U.S.-Middle East Free Trade Coalition

October 15, 2011

US-Middle East Free Trade Coalition Discussion with USTR
On a New MENA Trade & Investment Partnership Initiative

The National Foreign Trade Council, in consultation with its members and the members of the U.S.-Middle East Free Trade Coalition* is pleased to submit the following comments on "ideas for deepening economic ties with and among MENA countries," in response to a request from the Office of the U.S. Trade Representative. The following comments represent a combination of the views of the National Foreign Trade Council, a cross section of its members, including U.S. companies and, trade associations active in the region, regional bilateral business councils and trade and Middle East experts who participated in a series of meetings over the past four months with the U.S. government, providing input to the President's announcement of the Trade and Investment Partnership Initiative with the Middle East and North Africa.

From these discussions a draft range of recommendations, observations and ideas for further consideration and development were formulated. Not all comments are endorsed by all who participated, and rather convey the range of thought on this important issue.

Key points and suggestions, which reflect all views expressed in these meetings, are outlined below.

Characteristics of the Trade and Investment Partnership Initiative-MENA Effort

Among key characteristics of the new MENA Trade & Investment Partnership Initiative is the desire to:

- Attract sustainable foreign investment to the region
- Increase access to the U.S. and European markets for countries in the region
- Increase intraregional trade within the MENA region
- Undertake a new approach of working together with the European Union to achieve these goals.

The EU has a different experience in MENA trade because of its physical proximity and traditional commercial ties. The initial focus of the initiative will be on countries that already meet or are committed to achieving certain basic standards for transparency of regulatory processes, rather than a one-size-fits-all, broad regional approach.

Egypt and Tunisia are likely initial priorities to aid in their economic reconstruction and growth to support their stability under new governments. The time frame and desired returns on investment that will be used to measure the success of this initiative are likely to be multi-phased. Therefore, ideas on both the most immediate and impactful initiatives as well as long term systemic efforts are welcome.

<u>Past Challenges Remain</u>

Past regional challenges to the success of any such initiative include:

- <u>Governance:</u> Lack of adherence to the rule of law, transparency, and accountability needed for good governance but also to attract sustained foreign investment is present in many countries and there is a wide disparity among countries in region in these areas.

- <u>Unemployment:</u> Widespread high unemployment, especially among youth, is exacerbated by a mismatch between the education system and skills demanded by the labor market.

- <u>Weak Private Sector:</u> The propensity of regional governments to create more public sector jobs hinders the more difficult long term necessity of reorienting the economy toward a free market with a strong private sector.

- <u>Conflict:</u> Political disagreements block intraregional trade. Major issues exist such as Israel and Palestine, the Iraq War, Iran, the response to terrorism, but also localized disagreements such as the dispute between Morocco and Algeria over the independence of Western Sahara impact economic cooperation. Intraregional trade would also benefit from improved incentives for trade between capital-rich and labor-rich MENA countries.

<u>The Foundation to Build Upon</u>

There are existing bilateral discussions and processes in the region to build upon, most notably the U.S. Free Trade Agreements (FTAs) with Bahrain, Israel, Jordan, Morocco, and Oman. All countries in the region have signed Trade and Investment Framework Agreements (TIFAs) with the U.S. except Syria and Iran. There is a Qualified Industrial Zone program with Egypt, Israel, and Jordan.

Some countries participate in U.S. Trade and Development Agency (USTDA) programs, some have signed agreements with the U.S. Overseas Private Investment Corporation (OPIC) and Ex-Im Bank and the Commerce Department's Commercial Law Development Program (CLDP) have programs in the region. Some of the projects in the State Department's Middle East Partnership Initiative (MEPI) promote entrepreneurship, women's economic empowerment, youth professional development, commercial and legal reform, and trade and investment. The State Department Bureau of Economic, Energy and Business Affairs also has a number of programs that promote entrepreneurship in the MENA region, such as the North Africa Partnership for Economic Opportunity (NAPEO).

Europe also has the Euro-Mediterranean Partnership, formerly known as the Barcelona Process. The EU found that existing FTAs between the EU and MENA countries did not always spur intraregional trade within the MENA region. Therefore in the new MENA Trade and Investment Initiative, the EU will likely try a new approach focused on countries that are willing to engage in reform rather than taking a broad regional approach.

Against this background, a wide ranging brainstorming session to think outside the box resulted in a range of observations and suggestions:

<u>Strategic Planning:</u>

- Include bold ideas. Feeble, modest attempts or repackaging of previous efforts will do more harm than good and risk alienating new governments by creating false expectations. Because of the bulge in the demographic pipeline, introducing vast numbers of young workers into the economy must be met with aggressive action, so efforts should be prioritized to reflect outcomes with the highest economic impact.

- In this economic climate of retrenchment, package bold ideas into a convoy approach. Actions such as increased agricultural market access or adjustments to tax policy in the context of Trade and Investment Partnership Initiative-MENA are not likely to succeed in Congress unless it is in the context of broad burden sharing from the EU and even possibly Asia.

- Don't backslide in U.S. programs for the region or merely transfer money from one pocket to the other but do target the full range of existing resources, including close coordination with the Middle East Partnership Initiative (MEPI) at the State Department. There has been momentum for reform for the past 6-7 years. Let's make sure that there isn't any loss of past progress. It is also counterproductive to assemble new initiatives when tried and true U.S. programs such as GSP for Tunisia, which produced tangible economic benefit, have been left to expire. Enhance bilateral investment treaties (BITs) with Egypt and Tunisia and diminish the role of carve-outs.

- It will be easiest to achieve tangible results in countries most receptive to reform. Perhaps the U.S. should also start on the hardest cases that require more capacity building and greater receptivity since there are more hurdles to overcome.

- Programs tailored to a specific country should focus on the areas of trade and investment most in demand (example: water technology in Saudi Arabia) and provide a mechanism to match U.S. companies to the relevant industry.

- Consider bundling an "Arab Spring" enhanced special facility at OPIC, TDA and Ex-Im.

<u>Engaging the International Community:</u>

- The planning phase occurring now should immediately engage additional stakeholders of multilateral bodies such as the Gulf Cooperation Council and the Arab Development Bank, the World Bank, the Multilateral Investment Guarantee Agency (MIGA), the IMF and others.

- Israel has an acknowledged direct vested interest in the success of efforts to stabilize new governments emerging as a result of the Arab Spring. The U.S. and the EU should engage Israel to explore partnering efforts in the initiative.

- Turkey also makes a natural and vital discussion partner due to its proximity and trade and investment ties to EU and MENA states.

- The U.S. could encourage regional development banks such as the African Development Bank or the European Bank for Reconstruction and Development to issue special facilities in support of SMEs.

- Engage a multilateral effort under the auspices of the OECD for a concerted push for MENA nations to sign on to the OECD anti-bribery convention, and couple it with a targeted capacity building technical assistance effort by the OECD to institutionalize necessary governance commitments to implement adherence to the convention. This could serve as a powerful and symbolic leapfrogging and break with the past in terms of demonstrated lack of commitment to rule of law and international standards of good governance.

- Fundamentally change the U.S. approach to engaging Gulf nations in this regional economic effort. The emergence of Gulf nations in the action in Libya has created a marked paradigm shift in their view of their role in the region. The U.S. should engage these countries as leaders rather than junior partners, and seek their guidance on this initiative. A range of variables has diminished the U.S. ability to lead in the region so the Trade and Investment Partnership Initiative-MENA provides a tangible opportunity to change our approach, serving more as a collaborator and facilitator, seeking Gulf nation guidance rather than approaching them with our view of how they should participate. This is especially relevant given both Gulf investment in the region and capacity to possibly absorb labor from other nations.

- It is important to consider best practices from other regions like Latin America and other countries like Turkey.

- In the realm of governance, transparency, anti-corruption and international cooperation, a focused strategy regarding illicit trade in the region should be developed with national governments and regional actors.

<u>Tax Policy:</u>

- To attract foreign investment, encourage a 10 year tax holiday for new investors by countries in the region, coupled with U.S. Congressional action to adopt a territorial treatment to U.S. company income generated from the new investment.

<u>Agriculture:</u>

- Agriculture is one notable area of trade with MENA countries. Because this new trade and investment partnership initiative involves both the U.S. and the EU, future market opening liberalization of agricultural imports from the region should be a joint U.S.-EU effort.

<u>U.S. Investment:</u>

- Reduced tariffs will also benefit U.S. investment in manufacturing in the MENA region. Bearing in mind that the EU and the U.S. are supposed to cooperate and not compete on this initiative, this effort represents an opportunity to encourage regional governments to enact tariff structures that do not assess higher tariffs for the import of goods (especially inputs) of U.S. origin compared to European origin. For example, Egyptian tariffs on the import of auto parts should not favor EU rather than U.S. sourced parts.

- There needs to be a focus on liberalizing tariffs at the border to promote a free flow of goods and liberal rules of origin. Some inputs for local production are tariffed. There are also tariffs on complimentary goods in some companies' product lines, which should be diminished to increase investment. We should also endeavor to reduce non-science based regulations/restrictions (SPS Barriers), particularly in agriculture.

- Reopening talks for a U.S – Egypt free trade agreement would be a positive signal for U.S. investors.

- Poor enforcement of judicial decisions remains a problem.

- There have been significant limitations on licensing in the region, usually to protect individual families' business interests.
- Documentation reduction will increase efficiency, decrease delays and decrease transportation costs.
- There are no foreign equity limitations in Egypt but they do exist in other countries in the region. Removing these limitations would increase U.S. investment.
- Corruption has been such a big issue in regional protests that government officials can be reluctant to enact new laws or regulations for fear that there will be retribution later. This is an issue in Iraq among other countries.

Services:

- One opinion holds that the U.S. should follow the EU plan to focus on trade in services in the MENA region, rather than promoting MENA manufacturing. There is some thought that there is a natural constraint to the expansion of MENA manufacturing capacity and that the region will never successfully compete with India, China or other powerhouse nations.
- Freedom of data flows, ICT, and transparency are the bedrocks of economic growth; the trade in services is essentially the trade in data. We therefore should emphasize improvements on protecting this, beyond all the work that has already been accomplished. We can base future work on the OECD principles, with the addition of language on transparency and a general enhancement of the standards.

Intraregional Trade and Investment:

- A fundamental economic fact is in that many ways, MENA countries are more similar than complementary. In terms of manufacturing, for the most part there are striking similarities in the range of products produced throughout the region. The complementary symbiotic relationship which should be energized is the export of capital, labor and knowledge among the countries of the region.
- The U.S. has devoted substantial efforts toward a Middle East Free Trade Area by creating a series of bilateral Free Trade Agreements between the U.S. and Israel, Jordan, Morocco, Bahrain and Oman. This trajectory should be strongly incorporated into any new initiative with a sustained effort to knit these agreements together through study to integrate or cumulate rules of origin and determine how existing FTA's play a key part in new initiatives.
- Previously, the U.S. came within weeks of announcing the initiation of Free Trade Agreement Negotiations with Egypt. Because the effort was commonly perceived to be suspended because of political issues with the Mubarek government, an FTA with Egypt is inextricably linked to tacit support of political reform. Therefore, an FTA now serves as a potent signal of support to not only the Egyptian efforts of economic and trade liberalization. An announcement of interest to re-opening discussions leading to initiation of a U.S-Egypt FTA will serve as a powerful catalyst to sustained economic liberalization and support for the new path upon which Egypt has embarked.

- The U.S. and the EU could form partnerships with capital-rich MENA countries to share funding and expertise for programs in capital-poor countries where their interests intersect. Regional leaders are likely to have their own opinions on U.S. and EU involvement in the region. Broad cooperation, where possible, could create multiple dividends.

- In consultation with stakeholders, identify a short list of very specific efforts to improve cross border supply chain cooperation. For example, remove the political and regulatory impediments to Algeria selling gas to Morocco for their phosphate fertilizer production.

- Transportation infrastructure between MENA states is key. Improve and increase the number of open skies programs and regional equivalents. This will be important for interstate trade. Encourage "principles of FTA Investment Agreements" to assist and streamline the system. Supplier trade missions could be useful as well.

- Current QIZ programs should be re-examined for their effectiveness. In Jordan, the U.S.-Jordan FTA supersedes the QIZ program. In Egypt, consultation with the new government to use QIZs more creatively to industries beyond textiles could be beneficial.

- The QIZ model could provide inspiration for other manufacturing export zones. A new type of QIZ would probably work best if it moved beyond Israeli content requirements and focused on diversifying the participating sectors.

<u>Actions to Diminish and Eliminate Illicit Trade</u>

- Good governance, including rational, consistent and enforced rules over the long term, have proven to be essential to the creation of a productive environment for entrepreneurs, investors and free enterprise. Strengthening and broadening coverage in the economic rule of law increases economic opportunity, and serves as a multiplier in enhancing public welfare and national security.

  Illicit trade in contraband and counterfeit goods through smuggling, illegal transportation, distribution, sales and black market activity increase the barriers to the unemployed and aspiring youth entrepreneurs to create new legitimate businesses in the region, avoids regulatory processes that provide for the health and safety of the population, and undermine national tax bases and government revenue. Such illegal trade channels finance criminal operations that extend beyond market goods to terrorism, drugs and human trafficking. In some cases, illicit trade channels threaten to overshadow nations' integration into a rules based global economy because they constitute unfair competition to legitimate business.

  Drawing upon the resources and expertise of the United States, the European Union international organizations and governments in the region, a coordinated strategic focus on dramatically curtailing illegal trade in contraband and counterfeit goods would not only enhance the environment for sustainable business growth, but it would promote security. Provisions in the most recent U.S. free trade agreements are not sufficient by themselves to create an enforceable legal framework to arrest illicit commerce, which includes activity beyond piracy and counterfeiting with respect to intellectual property rights (IPs). Additional focus is needed not only with respect to the customs and IP provisions, but in additional areas of discipline. Moreover, to arrest illicit commerce will require concerted focus by a range of government actors and stakeholders. Recognizing this, the Trade and Investment Partnership Initiative - MENA offers a new opportunity for collaborative effort in this area.

Education and Employment:

- Some GCC countries have educational partnerships between local universities and U.S. or European institutions, as well as branch campuses of foreign universities. Countries outside the Gulf would also benefit from such partnerships.

- Education efforts should be carefully thought out to address labor market trends. In addition to universities, many countries need basic childhood education reform and access. Education efforts in general should be balanced to serve not just the elite and economically advantaged. Vocational and skills training is sorely needed and could produce more immediate results. In the longer term there are lessons to be learned from the experience of India in balancing the creation of universities with technical training and part time and continuing education to reach the masses.

- The sheer volume of young people entering the labor market dictates that bold efforts to inspire entrepreneurial business creation must occur. The World Bank "Doing Business" benchmarks the regulations that enhance business activity and those that constrain it serves as a good tool to identify specific needed improvements in various countries. The April 2011 report on "Doing Business in the Arab World" may be found at: http://www.doingbusiness.org/reports/regional-reports/arab-world

***U.S.-Middle East Free Trade Coalition**

Since 2004, the U.S.-Middle East Free Trade Coalition, with more than 100 U.S. member companies, trade associations and other organizations, has supported the expansion of trade, investment and commercial ties to foster economic development with countries of the Middle East. Managed by the National Foreign Trade Council, the coalition supports the negotiation and conclusion of commercially meaningful free trade agreements between the United States and nations in the Middle East; accession to the World Trade Organization by Middle Eastern nations; and other efforts to build trade capacity and economic liberalization to facilitate more robust trade within the region. The coalition also supports renewed U.S. government efforts to build on existing agreements to promote greater integration with U.S. and European markets, and open the door for those countries who adopt high standards of reform and trade liberalization to construct a regional trade framework.

National Foreign Trade Council

Advancing Global Commerce for Nearly a Century - The National Foreign Trade Council (www.nftc.org) is a leading business organization advocating an open, rules-based global trading system. Founded in 1914 by a broad-based group of American companies, the NFTC now serves hundreds of member companies through its offices in Washington and New York.