

IAI8639

ON THE IMPORTANCE OF ECONOMIC COOPERATION  
BETWEEN GREECE, ITALY AND TURKEY

by Giacomo Luciani

paper presented at the International Seminar  
"Prospects and Problems of Cooperation Between  
Greece, Italy and Turkey"

Villa Montecucco, Castelgandolfo, 20-22 December, 1986

1. The significance of geography has seldom been fully recognised in the literature on international economic relations. There is generally a tendency to discuss trade, capital and labour movements as if distance or proximity did not matter, and the regional environment was not in any significant way more important than the international, global environment. In this view, boundaries are solid, and create a sharp distinction between the "domestic" and the "rest of the world"; the latter, however, is extremely flexible or homogeneous and it is assumed to be basically the same for any country. It is recognised that only certain types of economic relations occur across borders, hence the distinction between "tradables" and "non-tradables".

If this perspective is accepted, today's discussion makes no sense at all: Greece, Italy and Turkey just happen to be physical neighbours, but from an economic point of view what matters is their individual relations with the rest of the world, i.e. their trade and exchange policies taken independently of each other.

The vision of the globe as an homogeneous environment in which proximity does not matter is supported by some well known cases of rapid growth in the post-World War II period. Japan experienced extraordinary growth by following a globally oriented export policy, starting from a situation in which she was very much isolated from her regional context, because of historical reasons and of the reaction to Japanese imperialism. Hong Kong is another striking example of a country totally isolated from her regional context, that succeeded in experiencing very rapid growth. In short, there may be advantages to being enclaves.

Yet, in a majority of cases it is seen that geography matters. The process of European integration has taken place between adjacent countries. The success of the EEC relative to the EFTA is due in part to the political dimension and impact of the former, in part to the fact that the latter was a disparate and geographically dispersed group. The attraction that the EEC exercised on the UK relative to the Commonwealth is also partly due to proximity and what is implied by it: ease and multiplicity of intercourse, mutual influence, common political and security interests.

Of the regions within the EEC that were initially considered to be backward and not sufficiently industrialised, those that lay in the center of Europe (in Belgium, especially) gained most from the process of European integration, and attracted significant investment from abroad. Other regions that were geographically peripheral have gained less.

Geographic factors are easily seen to be extremely important also in the North American context, as they affect the economic structure and international economic orientation of Canada and Mexico. In the latter country, the maquiladora industries are located in the northern border towns, that until a few years ago had been a poor and sparsely populated part of the country. The importance of regional and geographic factors is manifested within the United States by the gradual shift of economic activity from the traditional industrial centers of the northeast and the central plains to the so-called Sunbelt. In the case of the west coast, rapid growth is at least in part connected to the attraction exercised by the fast development of the Pacific Rim: indeed, even if, as we mentioned, Japan and Hong Kong started off in their industrialisation effort as countries isolated from their regional contexts, the situation is rapidly changing, and regional factors in the Pacific are becoming extremely important in stimulating economic growth in the established industrial producers (Japan, Hong Kong, Taiwan, South Korea, Singapore) as well as in the new entrants such as Indonesia, the Philippines, Thailand, Malaysia, etc. This is especially the case since China opened up to increased international intercourse, creating a powerful focus of regional attention and opportunity.

2. Is it surprising that regional factors matter? The tendency to disregard distance as an important economic variable is the consequence of prevailing perceptions in the age of mass-produced industrial goods. Distance, or geographic conditions, have always mattered in the production of agricultural goods and primary commodities. Location was also very important in the early days of industrialization, but then conditions were gradually created in which industrial production could be carried out with minimal attention to geographic circumstances. Thus the impression was created that technology would gradually free production from locational constraints. However, more recent trends point to the fact that, quite to the contrary, geographic factors are bound to play an increasing role in the next phase of economic growth and development.

Agricultural production was in the past geographically constrained because of climatic conditions and because of the difficulty in transporting perishable products over long distances. In both respects, technology has introduced extraordinary changes, and the market for agricultural products is effectively becoming globalized. As far as agriculture is concerned, furthermore, it is not clear that proximity favours economic cooperation, because it generally leads to similarity of climate, and therefore to competitive, rather than complementary, production patterns.

The production of primary commodities of mineral origin remains geographically constrained by the availability of deposits. As far as our three countries are concerned, by far the most important consideration is the limited availability of minerals in each of them, coupled with the abundant availability of hydrocarbons in the neighbouring countries of the Middle East. Geographic factors are of minor importance in the case of oil, which is very easily transported. On the contrary, they are very important in the case of natural gas (methane). Indeed, for the latter the cost of transportation is a very significant fraction of the final cost to the consumer, and the cost of transportation increases very rapidly with distance. The latter fact has generally not been recognised, because up to now the tendency prevailed among gas producers to equalize the price of gas to the final consumer independently of distance; This is, however, basically an irrational pricing policy, which we expect will gradually be changed as the market for hydrocarbons becomes more competitive.

The cost of alternative sources of energy may be distance-related as well. Coal is difficult to transport, and there are transmission losses in the long-range transportation of electrical energy. The latter imply that certain sources of energy, such as hydroelectric power, have a regional impact and significance.

In the past, the availability of energy constrained the location of industry. Thus in the early days of industrialization, factories were located close to streams that provided power. However the gradual shift to electricity and/or oil, as well as the growing importance of road, as opposed to railroad, transport, greatly freed locational decisions. It is only in a few cases, such as for steel mills or refineries and petrochemical plants, that proximity to transportation infrastructure (essentially, deep water harbours) continued to be important.

To all other industry, man-made environmental conditions became more important. Availability of labour and certain minimal services, particularly financial, were the key to attracting economic activity, and since these environmental conditions were best found in locations in which some industry had already developed, the well known tendency of industrial activity to concentrate geographically ensued. At the same time, from any suitable location - most locations being essentially equivalent to each other - production could be initiated for sale in any market, distant as well as geographically closer to production.

3. In some cases, however, transportation was difficult, or too costly relative to the value added embodied in the product, and production was always carried out close to the market. Hence the well known distinction between tradables and non-tradables: the latter being, essentially, products that are difficult or altogether impossible to transport.

A prevailing emphasis on international trade and competitiveness led to downplay the importance of the non-tradable sector in development economics. It is, however, a very important sector in any economy indeed. Part of the confusion derives from the terminology itself, which, as we mentioned, is based on the assumption that goods travel freely within a country but absolutely cannot cross her borders. This, of course, is not the case, and one should more meaningfully speak of regionally versus globally traded goods.

A wide range of products is almost exclusively regionally traded. From construction to the food industry, it is the size of the regional market that determines the size of the industry. There are a few well known exceptions: cases in which entire plants have been transported across oceans to be put in operation, "plugged in" as it were in locations in which construction would have been prohibitively expensive, as well as there being countries that import even UHT milk and cookies from far away because of the (temporary) lack of suitable regional producers. These are, as we just said, exceptions, and only serve to highlight the rule.

Even in cases in which production is carried out by multinational corporations under the same brand name all around the world, it is still normally true that production facilities are located in proximity of major markets. It would make no sense to centralize worldwide production of Ritzes in a single location.

Thus, in this respect what matters is the size of the regional market. In this case, regional must be understood as meaning "easily and inexpensively accessible through existing transportation facilities". Two locations in the same country may not belong to the same regional market if they are separated by great distances or if transportation is difficult. Belonging to a same free trade area is important but it is not the only important factor, indeed in most

cases not a crucially important factor. Finally, locations may be geographically close but economically distant, if transportation infrastructure is inadequate.

The importance of the size of the regional market in determining the location of production facilities for regionally traded goods is a simple but nevertheless crucially important argument to underline the importance of transportation infrastructure. The latter has fallen out of fashion a long time ago, because it has always been recognized that one of the primary tasks of the State is to guarantee adequate transportation infrastructure, and the attention of most economists has been focussed on the effort to argue that it should do more than that. Also, it is difficult to evaluate the demand for transportation infrastructure, and the extent to which the availability of it will create its own demand. It is quite clear that it does so in some cases, but equally clear that it fails in others. The adoption of strict cost-benefit analysis tends to underestimate the importance of infrastructure, and a common mistake in industrializing countries has been to underinvest in this sector. The fact is that industrialized countries continue to attribute importance to transportation infrastructure, especially at the local level, where the perception of the economic impact of access to the neighbouring world is bound to be more acute.

4. The geographic determinants of economic development are bound to become increasingly important as the share of services in GDP increases to the detriment of the share of industry, and, within the latter, the traditional sectors producing low-technology goods for mass consumption are outgrown by the new lines of production, characterized by higher inputs of technology, greater product differentiation, importance of design and style. We should be aware of the fact that we are approaching, or possibly already live in, the post-industrial era.

In many cases, services cannot be transported. Most personal services must be offered at the location where customers are, and this includes public services such as health, education, public transportation. Here again, there are exceptions: a few may travel to study or obtain medical attention abroad, but it is only a tiny minority that will be able to do so. The same holds for banking and financial services, or insurance.

Some service industries are immobile by definition: such is tourism, a case in which the customer must move.

As the importance of these activities grows as a proportion of income worldwide, economic development will increasingly become a function of the ability to offer such services. And it is a characteristic of these services that they can best be offered in locations that enjoy easy communications with other locations where similar services are also offered. Intensity of communication provides for mutual knowledge and imitation, for competition, for circulation of individuals possessing the skills that are needed to provide such services.

This cumulative locational factor is reinforced by the shift in industrial production because the new, fast growing lines are very closely connected to these same services. High technological content, differentiation and importance of styling are all related to levels of education, development of the media, development of long-distance communications, availability of financial services etc.

While it is possible for a country to compete on the global market for "old" industrial products by aggressive export promotion, the socio-economic texture that breeds the newer economic activities can only be created under certain conditions. The key seems to be that the new lines are more

complementary than they are competitive. The fact that a multiplicity of sophisticated services and products are manufactured and produced in certain areas seems to induce further and further new entrants, in an endless, self-supporting game. Some people jokingly ask who will produce the goodies while we are all busy cutting each other's hairs, but in fact the advances of automatisisation on the production line have outpaced the creation of new service jobs, thus leading to increasing unemployment, and no danger of insufficient supply of material goods seems imminent.

These new realities create serious dilemmas for peripheral and relatively less advanced countries, such as Southern Italy, Greece and Turkey. Because of their lower per capita income and geographic remoteness, these regions face the risk of being marginalised for good, and excluded from a process of economic development that will tie the major European centers lying between London to the north and Bologna or Florence to the south in a closer and closer web of mutual intercourse.

5. Responding to the new challenge will be an arduous task in any case, and it is not clear that it will be at all possible within a foreseeable future. If success is at all possible, it requires that the condition of geographic peripheralism of our three countries be overcome.

We can measure the importance of regional factors by looking at the transformation that was brought about by the era of high oil prices. The sudden shift in purchasing power and increased economic weight of the Arab oil producing countries initially had a predominantly negative effect on the economies of our countries, as we faced the costs, while other countries reaped the benefits of increased exports to the Arab region. However, with time some necessary adjustments took place, and the importance of southbound trade has dramatically increased for all three countries.

The current extremely low price of oil cannot be extrapolated into the future. If, as all experts seem to agree, the price is bound to increase again to a level of 18 or 20 dollars per barrel, the need to utilize scarce financial resources more efficiently may prompt the Arab countries to pay greater attention to the costs of supplies, and this would benefit regional suppliers. Thus, when consideration is taken of the continuing importance of oil in the global energy balance (a point on which, after Chernobyl, little doubt is left) and of the concentration of oil reserves in the Middle East, we should recognize that the emergence of a pull factor to the south may be of considerable help in overcoming our peripheral position with respect to the rest of the EC.

All the more so if attention is paid specifically to the prospects for greater utilization of natural gas. (In the case of Turkey, the redirection of oil flows from the Gulf to the Mediterranean because of political conditions in the Gulf is also important; however, this factor does not affect Greece and Italy). As we mentioned already, the cost of transportation is a major obstacle to the development of gas trade. The European market for natural gas is likely to be saturated mostly with supplies from the Soviet Union and Norway that are either in existence or have been contracted for. The full utilisation of the underwater pipeline connecting Algeria and Italy may be jeopardized if gas does not prove to be sufficiently competitive to the final consumer.

A fortiori the very important reserves that have been found in the Gulf face the immediate danger of remaining undeveloped for at least two decades. While this prospect, although not a brilliant one, may still be acceptable to a country such as Qatar (where some very large gas fields are located), it certainly is unacceptable to Iran (which has much larger gas reserves than it

has oil reserves) or Iraq (whose gas reserves are a bit of a mystery, but could also be significant). It follows that these countries will need to market their gas very aggressively if they want to compete on the European market, and the best way to do so is to develop a market and transportation infrastructure in the countries that are in between. Thus, our three countries could bid for competitively priced gas supplies from the Gulf in the context of a drive from those countries to reach the Central European market with their gas.

This could prove an important locational attraction for industrial activity, and a boost to economic activity generally. The realisation of any such project, however, requires close coordination and cooperation between our countries, because alternatives exist. Thus, the gas could be transported in liquefied form (as LNG), or Iran could enter into a swap agreement with the Soviet Union - resuscitating the agreement which had been signed by the Shah and was later rescinded by the ayatollahs. In both cases, all three countries would be entirely bypassed. Alternatively, the gas could still be transported by pipeline, but the latter could cross from Turkey into Bulgaria and connect with the East-West lines that are used to export Soviet gas, bypassing Greece and Italy.

6. A further area where cooperation could be extremely important is tourism. This is a sector which is bound to experience further growth, with continuing or growing affluence in Central and Northern Europe. Our countries can offer some extraordinary historical and natural environments, and governments are increasingly realizing the economic importance of these assets and the need to protect them.

As for other service activities that we mentioned before, the complementary factors in tourist development are likely to overcome the competitive ones. While, in the end, it is true that each tourist will normally visit either one or the other of the three countries, the total volume of tourist traffic is enhanced by the availability of a variety of potentially attractive destinations in contiguous areas. Tourists will change their destination from one year to the next and visit places that they simply missed this time. As tourists become more sophisticated, the relative importance of strictly resort-related tourism will decrease, and the importance of the availability of tourist services over a broader area will increase.

For these reasons, there is a strong complementarity in developing the kind of infrastructure that will facilitate the channelling of tourist traffic from Central Europe to our countries.

In the longer run, the development of tourism opens the possibility of a gradual shift in the European economic center of gravity towards the Mediterranean. Indeed, this is how a similar process was initiated in the United States, and although conditions in Europe are in many respects different, in the long run life along the Mediterranean is likely to be consistently more pleasant than life in Essen, if personal income is kept constant.

7. When we combine all the considerations that we have been developing so far (importance of production of regionally traded goods, importance of location-specific services, importance of horizontal communications between urban production and service centres) we come to the conclusion that cooperation between Greece, Italy and Turkey could be crucially important for the further development of each of them (in the case of Italy: of the southern regions, as the northern regions are effectively part of the Central European economic system). But what kind of cooperation is needed?

The approach we have taken is a liberal and minimalist one. No great schemes are envisaged: private enterprise is best poised to pursue emerging opportunities and give content to cooperation. Governments should provide transportation infrastructure, and improve on their general services to the public, as this is simply an increasingly important part of a nation's well-being.

Minimal as these indications may appear, they are not trivial. The fact is that horizontal communications between our countries are insufficient to sustain the increased level of economic intercourse which is envisaged here. The ferries linking Italy and Greece mostly operate between Brindisi and Patras; a majority of them also stops in Corfu and Igoumenitsa, but these stops are almost useless to commercial traffic due to the poor conditions of the inland road from Igoumenitsa. On the Italian side, the loading and unloading arrangements in Brindisi are extremely messy, and commercial traffic is seriously slowed down, while tourists are confused and harassed. On the Greek side, the journey to Patras doubles the time - relative to Igoumenitsa - and tends to channel the traffic towards congested Athens. If an East-West road axis were created, linking Igoumenitsa to Salonika and then on to Turkey, the poorer northern regions of Greece would get a benefit. Finally, road communications between Greece and Turkey have not been upgraded for a long time.

Thus, there is a lot to do with respect to improving transportation infrastructure; at the same time, other conditions must be met to allow the private sector to engage in horizontal economic intercourse. In this respect, however, I shall note that in all three countries there is a tendency to greater liberalization, including the opening up to foreign imports and promoting exports, allowing greater freedom to the financial sector, encouraging capital inflows. Obviously, in all three countries a great deal of unnecessary regulations still are in force that hinder private enterprise and harass the individual citizen that engages in activities across borders. One cannot hope that these disappear overnight, but it is certainly necessary, in the long run, that they be phased out if increased intercourse is desired.

It is in this context that the question of membership into regional agreements should be discussed. Greece and Italy are members of the EC, and Turkey is associated to the latter and intends to become a full member. Some present members of the EC object to a full membership for Turkey, and as a consequence the latter result cannot be taken for granted. Is this important to our discussion of horizontal cooperation?

I believe membership in the EC to have a prevalent political meaning. The difficulties that are still met in unifying the European domestic market prove that membership is not per se a magic formula to create conditions conducive to economic cooperation. Conversely, the experience of European countries that are not members but maintain very fluid and active intercourse with the rest of Europe, the clearest case being Switzerland, shows that effective cooperation can be achieved in the absence of membership. Indeed, it should never be forgotten that the EC is much more than a mere customs union; it is a political project. Any discussion of membership in the Community that primarily emphasizes economic costs and benefits is silly, because all of the economic benefits of membership can be achieved in the absence of it, and possibly at lower costs. It is the political benefits that matter.

A convenient implication of what we just said is that I may, in this paper, refrain from expressing my view regarding Turkey's membership, and save the space that would be needed to argue for it.

8. A discussion of alternative scenarios of regional aggregation is nevertheless appropriate. We may ask why priority should be given to horizontal cooperation between our countries relative to possible alternatives.

In this respect, let me note, first of all, that the approach that I proposed does not need to be alternative to any other scheme. Indeed, if cooperation is further developed in other directions, and the web of economic interrelations is extended, then the peripheral condition of our three countries is lessened, and the incentive to cooperation between them increased. This is particularly true with respect to cooperation with the Arab countries, which can and should be actively promoted by each of us, independently of each other as well as in cooperative fashion. The same also applies to cooperation with Eastern Europe, which all EC countries are actively seeking.

In this respect, it should be noted that our horizontal cooperation should also include Yugoslavia, although the different economic system existing in that country may be expected to act as a complicating factor in a project which is essentially based on private enterprise.

But let us turn the question around, and ask what alternative each country has in case the envisaged horizontal cooperation does not develop. In this respect, it appears that Turkey is well positioned to improve her regional ties to the rest of the Middle East, while basing her relations with central Europe on classic international trade (and migration). Some regions in the Italian south have benefitted from increased trade with the southern shore of the Mediterranean, and the long-run commitment of the Italian government to achieve equalisation of economic conditions between north and south may substitute for the insufficiency of spontaneous economic processes in keeping the southern regions in line with the rest of Europe. Greece, on the other hand, appears to be weakly positioned for the development of regional trade, notwithstanding her position as member of the EC, because of distance and of the nature of economic systems in the countries that share her northern border. Although, as we just said, there is no reason to downplay the importance of cooperation with the East European countries, there are obviously limitations in the gains that can be achieved. The weakness of Greece's regional position is compounded with the smaller size of her domestic population and adds up to a relatively small incentive for the location of production of regionally traded goods. Thus, while I think that no policy conclusion ought to be drawn out of this consideration, I also think that it is appropriate to say that Greece is bound to gain most from the proposed horizontal cooperation.

9. It has always been the case, in the history of the Mediterranean, that traders have been the unifying factor while politicians acted as a disgregative force. My argument is a humble plea to let individuals and private entrepreneurs create the basis for cooperation and improved political relations in the future. It is obvious that continuing conflict involves a high cost, but since cooperation was not allowed to develop to begin with, the cost is not borne out by anyone in particular, and consequently there is no lobby to improve relations and overcome conflict. This is an old argument, but still a good one. Also, the proposed cooperation has the advantage of carrying little risk: if needs be, it can be easily undone.

In judging the importance of cooperation, one should not lose sight of the broader international environment. International competition in manufactured products markets is bound to increase dramatically as an increasing number of countries reach the stage of being able to aggressively promote their exports. While in recent decades most NICs have been relatively small countries, some very large countries such as Brazil, India and China already are or will soon become forces to be reckoned with. The Central European economy will be put

under stress by the need to readjust, and will not be able to resist political pressure to reduce protectionist barriers to entry. In short, the extent and meaning of Community preference will inevitably decline.

In the absence of a healthy regional economy, our countries do not stand a chance of resisting in the international competitive game. They will be backwaters: possibly pleasant ones, that one visits from time to time in order to enjoy the scenery and experience the suggestion of historical memories, much as one would visit the village of his ancestors. But life and opportunity will not be there.

Table 1: Exports of Greece, Italy and Turkey to the Oil Exporting Countries, 1975-81 (per cent share of total exports)

Country/Year	1975	1976	1977	1978	1979	1980	1981
Greece	12.6	14.0	14.5	14.5	14.7	15.3	18.6
Italy	10.6	11.4	12.9	12.4	10.6	12.5	16.9
Turkey	9.4	6.4	8.5	8.9	9.5	13.2	32.7

Source: IMF, Direction of Trade Statistics Yearbook, 1982

Table 2: Exports of Greece, Italy and Turkey to the Middle East, 1979-85 (per cent share of total exports)

Country/Year	1979	1980	1981	1982	1983	1984	1985
Greece	19.8	20.8	25.8	22.2	20.0	16.6	14.2
Italy	10.5	12.0	16.4	14.7	14.5	12.6	9.9
Turkey	17.3	21.6	39.9	44.0	42.3	38.6	na

Source: IMF, Direction of Trade Statistics Yearbook, 1986

Note: The IMF has changed the definition of areas, obliging to utilise the group of the oil exporting countries for certain years and the Middle East for others. The former group also includes non-Middle Eastern producers, such as Indonesia, Venezuela and Nigeria which, however, are not very important for the exports of Greece and Turkey (somewhat more important for Italy); at the same time, it excludes Middle East countries that are not oil producers. The trend, however, is clear.

iai ISTITUTO AFFARI  
INTERNAZIONALI ROMA

---

n° 177.9476