EFFECTS OF TRADE LIBERALIZATION ON JORDANIAN ECONOMY

ABSTRACT

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ABSTRACT

Jordan became an independent country in 1946 from the colonial rule of United Kingdom and adopted monarchy system of governance. After independence this country came to be known as the Hashemite Kingdom of Jordan. This is a small country and covers the territory of about 91880 square kilometres. The country is geographically located at 31°00′N 36°00′E latitude in South West Asia. Syria, Iraq, Saudi Arabia and Israel are the neighbouring countries. During 1950 to 1967 this country claimed and ruled over an additional land of 5880 square kilometre popularly known as West Bank. But because of continuing occupation of Israel in this area King Hussein relinquished the Jordanian claim over this land in favour of Palestinians.

Over the years Jordan has evolved as a knowledge economy but lacks in water supply which is one of the major obstacles of the development. For its energy sources the nation is almost totally dependent on the oil import whose prices and supply is totally volatile because of the regional instability. Hardly 10 percent of its land is arable and makes the country more vulnerable in the presence of low and irregular rainfall. The natural resource base is also poor and the country mainly depends on its phosphate and potash resources. The climatic conditions are also not favourable along with the natural resource base which made this economy as a developing economy.

Despite all these odds the country performed very well during 1970 but slowed down in 1980s. The period of 1990s brought good news for the country and the economy moved on the path of recovery by realising a GDP growth of 36 percent. This recovery of the economy was based on the trade reforms, the country had started during mid 1990s.

To registered its presence in European Union (EU), Jordan signed an agreement with European Union that is popularly known as Jordan-EU Association Agreement (JEUAA) which practically realised in 2002 (Jordan Enterprise Development Corporation, 2010). This was an agreement to look into the matter related to promotion of trade between Jordan and EU so that the free trade zone between these two regions may be established by 2014. Other than these trade agreements there are many more that Jordan has signed for the promotion of trade but
the year 2000 is marked as the year of trade liberalisation when this country became the member of WTO (WTO, 2000).

Through this process of trade liberalization Jordan had many expectations. The first and the most important impact that was assumed to be realized by the Jordan was the improvement in its trade volume. The improvement in its trade volume may result in the increase in share of the country’s trade in world trade that can give recognition to this country at international level. A good recognition at international level may earn good reputation and recognition which can help in creating the market for its products in global market and may bring down the trade deficit of the country and can positively contribute in solving the balance of payment problems. Further the process of trade liberalization has also implications for a change in direction of trade. Country’s trade was supposed to be directed towards those countries with which Jordan has trade agreements. In continuation to this it was also expected to realize diversification in Jordan’s trade basket which may move in favour of manufactured goods and services from primary sector based trade.

The best reason why a country chooses the path of trade liberalization is the correction in its balance of payment situation. The growing world market provides an opportunity for the country to realize many types of economies of scale and become able to sell more at international level at competitive prices to generate more income through exports that minimizes/eliminates the deficits at both current and capital account. The liberalized economy attracts more foreign direct and foreign institutional investments along with technical support that not only solve the problem of capital but also improves the productive capacity of the country that puts the economy on the path of growth. Jordan was also expecting the same from the trade liberalization. Hence in this research endeavour an attempt has been made to analyze all these effects of trade liberalization on Jordanian economy.

Objectives of the Study

In the light of the above discussion and theoretical background the present research work tries to measure the effect of trade liberalization on Jordanian economy in general and is based on the following objectives;
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(i) Analyzing the impact of trade openness on the size of Jordan’s trade volume and its growth, share in world trade and composition and direction of trade.

(ii) Investigating the effects of trade liberalization on balance of payment situations.

(iii) Assessing the effectiveness of trade liberalization in attracting Foreign Direct Investment (FDI), Foreign Institutional Investment (FIIs) and foreign remittances.

(iv) Determining the efficacy of trade liberalization in promoting the growth of the Jordanian economy, and

(v) Finding out the policy implications of the present study.

Hypotheses of the Study

The present study is based on the following hypothesis and tries to know the statistical significance of the above objectives.

(i) The process of trade openness has not been very much successful in affecting the size of Jordan’s trade volume and its growth; share in world trade and composition and direction of trade.

(ii) Jordan’s trade liberalization has failed in solving the problems of balance of payment.

(iii) There is no impact of trade liberalization on Foreign Direct Investment (FDI), Foreign Institutional Investment (FIIs) and foreign remittances in Jordan.

(iv) Trade liberalization in Jordan has been ineffective in promoting the growth of the economy.

Data Sources and Methodology

The second chapter that deals with trade liberalisation and foreign trade in Jordan is divided into four sections. The first section studies the trend analysis of the foreign trade in Jordan and the second section focused on the role and performance of Jordan’s foreign trade in relation to the World for the period between 1965 and 2017.
The third section deals with the composition of exports and imports during the period from 1990 to 2017 while the fourth section analyses the direction of exports and imports over the period of 1995 to 2017.


The data for indicators of foreign trade are shown in absolute term while the data for composition of trade i.e. share of different commodities and direction of trade i.e. Jordan’s trade with partner economy are written in percentage form. To know the status of various commodities and various trading partner composition and direction of trade total data is mentioned in absolute form. To show the trend of foreign trade and country’s GDP the growth rate has been calculated. To study the impact of trade liberalisation on economic growth OLS Model has been used.

The second chapter discusses the changes in trade balance, composition of trade and direction of trade observed by Jordanian economy and found that the merchandise export and merchandise imports in 1965 was US$27.75 million which reached to US$7511.48 million in 2017 while imports was observed at US$157.00 million in 1965 but in 2017 it was US$20498.20 million. The data shows that both are increasing but imports are higher than increase in exports.

The study reveals that in 1965 the share of Jordan's exports in world's exports was only 0.02 percent and it declined to 0.01 percent in 1970 and increased to 0.03 percent in 1979. It further increased to 0.04 percent in 1981 and declined to 0.03 percent in 1990. However, Jordan's share in World's exports has reached its highest level of 0.05 percent in the years 2008-10, and 2015-16 while it again reached at 0.04 percent in 2017.

The share of major products in Jordan’s exports before and after trade liberalisation it clearly observed that total merchandise has highest share in Jordan’s trade and in terms of share trade liberalisation has negative effect. On the other hand manufactures trade liberalisation has positive effect on manufactures as its share
increases from 20.71 percent in 1990 to 24.93 percent in 2017 which is shown in figure 2.6 and 2.7. Fuel and mining products and chemical also shows that it share decline in 2017. Machine and transport equipment share marginally declined but the share of cloth increased by almost 20 times i.e. from 0.38 percent in 1990 to 6.93 percent in 2017. But in terms of absolute value these products increased.

The share of total merchandise marginally declined but has positive effect. Machinery and transport equipment rose to 8.69 percent in 2017 as it was 6.27 percent in 1990 while the share of agriculture product also declined by about 50 percent in 2017. Automobile products have the positive impact and transport equipment share also declined. As far as the share is concerned it has slightly declined or remained stable but in absolute term its value has increased.

It observed that the share of China in Jordan’s import was only 2.28 percent in 1995 but in 2017 it rapidly increased and reached to 13.55 percent. The share of Saudi Arabia has also increased by 4 times during the same period i.e. from 1995 to 2017. Before trade liberalisation Germany and United States were the major import partner of Jordan but in 2017 former was declined while later remain stable. The share of United Arab Emirate also has positive effect of trade liberalisation.

The study shows that before trade liberalisation the share of Iraq in Jordan exports was highest i.e. 17.06 percent which declined to 7.26 percent in 2017. On the other hand the share of India was 9.21 percent but it also show declined trend during the period 1995-2017. United States has tremendously increased to 21.46 percent in 2017 whereas it was 3.86 percent in 1995. It also reveals that Jordan exports to Saudi Arabia increased to just double. The free zone area shows that previously its share was 6.12 percent which in 2017 reached to 12.49 percent. In this way it can be concluded that the process of trade liberalisation has helped Jordan and its trade volume has increased along with changes in composition and direction of trade and we accept the first hypothesis.

The third chapter concludes that since trade linearization in Jordon, the condition of balance of payment did not improve. The current account has deteriorated further after trade liberalization particularly after 2004. The current account stayed negative since trade liberalization which does not make any sense to liberalize the Jordon economy if it has negatively affected the current account. The
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deficit in current account reflects that Jordon is exporting less than import. The import has been shooting up after trade while on the other hand export has not increased.

The trade liberalization is known to be as ambassador of economic development, however in case of Jordon it has not been successful, instead it escalated problem in Jordon. The balance of payment in Jordon has not improved while it has become the problem of Jordon that after trade liberalization current account has been deteriorate further. The current account in Jordon has always been negative due to heavy import and export has not accelerated due to deep rooted structural bottlenecks in the country and could not be removed which has made Jordon feeble economically, however by the mid-1990s Jordon started to reform its economy but pace of the economic reform has been very slow. So it has been found that trade linearization do not have impact on balance of payments and has further worse off the balance of payment situation in Jordon and therefore we accept the second hypothesis which says that trade liberalisation has failed in solving the problems of balance of payments.

As far as export is concern after trade liberalization, it has improved and contributed in raising the standard of living in Jordon. It would be suffice to say that trade liberalization has not reduce current account deficit. As matter of fact Jordon should promote the domestic industries to increase the export performance and should ensure the level playing field for infant industries of home countries. There should be single window for providing the permission to the small scale industries. To extract the maximum benefit from the foreign direct investment then the government of Jordon should invest in social overhead capital or in human capital which can help the Jordon to develop faster as compare to other developing nation.

While discussing the impact of trade liberalisation on economic growth in chapter four the study found that international trade in Jordan has been intensified after 1990 and it has immensely increased growth of the countries. In 1998 Jordon was going through a lot of structural reform and it also felt that there is need to integrate the economy with rest of the world and eventually Jordon opened the economy which earned a significant improvement in economic growth. After trade liberalisation it has increased its export and import which ultimately improved the per capita income of the Jordon’s people. Multinational Corporation also started
investment in the form foreign direct investment as well as in domestic industry which has provided the employment to the people. People also started to move in other countries which brought a lot of foreign exchange by sending back remittance to their family after export remittances played pivotal role in increasing economic growth in Jordon. Overall it can be said that the process of trade liberalisation has been successful in improving the GDP growth of Jordan and we accept the third hypothesis with an exception for FDI. Foreign direct investment did not influence much of economic growth so we need to introspect what is the problem with FDI not to affect growth because FDI can be good source to raise the capital in domestic market. There is need to make good foreign policy for attracting more FDI into the country. It would not be suffice to say that trade has been proved as an engine of growth in Jordon and hence our fourth hypothesis is disproved.

The fifth chapter is the concluding part of the study that summarises the findings of the study and suggests policy implications along with the area of further research. Based on the study results, it can be said that trade liberalization has significant positive effect on economic growth in Jordan. But, this effect was less effective during the recent fall in World crude oil price in 2015. The country has been importing more than exporting which led the country to suffer continuous trade deficits. Therefore in order to enjoy fully the benefits of trade liberalization, the study has following recommendations:

There is need to enhance trade balance through increasing Jordanian exports as much as possible. The study highly recommended exporting processed products because manufactured products achieve higher prices in the market. Therefore, Jordan industries must be developed in order to expand production and export capacity in the country.

1- There's need to attract more foreign trade and investments in order to enhance the economic growth, through provided an incentives for the investors who are interested in investing in Jordan.

2- The Jordanian government needs to make some reforms in order to adjust with changing economic environment, through elimination of trade barriers.

3- There is need for enhancing transport and communication means in order to facilitate foreign trade. In addition, the existing infrastructure need more
develop because it's relatively not sufficient and weak. Also, there's need to rehabilitation of roads and railways in order to reduce transportation and transaction cost.

4- The results in this study have important policy recommendations with respect to future trade liberalization reforms in Jordanian economy. They suggest the need to improve the level of infrastructure in the region. This infrastructural development will increase the response of exports to trade reforms in the early stages and could potentially curb the risk of balance of payments problems stemming imports growing faster than exports. Also, further trade reforms should be accompanied by efficient export incentive schemes which may be in the form of exempting exporters from transportation taxes and duties on their inputs.

5- Finally, the success of alternative trade liberalization policy reforms requires external support in terms of finance, technical assistance and, most important, market access.