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POLICY ISSUES IN THE ESCWA REGION**FINANCING FOR DEVELOPMENT IN THE ESCWA REGION**

Follow-up to implementation of the Monterrey Consensus in ESCWA member countries

Summary

This report reviews the progress made by countries members of the Economic and Social Commission of Western Asia (ESCWA) in implementing the Monterrey Consensus, which was adopted at the International Conference on Financing for Development that was held in Monterrey, Mexico, from 18 to 22 March 2002. It indicates that it is necessary for member countries to work towards confronting the challenges of financing development goals by means of six principal measures.

With regard to mobilizing domestic financial resources for development, over the past three years member countries have made progress in increasing general revenue. Similarly, a large number of countries were successful in increasing gross domestic savings, both in terms of absolute value and as a percentage of gross domestic product (GDP). Most member countries have established capital markets in order to provide additional platforms for mobilizing domestic and foreign savings.

In terms of mobilizing international resources for development, particularly foreign direct investment (FDI), member countries, especially Egypt, Saudi Arabia and the United Arab Emirates, have made great progress.

With respect to international trade as an engine for development, member countries have succeeded, through various measures, in increasing the value of their exports, both in terms of absolute value and as a percentage of GDP.

Regarding increasing international financial and technical cooperation for development, donor countries have increased official development assistance to developing countries, with Iraq, followed by Palestine, receiving the most assistance because of prevailing economic and political conditions.

Member countries that were suffering from the burden of external debt have made progress in reducing debt servicing costs.

With regard to enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development, the major industrial countries continue to control the management of those systems. The role of developing countries, including ESCWA member countries remains very limited, despite the fact that those countries are affected by the international economic environment.

In general, notwithstanding the fact that member countries have made significant progress in implementing the Monterrey Consensus, some problems continue to obstruct its full execution.

The report concludes with a list of recommendations to ESCWA member countries that aim to promote completion of the Monterrey Consensus, in order to provide the necessary financing for development.

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Introduction

1. This report contains an analysis of the most important issues addressed by the Monterrey Consensus, which was adopted at the International Conference on Financing for Development that was held in Monterrey, Mexico, from 18 to 22 March 2002. The Monterrey Consensus comprises six principal areas for action, namely, mobilizing domestic financial resources for development; mobilizing international resources for development: foreign direct investment (FDI) and other private flows; international trade as an engine for development; increasing international financial and technical cooperation for development; external debt; and addressing systemic issues: enhancing the coherence and consistency of the international monetary, financial and trading systems in support of development.
2. The report reviews the most significant achievements realized by member countries in that regard in the 2002 to 2006 period. With respect to mobilizing domestic financial resources for development, the roles of domestic savings, tax revenue, commercial banks and capital markets in financing for development will be considered. As regards mobilizing international resources for development, the report focuses on the roles of FDI and worker remittances in financing for development, particularly in Egypt, Jordan, Lebanon, the Syrian Arab Republic and Yemen.
3. Concerning international trade as an engine for development, the report considers the importance of international trade in development as, on the one hand, a source of foreign currency and, on the other hand, a source of Government revenue. It mentions the efforts exerted by member countries in order to join such international and regional trade blocs as the World Trade Organization (WTO) and the Greater Arab Free Trade Area (GAFTA).
4. With respect to external debt, the report addresses the scale of that debt, the cost of debt servicing as a percentage of goods and service exports and debt management, and countries which use the facilities offered in that regard. The report also notes that sizeable debts place a burden on the economies of member countries and have a negative impact on their development.
5. Regarding increasing international financial and technical cooperation for development, the role that official development assistance (ODA) plays in financing for development in some Arab countries, particularly Egypt, Jordan, the Syrian Arab Republic and Yemen, is emphasized.

I. MOBILIZING DOMESTIC FINANCIAL RESOURCES FOR DEVELOPMENT

A. MOBILIZING DOMESTIC SAVINGS

6. In terms of the ratio of domestic savings to gross domestic product (GDP), member countries are divided into two groups: the first group comprises member countries in the Gulf Cooperation Council (GCC) which are characterized by an increase in domestic savings as a percentage of GDP and no lack of financial resources, which means that domestic savings are able to finance gross investment. Figures indicate that that ratio increased in Qatar from some 65 per cent in 2002 to 70.3 per cent in 2005; notwithstanding a reduction in the ratio in 2006 to 65.3 per cent, it remains the highest in that group of countries. During the aforementioned period, only Kuwait experienced a bigger increase in the domestic savings:GDP ratio, namely, from 25.1 to 59.1 per cent. In Saudi Arabia, that ratio increased from 37 to 49.3 per cent, and in Oman from 33.1 to 45.6 per cent.
7. The second group is composed of the remaining ESCWA member countries which, to various degrees, suffer from resource gaps because the domestic savings:GDP ratio is low. In Egypt, that ratio increased from 13.6 per cent in 2002 to 16.3 per cent in 2006, whereas in the Syrian Arab Republic, it decreased from 28.4 to 13.7 per cent in the same period.

B. THE ROLE OF TAXES IN FINANCING FOR DEVELOPMENT

8. With respect to the role of taxes in financing public expenditure, ESCWA member countries are divided into two groups. The first group is comprised of countries with more diversified economies and less growth, namely, Egypt, Jordan, Lebanon, the Syrian Arab Republic and Yemen. Tax revenue plays an important role in those countries in financing public expenditure, including capital expenditure, thereby contributing to an extent that varies from country to country to the financing of public sector development projects. In recent years, as part of economic reform programmes, those countries have implemented measures for reforming their tax systems and have made progress in that regard on the legislative, organizational and administrative levels, to the extent that between 2001 and 2006, tax revenue represented an essential component of all public revenue in those countries, particularly in the Syrian Arab Republic (73 per cent), Lebanon (72 per cent), Egypt (65 per cent), Jordan (40 per cent) and Yemen (25 per cent).

9. Between 2001 and 2006, the ratio of tax revenue to total public expenditure reached some 63 per cent in Lebanon, 47 per cent in Egypt and 39 per cent in Jordan, while in Yemen it was no higher than 25 per cent.

10. Nevertheless, the ratio of tax revenue to total fixed capital formation increased significantly in those five countries, reaching 100 per cent in Lebanon, 93 per cent in Egypt, 79 per cent in Jordan, 59 per cent in the Syrian Arab Republic and 51 per cent in Yemen.

11. The tax revenue: gross national income (GNI) ratio between 2001 and 2006 indicates a continuous drop in the aforementioned countries, particularly in Yemen, where that ratio did not exceed 6.8 per cent. In Jordan, the ratio averaged some 18 per cent, in Egypt 16 per cent and in Lebanon 14 per cent, while in the Syrian Arab Republic it did not exceed 13 per cent.

12. Concerning direct/indirect taxes, it may be noted that the aforementioned countries largely depend on indirect taxes, particularly sales taxes, in funding public expenditure, including capital expenditure. Statistics available for the 2001-2006 period indicate that indirect taxes account for an average of 82 per cent of tax revenue in Jordan, 71 per cent in Lebanon and some 55 per cent in both Egypt and Yemen. Despite that improvement, the tax revenue:GNI ratio in all of those countries has decreased and consequently, further tax reform efforts are required, especially with respect to fighting tax evasion, expanding the tax base and improving the performance of tax administrations, in order to benefit from tax revenue in financing development projects.

C. ENHANCING THE ROLE OF DOMESTIC BANKS

13. Reform of the banking sector in member countries has led to an increase in competition, particularly in countries which have authorized the operation of Arab and foreign banks, thereby prompting domestic banks to increase their efficiency and adopt modern banking systems. An improved banking environment undoubtedly increases saver confidence in the sector's ability to transform and manage savings for investment. Similarly, the presence of foreign banks strengthens the confidence of citizens in the banking sector and their reliance on banks as a link to investment opportunities. That could explain the number of private sector deposits in the banking sector between 2001 and 2006, when there was a sizeable increase in private sector shares.

14. In recent years, it has been observed that the banking sector has increased the facilities granted to the private sector, in view of the increasingly important role of that sector in development and investment. In December 2006, the ratio of credit offered to deposits in GCC countries was 80 per cent in Saudi Arabia, and some 98 per cent in Kuwait. In non-GCC countries, that ratio was 31 per cent in Yemen, 58 per cent in Egypt and 85 per cent in Jordan. In Lebanon, it was 34 per cent, a decrease is attributable to the fact that a large proportion of the holdings of Lebanese banks are invested in Government bonds. In Yemen, the banking sector continues to perform more modestly than in other member countries. With the exception of in the United Arab Emirates, it may be noted that private sector deposits continue to exceed the credit offered to

the sector, indicating that some of those funds are deposited abroad. There are no accurate figures on the provision of banking credit to the private sector, either in terms of investment or consumption. It is imperative that field research is conducted in order to precisely identify the parties to which facilities are offered.

15. In a number of countries and, in particular, Saudi Arabia, banks have given loans to the private sector for investment in stock markets, and have significantly suffered from the slumps in those markets. In Lebanon, the Syrian Arab Republic and Yemen, most credit is still directed at the public sector, one of the most important reasons for which is that the sector dominates economic activity and, consequently, investment in those countries. In general, it can be said that credit available to the private sector has increased in the GCC countries and Jordan, while it has decreased to differing extents in the other member countries.

16. The value of both local and foreign currency private sector deposits in commercial banks increased in member countries between 2001 and 2006, indicating that, in such countries, private sector involvement in the national economy has increased as a result of the implementation of economic reform programmes.

17. In Egypt, the value of bank deposits increased from 341 billion Egyptian pounds (LE) in 2002 to LE 570 billion in 2006. During the same period, deposits in foreign currencies increased from LE 91 billion to LE 168 billion. In terms of sectors, the family sector held the largest share of those deposits, increasing from LE 266 billion to LE 388 billion, while during the same period, Government sector deposits only increased by some LE 10 billion, from LE 39 billion to LE 49 billion. With respect to the time frame of those deposits, long-term deposits and savings accounts ranked first, increasing from LE 287 billion in 2002 to LE 480 billion in 2006.

18. The largest number of deposits in foreign currencies in Egypt was in the industrial sector, where their value increased from LE 55 billion in 2002 to LE 92 billion in 2006. During the same period, foreign currency deposits in the Government sector only increased by some LE 16 billion, from LE 13 billion to LE 29 billion.

19. During the period when the industrial sector had the largest share of deposits in Egypt, the business sector had the largest share of loans, which rose from LE 144 billion in 2002 to LE 150 billion in 2006, while the public sector was in third place in respect of loans. The same applies to loans in foreign currencies, which increased in the private sector from LE 41 billion to LE 64 billion, while at the same time, in 2002, loans in the Government and public sector were no greater than LE 10 billion and LE 6 billion respectively.

20. In Saudi Arabia, bank deposits increased from 338 billion Saudi Arabian riyals (SRIs) in 2002 to SRIs 591 billion in 2006. However, the majority of those were demand deposits that increased from SRIs 150 billion to SRIs 243 billion. Long-term and savings deposits increased from SRIs 108 billion to SRIs 226 billion during the same period. Such deposits therefore registered a greater average increase rate than demand deposits.

21. In Saudi Arabia, as in the other GCC countries, private sector deposits rank first, having increased from SRIs 286 billion in 2002 to SRIs 475 billion in 2006, while in the same period public sector deposits rose from SRIs 52 billion to SRIs 116 billion. As in all other member countries, deposits in local currency dominated, rising from SRIs 278 billion to SRIs 489 billion, while during the same period deposits in foreign currencies also increased from SRIs 60 billion to SRIs 103 billion.

22. The private sector had the greatest share of credit granted by commercial banks in Saudi Arabia, increasing from 62 per cent in 2004 to 73 per cent in 2007, the majority of which went to the trade, building and construction and industrial sectors. The available figures suggest that the trade and finance sectors claimed some 24 and 13.4 per cent respectively of total bank credit in 2006, while the building and construction sector represented 8.2 per cent and the industrial sector 8.1 per cent.

23. In Kuwait, the private sector enjoyed the largest share of private sector deposits, which rose from some 12 billion Kuwaiti dinars (KD) in the 2004-2005 period to KD 16 billion in the 2006-2007 period while during the same period, Government deposits rose from KD 595 million to KD 1.6 billion.

24. Concerning obligations, the value of debt owed by the Kuwaiti Government to the banking sector decreased from some KD 2.8 billion in 2004-2005 to KD 1.9 billion in 2006-2007. In that period, private sector debt increased significantly, from KD 11.1 billion to KD 17 billion.

25. In the Syrian Arab Republic, private sector deposits registered an initial increase in 2005 as a result of the entry of foreign private banks into the Syrian economy. Nevertheless, public sector deposits continued to represent the majority of banking sector deposits including demand and long-term deposits. Private sector foreign currency deposits, increased with effect from 2006, to surpass those of the public sector.

26. Figures from the Central Bank of Syria indicate an increase in public sector deposits in foreign currencies from 55 billion Syrian pounds (LS) in 2004 to LS 83 billion in 2007, while during the same period, public sector deposits rose from LS 10 billion to LS 100 billion. Albeit the public sector remains dominant in terms of deposits in local currency, the private sector leads in respect of deposits in foreign currencies. In general, however, the public sector continues to dominate commercial banking activities in the Syrian Arab Republic, as opposed to the situation in GCC States and Jordan, where economic reform programmes have greatly increased private sector deposits and loans.

27. In the Syrian Arab Republic, the public sector also continues to dominate with respect to loans from the banking sector: its share of such loans increased from LS 161 billion in 2002 to LS 287 billion in 2007. However, there was a significant increase in the scale of loans allocated to the private sector during the same period, which was the result of an increase in the activity of private banks and the Syrian economy as a whole, as well as the beginning of economic liberalization. Private sector loans increased from LS 72 billion to LS 280 billion, bringing the value of such loans almost to a par with those given to the public sector. That situation is indicative of the improvement in the credit environment and banking activities which has taken place in the Syrian Arab Republic over the past 30 years.

28. Loans given by the banking sector in the Syrian Arab Republic between 2002 and 2007 benefited three sectors, of which the wholesale and retail trade sector claimed the largest share, increasing from LS 126 billion to LS 272 billion. The real estate sector came in second place, rising from LS 30 billion to LS 86 billion, while the agriculture sector claimed third place, with loans increasing from LS 61 billion to LS 84 billion, which is logical in view of the fact that the agricultural sector plays a primary role in the Syrian economy in terms of non-oil exports.

29. In Yemen, the assets of commercial and Islamic banks increased from 464 billion Yemeni riyals (YRIs) in 2002 to more than YRIs 1,000 billion in 2006, while credit provided by those banks increased from YRIs 184 billion to YRIs 472 billion. While loans extended to the Government increased in value from YRIs 75 billion to YRIs 203 billion, those made available to the private sector also increased in value, rising from some YRIs 109 billion to YRIs 266 billion, reflecting the increase in private sector activity and its reliance upon the banking sector to finance its activities.

30. As regards the distribution of deposits between the public and private sectors, Government sector deposits increased from YRIs 38.1 billion in 2002 to YRIs 76 billion in 2006, while during the same period non-Government sector deposits also increased, rising from YRIs 388 billion to YRIs 851 billion. Moreover, the amount of non-Government sector deposits in foreign currencies increased from YRIs 199 billion in 2002 to YRIs 412 billion in 2006.

D. STRENGTHENING THE ROLE OF LOCAL CAPITAL MARKETS

31. Over the past six years, stock markets in the ESCWA region have witnessed unprecedented growth rates, with market capitalization in the ESCWA region swelling from some \$141 billion at the end of 2001 to

some \$827 billion at the end of 2006. The capital markets index attained its highest levels ever in 2005, reaching \$1,253 billion. In 2005, the Saudi stock market represented the fifteenth largest global market. According to a Global Financial Centres Index report that was published in September 2007, Bahrain, Dubai and Oman were among the top 50 financial centres in the world. The improvement observed in the performance of stock markets in the ESCWA region can be attributed to a number of factors, the most significant of which are the increase in the oil revenues of GCC countries that resulted from the boom in oil prices, the growth of public expenditure, the increase in liquidity caused by the repatriation of some Arab capital invested abroad and the expansion of private sector activities.

32. In terms of economic performance in GCC States, 2006 was the best year since 1986: GDP rose by 18 per cent. Statistics from the Arab Monetary Fund indicate that the market value of stock markets in the ESCWA region fell by some 34 per cent in 2006 against 2005. Some economic reports estimate that the losses experienced by stock markets in GCC countries amounted to some \$907.7 billion, or 160 per cent of regional GDP, the value of which was \$565.7 billion. The recession in the performance of financial securities markets in the Arab region, particularly in GCC countries, may be attributed to structural defects, including lack of institutional investment, that prompted deep reform in those markets. The majority of investors are individuals who buy shares in order to speculate and make quick profits rather than to invest, which is what led to a sharp increase in share prices in 2004 and 2005. Moreover, the sizeable demand for initial public offers (IPO) led to a recession in GCC securities markets. The excessive loans that banks had extended, which had helped to finance IPOs, were amongst the factors that caused the GCC securities market crash.

33. Statistics indicate that the average market capitalization of financial securities markets in the Arab region, excluding the Saudi stock market, is less than the average market value of emerging markets, which equals \$175 billion. With the exception of the Cairo, Alexandria and Amman stock exchanges, the stock markets in the ESCWA region are considered to be small because of the number of companies involved, which averages some 63 in each, apart from Egypt and Jordan. In other developing countries, the comparable figure is 597.

34. In comparison with the scale of the economy, the average ratio of market capitalization to GDP in stock exchanges in the ESCWA region exceeds those attained by emerging economies, being 79 per cent in the former against 55 per cent in the latter.

35. Arab stock exchanges do not reflect the true importance of the various sectors. While the industrial sector dominates the economies of GCC countries because of oil production, it nevertheless represents only a small portion of the market capitalization of all GCC stock markets, with the exception of that of Saudi Arabia, which may be attributed to the fact that the majority of oil companies are Government-owned and not listed in financial securities markets. Similarly, the communications sector represents 20 per cent of the market capitalization of the Egyptian stock exchange, even though it constitutes less than 7 per cent of GDP.

36. The banking and financial services sector constitutes a significant portion of the market capitalization of a number of Arab stock exchanges, particularly those in GCC countries. That sector dominates the Bahrain Stock Exchange and the Muscat Securities Market, with a market capitalization that exceeds 80 per cent, and represents more than 60 per cent of the market capitalization of the Beirut Stock Exchange and 30 per cent of total market capitalization of the Amman Stock Exchange.

37. Despite all the attempts that have been made since 1982 to link the Arab stock markets, which have taken such forms as attempting to forge bilateral and trilateral links between those markets, there is a continuing lack of regional connectivity. The Union of Arab Stock Exchanges project constitutes the most recent of those attempts, but has not as yet been implemented. Experts claim that the failure to link Arab securities markets is largely due to differences in the regulatory legal systems, and differences in development: each market has its own mechanisms and nature.

II. MOBILIZING INTERNATIONAL RESOURCES FOR DEVELOPMENT: FOREIGN DIRECT INVESTMENT AND OTHER PRIVATE FLOWS

A. FOREIGN DIRECT INVESTMENT

38. Member countries have taken a series of measures in order to promote FDI flows and increase their share of global flows of that important form of foreign investment. Those measures include the promulgation of laws that permit the economies of those countries to be opened for the inflow and protection of more FDI. Such laws do not differentiate between domestic and foreign investment in terms of operations and incentives offered. Many countries have allowed for full ownership of FDI-managed projects, including possession of the land and real estate necessary for such activities. Furthermore, as part of efforts to support private investment flows, including FDI, taxes on companies have been cut and a number of measures taken in order to liberalize foreign trade that have helped to expand FDI activity. Several countries, particularly those that do not have a sizeable specialized labour force, have issued flexible new labour laws with a view to allowing the private sector access to domestic or foreign supplies of such labour, which is considered to be an important factor in attracting FDI.

39. Member countries have opened most economic sectors to FDI participation and established offices and bodies in order to encourage and facilitate such investment by issuing permits and providing land and real estate. Efforts to strengthen FDI are not exerted only by countries that have a deficit of financial resources, but also by wealthy countries, because the benefits of FDI are not restricted to the provision of financial resources, but include access to modern technology, advanced methods of production and management and the opening of new markets for domestic exports. There is therefore stiff competition between countries, including developed countries, to increase their share of FDI.

40. The figures indicate that such measures have contributed to increased member country shares of FDI flows from \$2.6 billion in 2001 to \$49 billion in 2006, an increase from 0.32 to 3.75 per cent. Those flows have been stable in recent years, having been variable in the 1970s, which indicates that member countries are capable not only of increasing but maintaining such investment.

41. In 2006, Saudi Arabia was the member country that had made most significant progress in increasing FDI flows, its share of which increased to \$18.3 billion as a result of Government efforts to encourage such investment flows and the opening of new sectors, including the communications sector. Significant progress was also made in respect of measures to attract investors, including those for obtaining entrance visas. Through the General Investment Authority, the Government has exerted considerable efforts to include FDI in the domestic economy. As a result of the increase in the scale of such investment flows, its share of all capital investment increased from 4.5 per cent in 2000 to 32.1 per cent in 2006.

42. In Egypt, which rated second in terms of the scale of FDI flows in 2006, flows increased from \$647 million in 2002 to \$10 billion in 2006. The Government succeeded in increasing its FDI share in most economic sectors, including infrastructure, communications, tourism and financial services, using a number of legislative and regulatory measures and financial and customs incentives. Consequently, FDI rates increased from 4.3 per cent in 2002 to 9.9 per cent in 2005.

43. In the United Arab Emirates, which ranked third in 2006 and first in 2005, Government efforts to increase FDI flows were successful, albeit there were no specific laws on such investment before 2006. Nevertheless, the easing of restrictions on the establishment of companies, reduction of the number of measures necessary to obtain permits for and establish operations, the opening up of many sectors to FDI involvement and flexibility with respect to employment were measures that played a significant role in increasing the share of the United Arab Emirates in global investment flows. That country is foremost among Arab countries in terms of ease of establishing operations and companies and low levels of taxes and customs dues, all of which are fundamental factors for encouraging FDI. The ratio of FDI to gross fixed capital formation decreased from 9 per cent in 2002 to 4.6 per cent in 2006.

44. In Bahrain, FDI flows increased from \$332 million in 2002 to nearly \$3 billion in 2006, and its ratio to gross fixed capital formation rose from 36 per cent in 2004 to some 99 per cent in 2006. Such figures indicate that FDI has become the most important source of foreign finance for gross fixed capital formation in Bahrain and highlight the increasing importance of FDI in the Bahraini economy over the past three years.

45. Notwithstanding the difficult circumstances of the past three years, the scale of FDI flows in Lebanon has continued to increase, rising from \$257 million in 2002 to \$1,993 million in 2004, and \$2,794 million in 2006; while its ratio to gross fixed capital formation rose from 52 to 72 per cent, which was close to the figure of 79.0 per cent reached by Singapore in 2006. That ratio greatly exceeded the average in developing countries, which stood at 14 per cent in 2006. Such figures attest to the increasing importance of FDI in non-oil-exporting countries that depend significantly on sources of foreign funding for development.

46. The figures indicate the importance of FDI in financing gross fixed capital formation in the main oil-exporting countries. Using 2006 as an example, it may be observed that the ratio did not reach 31 per cent in the United Arab Emirates, 32 per cent in Saudi Arabia, 12 per cent in Qatar, and was less than 1 per cent in Kuwait. To a large extent, the figures for Saudi Arabia and the United Arab Emirates are attributable to the scale of gross fixed capital formation. In Kuwait, however, they indicate a decrease in the scale of FDI flows compared to Saudi Arabia and the United Arab Emirates.

47. Despite the increase in the shares of member countries in FDI, the following factors should be noted:

(a) A limited number of member countries obtained the largest share of such flows. In the past two years, Egypt, Saudi Arabia and the United Arab Emirates have secured over 50 per cent of all FDI flows to member countries;

(b) FDI flows in member countries have been limited to finance, and have not led to any increase in modern technology flows or any significant increase in exports from those countries, indicating that not all the advantages of FDI flows to member countries have yet been realized;

(c) No significant interaction has taken place between FDI companies and local companies, which is the most important matter in terms of FDI. Local companies have not achieved such interaction, either through FDI-managed projects, or through cooperation in such fields as management training and other activities that are important for increasing the competitive capacities and enhancing the potential of local companies.

(d) Research and development-related FDI activities remain limited in member countries, and have only minimally assisted in the establishment of research and development methods, advanced research centres and training centres, while the economies of member countries have not yet experienced the benefits that had been hoped for by efforts in support of such investment flows;

(e) Some countries have yet to achieve significant progress in increasing FDI flows and should redouble efforts to overcome the legislative, administrative, regulatory and promotional obstacles to any increase in their share of global FDI flows.

B. WORKER REMITTANCES

48. With regard to worker remittances, ESCWA member countries are divided into two groups. The first group is composed of countries that have surplus labour which they export receiving labour remittances in return, namely, Egypt, Iraq, Jordan, Lebanon, Palestine, the Syrian Arab Republic and Yemen. The second group comprises those GCC countries that have a labour shortage and thus receive foreign labour and are sources of remittances, namely, Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates. It is worth mentioning that the GCC countries attract more than half of the Arab labour force, and thereby contribute to reducing the unemployment rate and alleviating poverty in labour exporting countries, in some of which worker remittances are a principal source of income. Furthermore, such remittances have important effects on the economy because, in contrast to other external sources of finance, they are manifested directly

and quickly. The majority of remittances go towards family consumption, land and real estate purchase, and financing small projects, particularly in rural areas. Over the past 20 years, Arab immigrant labour in GCC countries has shifted from the public to the private sector, which offers more employment opportunities and better salaries.

49. Exporting and receiving countries have benefited equally from the movement of labour. Those that receive labour have benefited from the experience of workers who have contributed to economic development, while those that export labour have used worker remittances from abroad to increase financial resource flows and enhance foreign currency reserves. Sometimes, exporting labour contributes to an increase in worker productivity because many workers acquire new experience and skills in the receiving country. Furthermore, worker remittances directly contribute to an increase in domestic consumption and investment and improvement of financial capacity in the receiving country.

50. Overall, worker remittances to their countries of origin are increasing. Between 2000 and 2006, such remittances increased perceptibly in Egypt, Jordan, Lebanon and the Syrian Arab Republic, while they have remained constant in Yemen and fluctuated in Palestine. It should be noted that the registered value of worker remittances is less than expected because records include only remittances that have been processed via the banking sector and exclude remittances in kind. Estimates indicate that a large percentage of remittances have been transmitted by means other than banks. It is expected that the value of worker remittances will continue to increase, particularly those from GCC countries, as a consequence of the oil boom and the steady increase in global oil prices.

51. When comparing the value of worker remittances to other sources of external finance, it was observed that such remittances are more stable than FDI and tourism and are not affected by the internal situation of the exporting country. Worker remittances represent an important proportion of deposits in foreign currencies in the banks of the labour exporting countries. In 2005, worker remittances constituted some 40 per cent of foreign currency reserves in Jordan, 16 per cent in Lebanon and 11 per cent in Egypt. In 2004, worker remittances constituted some 18 per cent of foreign currency reserves in Yemen.

52. Considering the positive role that worker remittances play in labour-exporting countries, it is imperative that the banking sector should offer greater exemptions and facilities for monetary transfer transactions, including reduced fees, in order to encourage workers to use banks to transfer their money. On the one hand, that will strengthen the role of the banking sector and will help to more accurately estimate the real value of remittances. On the other hand, countries receiving remittances should use part thereof to support medium and small-scale projects and stimulate the economy.

III. INTERNATIONAL TRADE AS AN ENGINE FOR DEVELOPMENT

53. International trade plays an important role in economic and social development. The revenue from goods and services exports is a significant source of the foreign currency needed not only for financing imports, including durable and capital commodities, but also for financing Government spending, including investment. Customs revenue represent a source of Government revenue and contribute to financing general Government expenditure, including investment.

A. FOREIGN TRADE POLICIES AND PERFORMANCE

54. Eight ESCWA member countries are members of WTO and are expected to honour trade commitments under the existing agreements, that focus on a number of such important issues as the reduction of customs tariffs. The commitments of countries differ according to the time that they became parties to those agreements. For example, those that are members of the General Agreement on Tariffs and Trade (GATT), namely, Egypt, Kuwait, Qatar and the United Arab Emirates, have lower rates of commitment with respect to customs tariffs than those that became party to GATT after the establishment of WTO in 1994, namely, Jordan, Oman and Saudi Arabia.

55. Member countries have achieved varying rates of progress in the foreign trade sector over the past six years by adopting open-market policies aimed at promoting exports, rather than import substitution policies, strengthening the competitive capacities of products and services and increasing the domestic value added of their exports.

56. Between 2002 and 2006, the value of foreign trade increased in all member countries. The United Arab Emirates achieved the highest increase, with the value of its foreign trade rising from \$69.5 billion in 2002 to \$226.2 billion in 2006, which raised the ratio of foreign trade to GDP from 91.8 per cent to 137.2 per cent. That huge increase may be attributed to the significant rise in oil prices over the past three years. In the same period, there was a remarkable increase in foreign trade in Jordan, from \$7.8 billion to \$18.8 billion, with a foreign trade:GDP ratio increase from 82.1 to 132.2 per cent. In the Syrian Arab Republic, the value of foreign trade increased from \$13.9 billion to \$31.2 billion, with a foreign trade:GDP ratio increase from 67.5 per cent to 96 per cent. Regarding the scale of foreign trade in 2006, Saudi Arabia ranked first with some \$261 billion, followed by the United Arab Emirates with some \$226 billion, then Egypt with some \$60 billion.

B. TRADE LIBERALIZATION IN MEMBER COUNTRIES

57. Commodity trade to GDP rates in member countries indicate that progress was made in trade liberalization in the 2002-2005 period, albeit to varying degrees. Such progress came about as a result of the implementation of economic reform programmes and the conclusion of such bilateral, regional and international trade agreements aimed at promoting trade liberalization and increasing exports as the partnership agreements with the European Union and the United States of America, and GAFTA. The commodity trade:GDP ratio indicator increased to various extents in all member countries except the Syrian Arab Republic, where the rate fell in the aforementioned period.

58. In terms of the ranking of Arab countries, Bahrain was first, with a commodity trade: GDP ratio of 154 per cent in 2005, followed by Oman, Kuwait and Saudi Arabia with 73.3, 67, and 63 per cent respectively.

59. The rate of commodity export growth indicates that performance in member countries has been disparate: some countries achieved an increase in the average growth rate, while others experienced losses therein. Yemen was one of the countries that recorded an increase in the average growth rate from 9 to 40.4 per cent in the 2002-2005 period. Iraq came second, with an average of 33.4 per cent in 2005-2006. That rate had been negative in 2002-2003 because of the 2003 war and the economic embargo that preceded it. In Jordan, the index increased from 11.3 to 25.1 per cent, while in Bahrain it rose from 14.6 to 25 per cent between 2002 and 2006. In the United Arab Emirates, the average growth rate rose only slightly, from 14.6 to 18.1 per cent, while in Oman it rose from 4.5 to 17.9 per cent between 2005 and 2006. In the same period in Egypt, Kuwait and Lebanon, that index fell, from 34.1 to 28.9, 32 to 28.9 and 46 to 25.4 per cent respectively.

60. It should be noted that the increase in the commodity trade:GDP ratio in the main oil-exporting countries over the past few years is largely the result of the increase in oil prices rather than in the quantity exported. The significant increase in the rate of oil exports distorts results, which must therefore be considered with caution.

IV. INCREASING INTERNATIONAL FINANCIAL AND TECHNICAL COOPERATION FOR DEVELOPMENT

OFFICIAL DEVELOPMENT ASSISTANCE

61. In some member countries, official development assistance (ODA) represents an important source of foreign financing. Egypt, Iraq, Jordan, Lebanon, Palestine and Yemen are among the countries that depend upon such assistance. Because of its current political and economic circumstances, Iraq has the highest ODA flows, which increased from some \$100 million in 2000 to \$8,662 million in 2006. In Palestine, such flows increased from \$637 million in 2000 to \$1,449 million in 2006, while the ODA: GDP ratio rose from 15.5

per cent to some 35 per cent. ODA flows in Jordan were stable during that same period, increasing only slightly, from \$552.5 million to \$580 million, whereas the ODA:GDP ratio decreased from 6.5 per cent to 4.1 per cent.

62. However, ODA to other countries decreased in the 2000-2006 period. In the Syrian Arab Republic, the decrease was from some \$158 million to \$27 million, while in Egypt it was from \$1,328 million to \$872 million.

63. ODA plays an important role in supporting economic cooperation between countries because it is part of the financial assistance offered by donor countries to developing countries in order to help them bridge the gap created by insufficient domestic finance. While donor countries pledged a rate of 0.7 per cent of GNP as ODA to developing countries, very few of them have honoured that undertaking, which means that ODA flows are below the level needed to finance development in developing and, in particular, the least developed countries. Albeit ODA increased in 2005 to some \$106 billion, the amount dropped by 5 per cent in 2006 because of the emergency aid offered to Asian countries that had suffered from the tsunami and to such countries as Iraq that are suffering from war and lack of political stability.

64. ODA is subject to some restrictions, and linked to political, economic or commercial conditions, which limits the ability of countries to use such assistance according to their development priorities. When donor countries are requested to provide unconditional assistance, the receiving country must be committed to being transparent about spending in order for trust to be built between the two sides.

V. EXTERNAL DEBT

A. EXTERNAL DEBT IN SOME MEMBER COUNTRIES

65. Notwithstanding the great improvement that has been made over the past few years by member countries in alleviating the burden of external debt by rescheduling, debt forgiveness or transfer to investment, those countries continue to suffer as a result of such debt. Figures indicate that the size of external debt in Jordan has decreased over the past five years from \$7,536 million in 2002 to \$7,305 million in 2006, and its ratio to GDP also decreased, from 78.8 to 51.3 per cent. However, debt servicing costs increased from \$580.9 million to \$627.5 million, while those costs as a percentage of total exports of goods and services decreased from 12.8 to 8.2 per cent. Those figures indicate that Jordan has been able to reduce debt servicing costs and, if it continues to do so, that there will be a positive impact on its economic capacity to provide domestic sources of financing for development.

66. In the Syrian Arab Republic, the balance of external debt increased from \$3,890.1 million in 2002 to \$5,333.6 million in 2006, and its percentage of GDP decreased from 18.8 to 15.6 per cent. The cost of external debt service also decreased, from \$368 million to \$336 million.

67. In Lebanon, external debt rose from \$14.3 billion in 2002 to \$20.1 billion in 2006, and its percentage to GDP also rose during the same period, from 76.5 per cent to 86.5 per cent. Debt service costs increased from \$2.2 billion in 2002 to some \$4 billion in 2006, making Lebanese debt service costs the highest of all member countries, especially given the modest volume of exports for the aforementioned period compared to Egypt, which ranks second in terms of external debt. While Egypt ranks first in terms of external debt balance, Lebanon ranks first for 2003 in terms of the duration of the debt service and its ratio to goods and service exports over that period. Lebanon is therefore the member country that most suffers from the burden of debt service, which is attributable to the fact that most Lebanese loans are provided by private banks at high rates of interest. Were it not for the debt relief measures that the State has been able to obtain in the past few years, debt service costs would be much higher.

68. As the result of debt relief measures, external debt in Egypt has been relatively stable over the past five years, amounting to \$28.8 billion in 2002 and \$28.9 billion in 2006. As a percentage of GDP, debt decreased from 33.9 per cent in 2002 to 27 per cent in 2006, indicating that Government policies aimed at

cutting the value of external debt were successful. During that period, external debt servicing costs increased from \$2 billion to \$3.5 billion.

69. In Yemen, total external debt fluctuated between \$5 billion in 2002 and \$5.5 billion in 2006, thanks to State efforts to reduce such debt and the cancellation of the debt owed to the former Soviet Union. Those measures led to a decrease in the ratio of external debt to GDP from 46.6 per cent in 2002 to 25.8 per cent in 2006. However, during the same period, debt service costs increased from \$184 million to \$227 million.

B. INTERNAL DEBT IN SOME MEMBER COUNTRIES

70. While member countries realized varying success in reducing external debt by means of rescheduling and debt forgiveness, there was an increase in the volume of internal debt because Governments borrowed from the domestic banking sector in order to finance current and investment expenditure.

71. While external debt only affected countries with more diversified economies, the problem of internal debt affects many member countries, including the GCC States. In terms of internal debt, Egypt ranks first, with a volume that increased from \$73 billion in 2002 to \$203 billion in 2006, and a ratio of internal debt to GDP that rose from 87.1 to 96.1 per cent. Saudi Arabia ranks second, despite the fact that its internal debt fell from \$176 billion in 2003 to \$47 billion in 2006 as the result of Government efforts to pay part of it, which led to a decrease in the ratio of internal debt to GDP from 77.8 to 13.5 per cent. Despite a decrease in levels of internal debt over the past few years, the Syrian Arab Republic continues to have one of the largest internal debt balances and ranks third in that regard, with a debt of \$13.4 billion in 2006. As a percentage of GDP, its internal debt decreased from some 75 per cent in 2002 to 39.3 per cent in 2006. Kuwait ranks fourth, with internal debt of \$9.2 billion in 2006, down from \$11.6 billion in 2002. That drop led to a decrease in the ratio of internal debt to GDP from 33 to 9 per cent.

72. Some countries used oil revenues to pay part of their internal public debt. Reductions therein are attributable to Government use of other tools, including bonds, to fund deficit and reduce direct loans from banks. The decline of the role of the Government in the economies of many member countries has led to a reduction in the value of loans taken out by Governments in order to finance expenditure, including investment. In recent years, the private sector has assumed a more important role, while the percentage of public sector investment has decreased.

73. Internal debt in member countries has decreased from one year to the next with the exception of in Bahrain, Egypt and Jordan, where it continues to increase, which means that those countries remain dependant on internal loans for funding budget deficits.

VI. ADDRESSING SYSTEMIC ISSUES: ENHANCING THE COHERENCE AND CONSISTENCY OF THE INTERNATIONAL MONETARY, FINANCIAL AND TRADING SYSTEMS IN SUPPORT OF DEVELOPMENT

MOST IMPORTANT DEVELOPMENTS

74. Without assistance, developing countries cannot achieve the goals of the Monterrey Consensus, which was adopted at the International Conference on Financing for Development that was held in Monterrey, Mexico, from 18 to 22 March 2002, particularly given the strong connection between the economies of developing countries and developed countries in the context of economic globalization. The economic decisions that have been made by developed countries directly affect the economies of developing countries with regard to, inter alia, interest rates, exchange rates and the protection of agricultural exports. If countries are to successfully implement the Monterrey Consensus, sound management of the international economy and the stability of the international economic environment are priorities that must be addressed. The economies of ESCWA member countries that have sizeable financial surpluses inverted in developed countries have a direct impact on the current fall in the dollar exchange rate and, as a result, revenues from such investment are negatively affected. The exchange rates of the currencies of many member countries have fallen as a result of the fall in the value of the dollar.

75. Developing countries continue to have little influence on the global economy, which is managed by certain developed countries and, in particular, the Group of Eight (G8). Currently, considerable efforts are being exerted with a view to reforming the global economic system. Those efforts were initiated by the United Nations in the 1980s during the period of the comprehensive negotiations. However, such efforts have not yet fully succeeded and the participation of developing countries remains limited. ESCWA member countries that have surplus finances abroad do negatively affect the value of the dollar, but they cannot influence decisions related to international economic policy, just as the International Monetary Fund (IMF) has not fully exercised its role of managing international monetary policy.

76. Finance markets in developing countries continue to suffer from financial crises because of the swift movement of capital caused by globalization, which does not leave Governments with any great ability to control such movements, that are occasionally very sudden, lead to fluctuations in financial market performance in those countries and limit the ability of those markets to play an active role in mobilizing savings for development.

77. It would be both useful and essential for there to be international measures, in the formulation of which developing countries are involved, to minimize the risks of rapid capital movements and the considerable economic and financial problems they cause for developing countries, particularly the so-called emerging markets, where the financial markets are ineffectual and under-developed, and therefore unable to deal with such problems.

78. A suitable framework must be formulated that can bring together developed and developing countries in creating a forum which would address problems in the management of the international economy that have a negative impact on the efforts of developing countries to finance development. National and international efforts must be integrated in order to implement the Monterrey Consensus and achieve its goals as well as the Millennium Development Goals. Consideration should be given to expanding G8 membership to include a number of developing countries with sizeable economies. The role of developing countries and their impact on international financial institutions, particularly IMF, and such international trade organizations as WTO, must be enhanced.

79. At the domestic level, developing countries should take measures to improve coordination between their monetary, financial and trade policies and the various ministries that preside over the implementation of such policies, in order to eliminate any inconsistency between those policies and the executive machinery. Central banks must be given a greater role in managing monetary policy without interference, in order to enable the formulation of a stable monetary policy that encourages investment and contributes to an increase in flows of financial resources for development.

VII. SUMMARY, EMERGING ISSUES AND RECOMMENDATIONS

A. SUMMARY

80. Set forth below is a summary of the progress achieved in implementing the Monterrey Consensus:

(a) Significant improvement has been made in the macroeconomic policies of member countries, which have applied comprehensive and stable economic policies that have eliminated the imbalances that were a feature of economic policy in past decades;

(b) Member countries have issued a series of laws and legislative measures aimed at improving the investment environment in order to increase their shares of global FDI flows. However, the number of countries that have succeeded in increasing their shares of FDI in the past three years has been limited, while the share of other countries has remained modest;

(c) Member countries have exerted great efforts in combating financial and administrative corruption, including passing laws that fight corruption and the squandering of money, however, such efforts have not yet fully achieved their goals;

(d) Member countries with more diversified economies have made great efforts to improve tax laws, increase tax revenue and facilitate tax collection, and have succeeded in increasing tax revenue to the extent that it has become the most important source of public revenue. Nevertheless, the problems of tax evasion and lack of cooperation within the Government tax collection apparatus persist;

(e) Member countries have begun to establish stock markets in order to attract and mobilize domestic savings for development, and have achieved remarkable progress in that regard;

(f) Member countries, particularly the GCC countries, have made remarkable progress in increasing exports. However, that increase may be largely attributed to the surge in oil prices and revenues, while little progress has been made in respect of diversifying exports. Several factors are responsible for that situation, including the poor quality of local products and consequent lack of ability to compete in global markets;

(g) Indebted member countries have achieved varying levels of success in alleviating the burden of external debt by means of debt forgiveness, rescheduling and transforming debt into investment. Nevertheless, many countries continue to suffer from external debt and require further efforts to alleviate it.

B. EMERGING ISSUES

81. The most important emerging issues in the implementation of the Monterrey Consensus are set forth below:

(a) The small scale of capital markets, their need for depth and openness, the fluctuation in their performance and the high cost of transactions; the smallness of commercial banks, of which there are a large number, and their need for reform in order to increase their competitive capacities;

(b) The rising level of inflation over the past two years, particularly in GCC member countries, which has negatively affected the stability of the economic environment which had been built up in previous years;

(c) The decline in purchasing power of oil export revenue and value of investments abroad in United States dollars, as a result of the sharp fall in the value of the dollar against other international currencies, especially the euro;

(d) The decline in transnational corporation activity in member countries except in the oil sector and, to a certain extent, in the communications sector, despite the control of such corporations over global production, trade and FDI and their important role in linking the economies of member countries to the global economy.

C. RECOMMENDATIONS

82. Set forth below are a number of recommendations to member countries concerning completion of implementation of the Monterrey Consensus:

(a) Member countries, especially those with more diversified economies, should increase their efforts to address the gap in domestic resources and mobilize those resources for development. At the same time, they should implement a just taxation system that would alleviate the burden of the poor sections of society, by pursuing a policy that is not based on increasing taxes, but on improving the efficiency of tax administration, preventing waste and expanding the tax base. Wealthy persons should be brought into that tax base, and tax evasion should be reduced to the lowest possible level;

(b) Stock markets should continue to be enhanced and expanded and their performance improved. Balance between sectors should be ensured and the fluctuations that are suffered by those markets, which are caused by their dependence on a limited number of financial companies and sectors, should be limited;

(c) Work should continue on the current reform of the banking system in order to improve the performance of domestic commercial banks and increase their cooperation with foreign banks, either through privatization or mergers, in order to reduce the number of banks in operation and ensure that they enjoy financial solvency and the ability to compete if financial services have not been opened to foreign competition;

(d) Efforts to increase member country shares of global FDI flows should be continued, and countries that have not yet made the progress required should lose no time in carrying out economic reform and increasing the participation of the private sector, including the foreign private sector, and linking local companies with those managed by FDI, in order to benefit from their knowledge, technology and modern management styles, thereby improving their performance and ability to contribute effectively to economic development. Linkages with the global economy should be strengthened as a first step towards integrating the economies of member countries with the global economy;

(e) All countries, including the main oil-exporting countries, should increase efforts to diversify exports and decrease dependency on oil exports in order to achieve some sort of economic stability. They should work towards improving the quality of domestic products with a view to increasing their competitive capacity on the global market, and participate effectively and in solidarity with other developing countries in WTO negotiations in order to defend their interests;

(f) Regional cooperation and integration should be supported and the GAFTA Agreement should be implemented in order to increase intraregional trade. Consideration should be given to activating the General Agreement on Trade in Services, in order to increase intraregional trade flows, and regional integration should be enhanced. Consideration should also be given to the feasibility of increasing levels of commercial relationships and establishing a customs union as the first steps towards an Arab common market;

(g) Countries that continue to suffer from heavy external debt, including Egypt, Jordan, Lebanon and Yemen, should increase their efforts to reduce that burden, while lender countries should offer assistance to those countries in order to alleviate the burden of debt, either by means of debt rescheduling, forgiveness or transforming some debt into investment in those countries;

(h) International organizations, especially the United Nations Conference on Trade and Development (UNCTAD), should offer technical assistance to all member countries, particularly indebted countries, in the area of debt management, in order to enable them to predict the cost of future debt service and adopt the measures necessary to honour those commitments in a timely fashion. Moreover, member countries should actively participate in the debt management expert group meetings and workshops that are organized by UNCTAD and conferences on the issue of debt management, in order to acquire expertise and share experiences with other countries that are similarly placed;

(i) More efforts should be exerted to implement the Monterrey Consensus and incorporate it into economic plans. Implementation should be considered an integral part of the process of strengthening the capacities of countries to mobilize domestic and international sources of financing for development;

(j) Countries should actively participate in the Follow-up International Conference on Financing for Development to Review the Implementation of the Monterrey Consensus, which is to be held in Doha from 29 November to 2 December 2008, harmonize their positions regarding the issues at hand, particularly those issues that are of priority to member countries, and coordinate with the countries in the Group of 77 and China in order to protect the interests of developing countries during Conference discussions;

(k) Experts in Conference issues, which are identical to those of the International Conference for Financing for Development that was held in Monterrey, Mexico, in 2002, should attend the Conference;

(l) Developed countries should be urged to meet their obligation to provide 0.7 per cent of their GNP and increase the share of member countries in total ODA, which amounted to \$1.6 billion in 2005;

(m) Developed countries should be urged to increase the technical assistance offered to developing countries in various fields, particularly in developing and modernizing financial markets, in order to permit them to play their required role in mobilizing domestic savings for development; expanding the private sector; managing projects; conducting feasibility studies; and eradicating corruption;

(n) Countries should cooperate with ESCWA in matters related to financing for development, including implementing the Monterrey Consensus and the outcomes of the Follow-up International Conference which is to be held in Doha, and actively participate in the meetings, seminars and workshops organized by ESCWA concerning financing for development.

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