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## **A THREATENING OPPORTUNITY: PRESIDENT BUSH'S PROPOSAL FOR A FREE TRADE AGREEMENT WITH THE MIDDLE EAST**

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On 9 May 2003, President George Bush proposed the creation of a free trade agreement (FTA) between the United States and the Middle East within ten years. A White House press statement confirmed that this was being proposed through the negotiation of bilateral FTAs.

The US has FTAs with Israel and Jordan and is discussing the creation of another with Morocco. The FTA with Jordan, which came into effect in December 2001 together with the operation of Qualified Industrial Zones, has led to a dramatic increase in Jordanian exports to the US: from, \$16 million in 1998, to \$412 million in 2002. This made possible the creation of 40,000 new jobs, mainly in the garment industry, at a time when Jordan faced the *intifada* to its west and the build up to war in Iraq to the east. US exports to Jordan were unchanged at about \$350 million a year, so Jordan's trade deficit with the US was eliminated.

In 2001, the United States GDP came was \$9,600 billion and it imported goods and services worth \$1,180 billion. Only \$31 billion came from the Arab world. Arab national income totaled \$560 billion, with exports of goods worth

about \$240 billion, of which only \$40 billion were manufactured goods. The US exported \$17 billion to the Arab world. These figures show the enormous disproportion between the Arab states and the US, but they also suggest huge potential for increased Arab exports. Such exports could provide vitally needed employment and income in the rest of the region, as they have in Jordan.

The US proposal is not the only one on the table. In The Barcelona Declaration of 1995, the European Union proposed the creation of a Euro-Mediterranean Free-Trade Area by 2010. The EU is also an economic giant, with a 2001 national income of almost \$8,000 billion and imports of \$1,300 billion (excluding exports from EU countries to each other). 2001 imports from the Arab states equaled \$67 billion, while exports to the Arab world came to \$73 billion. The EU's aim was to link the 15 EU member states and with the 12 Mediterranean non-member partners. Together with European Free Trade Area (EFTA) states and the Central and Eastern European candidate countries that will begin joining the EU in 2004, this zone could

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eventually include some 40 States and 600-800 million consumers. Given Europe's proximity to the Middle East, the Euro-Med FTA may have greater potential than the American-proposed plan.

The World Bank's chief economist has stressed the importance of improving access for developing countries to the markets of the developed world. The Bush proposal does just this: it offers duty free access to US markets for goods and services made in the Middle East. The US is more liberal than the EU in its interpretation of international trade rules. One crucial issue is that of rules of origin: how much of a product's inputs can be imported before it can no longer be defined as locally produced. A more liberal interpretation of the rules of origin allows and even encourages countries to cooperate in production, thus providing incentives for the creation of free trade zones *within* the Middle East.

Outside the Middle East, many countries have benefited from increased integration into the international economy. South Korea, China, India and Vietnam have all massively increased their manufactured exports, employment and income levels as a result. Israel and Turkey have done the same. Between 1989 and 1999, these six countries increased their merchandise exports by over 120%. Of the non-oil states in the Middle East, the more liberal economies of Morocco and Tunisia increased their merchandise exports by 113% while the relatively inward-looking economies of Egypt, Lebanon and Syria increased theirs by only 28%.

The economic danger for Arab states of a free trade agreement with the US (or the EU) is that they will be flooded with imports as their import taxes and other restrictions fall. This would affect both domestic production and a revenue base that relies on easy-to-collect import taxes. Egypt signed an FTA agreement with the EU in 2001 but is in the middle of a prolonged debate about ratification which is colored by precisely these considerations.

The US clearly wants to increase its exports to Arab countries. Encouraging their economic development and thus their appetite for imports can help this to happen. So can free trade arrangements that surpass or at least compete with those offered by Europe. Although the EU wants to protect its large market share in these countries, it also wants to promote their general development, not least because it fears that the exodus of unemployed Arab workers will increase if Arab economies do not improve. And like the US, it also wants to maintain its supplies of energy from the Middle East. Despite this, the EU has not fully opened its markets for agricultural commodities and certain basic manufactures in which non-oil Arab states have comparative advantage.

Selling abroad is not easy and free trade agreements do not automatically mean the end of all restrictions, which also include such pernicious, hidden trade barriers such as subsidies to agricultural producers in rich countries – on which in 2001 the EU spent \$95 billion and the US \$49 billion. Developing countries need marketing skills, quality control, and efficient ports and transport systems to get their goods to foreign markets. They also need business-friendly governments. All of these factors are in short supply in the non-oil Arab states, although the situation is better in Morocco and Tunisia than in Egypt and Syria.

Freer trade implies a larger role and greater autonomy for the private sector and a smaller role for government. Although authoritarian regimes in other parts of the world have managed to push economic liberalization while maintaining political control, in the Arab world, political and economic control usually go hand-in-hand. For this reason, it is not surprising that governments in the region have been ambivalent in their responses to free trade proposals, whether they emanate from Europe or the United States.