. We will try to explain why some countries of Western Asia experience more trade growth than others.

Lastly, the third data set we will examine is foreign direct investment. We will try to explore the trends and problems behind its growth.

ANALYSIS OF DIVERGENCE OF WESTERN ASIA IN TERMS OF ECONOMIC GLOBALIZATION

If we open a Journal of Economic Literature (JEL), published before 1984, we would not find a single article containing the term "globalization" in the title. By today the search gives us thousands hits, which means that the concept of globalization has become widespread. At the same time, the concept is rather controversial and there is no general agreement on its definition.

There are three general points of views on the parameters of globalization: hyper globalists, transformationalists and skeptics (Griffiths 2010). Hyper globalists argue that market forces have undermined state control over national economies and weakened the authority of national governments. Sceptics argue that market forces can still be brought under control, *if* the main international actors can agree on collective actions. Transformationalists consider globalization as more complex phenomena than merely free markets. They argue that it involves social and cultural factors.

In order to measure globalization, in our study we use KOF Globalization index[1], created by the Swiss Economic Institute in Zurich. The index is composite and is made up of three components: economic, social and political. We focus on economic part of the index, which consists of two components weighted equally: international economic transactions and restrictions. KOF Economic Globalization index is listed from 100 to zero, where 100 stands for the most globalized economy (Table 1).

Table 1. 15-top and 15-bottom globalized world economies, 2015

Top-countries	Economic Globalization Index	Bottom-countries	Economic Globalization Index
Singapore	95.69	Tanzania	39.1
Ireland	92.59	Pakistan	37.9
Luxemburg	91.12	Argentina	37.52
Netherlands	90.33	Burkina Faso	37.23
Malta	90.31	Chad	36.58
Belgium	87.99	Niger	36.09
United Arab Emirates	87.79	Bangladesh	35.28
Estonia	87.39	Benin	34.66
Hungary	86.35	Central African Republic	33.9
Finland	84.77	Guinea Bissau	32.6
Bahrain	84.71	Iran	30.18
Czech Republic	84.59	Sudan	28.05

[1] KOF is a German abbreviation.

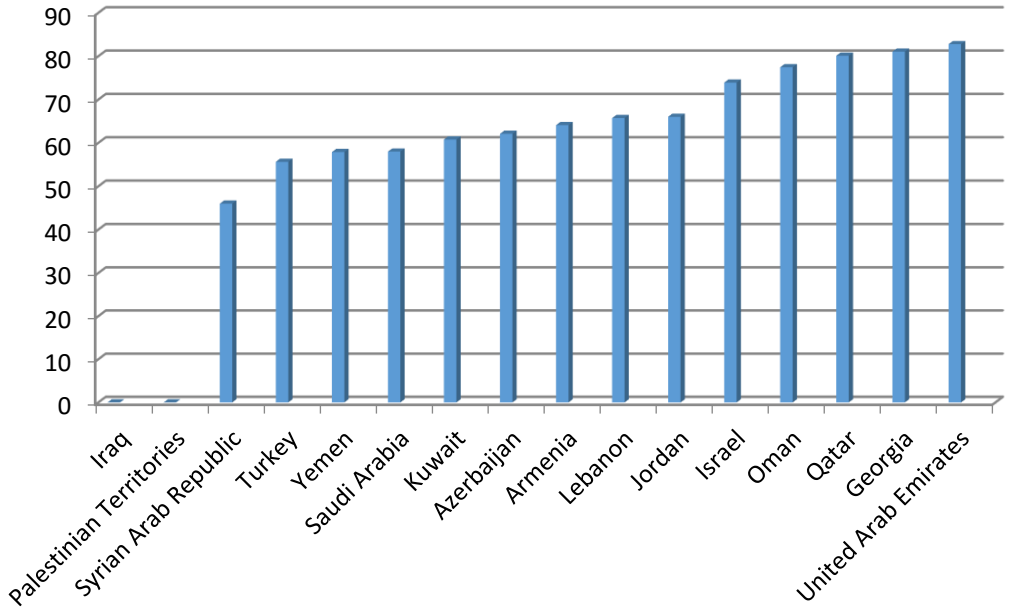
Top-countries	Economic Globalization Index	Bottom-countries	Economic Globalization Index
Mauritius	84.50	Nepal	26.77
Austria	84.16	Ethiopia	25.99
Sweden	83.21	Burundi	21.79

Source: author's table, data used from KOF Index of Globalization 2015

The Table 1 shows that the most globalized country in the world is Singapore, followed by Ireland and Luxemburg. In the list are also two countries from Western Asia: UAE and Bahrain.

Now we are going to investigate Western Asia region in terms of economic globalization. There is a Figure 1 below showing the economic component of the KOF Globalization Index; the countries are sorted in ascending order by the index value.

Figure 1. KOF Economic Globalization Index, 2015



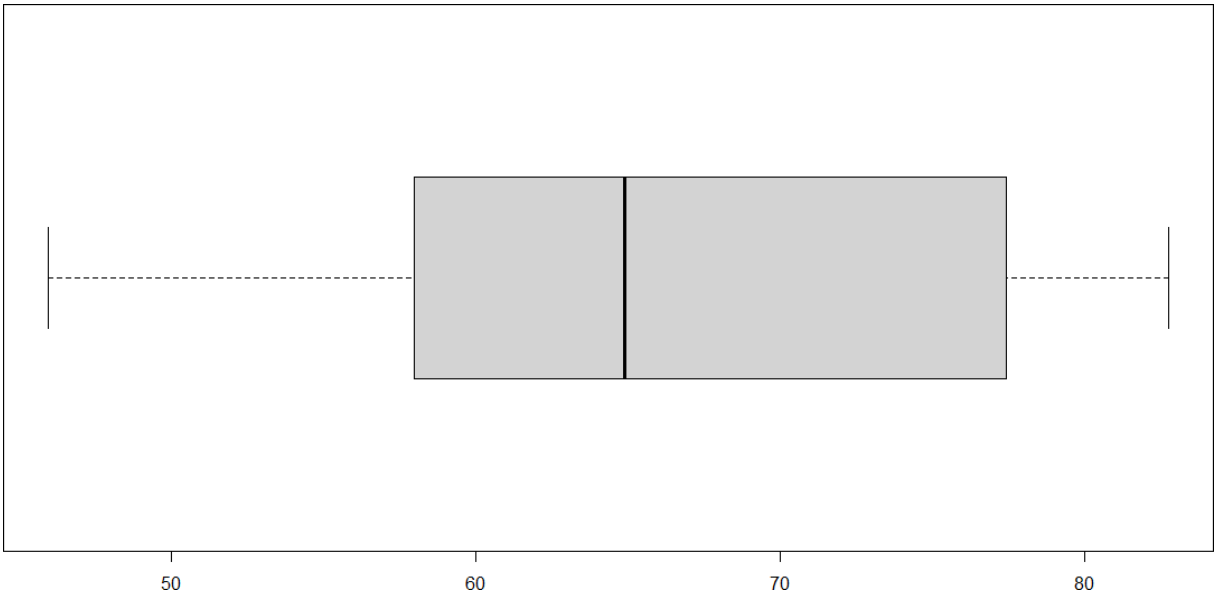
Note: no data on Iraq and Palestine

Source: author's diagram, data used from KOF Index of Globalization 2015

For the purpose of our analysis, we have ranked the economic globalization index values of all world countries and divided the world map of economic globalization into deciles. Then we place our target region across the world spectrum of economic globalization. The results are as follows.

In terms of economic globalization, countries of Western Asia scattered randomly, but the box plot below shows that most of the countries gravitate to the bottom along the spectrum of the world economic globalization (Figure 2). The distribution of scores is right skewed, the median is 64.90 and the mean is 66.53.

Figure 2. Distribution of Western Asia countries in terms of economic globalization



Source: author's boxplot, data used from KOF Index of Globalization 2015

The countries of our region diverge radically. The most globalized country of the region is UAE (2nd decile). It is followed by Georgia, Qatar and Oman. Israel is in the 3rd decile. Lebanon and Jordan are in the 4th decile. Azerbaijan and Armenia are in the 5th decile. Yemen, Kuwait and Saudi Arabia are in the 6th decile. Turkey is in the 7th decile and Syria is the 8th decile with the lowest position. For Iraq and Palestine we have no data.

Since there are no generally recognized features and definitions of globalization, we will try to measure it based on such criteria as trade and market access. Transnational Corporation (TNK) are involved in 80 % of global trade (World Investment Report 2013, p. 162) and typically control global value chains. Some Western Asia countries (see the Figure 1) demonstrate relatively low index values due to the political and economic reasons (either state ownership, or not very favorable investment climate, or orientation mostly on domestic demand, or poor with resources, or politically unstable, etc.) TNCs do not play an important role in trade.

Relatively more globalized are oil-rich countries where there are foreign companies (capitals) working on exploration and oil extraction. UAE and Qatar also pay a lot of attention to trading opportunities, creating free market zones, providing preferences to foreign investors, attracting investments in education, telecommunications and other spheres. In comparison with other world countries, index values of these countries are relatively low. The explanation might be as follows. Countries that have significant shares of natural recourses in their exports and stay at the "beginning" of global value chains need fewer foreign inputs and tend to have higher shares of domestic value added. Additionally, large economies, as Turkey, also tend to have significant internal value added chains and to rely less on foreign inputs (size of an economy is described in World Investment Report (2013, p. 158)). That is why Turkey does not have high globalization index. Thus, divergence of Western Asia countries is explained by the fact that national economies are involved in international trade in different proportions.

TRADE

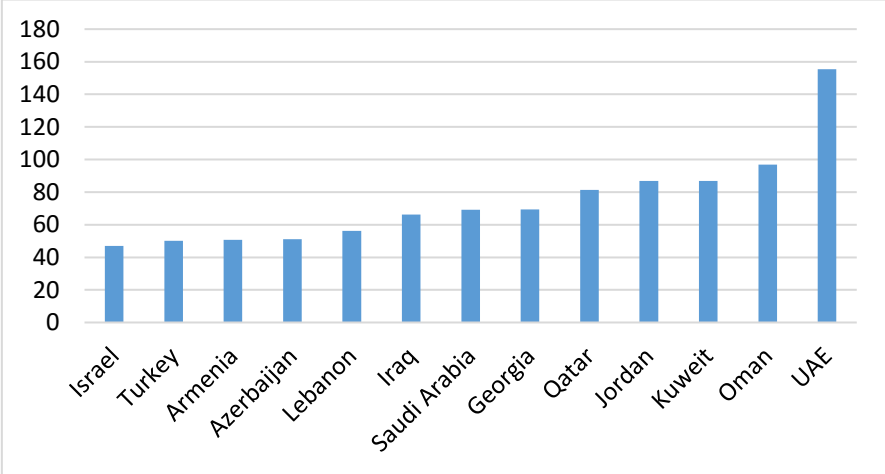
Data on international trade helps us to understand better the concept of globalization. However, we have to note that there are several problems involved with international trade statistics. Firstly, national income is counted as a sum of additional values between transactions, while in international trade the total value of a product is counted every time it crosses a border. Secondly, when a country exports a

final product, a proportion of its value may return (value chain). Thirdly, unrecorded cross-border trade leads to major distortions.

World trade flows, measured in terms of import volumes, continued to grow at a slow pace in 2014, expanding at about 3.3 per cent, slightly faster than in 2013 but still well below the long-term trend of the decades before the global financial crisis (Key Statistics and trends in trade policy 2015, p. 35).

Here we are going to configure our target region in terms of international trade (Figure3). Merchandize trade is trading goods and trading services.

Figure 3. Merchandize trade (% of GDP), 2011–2015



Note: no data on Palestine, Syria and Yemen

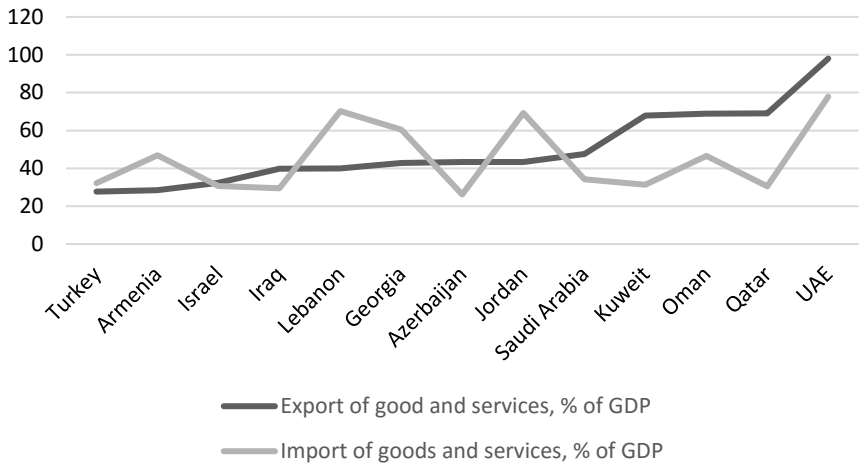
Source: author's diagram, data used from World Development Indicators 2015

As for the trade, countries in Western Asia locate rather randomly, with the average trade rate 74.39 % across the region. UAE has the trade indicator making up 155.5 % of country's GDP, and in this spectrum of regional countries UAE is the leader (Figure 3).

The GDP of overwhelming majority of countries in the region consists of more than 50 % of trade (except Israel, but its trade percentage is also close to 50 %, and accounts for 46.9 %). Turkey is close to Israel in terms of merchandize trade, with the indicator 50.1 %. In the 1st decile we observe UAE. Jordan, Kuwait and Oman are in the 3rd decile. Qatar is in the 4th decile. Saudi Arabia, Iraq and Georgia are in the 5th decile. Armenia, Azerbaijan, Lebanon and Turkey are in the 7th decile. Israel is in the 8th decile.

Thus, almost all the countries in the region are characterized as open economies. UAE is among largest merchandize exporters in the region (Figure 4).

Figure 4. Export and import of goods and services in Western Asia (% of GDP), 2011-2015



Note: no data on Palestine, Syria and Yemen

Source: author's diagram, data used from World Development Indicators 2015

UAE, Qatar, Kuwait, Saudi Arabia, Azerbaijan trade with fuel resources (big export amounts). Export of Iraq is largely based upon oil trade. Smaller countries (in population terms) have less developed processing sectors of their economies; most countries of the region have deserted climate (water scarcity, draughts) so there are less opportunities for agriculture. These and other factors make them to import a great variety of agricultural products, merchandise, etc. Oil-rich countries do not rely just on trade with fuel resources, which are limited in the long-run perspective. For this reason, they develop trade in goods and services. Countries of the region have a tendency to diminish tariff and non-tariff trade barriers, reduce transaction costs (freight cost, time cost and administrative fees), and create free market zones, trading preferences and attractive investment opportunities.

Currently in Western Asia, the major oil exporters have seen a slight decrease in oil demand, which, combined with the fall in oil prices, has lowered export figures for oil exporters such as the Cooperation Council for the Arab States of the Gulf (GCC) countries. These trends are expected to continue into the forecast period, with potentially still sharper falls in the value of oil exports from the GCC countries over the next few years, depending on whether oil price trends continue (World Economic situation and prospects, p. 54).

Conversely, Turkey has benefited from the depreciation of its currency, which has increased the competitiveness of its exports. The depreciation has caused Turkish imports to fall. Additionally, Turkey uses trend defense measures. In general, these measures are imposed mainly by developed and emerging economies, and are largely targeted against products originating from China, the European Union and United States. As of 2014, about 2/3 of trade defense measures in the world were targeted at firms operating in two sectors: chemicals and basic metals (Key Statistics and trends in trade policy 2015, p. 20).

Exports from Western Asia are estimated to have rebounded slightly from low growth in 2013 to growth of 3 % in 2014, but this remains below pre-crisis trends. Export growth is expected to grow at the same pace in 2015 and then increase to 5.3 % in 2016. Despite the falling oil prices, import volumes have remained strong in the region, growing by 4.9 % in 2014, and are expected to rise by 7.4 % in 2016, driven by large-scale infrastructure projects (World Economic situation and prospects 2015, p. 54).

FOREIGN DIRECT INVESTMENT

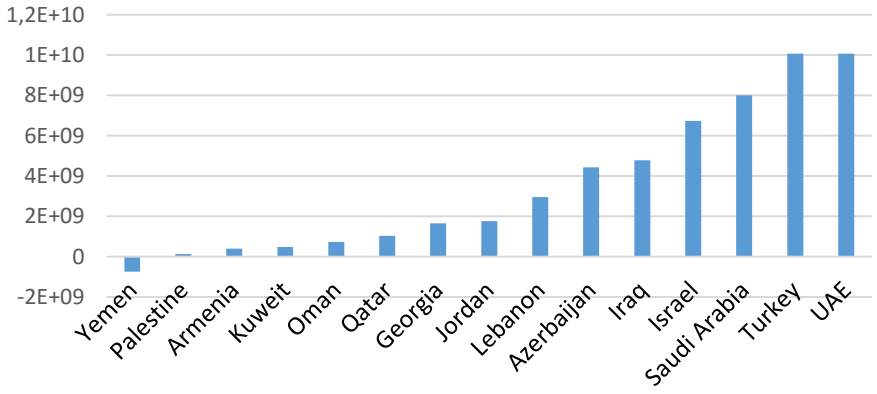
Foreign Direct Investment (FDI) involves the purchase, or expansion, of a business in one country, by a business in a foreign country. It can take several forms: purchase of shares, a merger, and the establishment of new business facilities and enlargement of existing foreign business (Griffiths 2010). Here we will configure the region of Western Asia in terms of FDI.

Global trends are as follows. FDI inflows declined in 2014. Global FDI inflows fell by 16 % to $1.23 trillion in 2014, mostly because of the fragility of the global economy, policy uncertainty for investors and elevated geopolitical risks. New investments were also offset by some large divestments. Inward FDI flows to developing economies reached their highest level at $681 billion with a 2 % rise. Developing economies thus extended their lead in global inflows. China became the world's largest recipient of FDI. Among the top 10 FDI recipients in the world, 5 are developing economies (World Investment Report 2015, p. 10).

FDI inflows of Western Asia account for 3.5 % of the world FDI inflows, or 43 billion dollars. As of 2014, it decreases by 3.7 %. This continuing decline stems from the succession of crises that have hit the region, starting with the impact of the global economic crisis, followed quickly by the eruption of political unrest that swept across the region and, in some countries, escalated into conflicts. This is deterring FDI not only in the countries directly affected − such as Iraq, the Syrian Arab Republic and Yemen − but also in neighbouring countries and across the region.

In Figure 5 we may see, FDI flows in 5 top host economies: UAE, Turkey, Saudi Arabia, UAE, Israel, and Iraq. It is reasonable to mention that since 2013 Turkish economy demonstrated high rates of development. Government has considerably improved investment climate since 2012 in order to attract FDI, and currently Turkey is one of the largest receiver of FDI in the region. EU is its largest market. However, recently it experienced fiscal tightening which consequently affected Turkish export demand and export-led FDI.

Figure 5. FDI, net inflows (current US dollars)



Note: no data on Syria

Source: author's diagram, data used from World Development Indicators 2015

In general, in Western Asia FDI remain sluggish even in the oil-rich Gulf Cooperation Council (GCC) countries, which have been relatively spared from political unrest and enjoyed robust economic growth in recent years. Flows to the UAE and Saudi Arabia − the region's second and third largest recipients − registered slight declines and remained about $10 billion and $8 billion, respectively. While flows to Jordan and Lebanon remained stable, deteriorating security cut short the recent resurgence of FDI to Iraq, where a significant part of FDI targets the oil sector. The crisis might cause delays in oilfield development and − together with the strong decrease in oil prices at the end of 2014 − is likely to deter new investors.

Outward FDI from Western Asia also declined by 6 % in 2014, driven mainly by divestment (negative intracompany loans) from Bahrain (World Investment Report 2015, p. 72). Kuwait, which has been the region's largest overseas investor, saw FDI.

The decline of FDI flows to Western Asia has occurred within a regional context of weakening private investment in relation to GDP starting from 2008, affected by the same factors that prompted the fall in FDI. The sharp fall in oil prices since mid-2014 is likely to have a significant direct and indirect impact on the construction market in the GCC, particularly in planned oil and gas projects.

However, huge fiscal reserves will still allow further State spending (World Investment Report 2015, p. 72). Priority will most likely be given to ongoing and strategic projects, including a number of big infrastructure projects associated with the 2022 World Cup in Qatar, the World Expo 2020 in Dubai, the $66 billion affordable housing construction programme in Saudi Arabia and infrastructure pipelines in Qatar – all set to provide major business opportunities over the medium term. If the oil price weakness persists, the GCC countries' strategy to prop up GDP growth through increased government spending may not be viable in the long run. Genuine economic diversification is crucial for GCC countries to reduce the dependence of economic growth on oil.

To sum up, FDI inflows in the region recently declined due to major factors: growing political uncertainty at the regional level; recovery from global economic crises in general is holding back foreign investors to invest in the region. Countries suffering in armed conflicts (Iraq, Palestine, Syria) are not attractive for investors because of instability in the region. Thus, their FDI flows are lower. Oil-rich countries (Saudi Arabia, UAE, Qatar), highly-technological (Israel), other Arabic countries have also attractive investment opportunities, so their FDI flows are relatively higher in the region in comparison with former USSR countries (Georgia, Azerbaijan, Armenia), which have the need of investment reforms.

CONCLUSIONS

In the research, we configured the region of Western Asia in three dimensions: economic globalization, trade, foreign direct investment. We conducted a comparative analysis putting our target region along the spectrum of the other countries in the world, as well as we made comparisons within the region. The results of analysis are largely influenced by statistical data, collection and measuring of which have some drawbacks. The research was conducted based on the latest available data. The major outcomes:

- In terms of economic globalization countries of Western Asia scattered randomly, however, gravitate to the bottom along the spectrum of the world economic globalization. Within the region, the countries diverge radically.
- Relatively more globalized are oil-rich countries where there are foreign companies (capitals) working on exploration and oil extraction. The most globalized country of the region is UAE, followed by Georgia, Qatar and Oman. In general, divergence of Western Asia countries is explained by the fact that national economies are involved in international trade in different proportions.
- In terms of international trade, almost all the countries in the region are characterized as open economies. UAE is among largest merchandize exporters in the region.
- The major oil exporters of Western Asia have seen a slight decrease in oil demand, which, combined with the fall in oil prices, has lowered export values for oil exporters such as GCC countries. These trends are expected to continue, depending on whether oil price trends continue.
- The sharp fall in oil prices since mid-2014 is likely to have a significant direct and indirect impact on the construction market in the GCC, particularly in planned oil and gas projects. Western Asia FDI remain sluggish even in the oil-rich GCC countries, which have been relatively spared from political unrest and unsustainable economic growth in recent years.

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