A Middle East Free Trade Area: Economic Interdependence and Peace Considered

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ABSTRACT:

The Bush administration hopes that through a Middle East Free Trade Area (MEFTA), peace and stability can be achieved through intra-regional economic cooperation. The current impediments to intra-regional economic cooperation, however, will make a MEFTA a hub and spoke trade relationship between the United States and the Middle East. Neoliberal arguments for the interrelation of peace and economic interdependence in the context of the Middle East are then considered.

Keywords: MEFTA; Middle East economic integration; US Economic Policy in the Middle East

A MEFTA: ECONOMIC INTERDEPENDENCE AND PEACE CONSIDERED

INTRODUCTION:

The Bush administration has recognized that peace and stability in the Middle East is needed to achieve the United States' long term national interest. Accordingly, the United States has recently embarked on an ambitious agenda to control the Middle East. Besides the Bush administration's political and military interventions into the region's affairs, the American government has recently proposed expanding trade and economic relations with friendly Middle East states. To advance America's strategic interests further, the administration has resorted to use its economic instruments of power. Robert Zoellick, then US Trade Representative, had proclaimed that the United States' credo would be to advance trade and economic liberalization- bilaterally, regionally, and globally- as tools toward enhancing American political control and influence.[1] This credo has been adopted in the US' plans for a Middle East Free Trade Area (MEFTA) to be completed in 2013.

The proposed MEFTA builds on previous administrations' attempts to increase intra-regional economic cooperation. The MEFTA plan would encourage Middle East states to adopt economic liberalization, join the World Trade Organization, protect American corporate investment, and modernize their political and economic systems. The US administration and Congress hope that MEFTA would spur friendlier relations with the Middle East and within the region. The US government has often cited the US-Jordanian Free Trade Agreement as a guide for other Middle East states to follow. The MEFTA plan could backfire, however, as structural barriers have limited past attempts to spur intra-regional economic cooperation and trade. A hub-and-spoke relationship

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[1]Robert B. Zoellick, "Our Credo: Free Trade And Competition" *The Wall Street Journal*, July 10, 2003,http://www.ustr.gov/speech-test/zoellick/2003-07-10_WSJ.htm.

results in minimal economic benefit accruing to the Middle East and in minimal intended political benefits to the United States. Moreover, past and present American intervention in the region have been skeptically viewed as forms of neo-imperialism. Increased economic ties with the United States could then exacerbate conflict and turmoil in the region. Like other American attempts to bring peace and stability to the region, the road to MEFTA can be a perilous journey.

THE ROAD TO MEFTA:

The Declaration of Principles signed in 1993, ushered in a great sense of optimism on the prospects of both political and economic cooperation in the Middle East. The future of the Middle East seemed relatively bright and promising as Israelis and Palestinians took a historic step toward peace and mutual respect. A peaceful Middle East, it was proposed, would usher in political stability and economic prosperity. In 1993, one leading architect of the peace plan, Israeli Shimon Peres, envisioned that:

> The next stage, after bilateral and multilateral relationships have been established, will entail formation of regional industries through the cooperation of international bodies and independent international consortiums. At this point, the regional economic process will be upgraded and the new reality, in which business precedes politics, will be instituted. Ultimately, the Middle East will unite in a common market- after we achieve peace. And the very existence of this common market will foster vital interests in maintaining peace over the long term.[2]

The ‘New Middle East’, as Peres called it, would become an economic bloc to compete with other regional economic associations. Trading partners in the Middle East do not have to initially like or trust each other, as was the case with the European Union and the Maastricht Treaty; with time, however, political and cultural harmony could be built upon the foundation of economic

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[2]Shimon Peres and Arye Naor. *The New Middle East* (New York: Henry Holt and Company, 1993) p.99.

cooperation.[3]

The Clinton administration wanted to bolster economic cooperation among prospective peace partners in the Middle East. The Clinton administration carried its message for economic integration to Middle East and North Africa (MENA) economic conferences. At the 1994 MENA conference in Casablanca, Secretary of State Warren Christopher stated that his government's mission was to:

> Transform the peace being made between governments into a peace between peoples. Governments can make the peace. Governments can create the climate for economic growth. But only the people of the private sector can marshall [sic] the resources necessary for sustained growth and development. Only the private sector can produce a peace that will endure.[4]

The US administration expressed similar messages of the need for economic cooperation in the region at subsequent MENA conferences in Amman, Cairo, and Doha. These annual MENA conferences, which were established pursuant to the Declaration of Principles, became a forum intended to help begin economic integration between Israeli and Arab participants.

Two American initiatives for Middle East economic cooperation, the MENABANK and the Regional Business Council, were formulated at the Casablanca Economic Summit. The MENABANK was a proposed regional bank for states that opted to participate in the peace process. The bank was to be located in Cairo and to have a startup capital of $5 billion with annual loan disbursements of $1 billion. Financiers of the MENABANK would have included several G-8 states, three Maghreb states and the United States; the latter would have been the largest contributor with

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[3]Rodney Wilson. "The Economic Relations of the Middle East: Toward Europe or Within the Region?" *Middle East Journal* 48, no.2 (Spring1994): 276.

[4]Warren Christopher, "Prosperity in the New Middle East: building the structures of peace," (Speech, 1995 Middle East/North Africa Economic Summit, Casablanca, December 1, 1994).

21% of the bank's proposed liquidity. The four core peace partners, Egypt, Jordan, Israel and the Palestinian Authority would also contribute 4% each to the bank's liquidity.[5] Another important American initiative inaugurated at the Amman Economic Summit, was the Regional Business Council (RBC). The RBC would coordinate private sector representatives from the peace partners to increase intra-regional trade. The council would work with the governments of peace partners and act as a quasi Chamber of Commerce. American financial and political support for both the MENABANK and the RBC were key to the realization of these initiatives.[6]

In 1995, President Clinton went a step further to promote economic interdependence in the Middle East. Clinton announced that he would propose expanding the existing US-Israeli Free Trade Agreement to include Jordan, Egypt, and the Palestinian territories. For the United States, the economic benefits of promoting this free trade area were few, but the political gains of long-term peace and stability in the region were invaluable. In presence of officials representing the proposed parties, President Clinton remarked:

> ...if you agree to establish industrial zones in the West Bank and Gaza and elsewhere, I am prepared to go to Congress and seek approval for extending duty-free treatment to products coming out of those zones. Of course, in the end, the economic and political cooperation among all of you will be the most important thing in reaping economic progress. But I want to do our part.[7]

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[5]David J. Dunford, "MENABANK: Would US Membership Help the Peace Process?" *Peacewatch* 159 (Washington Institute for Near East Policy, March 20, 1998), http://www.washingtoninstitute.org/watch/peacewatch/

[6]Dalia Dassa Kaye, "Banking On Peace: Lessons From The Middle East Development Bank" *IGCC Policy Papers*. (Working Paper, Institute on Global Conflict and Cooperation, October 1, 1998). p5.

[7] William J. Clinton, "Remarks at a Meeting with Middle Eastern Leaders, February 12, 1995," *Public Papers of the Presidents of United States*. 1 (Washington, DC: GPO, 1995),193.

The Clinton administration was slowly enticing peace partners into a vision for regional economic integration, hoping that this would achieve American strategic interests in the Middle East. Prior to publicly announcing the free trade plan, the White House attempted to get Congressional support, but this quickly dissipated.[8] Legislative difficulties in implementing Clinton's proposals were evident, as Congressional members wanted to avoid endorsing the Clinton plan.

The Clinton administration managed to initiate the 1996 Qualifying Industrial Zones (QIZ) program amid Congressional opposition. Under the QIZ program, Jordanian exports from specific industrial parks, or zones, were given duty-free access to the US market. Products that were eligible under the QIZ required 35 percent of their value-added be of either Israeli, Jordanian (QIZ) or West Bank/Gaza origin. Jordanian export products also required 8 percent of Israeli content. Israeli-Jordanian customs officials jointly controlled and valuated rules of origin. The QIZ program, with no expiration date, gave Jordanian textile manufacturers unprecedented and valuable access to the lucrative US market. Jordan became the first beneficiary of the Clinton vision for Mideast economic integration.

In the Clinton administration's second term in office, the administration had a difficult time in advancing earlier Mideast economic proposals; these difficulties were attributable to both external and domestic factors. In Israel, the 1996 election of the right-wing government of Benjamin Netanyahu had soured peace efforts in the region. Many Arab countries, including Egypt, had boycotted the 1997 Doha economic summit in protest to the policies of the Netanyahu government. By 1998, Congress was firmly against funding the MENABANK and several other international

[8] John Maggs, "Clinton Proposes Broader Mideast Trade Accord Plan Involves Zone Shared by Israel, Jordan and Egypt," *Journal of Commerce Newspaper*, (February 14, 1995), http://www.joc.com/news.

financial institutions. Overall, there appeared to be little interest in continuing talks on Arab-Israeli economic integration due to stalled peace negotiations. By 1999, the MENA conferences, the regional bank, and the RBC seemed to be an illusive dream.

Despite a series of political setbacks, the Clinton administration initiated US-Jordanian trade talks near the end of its term. At the time, US Trade Representative Charlene Barshefsky stated that "free-trade talks are not a substitute for peace negotiations, but they can help by giving countries a stake in each other's prosperity.".[9] Signing of the US-Jordan Free Trade Agreement (FTA) on October 24, 2000, reinvigorated interest in advancing economic cooperation in the Middle East. The US-Jordan FTA was the first of its kind with an Arab country and fourth only to Israel, Canada, and Mexico. The FTA included removing tariffs on manufactured goods and farm products by 2011, removing all trade barriers in services, and enforcing intellectual property rights in Jordan. Proponents of the US-Jordan FTA note that the agreement was historic and progressive for including labour and environmental protection within the agreement as opposed to being in a side agreement. Products eligible under the US-Jordan FTA required 35 percent Jordanian content, intended to spur local production. In its first year, Jordan increased exports by 213 percent from, created 30,000 new jobs, and developed its textile sector.[10] Moreover, by 2002 Jordan had a marginal trade surplus with the United States. Overall, the United States hoped that a US-Jordan FTA would demonstrate the positive effects of intra-regional economic cooperation to other Arab countries.

President Bush again refreshed interest in furthering regional economic cooperation on May

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[9]Reuters, "US, Egypt should consider trade pact," December 13, 2000, http://www.arabia.com/..

[10] Jordan Times, "Fact Sheet: US-Jordan bilateral trade," December 9, 2002, http://www.jordanembassyus.org/12092002005.htm.

9, 2003, in an address on the prospects for peace in the Middle East. Bush remarked that

> Across the globe, free markets and trade have helped defeat poverty, and taught men and women the habits of liberty. So I propose the establishment of a US -Middle East free trade area within a decade, to bring the Middle East into an expanding circle of opportunity, to provide hope for the people who live in that region. We will work with our partners to ensure that small and mid-sized businesses have access to capital, and support efforts in the region to develop central laws on property rights and good business practices.[11]

With Congressional approval for general fast-track authority, the President's proposal for a Middle East Free Trade Area (MEFTA) had been given the green light. The Bush administration launched his initiative at the 2004 G8 summit in Sea Island. The Bush administration planned to see a MEFTA materialize within ten years. The President's MEFTA proposal is based on a six-prong approach.[12]

First, the US government intends to support Middle East countries' accession to the World Trade Organization (WTO). At the moment, Egypt, Israel, Jordan, Bahrain, Morocco, Oman, Turkey, and Kuwait are WTO members. The United States helped Saudi Arabia to join the WTO in late 2005, and is helping Lebanon, Algeria, and Yemen in negotiations with the WTO.[13] The oil-rich Arab Gulf states were among the last of Middle East countries to join the WTO. Analysts had argued that it would be difficult for many Arab Gulf states to fulfil the needs and requirements of WTO accession, as their wealth has delayed economic liberalization.[14] The United States effectively

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[11]George W. Bush, "President Bush Presses for Peace in the Middle East," *White House News Releases*, May 9, 2003, http://www.whitehouse.gov/news/releases/2003/.

[12]Office of the United States Trade Representatives, "Middle East Free Trade Initiatives" *Trade Facts*, June 23, 2003, http://www.ustr.gov/.

[13]Robert Zoellick, "Global Trade and the Middle East: Reawakening a Vibrant Past," (Remarks, World Economic Forum, Dead Sea, Jordan, June 23, 2003), http://www.ustr.gov/.

[14]See Cecilia Klein, "Joining the Global Rules-Based Economy: Challenges and Opportunities for the GCC," (Remarks, Twentieth in the Capitol Hill Conference Series on US

helped to encourage Gulf states' membership into the trade organization.

Second, the United States will continue to negotiate Trade and Investment Framework Agreements (TIFAs). These agreements work to advance economic liberalization in developing countries. Specifically, many agreements work to advance intellectual property rights protection, liberalize services, protect and advance US investment, and enhance bilateral trade. Many see the TIFAs as springboards to free trade with the United States. That said, Egypt has worked very hard to achieve a free trade agreement with the United States despite having one of the longest TIFAs in the region.[15] This is telling perhaps, that despite Egypt being the second largest US foreign aid recipient, it has not achieved a bilateral FTA. The United States has existing TIFAs with Morocco, Egypt, Turkey, Tunisia, Algeria, Bahrain, and other Middle East states (see Table 1).

Third, the US government will enlarge its Generalized System of Preferences (GSP) program to encompass more Middle Eastern products. The GSP gives one-way tariff exemption for more than 4,650 products, excluding most textiles, from a list of eligible developing countries. Most of Middle Eastern countries are eligible, excluding the oil-rich Gulf states (See Table 1 for complete list). Despite being deemed ineligible for the GSP program under Saddam Hussein, the US government helped qualify Iraq, in an effort to jump-start Iraq's export economy.[16] It should be noted that Congress has renewed the GSP program to 2006, granted under the Bush administration's fast-track

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Middle East Policy, Middle East Policy Council, Washington, DC, February 1, 2000), http://www.mepc.org/public_asp/forums_chcs/20.asp/.

[15]See Bessma Momani. "Promoting Economic Liberalization in Egypt" *Middle East Review of International Affairs*. 7, no. 3 (September, 2003)

[16]See Robert Zoellick, "Roundtable with Robert B. Zoellick," (Remarks, at the Marriott Hotel, Dead Sea, Jordan, June 23, 2003), http://www.ustr.gov/releases/2003/06/2003-06-23-jordon.PDF.

authority, however, the GSP program has expired and lapsed in the past due to Congressional stonewalling. Therefore, the administration cannot promise Middle East countries access to the US market under the GSP program beyond 2006.

Fourth, the US government will try to negotiate Bilateral Investment Treaties (BIT) with Middle Eastern states. The BIT program protects American private business interests in foreign countries. This protection includes fair admission treatment of American investment under domestic laws, proper reparation in case of expropriation, right to repatriate capital profits and right to a dispute settlement outside of the host country. The United States further requires signatories of the BITs to commit to complying with the WTOs Trade Related Aspects of Intellectual Property Rights (TRIPS).[17] Bahrain, Egypt, Jordan, Morocco, Turkey, and Tunisia are all signatories of the BIT program.

Fifth, the US government will set up a Middle East Partnership Initiative (MEPI) plan, of an additional $29 million to the $1billion already committed to help finance development projects in the Middle East. The MEPI plan, originally announced by Colin Powell on December 12, 2002, attempts to address unemployment, women's issues, political governance issues and education.[18] The US MEPI will address social, political and economic shortcomings that were highlighted in the Arab Human Development Report 2002, written by Arab academics under the auspices of the United Nations Development Programme.

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[17]US State Department, "U.S. Bilateral Investment Treaty Program," http://www.state.gov/e/eb/rls/fs/22422.htm

[18]Colin Powell, "The US-Middle East Partnership Initiative: Building Hope for the Years Ahead," (Speech, at the Heritage Foundation, Washington, DC, December 12, 2002), http://www.state.gov/secretary/rm/2002/15920.htm.

Finally, and most important, the United States intends to bilaterally negotiate free trade agreements with Middle East countries that agree to economic liberalization. A US-Morocco FTA was finalized at the end of 2003, negotiations on a US-Bahrain FTA were completed in 2004 and Congressional approval is still pending, and the US administration signed a trade agreement with Oman and has been in negotiations with the United Arab Emirates. Trade agreements with Morocco and Bahrain would give the United States an Eastern and Western point of trade in the Middle East, with Jordan in the centre. The United States hopes to encourage intra-regional trade along the East-West axis and create a domino-effect of potential signatories. 'Cumulation clauses' in US-FTAs would facilitate this domino-effect, where neighbours of US trading partners could have their input products be considered for tariff exemption.[19] Egypt, Tunisia, and Saudi Arabia are expected to sign US FTAs in the medium-term. A US-Egypt FTA has been under negotiations since the mid-1990s. In late 2004, Egypt signed a pact with the United States and Israel to set up Qualifying Industrial Zones that gained Egyptian products made with Israeli content access to the US market. Before accepting a US-Egypt FTA, Egypt has to complete customs reforms, intellectual property right reforms, and remove textile and meat bans.[20] The fate of Iraq in MEFTA had been initially undecided. The US government claimed it first wanted to ensure security, lift the oil sanctions, resolve outstanding Iraqi debt, and develop commercial laws before addressing Iraq's role in

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[19]Zoellick, "Global Trade and the Middle East: Reawakening a Vibrant Past,".

[20]Robert Zoellick, "Transcript of the Press Availability," (Remarks, at Jollie Golf Conference Center, Sharm El Sheik, Egypt, June 22, 2003), http://www.ustr.gov/releases/2003/06/2003-06-22-sharm.PDF ; David Welch, "US Ambassador's Speech to the American Chamber of Commerce in Egypt" (Speech, American Chamber of Commerce in Egypt, Cairo, May 28, 2003), http://amcham.org.eg/operation/events/Events03/David%20WelchSpeech.asp.

MEFTA.[21] However, Iraq signed a TIFA in July 2005, received access under the GSP, and is now in negotiations with the WTO, despite not having achieved the political stability first laid out by the US administration.

Following President Bush's announcement of a proposed MEFTA, members of the US Senate and House of Representatives introduced the Middle East Trade and Engagement Act of 2003. The bill proposes an expanded Middle East Free Trade Area to any country that promotes economic liberalization and "supports a peaceful resolution to the Israeli-Palestinian conflict".[22] Notably excluded from the plan would be Sudan, Libya, Syria ,and Iran.[23] Eligible Middle East countries will be invited to annual trade meetings with high-level US officials from the Departments of Commerce, Trade, State, and Treasury. These meetings, referred to as US-Middle East Trade and Economic Cooperation Forums, will serve to discuss advancing bilateral and intra-regional trade and investment.

In June 2003, US Secretary of State Colin Powell and US Trade Representative Robert Zoellick, went to the World Economic Forum, hosted by Jordan, to sell the US MEFTA plan to the Middle East, to private investors and to the world. At a meeting of regional and world leaders, Powell commented that:

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[21]See Zoellick, "Roundtable with Robert B. Zoellick,".

[22]US Congress, House, Committee on Ways and Means, *Middle East Trade and Engagement Act of 2003*, HR 2267,108th Cong., 1st sess., May 22, 2003.

[23]Based on the Bush Administration's proposed Middle East Trade and Engagement Act of 2003 before Congress, eligible countries will include: Afghanistan, Algeria, Azerbaijan, Bahrain, Bangladesh, Egypt, Iraq, Kuwait, Lebanon, Morocco, Oman, Pakistan, Qatar, Saudi Arabia, Tunisia, Turkey, United Arab Emirates, and Yemen. The Palestinian Authority, and any potential successor is eligible as long as it does not partake in terrorism and accepts the state of Israel. Libya's status still remains unclear despite a warming of relations with the West.

> We want peace in the region, but with peace you need economic development or the people will not benefit from that peace, and to get economic development you also need investment in the human capital that exists in the region...Peace, economic development, infrastructure development, investing in human capital, breaking down barriers to trade, making sure systems are transparent, making sure that we are in trading systems that rest on the rule of law, and that there is confidence in each of these countries, so that investors will go there with confidence that they will not be putting their capital at risk and get a return on their investment and at the same time invest in the future of their country.[24]

President Bush again sold the idea to Middle East leaders at the 2004 G8 Summit meeting in Savanah, Georgia. More than a decade after the signing of the Oslo Accords, the US government is again reinvesting into the idea that economic interdependence can bring peace to the Middle East. The United States hopes that a MEFTA will foster intra-regional economic cooperation, particularly with Israel, and peace and stability in the conflict-ridden Middle East.

STRUCTURAL BARRIERS TO INTRA-REGIONAL ECONOMIC COOPERATION:

Despite relative similarities in culture, language, and tradition, intra-regional economic cooperation in the Middle East is one of the lowest throughout the world. According to the World Trade Organization, for example, intra-regional exports of merchandise in the Middle East have accounted for 5.6 percent of total exports in 2004, down from 7.6 percent in 2002; these figures are even lower than intra-regional exports in Africa.[25] In contrast, members of APEC, NAFTA, and the EU each have more than 50 percent of their exports directed within their respective regions (See

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[24]Colin Powell, "Joint Press Briefing at the World Economic Forum With Jordanian Foreign Minister Marwan Muasher; Robert B. Zoellick, U.S. Trade Representative; and Jordanian Minister of Trade Salah Bashir" (Remarks, at Dead Sea, Jordan, June 23, 2003), http://www.state.gov/secretary/rm/2003/21982.htm.

[25]World Trade Organization, *International Trade Statistics 2002; 2004.* (Geneva: WTO, 2002; 2004), 42. These statistics include Israel, Iran and Cyprus but exclude Arab North African states.

Figure 1 for a comparison).[26] Even if one were to argue, as a team of World Bank economists had suggested, that intraregional Arab trade is not as dim if oil is factored out, the nominal amounts of intraregional arab trade is still one the lowest of all regions.[27] Moreover, if one were to exclude oil exports from Arab intraregional trade, Arab countries exports within the region exceeded 30% of total exports in two of 40 years examined (See Figure 2).

Attempts to increase intra-regional economic cooperation from within the region have been initiated. Recently, the Gulf Cooperation Council- comprising of Saudi Arabia, United Arab Emirates, Oman, Kuwait, Qatar, and Bahrain- have been working toward regional integration of their oil-rich gulf states by establishing a customs union, harmonizing customs tariffs, and planning for a common currency. They have significantly increased nominal intraregional trade, but this still accounts for a very small fraction of their total exports. More significantly than the GCC, has been the 1997 Arab League agreement for an intra-regional free trade agreement, called the Greater Arab Free Trade Area (GAFTA). The GAFTA requires Arab states to remove tariffs on agricultural and manufactured goods, phased in through 2008. Intra-regional economic cooperation and trade, however, continues to be limited because of four interrelated factors that are chiefly structural.

First, Middle East countries in their respective subregions have similar resources and production structures; accordingly, each country has a low comparative advantages with its

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[26]Ahmed Galal and Bernard Hoekman, “Arab Economic Integration Between Hope and Reality,” *Policy Viewpoint* no.12 (Cairo: The Egyptian Centre for Economic Studies, October 2002), 1.

[27]See Kemal Dervis, Peter Bocock, and Julia Devlin. “Intraregional Trade Among Arab Countries: Building a Competitive Neighborhood. Paper presented at the Middle East 52nd Annual Conference. Washington, D.C., (1998).

neighbour.[28] Although there are distinctions within the Middle East, namely oil-exporting rentier states and import-substitution industrialization states, there tends to be little complementary trade patterns. This lack of complementing trade patterns explains why countries of the Middle East trade with the European Union, a large market and source of goods that is geographically close. Moreover, it has been noted that for some countries the difficult physical terrain of the Middle East discourages East-West trade and for the Arab Maghreb encourages North-South trade with Europe.[29]

Second, each Middle East economy is relatively small and unable to provide economies of scale in production.[30] There is a significant amount of state-ownership in the region, spurring inefficient and protected industries that further limit the successful adoption of an export strategy. Moreover, state-owned enterprises inhibit intra-industry trade, as few input goods are used from neighbouring Arab states. The lack of intra-industry trade is particularly prevalent in the oil-rich countries that are protective of its oil industry.[31]

Third, there is a wide disparity of income among Middle East countries; therefore, states

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[28]Samiha Fawzy, "The Economics and Politics of Arab Economic Integration," in *Arab Economic Integration* Ahmed Galal and Bernard Hoekman (Eds.) (Washington, DC: Brookings Institution Press, 2003).

[29]Hassan Al-Atrash and Tarik Yousef, "Intra-Arab Trade: Is it too Little?" *IMF Working Paper* WP/00/10 (Washington DC: IMF, January 2000), 9-10.

[30]Bernard Hoekman and Patrick Messerlin, "Initial Conditions and Incentives for Arab Economic Integration," *Policy Research Working Paper* No.2921 (Washington DC: World Bank, October 2002), 13.

[31]Hoekman and Messerlin. "Initial Conditions and Incentives for Arab Economic Integration," p.15.

have different consumption patterns and production strategies.[32] For example, oil-rich Arab states prefer to import European and American high-end goods, not efficiently produced in Arab production states. Also, Israel's comparative advantage in high technological products, imported by American and European firms, are unsuitable to Arab countries' production strategies.[33]

Fourth, the Middle East is characterized by a high degree of both tariff and non-tariff barriers. In a survey of Middle East business people, among the hurdles to intra-regional economic cooperation were non-tariff barriers that included

> business licensing, public sector monopolies, exclusive agency laws, requirements to employ nationals, weak systems of contract enforcement, prohibitions on foreign ownership of real estate, limitations on majority equity ownership by foreigners and corruption and red tape...[34]

Moreover, these policies discourage both foreign investment and intra-regional investment. Proponents of intra-regional economic cooperation suggest that these non-tariff barriers are changeable with policy reforms. It is argued, however, that these policy reforms in the Middle East require a fundamental reversal of the social contract and of state-civic relations. Others add that the very authoritarian political structures of many Middle East states is the underlying structural barrier to economic integration with the Middle East.[35] That said, many Arab states

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[32]Hoekman and Messerlin. "Initial Conditions and Incentives for Arab Economic Integration," p.13.

[33] Paul Rivlin, "Trade Potential in the Middle East: Some Optimistic Findings," *Middle East Review of International Affairs*. 4, no.1 (March 2000): 57, http://meria.idc.ac.il/journal/2000/issue1/jv4n1a6.html.

[34] Bernard Hoekman and Patrick Messerlin, *Harnessing Trade for Development and Growth in the Middle East* (New York: Council on Foreign Relations, 2002),13.

[35]Mehran Kamrava "Structural Impediments to Economic Globalization in the Middle East," *Middle East Journal* Vol.6, No.4 (Winter, 2004).

have reformed laws, but their continued lack of enforcement will deter real change, as is the case of Egypt and other countries experimenting with economic liberalization. Reforming the paternalistic state in both production and rentier economies will be difficult because statism is integrated in the social, political and economic systems of Middle Eastern countries. As a result, it is most likely that in the short-term Arab economies will continue to be inward-looking and relatively isolationist.

A HUB AND SPOKE MEFTA:

It is argued that a US plan for a MEFTA will become a hub and spoke relationship, due to the structural impediments to economic cooperation in the Middle East. The United States, as the hub, will export higher value-added manufactured goods and services; Middle East countries, as the spokes, will export unprocessed primary goods to the United States. The negative economic implications of a hub and spoke relationship on Middle Eastern states are numerous. A hub and spoke MEFTA could potentially divert foreign investment away from the Middle East, as investors would prefer to set up manufacturing or service facilities in the United States and get duty-free access to all of the Middle East spokes. Again the lack of trade complementarity in the Middle East will exacerbate this. Companies will see little advantage to setting up facilities in the Middle East, where intra-regional trade is already low. Intra-regional economic cooperation will slow further under a MEFTA. Moreover, American businesses will be deterred from setting up manufacturing facilities in the Middle East as conflict continues in the region.

What this means for European efforts to create a similar EU-MEFTA plan is also telling. Building on the 1995 Barcelona Conference of European and Mediterranean states, the subsequent European Neighbourhood Policy, and the 2004 Agadir Agreement (among Egypt, Morocco, Tunisia and Jordan), the EU envisions a series of bilateral FTAs that will also prompt regional integration. Some have argued that an EU-MEFTA might fulfill the realization of the original Greater Arab Free Trade Area. It has even been suggested that the EU provided more political capital to promote Middle East economic integration than the Arab League.[36] In a study commissioned by the EU, however, there were clear signs of cautioned optimism. As Wippel notes:

> With regard to the Pan-Arab project, the Agadir Agreement could be seen as an avant-garde initiative bringing together the Arab world states that introduced economic reforms relatively early and with a comparative degree of earnestness. It did not, however, accelerate trade liberalisation, since free trade was not in force any earlier than between Arab countries and the advantage of allowing no exceptions eroded with their (theoretical) phasing out in GAFTA.[37]

While the study notes the possibility of improved liberalization in trade of services, there is a similar acknowledgment of the limited history of intra-regional arab trade as an important factor. How successful has the EU been in its own MEFTA project? A recent study has found "...no evidence of trade creation for the EU's exports to MENA [Middle East and North Africa] countries, following the implementation of the Euro-Mediterranean FTA.".[38] It is argued that many of the structural impediments to regional trade remain in the Middle East, regardless of whether the EU or the US initiated the plans. The United States unlike the EU, however, will

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[36]See Steffen Wippel. "The Agadir Agreement and Open Regionalism," EuroMeSCo Papers. Lisbon. Septebmer 2005: p.10. http://www.euromesco.net/media/euromesco_paper_45.pdf

[37]Wippel. "The Agadir Agreement and Open Regionalism,". p.16-17.

[38]Nicolas Peridy. "Towards a New Trade Policy Between the USA and Middle-East Countries: Estimating Trade Resistance and Export Potential" *The World Economy*, 28, no. 4,, (April 2005): 516.

have a stronger power advantage in many parts of the Middle East that could further negatively affect the FTA outcomes.

As the United States continues to negotiate each FTA bilaterally on its own terms and preferences, Middle East countries will have little say in what each new trading partner brings to the negotiation table. New trading partners will either have better access to the US market or new partners will undermine workers' conditions and environmental standards. Consequently, a hub and spoke MEFTA will result in Middle Eastern countries involved in a race to the bottom, where each country will continue to lower wages, erode labour rights, and soften commercial regulations to attract American investment away from other signatories. Although the United States is quick to highlight the economic benefits of the US-Jordan FTA, as an example for other Middle Eastern states to consider, these benefits are challenged.

It has been argued that the US-Jordan FTA has been a disappointment. First, although the US-Jordan FTA was intended to stimulate Israeli investment into Jordan, 80 percent of investment into Jordan's QIZ industrial parks are South Asian companies. These mostly textile manufacturing firms have five year leases that are not expected to be renewed, because removal of the Multi-Fibre Act will open worldwide duty-free access to the United States market. Jordan's QIZ will have little comparative advantage in textiles manufacturing once the Multi-Fibre Act has been removed. Second, most of the $3.50/day jobs were filled by non-Jordanian workers. Third, working conditions in the QIZ are negative; despite, labour regulations heralded in the US-Jordan FTA agreement.[39] Most recently the US' American Federation of Labor and

[39]For points one to three, see Peter W. Moore, "The Newest Jordan: Free Trade, Peace and an Ace in the Hole," *Middle East Report*, June 26, 2003, http://www.merip.org/mero/mero062603.html.

Congress of Industrial Organizations (AFL-CIO), an umbrella organization of 53 union organization, and the National Textile Association filed a complaint against Jordan for its violation of International Labour Organization standards, particularly treatment of foreign workers.[40] Jordanians have received little of the working benefits of the FTA and foreign workers have been allegedly mistreated. Although Jordanians are optimistic about their economic future, most believe that their economic situation remains poor and average Jordanians attribute little benefit to the FTA.[41] Finally, despite initial success of Jordan's trade surplus with the United States, which was relatively insignificant- for example, American exports to Jordan for 2001 accounted for 0.05 percent of overall US exports[42]- in recent years Jordan has been reporting a trade deficit with the United States (See Table 2).

The US-Jordan FTA has been insignificant to the overall US economy, and has raised criticism of a MEFTA. Business interests in the United States, for example, have been confounded by the Bush administration's focus on small and relatively insignificant Middle East countries. Prominent business groups have argued that trade with the Middle East has diverted the Trade and Representative Office's attention away from more important negotiations with

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[40]See AFL-CIO. AFL-CIO and National Textile Association Complaint under the U.S.-Jordan FTA Labor Chapter: Executive Summary. September 21, 2006. http://www.aflcio.org/issues/jobseconomy/globaleconomy/upload/Jordan_Executive_Summary

[41]The Pew Research Center for the People and the Press, *What the World Thinks in 2002* (Washington DC: Pew Research Center, 2002), 89.

[42]Office of Trade and Economic Analysis, International Trade Administration, U.S. Department of Commerce, "Export Statistics Express," http://ese.export.gov/ITA2002.htm.

South East Asian countries.[43] The US Chamber of Commerce President, Thomas J. Donohue, expressed similar criticism in a March 29, 2001 testimony before the House's Committee on Ways and Means. Donohue stated that:

> The last administration made known its intention that the JFTA [Jordan FTA] serve as a "template" by which subsequent trade agreements with other countries should be crafted. We respectfully but strongly disagree. Jordan has made admirable progress against the backdrop of continuing Middle East crises as it pursues economic modernization and liberalization. However, modeling [sic] our global trade negotiating strategy on our relationship with an economy as small and relatively uncomplicated as Jordan's would necessarily result in the neglect of a plethora of vital and much more complex U.S. national interests.[44]

For American business interests, the economic benefits of a MEFTA are relatively small, but for the US administration the prospects of creating political peace in the region makes a MEFTA worthy. The United States hopes that a MEFTA will create economic linkages that can normalize strained relationships and offer institutional mechanisms to resolve and prevent political disputes in the Middle East.

ANALYSIS OF ECONOMIC INTERDEPENDENCE AND PEACE

The US administration and Congress both share a neoliberal vision of peace in the Middle East. For example, Assistant Secretary for the Bureau of Near Eastern Affairs, William Burns,

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[43] Magnusson and McNamee, "Bush's Free Trade Diplomacy Has Corporate America Steaming,", 39.

[44] Thomas J. Donohue, speaking for the U.S. Chamber of Commerce, on March 29, 2001, to the Subcommittee on Trade of the House Committee on Ways and Means Hearing on Free Trade Deals, 107th Cong., 1st sess., "Is the United States Losing Ground as its Trading Partners Move Ahead?", http://waysandmeans.house.gov/legacy.asp?file=legacy/trade/107cong/3-29-01/3-29dono.htm.

expressed American hopes for MEFTA and peace in his remarks to the Center for the Study of Islam and Democracy. Burns stated that:

> As things stand now, the economic outlook for many Arab regimes is far from hopeful...And that is why President Bush, in his May 9 speech, and Secretary Powell, in his Partnership Initiative speech late last year, have laid such heavy emphasis on innovative new steps such as pursuit of a Middle East Free Trade Area....If we can apply American power with a sense of purpose and perspective as well as humility; if we can support democratic change in the framework of a broader strategy for economic modernization, Israeli-Palestinian peace, and a prosperous new Iraq; if we can understand the connections between those issues and what's at stake for American interests for many years to come -- then a time of crisis can become a turning point, a turning point in which hope begins to replace the despair on which violent extremists breed.[45]

Members of Congress also purport a vision of Middle East peace and trade. The Middle East Trade and Engagement Act of 2003 states that:

> (1) it is in the mutual interest of the United States and the countries of the greater Middle East to promote stable and sustainable growth and development throughout the greater Middle East; (2) Congress views democratization and economic progress in the countries of the greater Middle East as important elements of a policy to address terrorism and endemic instability; (3) free trade relationships are not a substitute for, but a complement to, necessary political and economic reforms that lead to political liberalization and economic freedom; (4) the countries of the greater Middle East have enormous economic potential and are of enduring political significance to the United States.[46]

The United States has adopted the neoliberal idea that economic interdependence attained through trade and investment will be a conduit for peace and stability in the Middle East.

Neoliberals posit that in the long term, citizens of free-market economies will prefer

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[45]William J. Burns, "Democratic Change and American Policy in the Middle East," (Remarks, to the Center for the Study of Islam and Democracy, Fourth Annual Conference Washington, DC, May 16, 2003), http://www.state.gov/p/nea/rls/rm/20713.htm.

[46]US Congress, *Middle East Trade and Engagement Act of 2003.*

making financial and material gains as opposed to military conquests.[47] Middle Easterners are generally receptive to free trade and economic liberalization, however, they will continue to be wary of American hegemony. In a 2003 Pew Research Center survey of select Middle Eastern countries, people overwhelmingly believed that they were better off in a free market economy and that increased trade and business ties improves their lot. At the same time, people surveyed overwhelmingly held a negative opinion of the United States and of its multinational corporations. This unfavourable view of the United States, after US invasion and occupation of Iraq, has led a significant number of Arabs to boycott American products.[48] Despite Arab governments' will, a defacto consumer boycott of both American and Israeli goods could be a potential problem with a MEFTA.

In policy terms, the United States believes that free trade will raise Middle Easterners living standards, decreasing the propensity of leaders to divert public attention to external conflicts. One example of this materializing is the recent Jordanian government's announcement of a 'Jordan First' motto, marketed to Jordanians as a new social contract in the Kingdom. In essence, the Jordan First motto reflects the monarchy's attempts to focus on national issues of economic development and liberalization, as opposed to pressing external issues that are beyond its control, namely in Palestine and Iraq. According to Jordanian national surveys, 86 percent of

[47] All neoliberal contentions are derived from John R. Oneal, Zeev Maoz and Bruce Russett, "The Liberal Peace: Interdependence, Democracy, and International Conflict," *Journal of Peace Research* 33, no.1. (February 1996),12.; Dale C. Copeland, "Economic Interdependence and War: A Theory of Trade Expectations," *International Security* 20, no.4 (Spring 1996), fn.2.

[48]The Pew Research Center for the People and the Press. *Views of a Changing World, June 2003* (Washington DC: Pew Research Center , 2003), pp.21-23, 71 and 104.

the populace like and agree with the Jordan First motto.[49] The Arab street will remain highly suspicious of US efforts in the Middle East and view US economic and political relations as forms of domination and imperialism. When the United States announced its plans for a $29 million MEPI, for example, the Arab media and various religious leaders reacted with much suspicion of US intentions in the region. Many argued that the US MEPI program was an attempt to undermine Middle East sovereignty and customs.[50] With a US sponsored MEFTA plan, the Arab populace will further resent American involvement in the region's economic affairs and MEFTA will hinder American-Arab relations.

Neoliberals posit that at an elite level, economic interdependence will create powerful distributional coalition groups with a vested interest in maintaining peace and trade. Economic interdependence further propels cultural exchanges, political dialogue, and diplomatic cooperation, minimizing the potential for political disputes. The United States expects a MEFTA to help normalize Israeli-Arab relations through cultural, social and business exchanges. One important example that undermines this American assumption is the high level of economic interdependence that currently exists between the Palestinian territories and Israel; yet conflict and violence has accelerated.[51] Moreover, the US-Jordan FTA and the required minimum Israeli

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[49]University of Jordan Center for Strategic Studies, "Current Issues: Jordan, Iraq and Palestine,"(Amman: University of Jordan, Public Opinion Polling Unit, January 2003), http://www.css-jordan.org/polls.

[50]The Middle East Media Research Institute, "Arab Media Reactions to The US-Middle East Partnership Initiative Part I: Opponents' Views," *Inquiry and Analysis Series.* no.115 (December 31, 2002), http://memri.org/bin/articles.cgi?Page=archives&Area=ia&ID=IA11502.

[51]Patrick Clawson, "Mideast Economies After the Israel-PLO Handshake," *Journal of International Affairs* 48, no. 1 (1994),142.

content in hopes of increasing positive business-to-business exchanges. Jordanian firms try to sidestep this requirement, however, by hiring Arab Israelis in managerial positions of their companies. The defacto Jordanian boycott of Israel continues. Jordanian business associations have also been lukewarm about fostering better ties with their Israeli counterparts and have boycotted trade shows attended by Israeli firms.[52] True, Jordan and Israel signed a historic free trade agreement in late 2004 that is set to reduce tariff barriers between the two countries in 2010; but, the significant amount of Jordanian street and political protests over the agreement bring significant doubt to any intended warming of people to people relations. In 2004, Egypt agreed to use the QIZ program as it feared significant losses when the MFA was set to expire. The US QIZ program required 11.7% Israeli content for Egyptian products to gain duty-free access to the United States. Like the Jordanians who have tried to avoid direct contact, the Egyptians have successfully lobbied to have Israeli software count as Israeli content. Again, real peace has not been created by US plans.

Undoubtedly, the Jordanian-Israeli and Egyptian-Israeli relationship are still relatively cold and Israeli firms have not rushed to invest in Jordan or Egypt. Moreover, a MEFTA might have a negative affect on both Israeli-Arab relations and Arab people-government relations as the Arab street remains highly critical of Israeli policies in the occupied Palestinian territories. Arab populace would increase their criticism of their governments and of Israel for circumventing peace negotiations in favour of economic profit. In absence of a political resolution to Middle East issues, economic interdependence between Arabs and Israelis remains delusory. Moreover, plans for MEFTA have irked a traditional US ally in the Middle East: Saudi Arabia. As argued

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[52]Moore, “The Newest Jordan”.

elsewhere, Saudi efforts to accelerate economic integration of the GCC is a reaction to US bilateral FTAs with GCC members.[53] The plan for MEFTA might make state elites also wary of US plans for dominating the region.

Furthermore, the neoliberal literature on the interrelation between economic interdependence and peace have suggested confounding factors that need to be explored in the case of MEFTA. Many neoliberals have argued that the liberal peace theory works in concert with the idea of democratic peace. It is democratic regimes that tend to be liberal economies that do not fight one another. The Middle East lacks democracies; regimes continue to justify limiting political liberalization on the basis of external threats: namely Israel and now the United States in Iraq. Factors such as enforcement of trade agreements, monitoring, level of symmetry between trading partners and the number of actors in the trade agreements can all affect the likelihood of a peaceful outcome.[54] The US-Jordan FTA does not have provisions for a binding and independent dispute settlement mechanism, leaving a small country like Jordan vulnerable. Presumably other Middle Eastern states invited to join MEFTA will not have a dispute settlement mechanism either, which could likely lead to the United States using its economic prowess to get its way in trade disputes. Potential trade disputes could then be exacerbated as more Middle Eastern states join MEFTA.

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[53]Bessma Momani. “"Reacting to Global Forces: Economic and Political Integration of the Gulf Cooperation Council". Presented at the ‘Regionalisation and the Taming of Globalization?’ Presented at the ‘Regionalisation and the Taming of Globalization?’ Conference Warwick, UK, October 26-28, 2005. See www.arts.uwaterloo.ca/~bmomani

[54]These points are highlighted in a survey of the economic interdependence and peace literature, see Katherine Barbieri and Gerald Schneider, “Globalization and Peace: Assessing New Directions in the Study of Trade and Conflict,” *Journal of Peace Research* 36, no.3 (1999), pp.397-404.

CONCLUSION

Since the Oslo Accords, optimists have envisioned a Middle East Free Trade Area that could foster economic interdependence and peace among Middle Eastern states. The Clinton administration, most notably in the first term, made some significant strides toward bolstering economic cooperation between Arabs and Israelis. The Bush administration, on the heels of pacifying and occupying Iraq, has proposed a more substantive policy for increasing intra-regional economic cooperation through the MEFTA plan.

The current structural impediments to intra-regional economic cooperation, however, will inhibit the prospects of an integrated Middle East economic system. Middle East economies do not complement one another to build an effective economic bloc on their own. Moreover, Middle East socio-political systems are predicated on remaining relatively isolationist and inward-looking. Middle Eastern states have little comparative advantage to increase economic cooperation; therefore, a MEFTA will create a hub and spoke relationship. Consequently, we will see Middle Eastern states acceding to the United States for purposes of keeping strong economic ties. While the United States promotes intra-regional trade and investment in the Middle East, it also raises the economic costs of disloyalty. Peace and stability will not be created because of economic interdependence among Middle Eastern states, as neoliberals would propose, but rather because of Middle Eastern states' acquiescence to American hegemony in the region.

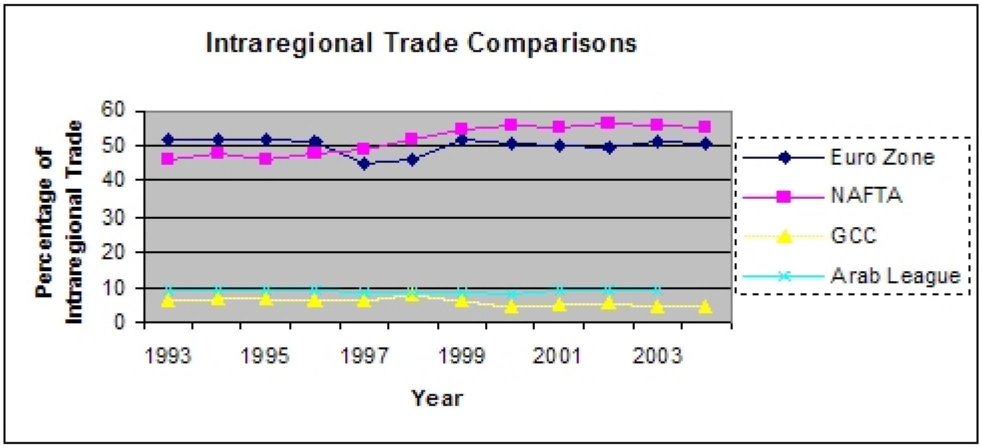
Table 1 U.S. – Middle East Free Trade Efforts

Country	FTA	TIFA	BIT	WTO	GSP
Israel					Not Eligible
Jordan					
Morocco					
Bahrain	Ratified				Not Eligible
Egypt					
Lebanon				Negotiating Accession	
Algeria				Negotiating Accession	
Tunisia					
Saudi Arabia					Not Eligible
Oman	Signed				
Kuwait					Not Eligible
UAE	Negotiating				Not Eligible
Yemen				Negotiating Accession	
Qatar					Not Eligible
Syria					Not Eligible
Iraq				Negotiating Accession	Not Eligible
Libya				Negotiating Accession	Not Eligible
Iran				Negotiating Accession	Not Eligible

Source: United States Trade Representative. (USTR). 2006

http://www.ustr.gov/Trade_Agreements/Regional/MEFTA/US_Middle_East_Free_Trade_Efforts_printer.html.

Figure 1: Intraregional Trade Comparisons



Source: UNCTAD. Statistics. 2005; Arab Monetary Fund. Statistics. 2005.