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U.S. ECONOMIC AND TRADE POLICY IN THE MIDDLE EAST

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CONTENTS

OPENING STATEMENTS

CONGRESSIONAL WITNESSES

ADMINISTRATION WITNESSES

PUBLIC WITNESSES

ALPHABETICAL LISTING AND APPENDIX MATERIAL

COMMUNICATIONS

U.S. ECONOMIC AND TRADE POLICY IN THE MIDDLE EAST

WEDNESDAY, MARCH 10, 2004

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 2:07 p.m., in room SD–215, Dirksen Senate Office Building, Hon. Charles E. Grassley (chairman of the committee) presiding.

Also present: Senator Baucus.

OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA, CHAIRMAN, COMMITTEE ON FINANCE

The CHAIRMAN. I am going to call the hearing to order. I do not have a gavel. I do not need a gavel, hopefully. I call the meeting to order and thank everybody for coming.

Today we are going to hear testimony on the issue of trade, particularly concentrated on the Middle East. We have economic stagnation and we have rapid population growth which is somewhat resulting in great frustration in the Middle East.

All too often, such frustration leads to political violence, and as a result, the news we hear about the region is frequently dominated by political violence. We obviously know about the security concerns that come to the United States from that part of the region.

But we know that there is another side to the Middle East that does not always get the news coverage it deserves. That is that it is a vibrant and vast region, full of promises. We are all pleased today to be able to focus on that aspect of the Middle East.

For a region to be truly thriving, we need stronger economic engagement between the United States and like-minded nations there in the Middle East. That is why I so strongly support the President's call for a Middle East Free Trade Agreement by 2013.

The dramatic vision articulated by the President can indeed become a reality, but it is going to take a lot of work to get it done. With his call for a Middle East free trade area, the President correctly recognizes that increased U.S. trade with and among Middle Eastern countries will foster long-term economic growth. Just as important, trade agreements entered into by the Middle Eastern countries would lead to, and in some cases lock in, needed political reforms.

The American economy will also benefit from more trade from these countries. The region's large and growing population offers Americans a great export market.

Countries in the Middle East, due to their difficult growing conditions, hold much promise for increased agricultural imports from the United States, which would be especially important to States like my State of Iowa.

The Bush Administration has taken a number of concrete steps to seize opportunities. First, President Bush pushed through Congress an important trade agreement with Jordan. Just last week, negotiations were completed with Morocco, and that has been a key ally of our against terrorism.

The U.S.-Morocco agreement further opens the Moroccan economy to imports from the United States. This agreement will have direct positive impact again on farmers of this country, particularly in the Midwest where corn and soybeans, to a greater extent, would go to Morocco, and tariffs down to zero on those products.

So I thank, personally, Ambassador Zoellick and our U.S. Chief Agriculture Negotiator, Alan Johnson, for their efforts on behalf of U.S. agriculture when negotiating agreements like that.

Likewise, with increased export opportunities to the United States and less expensive imports from the United States, the Moroccan people benefit from freer trade. Moreover, Morocco will likely receive a greater foreign investment due to its enhanced economic status on account of the free trade agreement. By improving the economic situation in Morocco, the FTA will bring greater stability to that country.

I am also encouraged by our negotiations with Bahrain. That country is not only a strategic ally of us, but has also demonstrated real commitment to liberalized trade. In addition, Bahrain is a leading nation in the Gulf Cooperation Council, and that happens to be an entity which contributes to a greater economic integration of the region.

It is my understanding that negotiations with Bahrain are proceeding rapidly and I commend Bahrain officials for their commitment to this process.

The U.S.-Jordan Free Trade Agreement, now probably 3 years old, I believe, through that one, as well as the U.S.-Moroccan agreement and a proposed U.S.-Bahrain, are important steps towards fulfilling the President's vision of this Middle East Free Trade Agreement.

I look forward to hearing from our witnesses today on what we can do to bring peace and prosperity to that region, with emphasis upon peace.

Senator Baucus?

OPENING STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator BAUCUS. Thank you, Mr. Chairman.

I will be fairly brief here. I thank all the witnesses who are here. We have a quite impressive panel. But I particularly want to thank Senator McCain for testifying. Last year, Senator McCain and I introduced what some know as the Baucus-McCain bill, but better known as the Silk Road bill.

That bill seeks to establish, as you know, Mr. Chairman, a preference program for countries of the Middle East, similar to programs we now have in sub-Saharan Africa, the Andean region, and the Caribbean Basin.

It would give the President the power to allow Middle Eastern countries that meet certain conditions, such as supporting the war on terrorism and reforming their economies, to export products that the President approves duty-free.

A trade preference program like the one we are proposing will help countries in the Middle East now in the short term. It is comprehensive. It offers economic help through increased trade to the entire region at once rather than gradually, country by country.

It will help prepare Middle Eastern economies to enter into the free trade agreements with the United States that is the cornerstone of the administration's Middle East trade policy. That is an important point.

Far from competing with the administration's policies, I believe the Silk Road bill will complement and support the administration's attempt to establish a Middle East free trade area.

Just look at history of the preference programs. The United States has essentially three regional trade preference programs today. We passed the African Growth and Opportunity Act, AGOA, in 2000. Now we are negotiating an FTA with five AGOA beneficiaries, the Southern Africa Customs Union, otherwise known as SACU.

We also have the Andean Trade Preferences Act, ATPA. For years, ATPA has provided incentives to farmers to switch from growing cocoa to growing flowers, coffee, and other legal crops.

The USTR recently announced that it would take the next step and negotiate FTAs with ATPA beneficiaries, Columbia, Peru, Bolivia, Ecuador. Finally, we have the Caribbean Basin Initiative, CBI. All five of the CAFTA countries with which we just completed FTA negotiations receive benefits under CBI. So does Panama, another future FTA partner according to the USTR.

So the evidence is clear. Preference programs help countries reform and develop their economies to the point where an FTA with the United States can become a realistic option.

In its recently released annual report, USTR stated, "AGOA has prompted important economic and social reforms across sub-Sahara Africa and delivered new jobs and opportunities for economic growth and development to the region."

This is precisely what the United States seeks to accomplish in the Middle East. If a preference program delivered these impressive results for sub-Sahara Africa, why would we not develop a preference program for the Middle East?

Surely it cannot be said that the Middle East is somehow less important than sub-Sahara Africa. The USTR also said in its annual report, "AGOA's successes are also creating new commercial opportunities for United States exporters" as African exporters explore new import sources in the United States.

New commercial opportunities for U.S. companies means jobs for U.S. citizens. In short, a preference program for the Middle East will help stimulate economies in the Middle East, create jobs both in the Middle East and here at home, and improve America's security in the process.

So I urge the administration to support this preference program. I think it is a good idea. It complements the administration's Middle East efforts.

I particularly thank the Senator from Arizona, Senator McCain, for spearheading this effort, not only this effort, but many other efforts that he spearheads, and thank him especially for this bill.

The CHAIRMAN. Thank you, Senator Baucus.

Now we welcome our colleague from Arizona, Senator McCain. Go ahead, Senator McCain.

STATEMENT OF HON. JOHN McCAIN, A U.S. SENATOR FROM ARIZONA

Senator MCCAIN. Thank you very much, Chairman Grassley. Senator Baucus, thank you for your partnership and thank you for your kind words. I thank you for the opportunity to testify before you, briefly, regarding U.S. economic and trade policy in the Middle East.

I want to start out by congratulating the committee on its many trade-related successes this session. The many actions taken on trade policy since the passage of the Trade Act of 2002 are to be commended—from the expedited consideration and approval of free trade agreements with Chile and Singapore last year, to the consideration, perhaps in the not-too-distant future of the recently concluded negotiations with Australia and Morocco. In addition, the benefits available to eligible nations covered under the African Growth and Opportunity Act are to be extended and possibly expanded.

Mr. Chairman, the United States is steadily regaining its leadership role on trade despite some counterproductive protectionist actions; however, we are feeling the after-effects of those actions and support for free trade is no longer as robust and vocal as in recent memory.

With your leadership, Mr. Chairman, and that of Senator Baucus, I believe it is possible to generate the support necessary to continue to approve strong trade deals that not only benefit the United States and promote market liberalization and transparency with our trading partners, but also provide them incentives to bring about political and social reform, when necessary.

Such a necessity clearly exists in the greater Middle East. Tom Freedman has written, "Many Arab economies are dominated by state oil revenues and state companies, with private enterprise very weak. Therefore, holding onto or being close to power are the only pathways to wealth. Control power, control wealth." Breaking the link between political power and wealth by creating a larger private sector independent of political control is an essential component of our efforts to help build democracy in the Middle East.

As we have witnessed in Bahrain, with whom we are in the final FTA negotiating stages, there is a willingness to begin this separation, as evidenced by laws now on the books. But perhaps the more crucial step will be the execution of those laws. We must remain vigilant on this issue to ensure those laws are enforced so our own financial services sector and others will be able to operate in a truly transparent and open market.

A key question for American policy is how to encourage such long overdue political, economic, and social changes in the Arab world. I believe we must expand our range of economic, cultural, and political tools to help give the people of the greater Middle East a stake and a voice in how they are ruled, with greater levels of democracy and prosperity serving as an antidote to the hatred whose malignancy was brought home to Americans on September 11, 2001. Trade preferences can help build prosperity in the Arab and Muslim worlds independently of state power and can help advance our political objective of more representative, accountable, and transparent rule.

We have successfully pursued trade preference programs with the Nations in sub-Saharan Africa, the Andean region, and the Caribbean Basin, with tangible results. Would anyone argue today that the greater Middle East is less important?

The bill that Senator Baucus and I introduced would establish a baseline of trade as an incentive to those countries that do not engage in activities that undermine our National security or foreign policy interests and support a peaceful resolution of the Israeli-Palestinian conflict, among other things.

This bill is designed to provide a reliable and even-handed approach toward improving relations with the Middle East through greater economic interdependence. It is not a panacea developed to solve overnight all the problems that exist in relations between the United States and the nations of the greater Middle East. We need to send a clear signal to the region that we are serious about finding peaceful solutions to the fires that have been fanned over the years, in part because of closed markets.

Engaging the region on this level will help spur increased investment in trade which can lead to a reduction in the risk posed by the severely restricted economic system under which a number of nations in the area operate. Reaching that goal would be no small achievement, given the likelihood of tremendous population growth and an average unemployment rate in the region hovering around 22 percent, an obvious recipe for disaster.

In an era when our trade negotiators expressly pursue trade agreements to advance broader foreign policy interests, liberalizing trade with key partners in the Middle East, Turkey, and South Asia should be a strategic priority of the United States.

We all understand the critical need to engage the region and promote stabilizing reforms. I support the President's vision and believe that extending preferences to eligible countries complements that vision by providing immediate, tangible benefits.

Mr. Chairman, I want to thank you and Senator Baucus for allowing me the opportunity to be here in part of your busy schedule, and I thank you for pursuing these efforts, these continued efforts which you have been successful in.

I wish you every future success. What you are doing, I think, will benefit our children and the children of the nations which will benefit from these agreements. I thank my colleagues.

Senator BAUCUS. Thank you, Senator, very much for your leadership. It makes a big difference and I know it is going to help a lot.

The CHAIRMAN. We obviously agree with your comments and the thrust of your action.

Senator MCCAIN. Some of these nations may even like to use ethanol over time. [Laughter.]

The CHAIRMAN. They must not be operating through American oil companies, then. [Laughter.]

Senator MCCAIN. Thank you, Mr. Chairman. Thank you very much.

[The prepared statement of Senator McCain appears in the appendix.]

The CHAIRMAN. Now it is our privilege to invite Grant Aldonas, Under Secretary, U.S. Department of Commerce and Hon. Alan P. Larson, Under Secretary, U.S. State Department, to come to the table.

I am not sure I know much about the protocol of calling two people on the same level, but since I nominated you first, Mr. Aldonas, go ahead.

STATEMENT OF HON. GRANT D. ALDONAS, UNDER SECRETARY, U.S. DEPARTMENT OF COMMERCE, WASHINGTON, DC

Mr. ALDONAS. Thank you, Mr. Chairman. Thank you, Senator Baucus. It is good to see you again. Good to see you back, frankly, and in good health.

Senator BAUCUS. Thank you.

Mr. ALDONAS. I wanted to submit my testimony for the record, if I could, and just open with a brief statement.

The CHAIRMAN. Please do that. Both of you will have your full statement put in the record without asking, if you want that done.

Mr. ALDONAS. Thank you, Mr. Chairman.

[The prepared statement of Mr. Aldonas appears in the appendix.]

Mr. ALDONAS. The first thing is, I appreciate both of your focus and commitment in terms of focusing on these issues. There is no region that is more important to the United States in terms of getting it right.

I know Al will touch on a lot of the security and development side, but even on commercial terms, what we have are countries that have for too long been outside the ambit of the world trading system.

One of the keys that I saw in Doha at the launch of the new WTO round was a real thirst in the developing world to find a way to reach the benefits of the world trading system to integrate themselves fully into the world trading system.

What you saw was a number of countries that in effect were saying, we have to find the route, because we see this not only as the primary tool for economic development, but a primary tool for economic reform in their own countries. That is as true of our friends in the Middle East and our trading partners in the Middle East as anywhere else.

It should not be lost on anybody that the WTO round was launched in the Middle East in Doha and, in the absence of the leadership of the Emir of Quatar, I can tell you, at the final day of the round, would not have been launched.

There is a deep commitment among these countries to move in the direction of trade liberalization. Certainly they have pursued with us their interest in moving ahead with free trade agreements and trying to engage in the international trading system.

When I was in private practice for many years, I had the pleasure and the opportunity to spend a fair amount of time working in the Middle East. What you saw, of course, were economies that were focused principally on oil that were making efforts toward diversification.

In the face of a lot of what I would describe as clogged regulatory frameworks and a variety of other things that keep their economy from growing, they are trying to find other routes. Certainly, opening to the world economy is one of the most significant ways they can do it, hence their interest, I think, in moving ahead with us on free trade.

But to go back to my main point, in today's world, half of the world's population lives on less than $2 a day. If the trading system works for anybody, it has to work for that group of people—even in the Middle East, 25 percent of the population lives on less than $2 a day. While they are further up on the economic development scale, this is a critical area where we do need to reach out.

That is the driving force behind the President's initiatives, both with respect to the Middle East Free Trade Area and the Middle East Partnership Initiative, which I know Al will touch on.

But particularly with respect to MEFTA, it is an opportunity, I think, to engage with countries that have been looking to us for the opportunity to negotiate free trade. It is clear that they are committed in that direction.

We are already moving in that direction with Morocco and Bahrain. Having successfully concluded negotiations with Morocco, I am very hopeful that we will have, in very short order, an agreement with Bahrain as well. There are a lot of candidates in the queue, frankly.

I applaud the committee's work in terms of moving the agreements through under fast track, which both you, Senator Baucus, and the Chairman did so much to bring about, and giving us that opportunity. Certainly it is an opportunity that the other countries in the Middle East want to pursue.

The second point I wanted to make, wholly apart from the openness of the Middle East to trade, and why I think that in some respects it is a fallow area for expanding our commercial relationship, is what we do at the Commerce Department to try and foster that, even in the absence of free trade negotiations with many of these countries.

Bill Lash, who I know you know, is our Assistant Secretary for Market Access and Compliance, and has been to the region five times. I have been there as well, as has Secretary Evans.

There is a real instinct on the part of our international companies in fields such as information technology, pharmaceuticals, and the arts, to think that they have a flourishing market in the Middle East.

In addition, we have focused hard on Iraq reconstruction by building a network of our commercial officers in the region to try and foster trade, and frankly reintegrate that blighted country back into the Middle East, as well as into the world trading system.

Again, we appreciate your support in terms of Iraq's potential membership in the WTO, and it is certainly a step forward in terms of trying to bring some economic relief there.

In addition, with the support of the Congress, we have been able to help Middle Eastern countries through economic reform with our Commercial Law Development Program.

The CLDP will supply a large portion of the technical assistance required to the U.S.-Morocco Free Trade Agreement. That is something which, I would say with any legislative initiative, I would like to see us continue to foster.

The program is a very solid one. And certainly if we are going to move ahead with economic reform in the Middle East, we are going to need that kind of technical assistance, regardless of the vehicle for trying to drive economic reform and trade forward.

In addition, we are establishing a Middle East Business Information Center which would be a focal point for providing information to U.S. businesses. Again, support for that would be consistent with any drive toward expanding trade in the region.

The last point I would like to make is actually something that both Al and I got to participate in, which was the World Economic Forum's meeting in Jordan this past year.

There are also some fairly significant developments in Palestine. I noted Israeli businessmen were now looking increasingly at the idea of investing in Palestine as a way of driving an agenda other than the peace process that could lead toward stronger developments there, and whatever support we could lend to that process through the President's initiative or the efforts of the Congress, I think, would be of great help.

Let me stop there and turn it over to Al.

The CHAIRMAN. Secretary Larson?

STATEMENT OF HON. ALAN P. LARSON, UNDER SECRETARY, U.S. DEPARTMENT OF STATE, WASHINGTON, DC

Mr. LARSON. Thank you very much, Mr. Chairman and Senator Baucus. I really welcome this opportunity to be here with my colleague, Grant Aldonas, and talk about the administration's initiatives with respect to the Middle East.

There is no other region of the world that presents as many challenges and opportunities as this one. President Bush has made it clear that it must be the policy of the United States to support the forces of reform, of freedom, and of opportunity in this critical region.

The recent United Nations Arab Human Development Report, which was written by representatives of the region, is really a call for change within that region. We have been given by the Congress, through the Middle East Partnership Initiative, some of the tools that we need to have to respond to that call for change.

As we prepare for the President's G–8 summit meeting in Sea Island in June, we are trying to consider additional ideas that could further expand opportunities in the Middle East, ideas like using information technology to support business development, promoting financial reform, the development of capital markets, and increased access for small businesses to capital, the promotion of private investment climates that will attract capital into the region, promotion of regional dialogue on economic and social reform, and expanding trade opportunities.

I recently had the opportunity to spend a week traveling in the region, including Ramallah, Palestine, Jerusalem, Amman, Jordan, Riyad, Saudi Arabia, and Cairo, Egypt. In that trip, as well one that my colleague, Under Secretary Mark Grossman made in the following week, we heard leaders that understand the need for economic reform.

They wish, naturally, that reform should be home-grown and that it should occur within the context of each country's historical and cultural traditions, and we, of course, agree with that.

But what was particularly striking was that in our leaders with young people, with business executives, and with leaders of civil society, there is very strong interest and very strong support for the types of ideas that we are talking about.

As a result of those discussions, we are refining our thinking on ways that we could best help reformers to provide more opportunity, educational opportunities so that girls and boys are equipped with the skills that they need to participate in the modern economy, economic opportunity so that they can start businesses and find jobs, and civic opportunities so they can play a role in shaping the future of their own countries.

We intend to work with the G–8, the European Union, as well as the countries of the region to further develop these ideas. Trade, of course, is a particularly powerful tool for promoting constructive change, and this is a region that is not now well integrated into the global economy. It accounts for only 5 percent of world exports and less than 1 percent of world FDI flows, and intra-regional trade is far below the levels of other regions.

Under MEFTA, the United States is pursuing an ambitious trade agenda. As has been noted, the FTA and QIZ with Jordan have shown the power of trade in promoting and sustaining economic reform.

The recent FTA with Morocco and the strong progress in negotiations with Bahrain show that the impulse for using trade to promote economic development extends from one end of the region to the other.

We welcome the fact that Saudi Arabia is actively pursuing WTO accession, a step that would encourage broader reform in that society. We are looking at using bilateral investment treaties, the GSP program, and TFAs, as well.

As we pursue trade liberalization and trade expansion, we have several motives. First, as other nations, including the European Union nations, extend agreements with these countries, we need to make sure that American exporters face a level playing field and are not disadvantaged.

Even when they are not disadvantaged with respect to other competitors, we want to make sure that we are doing everything we can to bring down barriers in these countries, to their benefit as well as to the benefit of our exporters.

Third, we do believe that trade policy disciplines will support economic reform, transparency, and the rule of law. Finally, by creating more opportunity and more hope, trade liberalization can help reduce the appeal of extremism, and even of terrorism.

So, we very much welcome, Mr. Chairman and Senator Baucus, the leadership of the committee in addressing these important issues and we look forward to an ongoing dialogue with you on them. Thank you.

[The prepared statement of Mr. Larson appears in the appendix.]

The CHAIRMAN. Let me ask my colleague. We normally take 5-minute turns. Would it be all right if we take 10-minute turns?

Senator BAUCUS. Sure.

The CHAIRMAN. All right. There are so many people here. So, all right.

The first question is meant to compare an issue that Saudi Arabia is dealing with, with what I think is opposite of what Europe is doing on biotechnology. I think Saudi Arabia is in the process of implementing mandatory labeling laws for agricultural biotechnology products. It is my understanding that other countries in the region might be considering adopting similar laws.

Do you believe that Saudi Arabia's biotech policies will spread to the adoption of similar laws in that region?

Mr. ALDONAS. Mr. Chairman, obviously it is a note of real concern, given the importance of that issue. We have seen this really start in the EU. We are seeing it in China. We are seeing it out in the rest of the world. So, I think the concern is a legitimate one. Certainly, it is a topic of conversation with the Saudis.

We do need to strike a balance. Obviously, in America, we have a very strong preference for informing consumers. But, the real concern is that these are going to cause barriers and create consumer preferences, frankly, that disadvantage American producers in the market. So, yes, it is very much a concern in terms of where else we are going in the region.

Having said that, the other countries in the region, in some respects, are moving somewhat faster than the Saudis in terms of moving toward trade liberalization and in terms of some of the underlying reforms.

There is an ongoing dialogue with many of them, whether it is Bahrain in the context of the FTA, or in the context of the trade and investment framework agreements where we can continue to raise those issues. I think they can see the benefits of having a stronger relationship with the United States relative to moving in a different direction.

The CHAIRMAN. I may have misspoken about Europe in the sense of opposite Europe. Europe is going in the direction of their labeling as well. But I was thinking in regard to, is there the same cultural, psychological, or maybe just economic barrier to biotechnology in the Middle East as there is in Europe? Secretary Larson?

Mr. LARSON. Mr. Chairman, I do not think there is the degree of popular interest in this issue that there is in a narrow segment of the European population. That has, to some extent, been stirred up by a small number of NGOs.

I think there is an ignorance, and one of the things that our administration is trying to do is dispel that ignorance through information so that regulators and consumers can make intelligent decisions.

As Under Secretary Aldonas was saying, I do not see, based on my contacts with other countries, this Saudi action spreading like wildfire throughout the region. It is a different political atmosphere than we saw in Europe.

The CHAIRMAN. On another matter, we have the success of preference programs such as the African Growth and Opportunity Act, and then also to some degree the Andean Trade Preference Act, leading some in Congress to embrace preference programs as needed stepping stones in preparing countries to negotiate free trade agreements with the United States.

Would you believe that to be true or does the extension of preference act as a disincentive for reform and cooperation, whether in a bilateral or multilateral forum?

Mr. ALDONAS. Well, I am not sure that I would see it quite as that dichotomy, Mr. Chairman. The first and most important thing, I know, based on my own experience in implementing the CBI back in the 1980s, is that it can help establish a predicate for where you want to go in trade. And certainly the fact that we have concluded recently an agreement with Central America is testament to the fact that we have advanced a lot within the framework of the CBI.

Using CBI, as well as the African Growth and Opportunity Act, was really because we lacked other tools to try and move forward with those particular regions. I think in this instance, while there may be room for that sort of preference program, we do, in the President's initiatives, have tools that are allowing us to engage both in terms of the focus on the trade and investment framework agreements, which do something similar in terms of discussing where we have to be going in our trading relationship before we can negotiate free trade, and then in terms of the overall MEFTA policies, which are really a very strong sort of seven-step program of trying to draw the region into the world trading system.

So in one sense we do have tools that are designed to do what both AGOA and CBI did in their respective regions to encourage countries into the trading system and then to become full participants.

The CHAIRMAN. Again, kind of on preference programs, in developing countries there in the Middle East, they currently receive trade preferences under GSP, although few of those countries take advantage of the opportunities to export products that we include in that program.

Do you have any idea or ideas on how to encourage countries in the Middle East to take better advantage of preferences available under GSP? Would additional preferences act as disincentives for reform and hinder the ability of countries to trade in reciprocal agreements?

Let me state, before you answer that, that Ambassador Zoellick stated yesterday that one of the causes of breakdown in the negotiations in Cancun was concern among developing countries that liberalized trade would cause them to lose their current preference advantages. Is that a view that you would share?

Mr. ALDONAS. Well, if I could, to start out, there does not necessarily have to be an inconsistency, but I think it really depends on the individual case. What we have got in the Middle East right now are countries that are eager to negotiate.

We do not need further preferences, really, to encourage them. Frankly, I think a lot of the failure to make use of GSP or any new preference program is simply reflecting the fact that the economies are not very diversified. They are very focused on oil.

I think, even where you look at areas like textiles, which presumably would be one of the areas where you could extend beyond the existing GSP program, the likelihood of further investment in the region—given that they are a little higher up on the development scale—once the quotas come off under the WTO agreement at the end of this year, is very slim.

So the question is how much more juice you might get out of the preference program, given that we already have folks who want to engage with us, not only in the framework of Trade and Investment Framework Agreements, TIFAs, but also in the framework of real, bilateral free trade agreements.

The CHAIRMAN. Secretary Larson?

Mr. LARSON. I would like to just add a couple of thoughts on this important issue. I know that Ambassador Zoellick, as well as Grant and I, were distressed in Cancun to hear some representatives of developing countries say they were worried about pursuing multilateral trade liberalization because there might be erosion of preferences, that their competitive margin would be less.

We felt that that was a very disturbing thing for them to say that, if carried to an extreme, undercut the whole push for multilateral global trade liberalization.

We do have the GSP program. I think that one of the things we must do in the Middle East, as elsewhere, is make sure that countries and the companies in countries that are prepared and capable of benefitting from this program understand how to do it. That is one of the things we try to address through our trade capacity building programs.

There is one other thought that I think is important here. That is, this is a region that not only does not trade with us as much as we would like, but it is also a region that does not trade with each other as much as we would like.

So, part of our trade strategy has to be not only getting more opportunities for them to access our market and more opportunities for us to access their markets, but get them to liberalize among each other so you could build a more cohesive regional economy, the sort of regional economy that has spurred stronger growth in places like southeast Asia.

The CHAIRMAN. Thank you for that.

Is it necessary for Bahrain to be completed before we would move into negotiations with other countries that are in the Persian Gulf?

Mr. ALDONAS. I do not think that is necessary at all. But on the other hand, I do think that one of the first things you always want to do with these agreements, which you can see has been a part of the process that we have followed, is to sit down and negotiate where you are going to get the highest standard in a particular region, so that the goal is out there for everyone else to shoot at. You can articulate a model that others should follow.

So the fact that we have advanced with Bahrain as quickly as we have, I think, means we can bring that agreement to conclusion fairly quickly. My guess is, just as a practical matter, we are likely to finish that before we start with anybody else in the region. But it is not necessarily a predicate for further negotiations.

The CHAIRMAN. Well, would it be finished by June, as we have heard?

Mr. ALDONAS. I think there is great likelihood it will. I think there are outstanding issues on market access. But you know how these things go, Mr. Chairman. I think when you are in the room and you can feel the mood, there is a real dedication and there is a sense of common enterprise in the negotiations. We all understand the goal we are reaching for, and that helps a lot in terms of trying to move past the difficult issues on market access.

The CHAIRMAN. Well, could you tell us then, if Morocco is done now, Bahrain might be done by June, what might be the next countries we would be negotiating with?

Mr. ALDONAS. There are a number of candidates, I think, such as, if you look at Qatar and our strong relationship there with a friend and ally in the region, certainly one that has been helpful as we have taken on a difficult task in Iraq, as well as in fighting the war on terror.

There are also others that I know are very interested, but at this juncture may not quite be ready under the circumstances. I think obviously there has been great interest in Egypt in negotiating a free trade agreement.

At the same time, we do have our challenges in the relationship with Egypt because there are times when they will walk back from the WTO obligations, and we need to work with them to try and get them back on course. But it is not the sort of thing that necessarily gives you the confidence to feel we are really prepared to take that next step.

Now, we are in negotiations with TIFAs with a number of countries, which I think starts to lay out a course where you could start to take this forward with some of the other countries in the region.

The CHAIRMAN. Again, getting back to biotechnology, because it is pretty important to American agriculture, and whether it is an impediment to exports, two things.

Number one, I know that Egypt is doing a lot of work in biotechnology, very advanced research, I am told. Second, we asked Egypt to join us in our WTO case against Europe on biotechnology and they were going to, and then they refused to.

I have received conflicting reports as to why Egypt refused to join the United States in that effort. What have you heard regarding that decision of Egypt, either one of you?

Mr. LARSON. First of all, we were extraordinarily disappointed by the reversal that the government took there. My sense is that this is a government that understands that biotechnology is important, and even important for their own economic prospects. As you said, Mr. Chairman, they are doing a significant amount of research and I think they see that there could be some significant economic benefits.

Sometimes you cannot get the full picture, but this is one case that I believe that very, very strong European Union pressure was placed on the government subsequent to the announcement that they were going to join us in this case, and that ultimately led to the reversal.

Mr. ALDONAS. If I could just add to that, Mr. Chairman. My own view with respect to Egypt in this particular event is that it reflected one of the most unhealthy aspects of what is going on in the context of the Doha Round.

There seems to be an effort under way to avoid agricultural reform on the part of the Europeans, so the goal is always to make sure that somehow the developing world is more on their side than ours in terms of where we want to go in the negotiations. I think the situation with Egypt reflects that.

Bluntly, it is less about Egypt for me and from my perspective than it is about Europe. We really do have to maintain the pressure on our European friends for agricultural reform. No amount of discussion with the rest of the developing world ought to take the spotlight off of the Europeans in terms of what we have to see.

The CHAIRMAN. I have just one last question, so I will go over 10 minutes just for one question.

Beyond these issues we have discussed about Egypt, and also I will add one more, Egypt's refusal to join in meaningful negotiations in Cancun by joining the G–21 group, do you believe that Egypt has made enough progress towards needed reforms to enter into free trade negotiations with the United States? It bothers me when Commerce defers to the State Department on this, particularly with Egypt.

Mr. ALDONAS. Well, you ought to appreciate this. You have got a Minnesotan and an Iowan in front of you who are always deferential. That is the problem.

The CHAIRMAN. Yes. Yes. In that case, I will take Mr. Larson's view first.

Mr. ALDONAS. That would be the right choice.

The CHAIRMAN. All right.

Mr. LARSON. Now, you said, have they progressed enough? I think that is a hard question to answer. I think it is important to stress that they have moved on trade policy in the last couple of years, and we welcome that.

They did move on the basic telecommunications law. They have adopted greatly improved intellectual property laws. They have corrected a major mistake that they made with respect to their WTO-illegal positions on textiles and apparel.

Then in areas related to trade, they have made progress in having a more appropriate market-oriented exchange rate policy. So, I think it is important to recognize that there is a lot of constructive change.

Both Grant and I have been impressed by the fact that they brought in someone as wise as Hernando De Soto to help them figure out some of the many problems in their own economy that could be fixed if they got an approach that emphasized private property rights, and so forth.

So the trend, more or less, is in a positive direction. At the same time, there is a long list of things that we think that they need to correct in the area of their trade policy, and we have been pretty explicit in communicating those to them.

Mr. ALDONAS. We need to strike a balance. On the one hand, you have a market in Egypt that is enormously attractive, the single largest market for U.S. wheat. Things like that really are attractive in terms of where we should be going in trade with Egypt.

The problem is, you continue to see the sort of hiccups along the way where you hope that you have made progress, but then suddenly there will be some action that is significantly WTO-inconsistent.

So, although we have had a TIFA since 1999 and we continue to work through the issues, and I think—correct me if I am wrong, Al—we, in working with the Egyptians, have resolved all of the individual issues we have, the question is whether, again, you have that sense of shared enterprise of where we should be going on trade that will give you the confidence that we would sit down and have a negotiation as we have had with other partners in the region where we are committed to the goal. And that helps you move past some of what will obviously be the difficult issues at the table.

The CHAIRMAN. When it comes to these biotechnology issues and agriculture, particularly midwestern agriculture, as Egyptian leadership might look at it, if the former ambassador to the United States is now still the foreign minister of Egypt, I am satisfied he understands Iowa very well because he, when he was ambassador, came to my State on three different biennial tours I have for ambassadors to tour my State.

So, he spent at least 15 days in Iowa during the period of time that he was ambassador here, so I do feel he has that sort of understanding, because we took him to all of our research institutions on biotechnology.

I am going to defer to Senator Baucus now. I am going to see some kids in the anteroom here from a high school while Senator Baucus is asking his questions.

Senator BAUCUS. Thank you, Mr. Chairman.

I would like to ask both of you how the provisions that I am going to read to you contained in the preferences bill that Senator McCain and I introduced might be used to help advance the ball here.

As you heard, my description basically gives the President power to allow Middle Eastern countries that meet certain conditions, such as supporting the war on terrorism and reforming their economies, to export products that the President approves duty-free. I know that is very general, but there is a lot of leeway there, given the President.

I just wonder if you could sit back a little bit and kind of just ruminate a little on how that could be used to advance our goals here, which basically is more trade, and maybe having a few trade agreement with one or all of the countries in the Middle East.

As you talk to these countries and talk to business people in these countries, officials and business people, commentators, observers, and whatnot, there may be some priorities of some kind either among countries or priorities within a country, without being presumptuous.

We do not want to tell people what to do, but at least as you see it. It might be financing. It might be the legal code. It might be anti-corruption laws. I mean, who knows what it might be. You are much closer to it than we.

How could the President use this authority, if it is granted to him, in a good, solid, and constructive way? The old, what ifs. What if the administration were to say this? What if it were to say that? You two know the area, you know the subject, you know the levers, you know the various components of all this. What kind of comes to mind that will be useful?

Mr. ALDONAS. I think, honestly, Senator Baucus, the most powerful attraction, in some respects, of the proposal is that it reflects a longstanding commitment, not only from the executive, but from Congress, with respect to what we want to achieve in the Middle East.

So part of the value is not simply the tools that the President could use, but the fact that Congress would be stepping behind us and saying there is a long-term commitment, regardless of the vicissitudes of the peace process in the Middle East, and saying that we have goals here that we want to achieve that would move the world and the region in the right direction toward peace and stability.

In point of fact, though, I think in discussing it with business leaders, they are moving very quickly in the direction of actually sitting down and negotiating with us and have looked to MEFTA as the vehicle to start to bring about the reforms that they would like to see.

Senator BAUCUS. What are some of those reforms they mentioned to you?

Mr. ALDONAS. I think they are absolutely relevant and very important because those are the sorts of things——

Senator BAUCUS. What are some of them? Can you give me some examples?

Mr. ALDONAS. What are some of the reforms? I think, certainly, openness to investment, eliminating some of the restrictive business practices, a rule of law and contracts. The fact that part of a royal family can simply appropriate your investment or things like that, that is not something that is going to encourage investment along the way.

Those are exactly the sorts of issues about which we want to be talking with them, and usually are, in the framework of the TIFA, and then would want to cement as part of a free trade agreement at the end of the day.

I think the balance that you try and strike in that context is, if they are already engaged with us in terms of the negotiations, is there more that would be helpful, balanced against the very powerful attraction of it, in part because it also reflects a commitment of the Congress, not just the President, towards solving the problems in the region, and because using economics is such a powerful tool to do that.

Senator BAUCUS. My understanding is, when we start to talk to Morocco, that gave leverage to reform elements within the country, even in advance of putting together an FTA. Could you talk about that a little bit and how that processed worked? Maybe Secretary Larson, or whoever. I am told that is what happened. Maybe it is not correct.

Mr. LARSON. I think that is the story. I think it is a story that repeats itself. I could begin by answering part of your earlier question. As I traveled on the most recent earlier trips, in my conversations with the business community, they focused on the importance of building out the private sector and particularly having more space in their economies for small businesses.

One of the things that I was particularly struck by in the testimony of Senator McCain was the emphasis on getting away from the government-managed, government-controlled economic systems into something where there was more scope for private enterprise.

So, that is one very consistent theme and something that is supported by trade liberalization, whether it is through a preference program or whether it is through a reciprocal program.

I did hear many business leaders on this most recent trip say that one of the reasons why they are attracted to MEFTA and attracted to the idea of FTA, is that they do believe that it will reinforce the sorts of reforms that they think are necessary anyway. It would be good for American companies, but it would be good for them as well.

The simple issue of transparency in areas like government procurement is an important issue, the issue of reducing regulatory red tape, the issue of the legal code, which Grant mentioned. These are all areas that are problems for would-be small businesses within these countries, just as they are problems for American companies doing business there.

Senator BAUCUS. Now, let us stick with small business and let us stick with those that you just mentioned. Can you give us a sense, if you know, which ones have the greatest bang for the buck in helping the small business person generally in a Mid-Eastern country?

You mentioned procurements, you mentioned transparency, you mentioned regulations, you mentioned the legal code. We cannot do everything all at once here. I was just wondering if you were talking with some of these countries, and where do we begin?

Mr. LARSON. You cannot do everything at once, but I think you can try to have a concerted approach. Let me give you an example, Senator, from a country that we consider part of the greater Middle East, even though it is not part of the narrow Middle East, and that is Pakistan.

Pakistan is a country that has made enormous progress in its economic policies and it has successfully completed an IMF program. It has done a lot of the things it needed to do to rectify its public finances. But it is a country that, according to the World Bank, where it takes 180 days to start a business.

Part of our dialogue with the government now is, you need to move to the next generation, the next stage of economic reforms. It is about unleashing the private sector. One part is deregulation, so it is easier for small businesses to get started and it does not take them 180 days.

Part of it is establishing greater clarity and transparency and even-handedness in the investment climate because there are a number of outstanding investment disputes there.

There even can be a role for the effective use of remittances because this is a country where a lot of the income comes from Pakistanis that work abroad, and finding ways to make sure that those financial flows can be used effectively to help people build homes or start businesses is another part of the story.

So, while you are quite right that you cannot do everything at once, you also need to make sure that, as you take away one barrier, that there is not another one that pops up right away to frustrate it. So I think you need a somewhat concerted attack on what are the major problems that you see in the business environment.

Senator BAUCUS. How much government resistance do you or these reform-minded businessmen encounter? Some of this might kind of upset the apple cart a little bit.

Mr. ALDONAS. There is no doubt about that. I wanted to go back to your earlier question, and I think it will flow through to the second one, Senator Baucus.

Senator BAUCUS. Sure.

Mr. ALDONAS. You almost have to differentiate between small business of different sorts. You are dealing with trading states that have been traders for millennia.

Senator BAUCUS. Right. Right.

Mr. ALDONAS. And the basic merchantman in these matters is very strong. That is something that is accepted. It is not something that, frankly, undercuts or eats away at some of the preferences that the royal family might enjoy, or something like that.

But when you start to really engage in diversification and you want to invest as a small business based on the fact you have got a strong university—you have been doing research, let us say, in biotechnology, as the Chairman was alluding to—that is when you start to build a base that is independent of the government, frankly, and its control.

I think there is a concern here, and this is where the economics and the politics come together, as to what kind of resistance you feel, because ultimately those countries that are already opening themselves to the trading system, frankly, are opting for something that says, we are going to let that flourish, and those that are a little slower in moving toward opening themselves to the trading system are the folks who are resistant to it, as much for the political as the economic reasons.

It is a phenomenon, of course, we see in China and a variety of other places where you have a command control structure that to a degree resists private equity and resists private markets. But yet everybody in the region understands the direction they are going to have to take.

That is where I go back to Al's point, which is, you see a country like Bahrain or like Qatar coming to us wanting a free trade agreement, in part, because they recognize that, to get the diversification, they are going to need to move in a different direction, both politically and economically. That is where you see that people are most interested in the openness.

Senator BAUCUS. How much is status and prestige a lever here? How much do these countries want that? That is, reaching an FTA with the United States. Does that matter?

Mr. ALDONAS. It does.

Mr. LARSON. I think it definitely does.

Senator BAUCUS. Does that mean we have a little more leverage in kind of getting what we want?

Mr. LARSON. I think it gives us added leverage.

Senator BAUCUS. My understanding is that the administration wants to expand and extend AGOA. If that is the case, why not raise the flag for the McCain-Baucus bill?

Mr. ALDONAS. I was sitting in my office yesterday and I was thinking, what would Senator Baucus ask me, and that was exactly the question I thought you would ask me. [Laughter.]

Senator BAUCUS. I knew there was a reason I liked you. [Laughter.]

Mr. ALDONAS. The fair point, Senator Baucus, is that we are going to be trying to advance the cause with respect to AGOA III, no doubt about that. I think the extension is important, at least to maintain the investments that have been based on something about which of course you showed an awful lot of leadership in putting in place.

There is a real attraction, I think, for that reason, to a similar sort of thing in the Middle East. What I think you have is a slightly different dynamic, which is, as you well know, we did not have any tools in Africa to begin a dialogue on trade.

And AGOA and the preference system were, in part, a first step toward that. It is a step that has fostered investment, it has fostered greater trade, and it has fostered a trade forum in which we have been able to start discussing the need to move further.

In some respects, I think we already have that in the Middle East. Then the question is, are we better off at this point trying to move ahead on the negotiations front where we do see real progress being made?

Again, in my own mind, you need to balance that against, on the other hand, not only could this be a valuable tool, but it is something where the commitment of the Congress, in terms of the Middle East, relative to the vicissitudes of the peace process, is also important. So, those are the sort of things that weigh on either side of the balance, as far as I can see.

Senator BAUCUS. Well, I just urge you to kind of overcome the one little impediment that we all know about that we are not talking about here so that we can get going here. It is important for trade, and so on, and so forth.

Mr. ALDONAS. It is important. No doubt about it.

Senator BAUCUS. Anything else you want to add about Egypt? I mean, in Egypt, we had a lot of promise not too long ago. The Chairman and you had a little discussion. Anything else you want to add?

Mr. ALDONAS. If I could, just to pick up on Al's point about the fact that, wholly apart from what we are doing in our relationship to try and encourage reform and movement, there is a real strong effort in this area inside Egypt, which is something that is new in some respects.

It reflects the fact that Egypt, for a long time, has been one of the central players in the region—certainly it has a very highly educated population—and it is going to have to use that as its lever in terms of its economic development strategy. That has brought people to start thinking hard about economic reforms internally.

My hope is that that matches the effort we have on the other side to say, let us engage in this process together. But what gives me some confidence after many years of fits and starts with Egypt, is that is the direction they seem to be headed internally.

Again, I think going to someone like Hernando De Soto to point out what they need to do to eliminate the friction inside the system is a good step toward what we could complement through our trade negotiations.

Senator BAUCUS. Al?

Mr. LARSON. If I could just add a couple of additional points on Egypt, since you asked. This is clearly a country that, if it is going to provide the sort of jobs that they need for the next generation of Egyptian young people, they are going to have to grow at a much higher rate than they have been growing.

They need to be aspiring to 6 or 7 percent economic growth. The only way I believe you can achieve that is through full participation in the global economy, growing their exports, attracting more foreign capital, developing these small businesses, and so forth.

I have traveled to Egypt for quite a while now. The most recent visit was certainly the most encouraging in terms of hearing a largely consistent message from the top levels of the government, and to the business community and to the young people.

In addition to meeting with senior government officials and the well-known leaders of established business community, I had a chance to meet with a group that was basically the young entrepreneurs, 40 of the most dynamic, young leaders in the business community.

What you see there is a very, very strong interest in moving forward, a recognition that this is a country that has gone through thousands of years of very strong state regulation, that this has become an impediment to their economic growth. They are making some significant changes.

I think it is a country that we want to work with to facilitate and accelerate those sorts of changes. We will never have a Middle East free trade agreement that is fully complete without Egypt being a partner in that, so it is in our interests to do that.

It is one of the largest markets in that part of the world, so it is important. But we need to make sure that they are ready to fully and wholeheartedly embrace what is going to be necessary to move to a free trade environment, and I think that is really the question.

Senator BAUCUS. One quick question. Unfortunately, it is a very complex answer. A lot of our staff has been over to the Middle East and have asked lots of questions about all this.

They came away with a very strong impression, at least people in the Middle East told our staffs when we asked what could we do to help, and the answer was, the United States is perceived as being disengaged in the Palestinian conflict. Solve that and things will work out. Now, of course, solving that is a huge problem. But, on the other hand, sometimes it is a chicken and egg question here.

How much, in your view, can this really help? Do the Israelis and Palestinians have to resolve that issue reasonably before there can be any significant Middle East trade, at least certainly in Palestine, Jordan, or Lebanon, or some of the adjacent countries, maybe even including Egypt.

Mr. LARSON. Your staff is quite right that you cannot travel in the Middle East without having this issue come up at every single occasion. I think there are two broad answers to the sort of messages that they were hearing.

One, is that the United States is committed to facilitating this peace process. The President is supporting the road map. We are working very, very hard to encourage both sides to carry out their responsibilities under it. The President has set out the goal of having an independent Palestinian state living side-by-side with Israel in peace.

But it is an extraordinarily difficult task. If I could, Senator, just in my very brief visit there, my first stop was going to be Ramallah for meetings with the Palestinian authority because we have an interest in promoting better economic and social conditions for the Palestinian people.

Within minutes of the time I was leaving to go to that meeting, there was a suicide bombing in Jerusalem. A number of people were killed. So, the first hour of our conversation with the Prime Minister of the Palestinian authority had to be about the importance of his ensuring that there was a secure environment, because that is part of their responsibilities under the road map.

At the same time, we saw firsthand all of the difficulties that the Palestinians are living under, including the separation wall and the internal barriers to movement that make it very difficult to get economic life going.

So, we are working hard on both the political and economic side of this, but it is a tough issue. The other answer, though, is that we cannot let our effort to promote broad reform be held hostage to the day-to-day ups and downs of the peace process.

The honest truth is, if peace broke out between the Israelis and the Palestinians tomorrow, we would still have these problems elsewhere in the region. So, we must work on them even as we work on the Middle East peace process.

Senator BAUCUS. I appreciate that. We have got real time constraints here. Briefly.

Mr. ALDONAS. Sorry, Senator. Just to reinforce that last point on balance.

Senator BAUCUS. I have to call the next panel.

Mr. ALDONAS. Yes. Regardless of the vicissitudes of the peace process, one thing we have to have is the commitment really on both sides to make sure that we are taking care of the economic circumstances.

As long as Hamas is delivering medical services, as long as it is providing education in Palestine, it is going to be difficult to say that there is another future. So part of what we need to do is make sure we are making the commitment to make those things happen.

I happen to think that that is going to require a similar move toward reform by the Palestinian Authority along the lines of all the other countries in the region, so there is a reason to continue working on this theme: so that we make the commitment economically, but also so we tell the Palestinians that they are going to have to move on all those sorts of issues we face with other countries in the region, so that we move away from corruption, we move away from the sorts of things that would prevent somebody from putting together an industrial park leading to investment and allowing business to go on.

Senator BAUCUS. Well, I thank you for your efforts.

Mr. ALDONAS. Thank you.

The CHAIRMAN. Thank you very much as well.

Now I call the last panel. We have three witnesses: David L. Mack, vice president, Middle East Institute here in Washington, DC; Mr. William A. Maxwell, director of International Trade Policy & Business Development, Hewlett-Packard Company, and Mr. Doug Boisen, corn farmer and chairman of the Joint Trade Team of the National Corn Growers Association and the U.S. Grains Council. He lives in Minden, Nebraska.

I think I would have you go in the order in which you were introduced.

I wonder if I could ask Mr. Mack to go first, then Mr. Boisen, because at 3:25 I am going to have to go over to the floor of the Senate.

Senator BAUCUS. I have to, too.

The CHAIRMAN. Oh. You do, too. All right.

Then what we are going to have to do, is we are both going to listen to the three of you, and then we will have to submit our questions to you to answer in writing. He and I have to go to the floor to debate aspects of the budget resolution as it relates to the work of this committee at that time.

So just proceed, Mr. Mack.

STATEMENT OF HON. DAVID L. MACK, VICE PRESIDENT, THE MIDDLE EAST INSTITUTE, WASHINGTON, DC

Mr. MACK. Thank you, Mr. Chairman, Senator Baucus. I am honored to appear before the committee to talk about my experience as it relates to these very important issues that you are considering.

I have submitted a full statement for the record, if you approve.

The CHAIRMAN. Yes. All three of you will not have to ask. Your statements will be put in, and then we ask you to summarize in 5 minutes.

[The prepared statement of Mr. Mack appears in the appendix.]

Mr. MACK. Trade and investment treaties, free trade agreements, and similar instruments prod governments in the Middle East and North Africa to adopt economic reforms.

Such measures strengthen the private sector, lead to greater transparency, and rule of law. This includes regulations that enforce measures against international crimes, especially including money laundering.

Given the proper incentives, the private sector can provide jobs and hope to young men and women whose families have invested in their education. Without constructive outlets, the emerging generation will be fodder for elements that foment hate and violence.

My perspective is based really on 40 years in dealing with this region as a U.S. diplomat, a businessman, and now as an educator. Despite promising exceptions, most of the Arab countries and Iran still have stagnating economies. Ties between government elites and relatively few family commercial empires tend to dominate economic activity and hamper the emergence of competition.

It is commonplace to describe Arab political economies as being subject to over-regulation, and certainly this is one of the primary problems in a country like Egypt. But we also need to acknowledge the problem of under-regulation in many of the newer states of the Gulf.

When I became ambassador to the United Arab Emirates in 1986, I found the UAE's small, but lucrative markets overflowing with fraudulent copies of brand-name consumer goods ranging from automobile spare parts to music cassettes.

UAE Federal institutions in this area were weak to non-existent. Rule of law, sanctity of contracts and transparency were, at best, unpredictable. Patents, trademarks, and copyrights had very limited protection. In effect, the UAE was becoming a pirate's cove with no meaningful intellectual property protection.

The U.S. Government offered negotiations to avoid retaliation. Our negotiations encouraged the UAE to take pride in meeting a high standard. Now the UAE is an increasingly valued commercial partner. Last year, the U.S. had a $2.5 billion favorable trade balance on our account with the United Arab Emirates.

In 1993, the Departments of State and Commerce launched the first of what became annual economic dialogues with the six states of the Arab Gulf Cooperation Council.

It was clear that the dominant oil and gas sectors of those economies were not creating jobs at anything close to the pace required to absorb the increasing number of graduates from universities and high schools.

Our intention was to inject new life into U.S. relations with our Arab Gulf political and economic partners by encouraging economic and regulatory reforms.

Results of that first annual dialogue were, frankly, quite disappointing. Both sides made resounding affirmations of shared interests, but showed a lack of serious self-examination.

Many speakers from the region were very long on assertions of opportunity for U.S. firms, but avoided commitments to the kind of reforms that the Departments of State and Commerce suggested were necessary. The United States made no commitments about what we might be prepared to do in response.

When, as chairman of the U.S. delegation, I made a very cautious call for gradual and orderly political reforms, that was met by a very chilly silence, even though I knew that I was echoing views I had heard from many of those businessmen and intellectuals from the region.

In the years since then, the Arab business communities have become more vocal in expressing the need for economic reforms. They know this is the price for entry into the global economy, either as members of the World Trade Organization or as partners with the United States in bilateral agreements.

They understand that the discipline these negotiations provide may be a necessary catalyst for internal change in their own economies, in their own societies, and political systems.

There is fear that change will upset a familiar and comfortable cultural order, but Arab business elites fear even more the social and political consequences of inaction. Various political leaders have now joined the more dynamic members of the business community to call for reform, including more relevant education.

From the U.S. perspective, trade negotiations are a business-like, and if I may say so, a non-sanctimonious way for us to promote positive change. Arab governments and business establishments see the connection between economic and social reform and their long-term security.

They know this has implications for the traditional political order, although commitment to change in that regard is very cautious. It requires vision to take risks and make uncomfortable adjustments. Resistance to high-profile U.S. pressure for political reforms is almost certain, and we are seeing it today.

The prospect for political reform requires that it emerge as an authentic expression of local aspirations, and we can support people who share these aspirations by trade negotiations.

Thank you very much, Mr. Chairman and Senator Baucus.

The CHAIRMAN. Thank you.

Now, Mr. Maxwell?

STATEMENT OF WILLIAM A. MAXWELL, DIRECTOR, INTERNATIONAL TRADE POLICY & BUSINESS DEVELOPMENT, HEWLETT-PACKARD COMPANY, WASHINGTON, DC

Mr. MAXWELL. Chairman Grassley and Ranking Member Baucus, thank you for providing me with the opportunity to speak to you today. I am here to discuss how the United States can improve security in the Middle East and globally by fostering greater economic opportunities in the area, and how free trade and other market-oriented-based economic incentives can serve as the foundational pillars for achieving a more stable and prosperous Middle East.

Several examples of countries having undergone transitions to free market economies since the 1970's, including Spain, Taiwan and South Korea, demonstrate the power of industry and commerce to facilitate social, political and regional stability.

In each of the aforementioned cases, political reform was not imposed on autocratic systems from the outside, but rather it was grown from the inside, largely by the rising middle class that demanded social and political rights, much as Ambassador Mack referred to.

Moreover, in each case the lure of participating in a regional trading bloc, in the case of Spain and the European community, and the benefit derived from already participating in such blocs, as in the case of Taiwan and South Korea, and we are talking now about APEC, the participation in these regional trading blocs will provide a powerful impetus for reform.

Perhaps it would be useful to think in terms of encouraging the creation of a similar organization in the Middle East, the Middle East Economic Cooperation Initiative. The creation of a common Arab market could yield similar dividends to the nations of the Middle East as they have in Spain, South Korea, and Taiwan.

Taken as a whole, the 22 Arab-speaking nations have a population of more than 200 million and it represents a region of great potential, both in terms of consumer demand and human capital.

However, while population is expected to grow at 5 percent a year, gross domestic product growth is projected to remain at 3 to 4 percent, which means that, absent some economic shift, it will be difficult to reduce current levels of unemployment, which run as high as 20 percent.

This demographic challenge has led many Arab leaders to acknowledge that part of the solution must be attempting to attract new businesses and foreign investment to the area.

However, this is precisely where much of the problem arises. Rather than one unified market, the Arab-speaking world today has 22 separate markets, each with its own rules, regulations, barriers to investment, and trade restrictions, all of which leads to a striking lack of regional cooperation.

During the 1990's, less that 7 percent of the Middle East trade came from other countries within the region. Contrast that with Europe, where more than two-thirds of all trade is among the countries of Europe, or Asia, where 30 percent of the trade originates within Asia.

The lack of unification and cooperation among Middle Eastern countries has also put the region at a competitive disadvantage in the global economy. For companies, like Hewlett-Packard, which operates in 178 nations around the world, it is less problematic and more cost efficient to conduct business in regions defined by cooperation, such as the European Union and APEC.

Such trade areas offer more hospitable investment climates, lower transactional costs, less restrictive barriers to entry, higher standards of transparency, and more access to capital.

In the 1950's, the per capita income level in Egypt and Korea were virtually equal. Today, Egypt's per capita income level is less than one-fifth of South Korea's. Similarly, Saudi Arabia's per capita gross domestic product was at one time higher than Taiwan's, but now is only half of Taiwan's output. To put these figures in perspective, the combined gross domestic product of all 22 Arab-speaking nations is less than the gross domestic product of Spain.

Integrating 22 Arab-speaking nations of the Middle East into one common market is not without obstacles. As many Arab leaders know, however, this is not about solutions being imposed from outside, but is an issue of fundamental self-interest.

The reason companies like Hewlett-Packard are so committed to the Middle East today is because we believe in the vast promise of the region. As Carly Fiorina, Hewlett-Packard's chief executive officer, CEO, said in a recent speech, "HP is privileged to do our part . . . in fostering the economic development of the area." HP has made a commitment to be an asset as well as a partner as the future of the Middle East takes shape.

We are proud today to be the largest information technology company operating in the area, working from Saudi Arabia to Egypt, Jordan to the UAE, to use IT to empower more people than ever before.

As Senator Baucus said in the statement accompanying the submission of Senate bill 1121, the Middle East Trade and Engagement Act of 2003, "Historically, the Middle East has played an important role in global trade. Economics and history proved that, as markets opened, business grows. As business grows, jobs are created, both in the regions of investment, as well as investing in nations."

Thus, Hewlett-Packard sees the economic growth in the Middle East as a means to revitalize and strengthen ties both between the countries in the region, as well as between the Middle East and the United States.

In this context, on behalf of Hewlett-Packard, please allow me to express our company's support for S. 1121, as introduced by Senator Baucus and Senator McCain. The bill promotes the notion of free trade and other market-based economic incentives that are fundamental to achieving stability and prosperity in the Middle East. Thank you, Mr. Chairman.

[The prepared statement of Mr. Maxwell appears in the appendix.]

The CHAIRMAN. Now, Mr. Boisen?

STATEMENT OF DOUG BOISEN, CORN FARMER AND CHAIRMAN OF THE JOINT TRADE TEAM OF THE NATIONAL CORN GROWERS ASSOCIATION AND THE U.S. GRAINS COUNSEL, MINDEN, NE

Mr. BOISEN. Thank you. Good afternoon, Chairman Grassley and Senator Baucus. I want to thank you for the opportunity to testify and to speak today.

I am especially pleased to be here today to talk about Middle East trade. Much of the demand in the region is targeted to satisfy the demand for protein-based animal products.

In 2001 and 2002, the total corn imports by countries in the region was approximately 11.6 million metric tons, of which the United States supplied 7.7 million metric tons, or 66 percent.

While imports to the region increased this last year, the U.S. market share dropped to 41 percent due to competition from Argentina and China. Despite this, U.S. corn imports are rising to historic levels with large purchases recently by Egypt, Israel, and others.

While many governments seek to increase production of various feed crops, the region's climate and scarce water supplies are expected to put these countries in a situation to rely even more on imports. Growth in income and population are fueling rising consumption of poultry, and to a lesser degree, beef, dairy and sheep products.

In addition, future growth will largely depend on demographic changes. Nearly a third of the population in these countries is below the age of 15 years. Changing eating habits of younger generations is impacting the demand for animal products. As a result, we expect the region to be an expanding market for U.S. feed grains in the future, given the economic and political stability.

Let me take this opportunity to highlight five countries in the current and future growth opportunities available to corn and feed grain producers.

Egypt's population of 68 million has grown at a 2 percent annual rate over the past decade, while per capita income has nearly doubled. Population growth, coupled with increase in consumer disposable income, has translated into increased demand for meat, milk and eggs, and, consequently, demand for imported feed grains.

This is reflected in Egypt's increased corn imports from 1.2 million metric tons in 1990 to 5 million metric tons in 2002. Consequently, Egypt has become our fourth-largest corn market.

The National Corn Growers Association was disappointed by Egypt's withdrawal as a co-complainant in the case filed by the U.S. Government against the European Union for its illegal moratorium on crops produced with biotechnology.

After initially committing to support the case, the Egyptian government withdrew support in May of 2003. Egypt's unwillingness to challenge the unfair trading rules illustrates the pressure the European Union is applying to its trading partners to sustain its trade-restricting policies toward genetically engineered crops and foods.

In Syria, the rapidly increasing population and rising expendable income suggests a bright future for the development of the poultry sector in that country. A strong demand for dairy products and limited commercialization of the dairy sector also holds potential for growth.

Syria imported approximately one million metric tons of corn last year, with the U.S. supplying almost 60 percent of that total. It is projected that corn imports will grow to 1.6 million metric tons by 2008.

Likewise, Saudi Arabia is import-dependent on most feed ingredients required to sustain its domestic livestock and poultry sectors, so much so that the government subsidized corn and soy meal shipments.

Once importing over a million tons a year from the United States, Saudi Arabia has looked to other suppliers recently. Although we hope to regain market share in that country in the near future, looming concerns over biotechnology could cripple U.S. presence in that market, as well as have repercussions in other parts of the region.

Turkey has been a moderate-sized market for U.S. corn for a number of years, based mostly on solid growth in the poultry industry and for industrial use. However, a primary obstacle to growth is the use of seasonal import duties that coincide with the Turkish corn harvest. The duties are held in place until the domestic crop is marketed and stocks are depleted. In these terms, it would make Turkey a prime candidate for an FTA.

One other country I would like to mention is Iraq. Through the 1980's, Iraq was a consistent importer of corn from the United States. In 1989, Iraq imported 650,000 metric tons of corn, nearly all of it from the United States.

Much of these imports went to a growing poultry industry, however, following the Gulf War in 1991, grain imports and the poultry industry collapsed. Rebuilding of Iraq will require significant expansion in both the poultry and livestock sectors just to get back to the per capita consumption levels of animal protein that Iraq had in the late 1980's.

We are working with the Foreign Agricultural Service and the American Soybean Association to rebuild Iraq's poultry sector. In helping to accelerate the rebuilding of this sector, we will also be building a viable market for U.S. feed grains.

As illustrated, the Middle East represents significant growth potential for corn and feed grain producers. The U.S. Government and organizations like the National Corn Growers Association and the U.S. Grains Council need to promote the benefits of trade liberalization in the Middle East and around the globe.

We look forward to working with the committee on this and other important issues in the future and I thank you again for the opportunity to address the committee.

[The prepared statement of Mr. Boisen appears in the appendix.]

The CHAIRMAN. Thank you.

Now, normally, as you know, we would ask questions of you. But we are debating the reconciliation part of the budget legislation, and that is why I have to go to the floor now. So, I am going to submit questions for answer in writing.

[The questions and responses appear in the appendix.]

The CHAIRMAN. I thank you all very much. The hearing is adjourned.

[Whereupon, at 3:32 p.m., the hearing was concluded.]

APPENDIX

Additional Material Submitted for the Record

Prepared Statement of Hon. Grant D. Aldonas

Thank you, Mr. Chairman, Senator Baucus, and Members of the Committee, for inviting me to testify before the Senate Finance Committee and thank you for holding this important hearing. I welcome the opportunity to discuss the importance of economic reform and diversification in the Middle East, particularly the extent to which U.S. trade policy and the Commerce Department's efforts can contribute toward those worthy goals.

I applaud your leadership in this area and commend you for sending a Congressional staff delegation to Morocco, Egypt, Bahrain and Yemen last month. Both your interest in the Middle East and your commitment to exploring the ways in which we can foster a stronger trade and commercial relationship with our trading partners there reflects an understanding of the need for increased engagement with the region.

In the absence of increasing contact and interchange between the United States and the Middle Eastern people, we will not build a relationship of trust and friendship, which is the key to a more peaceful and secure world. Those contacts can begin, as they have for centuries in the Middle East and elsewhere, with the most basic of human relationships—the free exchange of goods and services that makes up the world of commerce.

What's more, despite the evident conflict in the region, the Middle East nonetheless represents fertile ground for the seeds of an initiative that would foster our commercial ties. I am certain that it is not lost on the Committee that the current round of World Trade Organization (WTO) talks were launched the Middle East. The Doha Development Agenda is not only a tribute to the members of the WTO and their commitment to using the world trading system as a primary tool of economic development, but also to the trading nations of the Middle East and the leadership of their officials, particularly the Emir of Qatar. That leadership proved instrumental in launching a trade round that could provide tangible benefits to the people of the Middle East, as well as every man, woman and child around the world.

There is one other and more fundamental reason that I refer to the launch of the new WTO round. Shortly after the events of September 11, I had the opportunity to be in Doha and see first-hand the thirst among the developing nations of the world for the benefits of free and fair trade. That thirst made real the need to extend the benefits of the world trading system to the developing world if we want to live in a world of peace and stability—a world in which there is hope for that half of the planet that currently lives on less than $2 per day.

The importance of the new round, and trade in general, to the developing country members of the WTO should surprise no one. Indeed, it is the developing countries that have the most to gain. A study by Joseph Francois of Erasmus University projects that global trade negotiations would generate between $90190 billion a year in higher incomes for individuals living in developing nations. It's no wonder that UN Secretary General Kofi Annan has said, "The poor are poor not because of too much globalization, but because of too little."

The Middle East/North Africa region, unfortunately, matches this description. While the region represents five percent of the world's population, it accounts for only two percent of world's income. According to the World Bank, the incomes and wages in the Middle East and North Africa are low (compared to those in other regions), and its population is growing; the annual growth in the labor force is projected at 3.4 percent a year from 2000–2010, which is twice the rate found in other developing countries.

As historian Bernard Lewis puts it in *The Crisis of Islam*, "The combination of low productivity and high birth rate in the Middle East makes for an unstable mix, with a large and rapidly growing population of unemployed, undereducated, and frustrated young men . . . . the Arab countries—in matters such as job creation, education, technology, and productivity—lag ever further behind the West." In fact, according to the Arab Human Development Report 2002, the combined gross domestic product (GDP) of the 22 Arab states ranks lower than Spain's alone. The region's trade integration has changed little in the past 20 years, and, apart from the Gulf countries, the region falls behind other developing countries in attracting foreign investment.

With a few exceptions, tariffs and quotas are no longer significant barriers in industrial economies, but they remain high in most of the developing world. This is counterproductive. Reductions in market access barriers can promote trade, in particular trade between developing countries (south-south trade), and improve investment flows. In general, liberalized trade improves the quality of life of those in the world, which is why we must move forward with our global trade talks. We must encourage our Middle Eastern counterparts to join us at the negotiating table—for their benefit as well as ours.

The Importance of Diversification and Reform

Mr. Chairman, President Bush's proposal to create a U.S.-Middle East Free Trade Area (MEFTA) by 2013 and the Middle East Partnership Initiative (MEPI) remain two important policy tools for promoting diversification and reform. The MEFTA offers a vision of openness, trade integration, and economic development. The MEPI includes economic reform objectives to promote entrepreneurship and private sector development in these markets. These both advance what the President calls "a forward strategy of freedom in the Middle East." In his speech to the American Enterprise Institute in February 2003, the President noted that, "Leaders in the region speak of a new Arab charter that champions internal reform, greater political participation, economic openness and free trade."

We need to work with those leaders, especially as long-term growth, employment and investment prospects in the Middle East and North Africa depend on economic reform and economic diversification. The countries in the region must remove impediments to foreign direct investment, strengthen labor markets, accelerate privatization, and further integrate into the global economy. Some of these reforms are already underway, but at varying speeds and degrees of commitment. The region needs to diversify away from oil-sector employment and public-sector growth toward more fully employing its fast-growing population. The region's non-oil producing countries over the past three decades have maintained real GDP per capita growth—unlike their neighbors who rely on petroleum. In many cases, the dependence on oil production has created parastatal structures that stifle private sector involvement in the economy and foster an enormous federal presence.

The region needs greater economic growth to create jobs—approximately 80 million new jobs are needed. According to the World Bank, the region's labor force will grow from 104 million in 2000 to 185 million by 2020. This will be difficult given the current 15 percent unemployment rate and a stagnant private sector. Diversification, especially through private sector growth, can produce many of those necessary jobs, provided that market forces are allowed to operate unhindered by government bureaucracy and corruption. Inadequate and restrictive insurance and monetary regimes also stifle growth. The World Bank projects that, if the region were to achieve non-oil export growth of about 15 percent a year, it could generate some 4 million jobs during the next five years. World Bank, 2003: *Trade, Investment, and Development in the Middle East and North Africa*.

While the MEFTA and the MEPI are not the only approaches that we might take to expand our trade and investment relationships with our friends in the Middle East, they have already proved to be catalysts for further thinking about the needs of the region and what would unleash the dynamism of the young people throughout the Middle East. I look forward to continuing our work together to foster our trade and engagement in the region.

Examples of Ongoing Reform and Diversification: Kuwait, UAE, Jordan

To reinforce the practical value of the President's proposals and initiatives focused on fostering trade in the Middle East, it is worth looking at the examples of ongoing reform and economic diversification that already exist. Certainly, at the Commerce Department, we continue to press for ongoing reform and economic diversification within the region, for the benefit of our trading partners and American firms engaged in the Middle East.

Kuwait, the United Arab Emirates (UAE), and Jordan seem to have heard and understood our message of open trade and economic reform, and they are beginning to reap the benefits. In the case of Kuwait, they have just begun to reform their economy and are looking forward to a closer relationship with the United States through the recently signed Trade and Investment Framework Agreement (TIFA). The UAE has begun to reform and diversify and has emerged as one of the most successful economies in the region. Finally, Jordan has begun to reap the benefits from its bilateral trade agreement with the United States

Kuwait is currently on the verge of implementing reforms and diversifying its economy away from oil. Bureaucratic inertia and the all-too-real threat from Saddam left the economic agenda behind. Currently, the private sector contributes to 22 percent of Kuwait's GDP, compared with 37 percent in 1982, according to the National Bank of Kuwait. The oil sector, which is part of the public sector in Kuwait, contributes a full 45 percent of GDP. In addition, the number of job seekers registering with the Kuwaiti Civil Service Commission has risen from 3,237 in 1997 to 21,213 at the beginning of 2004. Projections indicate that 25,100 Kuwaitis per year will have to find jobs outside the public sector.

Reform has been occurring, albeit slowly. Kuwait recently passed a new investment law allowing 100 percent ownership in nearly all sectors of the economy, excluding the press and publishing. Banking and financial services, healthcare, information technology, transport, tourism, and real estate are all now open. Significantly, the new law stipulates a 10-year tax exemption granted to foreign owned businesses. Before this provision went into effect in October 2003, foreign firms in Kuwait had to pay a sizeable 55 percent excise tax on profits from the start of operations. Kuwait also recently liberalized its commercial airline sector, allowing competition with the state-owned Kuwait Airways. Impressively, Kuwait plans to allow a larger foreign presence in the oil sector, with a public, international tender for the development of their northern oil fields.

The UAE has made great strides in tenns of economic diversification and reform. Although the overall performance of the UAE's economy remains heavily dependent on oil exports, which account for nearly 30 percent of total GDP, the non-oil sectors of the UAE's economy are experiencing strong growth, particularly the petrochemicals and financial services sectors.

The UAE has created an inviting business environment and transformed itself into a truly international center for commerce and trade. It has the third busiest port in the world in terns of volume, with UAE's Dubai Jebel Ali port ranking behind Singapore and Hong Kong. More than 200 factories operate at the Jebel Ali complex in Dubai, which includes a free trade zone for manufacturing and distribution in which all goods for re-export enjoy a 100 percent duty exemption.

In recent years, the UAE has undertaken several projects to diversify its economy and to reduce its dependence on oil and natural gas revenues. The Abu Dhabi Investment Authority works to bring foreign investment into the country, while Etisalat, the local telecommunications company, has succeeded regionally. The non-oil sectors of the UAE's economy presently contribute about 30 percent of the country's total exports.

Dubai has become a central Middle East hub for trade and finance, accounting for about 85 percent of the Emirates re-export trade. Additionally, the government has programs to educate the local business community and encourage understanding of the Internet and its capabilities. The Dubai Internet City is a successful example of government investment and growth incentives leading to a thriving local business sector. Several Commerce officials, including former Deputy Secretary Bodman and Assistant Secretary Lash, met with officials from the Dubai Ports Authority and the Jebel All Free Zone during missions to the region to encourage the free-enterprise initiative.

Jordan has been at the forefront of creating business opportunities and economic growth in the Middle East. Jordan supports an open investment climate, codified by the 1995 Investment Promotion Law, which offers incentives and national treatment to investors. In 1998, Amman embarked on an ongoing privatization program that includes the sale of the Jordan Flight Catering Company to Alpha, a U.K. firm, the sale of the remaining 14.3 percent Government of Jordan (GOJ) stake in the Jordan Cement Factories Company to the Social Security Corporation, and the sale of the 10.5 percent GOJ share of Jordan Telecom via an initial public offering. In October 2003, the GOJ sold 50 percent of its stake in the Arab Potash Company to a Canadian company. The GOJ continues to seek a strategic foreign partner to buy up to 49 percent of Royal Jordanian (RJ) Airline's operating division.

Jordan acceded to the WTO in April 2000 and seeks to become a business gateway and trade hub for the region. It signed free trade agreements with numerous Arab countries and has had an Association Agreement with the EU since 1997. With the

United States, Jordan has a Qualified Industrial Zones agreement, a bilateral investment treaty that entered into force in 2003, and a Free Trade Agreement signed in 2000, which came into force in December 2001.

Jordan's economy has grown since King Abdullah ascended to the throne in 1999. It grew by five percent in 2002, 4.1 percent in 2001, and over the last four years, economic growth rates in real terms averaged 3.5 percent. The strongest growth has been in the export sectors, particularly pharmaceuticals and textiles. Growth in 2003 slowed to about 3 percent due to the disruption of the country's traditional relationship with Iraq, which it had obtained oil at below market prices.

But, that recent downturn simply highlights the importance of the initiatives under way in Jordan under the King's aegis. Jordan's information technology (IT) sector, for example, is at the top of the national agenda, as Jordan has a higher proportion of university graduates in the technology field than any other Arab country. However, Jordan continues to face numerous economic challenges, especially given its limited natural resources and high population growth rates (2.8 percent annually). Up to 30 percent of Jordan's population lives below the poverty line, and 15 percent of the labor force is unemployed. Our trade with Jordan can ensure that more young Jordanians will see their future in a burgeoning information technology sector, rather than in poverty.

Commerce Activities to Foster Regional Reform and Diversification

Consultations, Negotiations

The President's strategy includes active U.S. support for WTO membership for countries in the region that are interested and eligible. WTO membership provides a platform on which we can build with other liberalizing measures, such as Trade and Investment Framework Agreements and comprehensive Free Trade Agreements (FTAs). My agency actively participates in TIFA council meetings.

We have established TIFA councils with: Algeria, Egypt, Saudi Arabia, Tunisia, Kuwait, and Yemen. We expect to hold meetings soon with the UAE, Qatar, and Oman. These formal consultations serve as the most direct method through which we influence and emphasize the importance of reform in the Middle East. We work closely with the United States Trade Representative on FTA negotiations and contribute sector, trade, and investment-issue expertise. I am pleased that we concluded the FTA negotiations with Morocco earlier this month and have made excellent progress in the negotiations that we began with Bahrain at the beginning of the year.

In addition, we are exploring the possibility of allowing 'regional cumulation' under our FTAs in the Middle East and North Africa, so that a country could meet the FTA's rule of origin with inputs from other U.S. partners in the region.

Market Access, Compliance and Capacity Building

We carefully monitor our trade agreements. Obligations are useless unless they are monitored and enforced. Assistant Secretary for Market Access and Compliance (MAC) William H. Lash has visited the region five times already, and he plans to return. MAC staff has worked with all the countries in the Middle East to protect intellectual property rights. With better protection, indigenous and international companies in fields such as information technology, pharmaceuticals, and the arts can flourish and provide jobs.

Our work to press for market access reforms coincides with diversification goals and can serve as a catalyst for structural adjustment. Working with the governments in the region to open markets creates new opportunities for foreign investment and knowledge transfer. These new opportunities in turn help to build a more stable and varied economy, which can better absorb the growing population and is less prone to volatile shocks caused by fluctuations in world oil prices.

Assistant Secretary Lash also wears another hat. He heads our task forces on Iraq and Afghanistan—looking at reconstruction and the continuing reform in both countries. Under his leadership, the Department's Iraq Investment and Reconstruction Task Force counsels U.S. business on opportunities in Iraq and advises U.S. companies about going into Iraq (*www.export.gov/iraq*). We work directly with the Coalition Provisional Authority to develop the commercial, legal, and regulatory environment in Iraq necessary for economic growth and private sector activity. Recently, with our support, the World Trade Organization accepted Iraq as an observer.

Most importantly for the region as a whole, Secretary Evans has created the Iraq Reconstruction Regional Initiative, through which Commercial Service officers in countries neighboring Iraq have formed a Regional Field Team to coordinate activities to support the efforts of those in Iraq and to maximize the positive impact on Iraq reconstruction. This team focuses on reaching out and helping U.S. firms and facilitating participation by host country national firms in the reconstruction of Iraq and the development of the Iraqi market through the sale of goods and services and the establishment of operations in Iraq.

Similarly, the Afghanistan Investment and Reconstruction Task Force assists companies by gathering and disseminating information on commercial opportunities associated with reconstruction activities in Afghanistan. The Task Force provides business counseling and assesses the feasibility of individual projects and proposals. Information can be found at *www.export.gov/afghanistan*. The Task Force coordinates with the National Institute of Standards and Technology (KIST) to bring international standards to Afghanistan. My Department and the Afghan Ministry of Commerce co-lead the U.S.-Afghanistan Commercial Working Group, an ongoing dialogue of all aspects of bilateral economic and commercial relations. Assistant Secretary Lash and the Task Force participate in outreach events to Afghan American communities nationwide. Finally, the Commerce Department and the U.S. Trade and Development Agency co-sponsored "Afghanistan: Rebuilding a Nation," conference in June 2003 with presentations on 35 projects to over 430 conference participants, including 300 company representatives.

The Commerce Department also assists Middle Eastern economies in their reform efforts through our Commercial Law Development Program (CLDP). Most of this effort is currently focused in North Africa and Egypt. CLDP will supply a large portion of the technical assistance required under the U.S.-Morocco Free Trade Agreement. In 2004, CLDP will spend $800,000 in four categories: IPR enforcement, transparency in government procurement, customs modernization, and compliance with U.S. standards. In providing this assistance, CLDP will help Morocco meet its FTA commitments and create a better environment for U.S. business investment.

CLDP leads the U.S. government's technical assistance efforts to help Algeria become a WTO member. The Department of Commerce, through CLDP, is easing Algeria's transition into the global marketplace by providing standards training, reviewing Algeria's draft IPR legislation, and showing Algerian judges how to adjudicate commercial disputes. CLDP has also targeted areas where U.S. expertise can best support Tunisia's efforts to liberalize its economy and open its markets. Projects have included training in trade remedies, competition law and policy, intellectual property rights protection, and e-commerce. Currently, CLDP programs in North Africa are being funded through the State Department's Middle East Partnership Initiative (MEPI) program.

In Egypt, the CLDP works in the general areas of trade-related institution building, intellectual property rights, regulatory and quality controls, as well as providing technical assistance for specific legislation drafting. CLDP continues to advise Egypt on e-commerce matters and sponsors Egyptian real estate officials to attend symposiums and workshops in the United States. CLDP provided Intellectual Property Rights (IPR) training to judges and attorneys after Egypt passed a comprehensive IPR law in 2002. The IPR law was a direct result of continuous consultation between our two governments, with the USPTO and CLDP providing technical support and review for the legislation.

Through MEPI funding, the Department of Commerce has created the Middle East Executive Training in the United States (MEET U.S.) program. The MEET U.S. program exposes Middle Eastern business executives to U.S. products and business practices, creating a cadre of executives who are predisposed to doing business with the United States. The program also facilitates trade between Middle Eastern companies and U.S. small and medium-sized businesses that otherwise might not have the resources to directly enter these markets. So far, the MEET U.S. program has conducted visits to the United States by Middle Eastern women entrepreneurs, as well as health administration executives.

Commercial Diplomacy, Private Sector Development and Trade Promotion

We currently have an office in Tel Aviv, Israel that has initiated Access Eastern Mediterranean (AEM). AEM brings together our CS colleagues in Israel, Egypt, Jordan, Lebanon, Turkey and West Bank/Gaza, to target opportunities for U.S. exporters of equipment and services in the Building Materials and Construction, Energy/Electrical, Environmental and Water, Medical and Healthcare, and ICT/Telecoms sectors. We currently have 17 Commercial Service officers and 78 local staff who work in 17 offices in the region: Abu Dhabi, Alexandria, Algiers, Amman, Beirut, Cairo, Casablanca, Dhahran, Dubai, Islamabad, Jeddah, Jerusalem, Karachi, Kuwait, Lahore, Riyadh, Tel Aviv. We plan to have an office with two to three officers in Baghdad by July 1.

This year, our Commercial Service will establish a Middle East Business Information Center (MEBIC), which will act as a focal point providing information to U.S. businesses about market conditions and opportunities in the Middle East, ITA functions and other US Government services to help U.S. companies access these markets. The Center will support the Administration's goal of fostering closer economic ties with the region and will be linked to the MEPI economic reform objectives to promote entrepreneurship and private sector development in these markets.

I want to assure you that we are regularly exploring new venues for fostering our trade and commercial relations in the Middle East as well. One salient example is the U.S.-Jordanian Entrepreneurship Forum, which will be held in Jordan on June 6–7, 2004, under the auspices of the U.S. Department of Commerce and the Jordanian Ministry of Industry and Trade. The goal of the forum is to foster the exchange of ideas between U.S., Jordanian, and Palestinian entrepreneurs, government officials, venture capitalists and academics, and to accelerate economic growth in Jordan and Palestine through entrepreneurship. The forum recognizes four key components important to the development of entrepreneurs and their companies—entrepreneurial training, capital formation, the legal and regulatory environment, and the role of innovation/use of technology.

Beyond that, we are exploring the formation of a U.S.-Palestinian private sector dialogue to promote Palestinian private sector development, as well as broader commercial cooperation between Palestinian and American businesses. This forum is expected to identify pressing commercial issues and highlight local and regional requirements, needs, and concerns regarding business development in the West Bank and Gaza. I expressly hope to include members of the Israeli business community in our approach given their stake in the economic future of the region and the benefits they saw from the implementation of the Qualified Industrial Zones in Palestine in the 1990s.

I was also heartened by a recent article in *The Wall Street Journal* reflecting the renewed interest of the Israeli business community in investment in Palestine. Their interest reflected an understanding that, unless there is an alternative to the forces opposed to peace in providing for the basic needs of life—a job, a roof over one's family, schools, access to healthcare, etc.—there can be little doubt that continuing strife will prevail. In my view, the interest of the business community, if combined with the energy and initiative of governments in creating a business-friendly environment, would attract investment and create jobs. In that sense, a commitment to expanding trade with the region represents one important part of a multi-faceted approach to fostering peace and stability in the Middle East.

Conclusion

Mr. Chairman, the region will see dramatic changes in the years ahead. Middle Eastern countries must develop their private sectors and open their economies, if they are to grow and meet the demand for jobs spurred by population growth. Without economic stability, we can have little hope of political stability. Our bilateral trade with the Middle East (minus Israel) amounted to just under $52 billion in 2003. This is less, individually, than out bilateral trade with Canada, Mexico, China, Japan, Germany, the United Kingdom, or South Korea.

Clearly, we need to do more. The Doha Development Agenda offers the best opportunity for deeper economic engagement on a global scale. MEFTA and MEPI also are strengthening bilateral ties. The MEFTA promotes cumulation among a framework of trade agreements and the use of the Generalized System of Preferences (GSP), which provides duty-free entry for many products from eligible developing countries. I hope we can count on your support for these initiatives.

Chairman Grassley, Senator Baucus—working on the African Growth and Opportunity Act with you and Senators Roth and Moynihan remains one of my proudest achievements. You were able to garner strong bipartisan support for the most generous trade preferences that we extend. You did this in the spirit of fostering regional integration and building democracy. These are worthy goals, and the process has benefited the people of Sub-Saharan Africa.

I know that same spirit animates your interest in the Middle East, and I applaud your interest and commitment. As Secretary Don Evans has said, "We believe it is through economic development and economic growth that we will lead the world to greater peace and prosperity." I cannot think of a more valuable goal.

Thank you.

RESPONSE TO A QUESTION FROM SENATOR HATCH

Question. Testifying before this Committee just yesterday, Ambassador Zoellick indicated to Senator Baucus that he believed that S. 1121 was a good initiative, but that there were sensitive topics. It seems to me, broadly speaking, the President's Middle East Free Trade Area is a medium- to long-term plan, but that, with the proper coordination, the Senate's initiative could assist in getting us down the road. Are there any irreconcilable differences?

Answer. While it does not rise to the level of an irreconcilable difference, there are differing views on the appropriate role of unilateral preference programs. It is worth noting that the U.S. trade strategy already includes benefits to the Middle East countries in the short-term. The President's U.S.-Middle East Free Trade Area (MEFTA) initiative will seek to expand the use of the Generalized System of Preferences (GSP) Program to increase U.S. trade linkages with the Middle East.

However, there is the risk with preference programs, as we saw during the Cancun WTO ministerial meeting last year, that they can unintentionally lead some countries to resist reduction of global trade barriers to preserve their benefits under preferential trade programs. In addition, we would want to avoid undercutting our leverage for negotiating FTAs by unilaterally awarding trade preferences.

RESPONSES TO QUESTIONS FROM SENATOR SMITH

Question 1. What is the Administration doing to ensure that additional free trade agreements don't undercut our FTA with Israel? Will Israeli inputs be considered on a duty free basis as the U.S. reaches FTA deals with these and other countries?

Answer. We are currently exploring the possibility of allowing 'regional cumulation' under our FTAs in the Middle East and North Africa, so that a country could meet the FTA's rule of origin with inputs from other U.S. partners in the region. For example, under the U.S.-Jordan FTA, the use of inputs sourced from states contiguous to Jordan could be used toward the FTA rule of origin requirement if the parties agree.

Question 2. In its effort to forge a Middle East-wide free trade agreement, is the Administration ready to push Arab countries to stop their economic, diplomatic and cultural boycott against Israel? What is the Administration's reaction to Saudi Arabia and Bahrain's continued participation in Arab boycott meetings in Damascus?

Answer. The U.S. Department of Commerce, through its Office of Antiboycott Compliance in the Bureau of Industry and Security, continues to enforce the laws that prohibit U.S. companies from complying with Arab boycott provisions.

Question 3. How does the Administration address such issues as religious tolerance in its efforts in forging a FTA with Middle East countries?

Answer. The Commerce Department works closely with our colleagues in the State Department and USTR in order to address broader foreign policy concerns in our FTA candidate evaluations.

Question 4. How does the United States rationalize virulent anti-Semitism with a trade partner?

Answer. We do not view any of the countries in the Middle East with whom we have FTAs as harboring ill will against Israel. Our current FTA partners, Jordan and Morocco, maintain economic relations with Israel. Jordan and Israel have full diplomatic relations.

Furthermore, the U.S. Commercial Service trains Foreign Commercial Officers in human rights so they can effectively counsel U.S. businesses on the human rights situation in their country. My office has worked with the U.S. Commercial Service to develop and deliver a two-day course, and currently, 72 Commercial Officers have been trained. The training provides an opportunity for Commercial Officers to explore human rights subjects and discuss how they affect international trade and the success of U.S. businesses.

RESPONSE TO A QUESTION FROM SENATOR BAUCUS

Question. As we discussed during the hearing, Egypt has undertaken significant economic reform and remains interested in negotiating an FTA with the United States. Negotiating an FTA with Egypt makes a lot of sense from an economic standpoint—it's one of the largest economies in the Middle East—and from a symbolic standpoint as well. As Under Secretary Larson noted at the hearing, it is difficult to imagine a meaningful Middle East free trade area that excludes Egypt. With that in mind, please list as specifically as possible the steps you believe Egypt must take before the United States would consider commencing FTA negotiations with that country. What further economic reforms are needed?

Answer. We recognize Egypt as a potentially lucrative market for U.S. products and industry, and hope to eventually solidify our trade relationship with them in an FTA. A decision to enter into an FTA with Egypt must be preceded by Egypt's commitment to both sustained economic reform and continued adherence to their WTO obligations. We have formed working groups under the U.S.-Egypt Trade and Investment Framework Agreement (TIFA), in which we are discussing with the Egyptian government the steps Egypt needs to take to get on the road to freer trade. These steps include cooperation with the Doha agenda, protection of intellectual property, and removing import barriers to U.S. goods.

We have seen some progress in Egypt on economic reform, but it has been slow, and there have been a number of setbacks. Some examples of progress: Egypt joined the WTO Basic Telecom Agreement and the WTO Information Technology Agreement last year. In January, Egypt cut tariffs on 700 items, including capital goods, spare parts, apparel, and computer equipment. Excessive apparel tariff rates well beyond Egypt's WTO bound rates had been a major issue for our textile industry for the past two years. The government enacted a comprehensive IPR law in 2002 and ratified the World Intellectual Property Organization's Patent Cooperation Treaty.

Some setbacks: Despite passage of it's new IPR law to comply with it's TRIPS obligations, including the protection of undisclosed test data submitted by pharmaceutical companies, Egypt's Ministry of Health has been issuing licenses for domestically produced copies of U.S. pharmaceuticals based on the confidential test data of U.S. firms that should be protected under Egypt's own laws. Copies of four U.S. drugs have received approval by the Ministry of Health and 30 more are in the pipeline. Although the Egyptian pound was "floated," the exchange rate is still being controlled and a black market for dollars still exists. Egypt's customs system is also in need of major reform. We are also looking for sustained Egyptian cooperation to advance the WTO Doha Development Agenda. These are some of the issues that Egypt needs to address to move towards an FTA.

PREPARED STATEMENT OF HON. MAX BAUCUS

Thank you, Mr. Chairman. Thank you for convening a hearing on such an important topic. And I want to thank all of the witnesses who have come to testify here today. We have a very impressive panel. I'm looking forward to hearing what they have to say, so I will keep my remarks short.

In particular, let me thank Senator McCain for testifying this afternoon. Last year, Senator McCain and I introduced the Middle East Trade and Engagement Act, better known as "Baucus-McCain," or "the Silk Road bill." That bill seeks to establish a trade preference program for the countries of the Middle East similar to programs we now have for sub-Saharan Africa, the Andean region, and the Caribbean basin. It would give the president the power to allow Middle Eastern countries that meet certain conditions, such as supporting the war on terrorism and reforming their economies, to export products the president approves duty free.

A trade preference program like the one we are proposing will help countries in the Middle East now, in the short-term. It is comprehensive in its scope—it offers economic help through increased trade to the entire region at once, rather than gradually, country by country. It will also help prepare Middle Eastern economies to enter into free trade agreements (FTA) with the United States that are the cornerstone of the administration's Middle East trade policy.

That's an important point. Far from competing with the administration's policies, I believe the Baucus-McCain bill complements and supports the administration's attempt to establish a Middle East free trade area. Just look at the history of preference programs. The United States has essentially three regional trade preference programs. We passed the Africa Growth and Opportunity Act (AGOA) in 2000. Now we're negotiating an FTA with five AGOA beneficiaries the Southern African Customs Union (SACU) countries.

We also have the Andean Trade Preferences Act (ATPA). For years ATPA has provided incentives for farmers to switch from growing coca to growing flowers, coffee, and other legal crops. The United States Trade Representative (USTR) recently announced that it would take the next step and negotiate FTAs with ATPA beneficiaries Colombia, Peru, Bolivia, and Ecuador.

Finally, we have the Caribbean Basin Initiative (CBI). All five of the Central America Free Trade Agreement (CAFTA) countries with which we just completed FTA negotiations receive benefits under CBI. So does Panama, another future FTA partner according to the USTR. The evidence is clear. Preference programs help countries reform and develop their economies to the point where an FTA with the United States can become a realistic option.

In its recently released Annual Report, the USTR stated that, quote "AGOA has prompted important economic and social reforms across sub-Saharan Africa and delivered new jobs and opportunities for economic growth and development to the region." This is precisely what the United States seeks to accomplish in the Middle East. If a preference program delivered these impressive results for sub-Saharan Africa, why wouldn't we develop a preference program for the Middle East? Surely it can't be said that the Middle East is somehow less important than sub-Saharan Africa.

The USTR also said in its Annual Report that, quote "AGOA successes are also creating new commercial opportunities for U.S. exporters, as African exporters explore new input sources in the United States." New commercial opportunities for U.S. companies means jobs for U.S. citizens.

In short, a preference program for the Middle East will help stimulate economies in the Middle East, create jobs both in the Middle East and here at home, and improve America's security in the process. I urge the administration to support a preference program in the Middle East, and to work with Senator McCain and me on the Baucus-McCain bill.

PREPARED STATEMENT OF DOUG BOISEN

Good afternoon. Chairman Grassley, Ranking Member Baucus and members of the Committee. My name is Doug Boisen. I am a board member of the Nebraska Corn Development, Utilization and Marketing Board, U.S. Grains Council and Chairman of the Joint Trade A-Team of the National Corn Growers Association and U.S. Grains Council. I would like to thank the Committee for giving me the opportunity to testify and speak today regarding trade opportunities in the Middle East. Today's hearing is very timely, and I commend the Chairman and the Committee for convening it.

One out of every five rows of United States corn is exported, and exports of value-added corn and co-products add to the importance of foreign markets for United States corn producers. In 2003, United States corn exports totaled 43 million metric tons with a value of $4.7 billion. This represents approximately 20 percent of total U.S. production, with the United States accounting for nearly 57 percent of worldwide production last year. Our two closest competitors in the international marketplace are Argentina and China with 14 and 17 percent of world production respectively.

As you know, corn growers are experiencing a rising level of competition in the international market. More so than any time in the past, corn producers operate in an international marketplace that is competitive. The importance of free trade agreements has never been more essential to the future success of our industry.

The Middle East

I'm especially pleased to be here today to talk about Middle East trade. As you may know, NCGA's sister organization, the U.S. Grains Council has been very active in the region for many years and currently has offices in Egypt and the United Arab Emirates. In addition, the Grains Council has programs to build markets and enable trade for U.S. feed grains in many of the Middle East countries.

The Middle East Region [1] is heavily reliant on feed grain imports to produce livestock and poultry to satisfy its demand for protein-based animal products. In 2001–02, total corn imports by countries in the region was approximately 11.6 million metric tons, of which the United States supplied 7.7 million metric tons, or 66 percent. While imports to the region increased last year, U.S. market share dropped to 41 percent due to competition from Argentina and China. Despite this, U.S. corn imports are rising to historic levels with large purchases recently by Egypt, Israel, and others.

While many governments seek to increase production of various feed crops, the region's climate and scarce water supplies are expected to put these countries in a situation to rely even more on imports. Growth in income and population are fueling rising consumption of poultry and to a lesser extent beef, dairy and sheep products. As a result, we expect the region to be an expanding market for U.S. feed grains in the future given economic and political stability.

Although red meat, especially lamb, is the preferred meat throughout the Middle East, the production of beef and mutton has remained static over the past 6 years. The only exceptions are Turkey and Iran where beef production has declined. The decline was most dramatic in Iran where production dropped by over 22 percent. The primary reason for the steady decline is the lack of adequate pastures and roughage sources in the area. As a result, most of the consumers in the Middle East are forced to turn to poultry meat, eggs and dairy products to fulfill their requirements of animal protein. This has resulted in the growth of the poultry sector

[1] Turkey, Syria, Jordan, Lebanon, Egypt, Israel, Saudi Arabia and the Gulf Cooperation Council countries.

throughout the Middle East ranging from 7 to 10 percent. It is projected that this growth will be maintained over the next five years.

Let me take this opportunity to highlight various countries and the current and future growth opportunities available to corn and feed grain producers.

Egypt

Egypt's population of 68 million has grown 2 percent annually over the past decade while per capita income has nearly doubled. Population growth, coupled with increases in consumer disposable income has translated into increased demand for meat, milk and eggs, and consequently, demands for imported feed grains. This is reflected in Egypt's increased corn imports from 1.2 million metric tons in 1990 to 5 million metric tons in 2002. Consequently, Egypt has become our fourth largest corn market. As with most countries in the region, protectionist trade policy barriers toward feed grain imports are not currently an issue with Egypt.

The other countries in the region, Iran, Syria, Saudi Arabia, Turkey and Israel, are sizable markets importing nearly or more than one million metric tons of corn per year. With the exception of Israel, those are also the countries which demonstrate the most potential for growth in the livestock and poultry sectors and feed grain imports. The dynamics of this growth is illustrated by demographic changes. Nearly a third of the population in these countries is below the age of 15 years. In addition, changing eating habits of younger generations is also impacting the demand of animal products.

Iran

With a population of 65 million, Iran is growing at 1.6 percent per year and per capita income will grow at a projected 3 percent rate over the next several years. With an arable land mass of only 10 percent and domestic corn production stagnant at 1 million metric tons, much of the required coarse grains will have to be imported. It is projected that by 2009, Iran will need to import 3.2 million metric tons of corn, double the import level of 2002.

Although strong trading partners prior to the Revolution in 1979, U.S. exports have been impeded by the political relations between the two countries. As a result, Brazil and Argentina have been the major suppliers of corn until this past year when China reportedly supplied over 700,000 metric tons to Iran. Although there are some opportunities for the U.S. to make sales to Iran under the right conditions, those opportunities are limited mainly due to the difficulties around the U.S. imposed trade sanctions.

Syria

In Syria, a rapidly increasing population and rising expendable income suggests a bright future for the development of the poultry sector in that country. A strong demand for dairy products and limited commercialization of the dairy sector also holds potential for growth. With only 26 percent of land suitable for crop production, the increased feed grain demand by those sectors will have to be met through imports. Syria imported approximately one million metric tons of corn last year with the U.S. supplying almost 60 percent of that total. It is projected that corn imports will grow to 1.6 million metric tons by 2008.

Saudi Arabia

Saudi Arabia is import dependent on most feed ingredients required to sustain its domestic livestock and poultry sectors, so much so that the government subsidizes corn and soy meal shipments. This has helped make Saudi Arabia self sufficient in eggs, fresh milk products and less so in poultry products. In 2003, corn imports were approximately 192,000 metric tons. Once importing over a million tons per year from the United States, Saudi Arabia has looked to other suppliers recently. Although we hope to regain market share in that country in the near future, looming concerns over biotechnology could cripple U.S. presence in that market as well as have repercussions in other parts of the region.

Saudi Arabia was the first to enact a biotech policy on foodstuffs containing or derived from biotech sources. In December 2001, the Saudi Ministry of Commerce implemented a certification and labeling requirement on all biotech origin food items imported into the Kingdom. A decision regarding bulk corn and corn products and the labeling of meat, milk and eggs produced domestically from biotech corn is pending. The Grains Council has been very active in working with partners in Saudi Arabia since 2001 to minimize the potential disruptions these biotech policies could have on trade in corn and corn products from the United States.

Other countries in the region may likely adopt similar policies as those in Saudi Arabia. Of particular interest is Turkey. I am told that the Turkish Government is developing a biotechnology position to be announced in May or June 2004. Given

Turkey's aspirations to join the European Union, the government intends to implement a policy similar to the recently adopted labeling and traceability regulations.

Turkey

Turkey has been a moderate sized market for U.S. corn for a number of years, based mostly on solid growth in the poultry industry and for industrial use. In 2002, Turkey imported approximately 1.5 million metric tons of corn with the U.S. supplying two thirds of that amount. However, a primary obstacle to growth is the use of seasonal import duties that coincide with the Turkish corn harvest. The duties are held in place until the domestic corn crop is marketed and stocks are depleted. These duty fluctuations, which are unpredictable in terms of timing and size, create significant uncertainties for importers and exporters, and reduce the overall market potential beyond what the government will allow.

While we have been effective in working with their poultry and wet milling industries, it is very difficult to place any kind of effective pressure on Turkey since they are well below their WTO binding tariff rate. Therefore, Turkey would be a good candidate for a free trade agreement.

Iraq

One other country I would like to mention is Iraq. Throughout the 1980s, Iraq was a consistent importer of corn from the United States. In 1989, Iraq imported 650,000 metric tons of corn, nearly all from the United States. Much of those imports went to a growing poultry industry. In 1989, domestic poultry production reached nearly 270,000 metric tons, a five-fold growth over the previous nine years. The government of Iraq began to privatize the industry, creating a strong incentive for further growth. However, following the Gulf War in 1991, grain imports and the poultry industry collapsed. Rebuilding of Iraq will require significant expansion in both the poultry and livestock sectors just to get back to the per capita consumption levels of animal protein that Iraqis had in the late 1980's.

Working cooperatively with the Foreign Agriculture Service and the American Soybean Association, the Grains Council is leading efforts to rebuild Iraq's poultry sector. The feed grain industry is carrying out capacity building activities with Iraq's poultry industry to address some of the obstacles it currently faces such as lack of financing for small and medium-sized producers, inadequate regulations for an orderly market, poor commercial contacts with international input suppliers, and insufficient storage for feed and feed ingredients among others.

In helping to accelerate the rebuilding of this sector, we also will be building a viable market for U.S. feed grains. In several years, it is possible that we will again see Iraq importing large amounts of corn. Critical to realizing these goals, Iraq will need credit assistance along the lines of a U.S. GSM program to import basic commodities.

Conclusion

No doubt, our future as agricultural producers is linked to trade. The United States Government and organizations like NCGA and the Grains Council need to promote the benefits of trade liberalization in the Middle East and around the globe. We cannot retreat from any region of the world.

We look forward to working with the Committee on this and other issues of importance in the future. I thank you again for the opportunity to address the Committee. I welcome your questions.

RESPONSES TO QUESTIONS FROM SENATOR GRASSLEY

Question 1a. You discussed Saudi Arabia's implementation of a biotech labeling law. How closely is the U.S. corn industry working with the United States government to see that Saudi Arabia's policies do not spread to other countries in the region?

Answer. The only biotech labeling law that has been enacted in the Kingdom is a labeling requirement for foodstuffs derived from biotech events. The Council in cooperation with Agricultural Trade Office in Riyadh was successful in getting the Ministry of Agriculture to accept the GIPSA disclaimer on GM corn, soybeans and their products as blanket certification requirement for the certification of GM corn, corn co products, soybeans and soybean meal. This means that the US suppliers only have to refer to that disclaimer when exporting those commodities to the Kingdom. It appears that Council and ATO's joint efforts have been successful in dissuading the government from imposing any labeling requirements on domestically produced meat, milk and eggs produced from birds or livestock fed on GM feeds. GIPSA disclaimer can be found on Biotechnology-Related Statements Available from GIPSA website www.usda.gov/biotech—statments.htm.

In an attempt to insure that neighboring GCC countries also adhere to a pragmatic approach on the issue, the Council and Agricultural Trade Office in Dubai held a biotech conference for key government officials from Qatar, Kuwait, Bahrain, Oman and the United Arab Emirates on the benefits of biotechnology and lack of a need for the labeling of biotech foods or feed ingredients.

Question 1b. Have you all spoken with U.S. officials about this issue in the context of Saudi Arabia's proposed accession to the WTO?

Answer. Extensive discussions were held on the biotech issue as impacted by Saudi Arabia's accession to the WTO with Quintin Grey, Regional Director, ATO—Riyadh. Mr. Grey was present in Geneva for most of the negotiations carried out on the issue with the Saudi's. Additionally, the Council has discussed this with USTR officials in Washington.

Question 2. I am aware that the U.S. corn industry is pleased with the outcome of the negotiations of the U.S.-Morocco Free Trade Agreement. Exactly how will this FTA benefit U.S. corn farmers.

Answer. The reduction and elimination of the tariff on U.S. corn in the U.S.-Moroccan Free Trade Agreement will benefit the U.S. feed grains industry both immediately and in the longer term. Upon implementation, the reduction in tariffs will provide lower feed costs to the Moroccan poultry and livestock industries which will allow further overall expansion of the Moroccan market for feed grains. In addition, the lower tariff applied to U.S. corn versus the MFN rates competitor countries will be subjected to will allow the United States to capture a larger portion of that important growth market.

In recent years, corn has become the highest valued U.S. agricultural export to Morocco. U.S. corn exports typically run from 500,000 to 600,000 metric tons, and in 2002 accounted for approximately 60% of Morocco's total corn imports. However, due to strong competition from Latin America, U.S. market share decreased to only about 10% of the over 1 million metric tons Morocco imported last year. Because the tariff for U.S. corn will be 50% lower than our competitors in year one of the FTA, U.S. exporters will have a significant advantage over other suppliers. With subsequent tariff cuts and ultimate tariff elimination, the U.S. potentially could capture near 100% of the market should Morocco keep its MFN rate where it stands today.

Responses to Questions From Senator Grassley

Question 1. Do U.S. agricultural exporters have difficulty with non-tariff barriers (such as sanitary and phytosanitary issues) that impeded market access for U.S. products in the Middle East? Which countries are the worst offenders?

Answer. There are no major non-tariff trade barriers that currently impede the importation of US coarse grains to the Middle East markets.

Question 2. As was discussed at the hearing, some countries in the Middle East are starting to adopt regulations on genetically modified organisms ("GMOs"). If the markets remain open to U.S. products, including those that have been genetically modified.

Answer. To date the only country to implement any GMO regulations is Saudi Arabia. Best information is that Syria are not going to implement any restrictive policies on bulk GM commodity imports, they will only restrict imports of GM seeds for planting. Although not finalized, it is expected that Turkey will eventually implement policies on GMOs that are harmonized with those of the EU in anticipation that they will be admitted to the EU.

Question 3. What is your view of GMO regulations in the region, both now and where you believe this issue is headed?

Answer. I do not foresee impeditive biotech policies for bulk GM commodity imports for Jordan, Lebanon or the GCC countries (excluding KSA which have been outlined above).

Prepared Statement of Hon. Charles E. Grassley

I would like to begin by thanking today's witnesses for appearing at this hearing. We look forward to your testimony. Today economic stagnation and rapid population growth is creating great frustration in the Middle East. This frustration all too often leads to political violence. As a result, the news we hear about the region is frequently dominated by stories of political violence and security concerns. But we know that there is another side to the Middle East that does not always get the news coverage it deserves. The Middle East is a vast and vibrant region full of promise. We are pleased today to be able to focus on that aspect of the Middle East.

For the region to truly thrive, we need stronger economic engagement between the United States and like-minded nations in the Middle East. That is why I so strongly support the President's call for a Middle East Free Trade Agreement by 2013. The dramatic vision articulated by the President can indeed become a reality. But it is going to take a lot of work to get this done. With his call for a Middle East Free Trade Area, the President correctly recognizes that increased U.S. trade with and among Middle Eastern countries will foster long-term economic growth in the region. Just as important, trade agreements entered into by Middle Eastern countries would lead to, and in some cases lock in, needed political reforms. The American economy will also benefit from more trade with Middle Eastern countries. The region's large and growing population offers Americans a great export market. Countries in the Middle East—due to their difficult growing conditions—hold much promise for increased agricultural imports from the United States, which is especially important for my home state of Iowa.

The Bush Administration has taken a number of concrete steps to seize these opportunities. First, President Bush pushed through the Congress an important trade agreement with Jordan. Just last week, negotiations were completed with Morocco, a key ally in the war against terrorism. The U.S.Morocco FTA further opens the Moroccan economy to imports from the United States. This agreement will have a direct positive impact on Iowa's farmers as Morocco's tariffs on corn and soybeans will go to zero. I would like to thank personally Ambassador Zoellick and U.S. Chief Agricultural Negotiator Allen Johnson for their efforts on behalf of U.S. agriculture when negotiating this FTA. Likewise, with increased export opportunities to the United States, and less expensive imports from the United States, the Moroccan people will benefit from the FTA. Moreover, Morocco will likely receive greater foreign investment due to its enhanced economic status on account of an FTA with the United States. By improving the economic situation in Morocco, the FTA will bring greater stability to that country.

I am also encouraged by our negotiations with Bahrain. Bahrain is not only a strategic ally of the United States but also has demonstrated a real commitment to liberalized trade. In addition, Bahrain is a leading nation in the Gulf Cooperation Council, an entity that is contributing to greater economic integration in the region. It is my understanding that negotiations with Bahrain are proceeding rapidly, and I commend Bahraini officials for their commitment to this process.

The U.S.-Jordan FTA, the U.S.-Morocco FTA, and the proposed U.S.-Bahrain FTA are important steps toward fulfilling the President's vision of a Middle East Free Trade Area by 2013. 1 look forward to hearing from our witnesses today about progress being made toward this vision and what we can do together to help bring greater peace and prosperity to this important region of the world.

PREPARED STATEMENT OF HON. ORRIN G. HATCH

Thank you, Mr. Chairman, for holding this hearing on this important subject.

The citizens of the Middle East are no less entrepreneurial, no less hard-working, and certainly no less interested in economic growth for their families and societies than citizens of any other part of the world. And, for the vast majority of the citizens of the Middle East, they would rather dedicate their energies to economic advancement than to political strife. Yet the region is dominated by conflict, and characterized by economic stagnation. The United States needs to become more active in promoting economic development, in order to match our military and political efforts in Iraq, as well as our diplomatic efforts in the Israel-Palestine conflict.

And I am particularly gratified to see the Administration's recognition that we need to redouble our efforts to promote economic development, through the proposed Middle East Free Trade Area, as well as the Middle East Partnership Initiative. I commend my Senate colleagues, Senator McCain and Senator Baucus, for the introduction of S. 1121, The Middle East Trade and Engagement Act. It is time that we offer this critically important region of the world the opportunity of greater commercial relations with our own economy, which has long been a source of dynamism for all economies that are open and transparent.

Everyone knows the challenges before us. Two statistics from the Administration testimonies I read highlight this challenge. Mr. Aldonas quotes the World Bank projection that, if the region were to achieve non-oil growth of 15 percent per annum, 4 million jobs could be created in region by 2008. Yet Mr. Larson reports, also from the World Bank, that 100 million jobs will have to be created by 2020. Mr. Maxwell, from Hewlett-Packard, quotes the often-repeated fact that, in the 1950s, Korea and Egypt were equal in per capita income, and yet today Egypt has one-fifth that of Korea. The challenges, as I say, are huge. Such a decline in real living standards in the Arab world is not a function of economies, but of governments and their policies. The U.S. is today engaging the Arab world like it never has, we have removed a global threat, are pressing for political reform, and now, both in the Administration and the Congress, are engaging the process of economic development through trade. We cannot delay.

PREPARED STATEMENT OF HON. ALAN P. LARSON

Mr. Chairman, distinguished Members of the Committee, I appreciate the opportunity to testify on U.S. economic and trade policy with respect to the Middle East.

THE MIDDLE EAST: CHALLENGES AND OPPORTUNITIES

I can think of no other region in the world today that is as vital to U.S. interests, yet poses as many challenges for us, as the Middle East. As President Bush declared in his speech last May, "What happens in the Middle East greatly matters to America."

Among those challenges, and the focus of my remarks today, is the growing thirst for opportunity that characterizes the Middle East, and thesubstantial efforts the United States is undertaking to respond to that demand. U.S. policies to stimulate economic reform and trade liberalization have much to offer, both in terms of generating growth and employment, and in solidifying our broad ties with this diverse and culturally rich region. At the same time, they promote U.S. economic and commercial interests.

During the last week of February, I had the opportunity to visit several Middle Eastern cities, including Ramallah, Jerusalem, Amman, Riyadh, and Cairo. Last week, my colleague Under Secretary Marc Grossman visited Rabat, Cairo, Manama, and Amman. In our meetings with a broad spectrum of individuals—from students to business and civic leaders to government officials—several consistent themes emerged:

- the people of the Middle East, and especially the young people, are yearning for greater economic opportunities;
- governments in the region increasingly understand the imperative for economic reform; but
- the many regional leaders—and we ourselves—believe that change and economic reform come from within, and that the region's cultural and historical legacy will be an important factor in shaping those reforms.

The widely quoted UNDP Arab Human Development Reports for 2002 and 2003 examine in considerable detail the challenges and opportunities for building a better Middle East. As the 2003 report concludes, a strategic vision for establishing a "knowledge society" in the Arab world requires diversifying economic structures and markets. This also requires upgrading the Arab presence in the "new economy," and in opening up to other cultures.

Grounded in home-grown ideas and a realization that change is necessary to generate jobs, there is growing support in the Middle East for the catalytic role of economic opportunity, a light that shines brightly, dispelling negativism and despair. I am encouraged by concrete demonstrations that the Middle East is taking ownership of this process; last September's U.S.-Arab Economic Forum in Detroit—the first ever—provided ample evidence of this energy and enthusiasm.

Of course, I do not want to downplay the formidable challenges and obstacles that lie ahead before a new, more open, and economically vibrant Middle East can be realized. The Middle East remains woefully unintegrated in the global trading system. The region's share of total world exports accounted for only 5 percent in 2001, and less than 1 percent of global foreign direct investment. Middle Eastern economies are characterized by structural rigidities, red tape, high unemployment, and a lack of export diversity, which have led to sub-optimal economic performance over many decades. Despite its abundant energy resources and oil wealth, the Middle East has not been successful in creating opportunities that engender a sense of a better tomorrow. This is turn has fostered a loss of hope, particularly among young people, which has increased their susceptibility to those who use terrorism as a means to channel their desperation.

Nonetheless, there is a growing awareness in the Middle East of the nature of the problem, and of the need to change. U.S. economic and trade policy is calibrated to support these nascent developments by promoting economic reforms, and by fostering economic ties and trade linkages. This in turn can help build the prosperity and stability needed to anchor lasting peace in the region.

Recent examples of developments that reflect positive movement in this direction include:

- Our **trading relationship with Jordan** has already borne considerable fruit; the **U.S.-Jordan Free Trade Agreement** has contributed to regulatory reforms, a dramatically improved investment climate, and increased investment in human capital. Indeed, Jordan and the United States have experienced an increase in bilateral trade of 205 percent from 2001 to 2003 alone. Jordan's economic reforms have also resulted in the establishment of eleven Qualifying Industrial Zones, wherein products manufactured in cooperation between Jordanian, Palestinian, and Israeli entities can be exported to the United States tariff free;
- The **U.S.-Morocco Free Trade Agreement**, which was just concluded on March 2 of this year;
- Substantial progress is being made in negotiating the **U.S.-Bahrain Free Trade Agreement**;
- **Trade and Investment Framework Agreements** were signed on February 6 with Kuwait and Yemen; agreements are also pending with Oman, Qatar, and the United Arab Emirates; and
- We are partnering with **Saudi Arabia** to facilitate its **accession** to the **World Trade Organization**, a process that is gaining momentum through technical cooperation.

RESPONDING AND SUPPORTING REGIONAL REFORMS

The **Greater Middle East (GME)** proposal reflects President Bush's "Forward Strategy for Freedom." This strategy seeks to support peace and security in the Middle East through the pursuit of freedom and promotion of democracy and human rights, through both words and deeds. In consultation with various European, G–8, and Middle Eastern partners, we are seeking ways to encourage and support those individuals, organizations, and governments in the region willing to embark on the path of reform and positive change. Our efforts should leverage U.S. resources and those of our partners for the maximum benefit of the region.

This approach has provoked a constructive discussion, launching open debate on the directions reforms should take, and on the means to achieve those ends. Countries of the Middle East are contemplating how better to define and organize their approaches to the reform process, and are engaging a broad cast of interlocutors. In short, the interest and energy of Middle Eastern countries provide impetus for change and the development of a social climate that increasingly accepts change.

As recently as last week's troika meeting with Irish Foreign Minister Brian Cowen, EU High representative Javier Solana, and EU External Affairs Commissioner Christopher Patten, Secretary of State Powell held productive discussions on how the EU and the United States can best work together to support indigenous voices for reform in the Greater Middle East. After the meeting between Secretary Powell and his European Union counterparts, the Secretary declared that the United States and the EU "see great opportunity and scope for cooperation on a Greater Middle East Initiative in the run-up to the G–8, U.S.-EU, and NATO summits" to be held this coming June.

The Greater Middle East proposal signals a readiness to undertake projects to address indigenous calls for change in areas defined by Arab reformers themselves. This self-diagnosis, outlined in the UNDP Arab Human Development reports, has produced the following priorities for the region:

- promoting good governance;
- building a knowledge-based society; and
- expanding economic opportunities.

The last of these, expanding economic opportunities, is essential for a variety of reasons. The UNDP Arab Human Development Report for 2002 notes that all Arab countries had a combined 1999 GDP of $531 billion, less than that of Spain alone. GDP growth, investment, and productivity have all declined in Arab countries over the past two to three decades. The World Bank also estimates that the Middle East will need to create 100 million new jobs by 2020 to keep pace with the growth in the labor force-age population. The region's persistent economic problems demand action in terms of increased economic growth and development, regional economic integration, and foreign direct investment.

As we prepare for the G–8 Sea Island Summit on June 8–10, we are considering a number of ideas that could expand economic opportunities in the Greater Middle East. Among them are:

- **information technology for business development**. With the world's lowest per capita Internet access, the Middle East suffers from critical information deficits. Training and technical assistance can address this vital need;

- **financial reform and the development of capital markets and increased capital access to small and medium-sized enterprises (SMEs)**. Increasing economic growth and job creation in the Middle East requires more efficient allocation of capital and a more vibrant private sector. Partners should cooperate to improve financial institutions and capital markets to improve the business environment for small and medium-sized enterprises, which comprise the vast majority of private businesses in the region;
- **promotion of good business practices and improving the investment climate**. Efforts in this area should include expanding modern business education, promoting best practices for businesses, and encouraging a level playing field to stimulate investment;
- **promoting regional dialogue on economic and social reform**. Partners should address the need for serious dialogue on economic and social reform by supporting regional fora, fostering discussion by government officials, regional and international financial and development institutions, private business leaders, and academics; and
- **improving trade opportunities**. Intra-regional trade in the Middle East is among the lowest in the world; furthermore, the area also suffers from low levels of integration with the global trading system. Partners should provide training and technical assistance to address this situation, and support regional trade initiatives to facilitate intraregional trade.

TRADE POLICY: EXPORT OPPORTUNITIES AND PROMOTING REFORM

The United States has several objectives in its economic and trade engagement with the Middle East, including:

- Ensuring a **level playing field for exports**, so that our goods and services are not disadvantaged in comparison to those of others, such as the European Union, in terms of their ease of market entry;
- Encouraging **greater market access** generally, so that the Middle East becomes more fully integrated into the world trade system, with minimal barriers to entry, and commercial transactions with a broader range of partners involving a greater scope of goods and services;
- Accelerating **economic reforms and trade liberalization** essential to the development of sound fiscal and monetary policies that provide the foundation for long-term, sustainable growth and employment creation; and
- Engendering **alternatives** to the often **stagnant economic situation** many countries face, which is all too often accompanied by rising unemployment, minimal technology transfer and skills development, and a lack of export diversification. Supporting innovative efforts to transform economies from sluggish to dynamic will pay social dividends, as countries become increasingly able to provide opportunities commensurate with rising expectations. This will offer alternatives to despair and acts of desperation, as societies afford a broader range of prospects for prosperity. Economic reforms will also provide opportunities for those, particularly the young, who might otherwise become disillusioned and hence vulnerable to exploitation by those who advance terrorism as a means to express their grievances.

The U.S. experienced a $17.9 billion dollar merchandise trade deficit with the Middle East in 2003. U.S. imports of crude oil and petroleum products represent over 55% of Middle Eastern exports to the United States. Without trade in crude oil and petroleum products, the U.S. would have run a $3 billion/year trade surplus with the Middle East.

In 2002, U.S. exports to the region reached a level of $23.6 billion, principally from sales of machinery, equipment, vehicles, manufactured goods, and foodstuffs. This, however, is dwarfed by the volume of exports from the European Union to the Middle East, which attained a value of $97.7 billion in 2002. In terms of total bilateral business activity, the U.S. traded $62.1 billion with the region in 2002, in comparison to $176.2 billion for the European Union.

Market access is therefore an area that needs to be addressed. Tariffs and quotas in the region remain too high and limit the opportunities for U.S. products in Middle Eastern markets. Moreover, U.S. goods and services have also been handicapped by the advantages European traders have enjoyed in the region. Building on its favored position, the European Union has an ambitious trade agenda for the Middle East. It has already entered into an Association Agreement with Egypt. It is essential that the United States strive to counter these trends in the Middle East to ensure that we gain equal market access and enjoy a level playing field. While that market is currently small, the potential for growth is large.

The United States is addressing this situation with abroad strategy of economic engagement activities. On May 9, 2003, President Bush reaffirmed the U.S. Government's commitment to promoting and supporting economic reform in the region. This broad policy initiative includes the proposed **Middle East Free Trade Area**, known as **MEFTA**.

The President's vision for **MEFTA** is to build, over a decade, on current free trade agreements with Israel and Jordan. MEFTA offers a framework for openness, trade integration, and economic development for the Middle East. Applying technical assistance, it seeks to promote trade expansion and policy reforms, re-igniting economic growth and expanding opportunities throughout the region. The U.S. Government is working with countries of the Middle East through a series of graduated steps tailored to their individual level of development.

Trade and Investment Framework Agreements—TIFAs—are typically the initial fora for ongoing dialogue with the U.S. Government on economic reform and trade liberalization. TIFAs promote the establishment of legal protections for investors, improvements in intellectual property protection, more transparent and efficient customs procedures, and greater transparency in government and commercial regulations.

As of mid-2003, the United States had signed TIFA agreements with Algeria, Bahrain, Egypt, Tunisia, and Saudi Arabia. In February 2004, we signed with both Kuwait and Yemen. Furthermore, TIFAs are currently under negotiation with Oman, Qatar, and the United Arab Emirates. Through this process, and the joint development of robust action plans, the U.S. Government can identify potential partners for further trade cooperation, such as free trade agreements.

In consultation with Congress, the U.S. Government is pursuing a series of **Free Trade Agreements** with Middle Eastern countries to build on those already concluded with Israel and Jordan. These agreements are designed to expand bilateral trade through commitments to high standards and comprehensive trade liberalization.

On March 2, following a year of intense negotiations, we concluded FTA negotiations with Morocco; which will immediately provide duty-free market access to 95 percent of traded goods, providing significant incentivesfor both countries to identify and target opportunities in each other's markets. This agreement covers all agricultural products, and provides substantial market access to the services sector, such as banks and insurance companies. Furthermore, the FTA affords legal protections for U.S. investors, as well as covering trademarks, copyrights, and patents. The Morocco FTA is a high-quality agreement that will set the standard for FTAs with other Middle East partners.

Building on the Morocco agreement, the U.S. Government hosted Round II of the U.S.-Bahrain Free Trade Agreement negotiations here in Washington last week. The round went well; based on progress attained so far, we look forward to concluding the agreement by mid-year.

Many Middle Eastern trading partners are in close and active consultations with us through the TIFA process, and have a strong interest in concluding an FTA with us, including the United Arab Emirates, Tunisia, and Egypt. More open markets in these and other countries will offer not only significant opportunities for U.S. exporters, it will also reinforce their economic reform efforts. We are actively engaged with these countries on a range of pending bilateral trade and economic reform issues through the TIFA Council process and other bilateral discussions. Continued progress in these areas will help pave the way toward eventual FTAs.

The U.S. Government has been working with countries of the region so that they can take advantage of the **Generalized System of Preferences** program. On March 1, President Bush announced that Algeria had qualified for GSP; on the same day, he also announced that Bahrain would graduate from GSP eligibility on January 1, 2006, as its per capita income had moved it above the World Bank's developing country threshold—a Middle East success story.

The U.S. Government is also actively engaged with several Middle Eastern countries—**Saudi Arabia, Algeria, Yemen, and Lebanon**—to expedite their **accession to the World Trade Organization**. The accession process involves countries voluntarily opting for economic reform and trade liberalization in order to join the rules-based world trade system. We see WTO accession as a key step forward, as it involves making commercially meaningful market access commitments for goods, services, and agricultural products.

So powerful is the interest to participate in the global marketplace that **Iraq** has already sought and gained WTO status as an **observer**. This will help accelerate its reintegration into the global trading system.

The United States would like to see countries of the region play a stronger role in advancing the World Trade Organization's **Doha Development Round**. Leadership, particularly by key countries such as Egypt, Morocco, Tunisia, and Jordan, as well as Pakistan and Turkey, would go far to reinvigorate this essential global dialogue about the future of the world's commercial transactions. Their concerted efforts could result in the preparation of a framework agreement by mid-2004 by leveraging participation by a broader spectrum of countries.

A major weakness the Middle East shares with other regions of the world is a lack of expertise and skills needed to promote greater trade. In recognition of this, the United States has committed, as a part of the Doha Development Round agenda, to a major effort to help these countries to develop these skills.

There are a variety of means that the U.S. Government is undertaking to **build trade capacity**, so that countries of the Middle East can take full advantage of increased trade opportunities with the United States. In addition to promoting trade-related policies that enhance the business environment, the **Middle East Partnership Initiative (MEPI)** plans to establish regional offices in Tunis and Abu Dhabi to coordinate trade capacity building efforts.

In 2003, the U.S. Government expended over $174 million in the Middle East in trade capacity building. Most of this assistance involved trade facilitation, financial sector development, support for governmental transparency, export promotion, and business services and training.

A key funding mechanism for trade capacity building and trade-related technical assistance derives from the MEPI. MEPI-provided assistance, carried out in cooperation with the USTR and USAID, includes a broad spectrum of economic reform and trade liberalization elements. It involves facilitating WTO accession, assisting in TIFA-driven policy restructuring, and supporting regulatory measures for ensuring compliance with FTA provisions.

Broadening the base of trade between the United States and the countries of the Middle East is necessary but not sufficient. It is essential that the U.S. Government also work to promote trade between Middle Eastern countries. Economic interdependence is key to forging strong linkages between countries of the region, which will promote mutual prosperity and increase the collective stake in regional peace and stability. This presents a complex issue, as many Middle Eastern countries have relied for too long on petroleum-based exports to drive their economies, versus building a more diverse export base.

Trade within the Middle East accounted for only 8 percent of the region's total trade in 2001. This is far below the intra-regional level of nearly 75 percent for Europe and 50 percent for Asia. Increased intra-regional trade not only promotes economic growth and development, it also enhances the political stability of the region through fostering interdependence.

The United States can foster greater intra-regional trade through several means, including supporting the efforts of the **Gulf CooperationCouncil** (GCC) to generate a greater volume of trade between its six member states through the **customs union** it launched in January 2003; the **Agadir Initiative**, wherein Morocco, Tunisia, Jordan, and Egypt are forming a free trade area; and the promotion of an economic policy dialogue within the region.

CONCLUSION

To summarize, Mr. Chairman, distinguished Members of the Committee, the countries of the Middle East have taken stock of their economic situation, and have decided to participate more fully in the world trade system. Recognizing that the future of their youthful societies lies in the creation of meaningful economic opportunities, the countries of the Middle East are increasingly open to making the sometimes difficult choices required to effect economic reform and trade liberalization.

The United States is responding to this thirst for economic opportunity. Through MEFTA, MEPI, and other components of our economic and trade policy, we are supporting efforts of Middle Easterncountries to reform and liberalize, while simultaneously increasing market access opportunities for U.S. goods and services—a "win-win" situation.

We look forward to continued close consultation with Congress.

RESPONSE TO A QUESTION FROM SENATOR HATCH

Question 1. Testifying before this Committee just yesterday, Ambassador Zoellick indicated to Senator Baucus that he believed that S.1121 was a good initiative, but that there were sensitive topics.

It seems to me, broadly speaking, the President's Middle East Free Trade Area is a medium to long-term plan, but that, with the proper coordination, the Senate initiative could assist in getting us down the road. Are there any irreconcilable differences?

Answer. The Administration agrees that the two methods have the same goal in common—that of expanding U.S.-Middle East trade. We share the objective of the Baucus/McCain bill to foster U.S. engagement with Middle East countries to enhance trade and investment ties, spur economic development, and strengthen the economic basis for peace.

And to some degree, we agree with the Baucus/McCain bill that trade preference programs can play a role in this effort. For example, the President's Middle East Free Trade Area initiative (MEFTA) foresees therobust use of the Generalized System of Preferences to expand quickly U.S. trade linkages with the Middle East.

One downside, however, with a major new preference program, as demonstrated during the Cancun WTO ministerial meeting, is that preference programs can unintentionally lead some countries to resist reduction of global trade barriers to preserve their benefits under preferential trade programs.

Under the MEFTA, we seek a broader, staged approach that links U.S. trade benefits to incentives for Middle Eastern countries to undertake ambitious and comprehensive economic reform, while providing reciprocal trade benefits to the United States.

RESPONSES TO QUESTIONS FROM SENATOR SMITH

Question 1. What is the Administration doing to ensure that additional free trade agreements don't undercut our FTA with Israel? Will Israeli inputs be considered on a duty free basis as the United States reaches FTA deals with these and other countries?

Answer. President Bush in May 2003 presented his vision for the achievement of a Middle East Free Trade Area by 2013. Through the MEFTA, the United States will work with its free trade partners to fashion a regional agreement that will enhance out bilateral economic relationships and encourage intra-regional trade, investment, and economic reform. Our goal of a regional FTA with the Middle East includes Israel.

A key objective of MEFTA will be to promote intra-regional trade and investment. An important means towards this end will be to allow countries in the region that are parties to Free Trade Agreements with the United States to count the value of one another's products for the purposes of meeting the value content requirement under the agreement. This "regional accumulation" mechanism would apply to Israel.

Question 2. In its effort to forge a Middle East wide free trade agreement, is the Administration ready to push Arab countries to stop their economic, diplomatic and cultural boycott against Israel? What is the Administration's reaction to Saudi Arabia and Bahrain's continued participation in Arab boycott meetings in Damascus?

Answer. The U.S. position against the Arab League boycott remains firm and unyielding; we oppose the boycott in all of its forms. We continue to remind the Arab League countries that perpetuating the primary boycott of Israel and the remaining secondary and tertiary boycotts of firms that have commercial relations with Israel is a barrier to improving relations with the United States, attracting more foreign investment, and expanding trade.

We regularly approach individual member governments before meetings of the Arab League, the Gulf Cooperation Council, and the Organization of Islamic Conferences to encourage them to maintain their trade, cultural, and diplomatic ties with Israel. U.S. ambassadors andembassy officers, senior State and Commerce Department officials, and even White House officials have delivered these messages to countries that still officially honor and enforce the primary boycott of Israel such as Kuwait, Lebanon, Saudi Arabia, Syria, Yemen, and the United Arab Emirates.

Since the second intifada began, the Central Boycott Office has held only one official meeting, in 2002. Ten member states attended. While many of these members had no interest in reviving the boycott, a few supported Syria's call, seeing their attendance as a political act signaling their strong opposition to Israeli policies with regard to the West Bank and Gaza. That support has evaporated. Governments in the region, such as Saudi Arabia and Bahrain, have told U.S. embassy officials that they have no intention of supporting this boycott effort.

Question 3. How does the Administration address such issues as religious tolerance in its efforts in forging a FTA with Middle East countries?

Answer. Religious tolerance is not a criterion for FTA candidate selection as directed in the Trade Promotion Authority legislation. Candidate decisions, however, are not solely based on economics, but reflect our broader foreign policy concerns. To ensure that these concerns are considered, the Administration consults extensively with Congress in evaluating FTA candidates.

Question 4. How does the United States rationalize virulent anti-Semitism with a trade partner?

Answer. We do not view any of the countries in the Middle East with whom we have FTAs as harboring ill will against Israel. Our current FTA partners, Jordan and Morocco, maintain not only economic but also diplomatic relations with Israel. Jordan established full diplomatic relations when it signed a peace treaty in 1995 and watched its exports increase five-fold as it joined forces with Israeli companies under a cumulation/QIZ agreement. The Government of Morocco established limited diplomatic ties in the 1990s, when it terminated adherence to the Arab League boycott of Israel.

To promote regional integration, USTR has and will insert a cumulation clause in all FTAs. Arab states clearly understand that this is being used a tool to promote greater regional integration, including economic cooperation with Israel.

RESPONSE TO A QUESTION FROM SENATOR BAUCUS

Question. As was discussed during the hearing, Egypt has undertaken significant economic reform and remains interested in negotiating an FTA with the Untied States. Negotiating an FTA with Egypt makes a lot of sense from an economic standpoint—it's one of the largest economies in the Middle East—and from a symbolic standpoint as well. As you noted, it if difficult to imagine a meaningful Middle East free trade area that excludes Egypt.

With that in mind, please list as specifically as possible the steps you believe Egypt must take before the Untied States would consider commencing FTA negotiations with that country. What further economic reforms are needed?

Answer. The Administration recognizes the importance of Egypt as a key player in President Bush's vision of a Middle East Free Trade Area (MEFTA), and is taking advantage of a number of opportunities—such as the April visit to Crawford by President Mubarak, the anticipated April Strategic Dialogue in Washington, and engagement through the U.S.-Egypt Trade and Investment Framework Agreement (TIFA) Council—to discuss economic reform and trade liberalization issues and provide a road map for the United States and Egypt to work towards an eventual Free Trade Agreement.

Before the United States makes a decision to enter into an FTA, however, we must be firmly convinced that Egypt is committed to fundamental and sustained economic reform from the most senior level of leadership on down, not only in terms of articulating policies, but also in consistently implementing them. This commitment includes clear, public expression by Egypt's leadership that it shares our vision for a high quality, ambitious FTA. Senior-level policy commitments need to be substantiated by a positive and sustained record of concrete economic reforms and steps to improve the bilateral trade relationship.

Some of the specific steps that Egypt should take to prepare for an FTA include constructive cooperation in the WTO Doha Development Round, full implementation of major domestic reforms, protecting U.S. intellectual property consistent with Egyptian laws and regulations and Egypt's TRIPS commitments, fulfilling commitments under the WTO, and removing import barriers to U.S. industrial and agricultural products.Can Trade Be a Lever for Reforms in the Arab World?

PREPARED STATEMENT OF DAVID L. MACK

CAN TRADE BE A LEVER FOR REFORMS IN THE ARAB WORLD?

I am honored to appear before this committee to provide my personal perspective on the likely effects of Free Trade Agreements in the Middle East. My focus will be on the potential for FTAs and similar instruments to prod governments in the region into adopting economic reforms that will strengthen the private sector and lead to greater transparency and rule of the law. This will include regulations that do not stifle free market competition but do enforce measures against international crime and terrorist activities, including money laundering. My perspective is based on over 30 years as a US diplomat dealing with this region, three years as a private business consultant and the last six years as vice-president of a non-profit educational institution. With regard to the latter, I do not speak for the Middle East Institute, a broadly based member organization which does not take positions on policy issues, but in my personal capacity as an observer of trends in this region during the last four decades.

Israel, despite shortcomings in its economic system and the disincentives to private investment following decades of political turmoil and violence, is firmly embedded in the global economy and, since the 1960s, has multiplied its per capita income many times over. By contrast, most of the Arab countries and Iran are still textbook cases of stagnating or only slowly growing economies. My focus will be on the relationships between governments and their economies, a relationship which often serves to retard meaningful foreign trade, and the extent to which governments can do anything positive. There is often a nexus of relationships between government elites and a relatively few family commercial empires that dominate economic activity and hamper the emergence of competition, in both the domestic private sectors and from abroad. This reinforces a traditional mindset based on the notion that the economic pie is relatively finite based on wealth obtained from oil or other state controlled commodity exports and that competition is a zero sum game. Typically, this leads to high profit margins based on government contracts or government licenses, investment in non-productive enterprises such as real estate, outflows of surplus capital and limited possibilities for job creation by a broadly based commercial sector.

To start with, things really are better than they used to be. Whatever the statistics may show, Arab businessmen and their governments are increasingly conscious of the need to get beyond the constraints of doing business exclusively inside national economies. It has been a long time since I heard serious arguments for the need to insulate economies from foreign trade and investment beyond transitional periods. Mind you, foreign trade often gets lip service while little is done to break down the government and private barriers against it.

One positive development is that the official Arab Boycott of Israel exists increasingly only as a curious relic of the past. Not so long ago, it was effectively preventing major breakthroughs in foreign trade and investment, with perversely negative effects on the people of the boycotting states. In 1964, the Arab Boycott scored a decisive "victory" over Coca Cola when I was a Fulbright Scholar in Egypt. The stereotype of an Arab with a coke disappeared. In Egypt we had to make do with the sugary Masr Cola. The dead hand of Arab politics had triumphed. The loser was Coca Cola, the Arab consumer and Arab owned bottling and distribution agents. Later in my tenure in the UAE, I saw the Arab boycott of Coca Cola and many other US companies begin to melt away. In that country, as in some others in the region, chambers of commerce and other business minded organizations provide what is perhaps the most energetic lobby for economic rationality and change.

It is commonplace to describe Arab political economies as being subject to over regulation. Certainly this is one of the primary problems in a country like Egypt or Syria where the layers of regulations and bureaucracies seemed to extend back to Pharaonic times in Cairo and the Byzantine period in Damascus. But we also need to acknowledge the problem of under regulation in many of the newer states of the Gulf. As Ambassador to the United Arab Emirates, I saw at first hand the growing corruption and power in the private sector of the Pakistani-managed and Lichtenstein-headquartered Bank of Credit and Commerce International (BCCI), as well as numerous failing local banks being propped up by the various emirates. US and British bankers in the UAE told me that it was a country that badly needed to regulate its banks. A young, American trained UAE banking specialist named Sultan Al-Suwaidi drew my attention to the fact that the BCCI was able to offer a higher rate for deposits and a lower rate for loans than any other bank, suggesting that it was not the result of more efficient Pakistani management! Some years later, it cost the Emirate of Abu Dhabi an estimated 4 to 5 billion dollars to clean up the resulting scandals. Sultan Al-Suwaidi, incidentally, is now the Governor of the UAE Central Bank and is credited by US government officials with implementing model banking regulations, including strict prohibitions of money laundering.

In 1986,1 found the UAE's small but lucrative markets filled to overflowing with fraudulent copies of brand name consumer goods, ranging from automobile parts to music cassettes. Each of the seven emirates of this confederation independently ran their commercial systems, a prerogative jealously guarded by the seven ruling families and the businessmen allied with them. As with the fledgling United States before adoption of the US Constitution, federal institutions in this area were weak to non-existent. The business establishments of the separate emirates were proud of along tradition of unrestrained free enterprise. Rule of law, sanctity of contracts and transparency were at best unpredictable. Patents, trade marks, and copyrights enjoyed only the most spotty protection. In effect, the UAE risked becoming a pirate's cove with no meaningful intellectual property protections. Today, the UAE's record is much better in this area. Part of the reason for the improvement is over a decade of complaints from the US Government and other trading partners, as well as from the licensed local distribution agents for the manufacturers of imported consumer goods.

It helped that we periodically insisted upon negotiated agreements to avoid the equivalent of commercial war. This was met, initially, with cries of outrage from the UAE textile manufacturers who were expatriates, mostly from south Asian countries with over subscribed textile quotas. A combination of education and the pressure of deadlines achieved results. We arranged for senior officials from the federal ministries to have a thorough briefing in Washington on the harsh realities of the US political and economic environments which led to textile quotas. They returned and organized meetings of the government authorities and chambers of commerce of the various emirates where agreements were reached on negotiating strategies. In the end, the UAE emerged with a textile industry that had room for modest growth but was capped at a level that did not threaten the US industry.

Subsequently, we went through a similar exercise on issues of intellectual property. Once again, it was partly a matter of educating the emirate authorities. But it also involved the Embassy in local politics as we mobilized the often influential UAE businessmen who were the partners and agents for American companies. Deadlines were useful but had to be packaged in ways that encouraged the UAE to take pride in being respectable. Federal ministers admitted to me that they never could have wrested meaningful authority away from the individual emirates without the Damocles sword of potential US trade sanctions. So far, the newly empowered federal ministries are exercising their authority in a generally positive way and not evolving into obstructionist bureaucrats.

Beginning in May 1990, I became Deputy Assistant Secretary of State for Near East Affairs. Following the liberation of Kuwait, we agreed to begin in 1993 the first of what became annual economic dialogues with the six states of the Arab Gulf Cooperation Council—Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the UAL We had already developed close political and security relations with these governments. Economic relations, especially in the development and marketing of oil and gas, as well as the sale of US goods and services to rapidly developing petroleum-related industries was longstanding and formed the base for other relations. We were, however, beginning to lose ground to competitors from Europe and the Far East, especially in industries like aviation and consumer goods. Moreover, it was clear that the dominant oil and gas sectors of these economies were not creating jobs at anything close to the pace required to absorb the increasing numbers of young men graduating from high schools and universities, to say nothing of the women graduating in roughly equal numbers. Our intention was to inject new life into US relations with our Arab Gulf political and economic partners by encouraging economic and regulatory reforms.

Results of this first annual dialogue were disappointing. From my perspective, they were characterized by resounding affirmations of shared interests but a lack of serious self-examination. Many presentations by speakers from the region were long on assertions of opportunity for US firms but avoided commitments to the kind of reforms we suggested were necessary. In my luncheon address to the conferees, I reiterated the legal and administrative reforms by their governments that seemed necessary to us, but I made no commitments about what we might be prepared to do in response. My cautious call for gradual and orderly political reforms was met by a chilly silence, even though I knew that I was partly echoing the views of businessmen and intellectuals from the region.

In the years that have followed, I visited the region nearly each year and have noted that members of the Arab business communities are increasing vocal themselves in expressing the need for economic reforms. They understand that this is the price for entry into the global economy, either as members of the World Trade Organization or as partners with the United States in bilateral agreements. While they often complain about specific details of US negotiating positions, they understand that the discipline provided by this process may be a necessary catalyst for internal changes that have been stalled by inertia and tradition. Opposition to reforms is partly based on the narrow self interest of the few business families that enjoy the closest relations with government leaders, but there is also a broader fear that change will upset a familiar cultural order. Increasingly, however, there is a shared effort by reforming political leaders and the more dynamic members of the business community to assure greater transparency and rule of the law in commercial affairs. Partly because of US prodding but also on their own initiative, they are adopting new laws and improving the enforcement of measures against international crime and terrorist activities, including money laundering. They are trying to do this in a manner that does not stifle free market competition but is consistent with emerging global standards.

The example of the Free Trade Agreement with Jordan has had a strong, positive effect. It is not so much the great percentage increase in US-Jordanian trade since the FTA went into effect. It is understood that this resulted partly from a very low base and that the actual volume remains modest. Far more important are the non-quantifiable reforms that the Jordanian Government adopted to meet the pre-conditions for the agreement. In effect, Jordanian leaders took advantage of this instrument, using it as leverage to take internal measures that were long overdue. Eventual implementation of FTAs with Morocco and Bahrain will encourage the proponents of reform elsewhere in the region to take steps on their own to keep pace. From the US perspective, trade negotiations are a businesslike and non-sanctimonious way for us to promote reform in Arab countries.

There are no guarantees in this process, but there is now a keener understanding by governments and business establishments in the region of the connection between economic and social reform, especially educational reform, and their long term security. Moreover, there is an understanding that this has implications for the traditional political order, although commitment to change in that regard will be more cautious. It requires the vision to take risks and make uncomfortable adjustments. Resistance to high profile US pressure for political reforms is almost certain. Fortunately, some Arab leaders are initiating cautious measures in the directions of greater transparency in governance and wider participation in the political process. The success of such measures depends in part on their emergence as an authentic expression of local aspirations. In the meantime, Washington's renewed interest in bilateral economic cooperation will encourage the leaders from both the governments and the business communities that share these aspirations.

David L. Mack is Vice President of the Middle East Institute, a non-profit educational institution that does not take substantive policy positions. His remarks are his own, based on experiences which include service as the US Ambassador to the United Arab Emirates and as Deputy Assistant Secretary for Near East Affairs.

Responses to Questions From Senator Grassley

Question 1. You spoke in your testimony about using trade as an incentive for reforms in Arab countries. I understand that some political and business leaders in the region believe that the initiation of free trade negotiations with the United States will help force internal reforms. In your experience, do you believe it would be more productive to insist that reforms be made before the initiation of negotiations, or do you believe that negotiations themselves are capable of leading to sufficient reforms?

Answer. Insistence on reforms as a prerequisite to initiating trade negotiations has not proven in the past to be very effective. Arab governments are often skeptical about the willingness of the US Government to actually respond to internal reforms, which often require very painful decisions on their part. It is more productive to at least have an initial round of talks to demonstrate US *bona fides* and to establish the understanding that trade liberalization is a mutual interest. This enables us to set out a road map of economic reforms that we would recommend in order to continue trade negotiations in a positive atmosphere.

Question 2. You mentioned that family commercial empires in some Middle Eastern countries inhibit the liberalization of economies in the region. Yet the governments of certain Middle Eastern countries are themselves largely run by families. Are some of those governing families also owners of the region's commercial empires? If so, couldn't we expect these governments to strongly oppose trade liberalization?

Answer. In most of the more traditional Arab political systems, the ruling families are large and diverse. Some of their members are not interested in reforms, and they often prosper from a status quo that rewards their political influence with commercial advantages. By contrast, there are a number of cases where more enlightened members of the ruling families are taking initiatives in the areas of economic, legal and educational reforms that challenge the status quo in a very constructive manner. In effect, they are foregoing short-term advantage for the long-term progress essential to maintain social stability and make peaceful political evolution possible.

Question 3. It is clear that increased economic opportunities for individuals in the Middle East will lead to greater stability in the region. You spoke about the oil and gas sectors no longer being able to employ the growing number of young men and women leaving universities. What opportunities do you see for these young people entering the workforce?

Answer. Most of the opportunities for expanding employment in the economies of Arab countries are in service sectors, including tourism. In a few cases, including Egypt, there is significant potential for increasing jobs in the manufacturing sector.

RESPONSE TO A QUESTION FROM SENATOR BAUCUS

Question. The cornerstone of the Administration's trade policy in the Middle East is to negotiate FTAs with countries that are ready for a close economic relationship with the United States. Yet there are many countries that are not ready to take this step. In your opinion, what can US trade policy do in the short term to help these countries? Do you believe a trade preference program like the one Senators Baucus and McCain are advocating can play a useful role?

Answer. I believe that a program of trade preferences for the countries of the Middle East would at least whet appetites for bilateral trade agreements. Together with the demonstrating effect of FTAs with Jordan, Morocco and Bahrain, a trade preference program like the one you and Senator McCain are advocating has the potential to focus the minds of business and political leaders on the need for reforms.

PREPARED STATEMENT OF BILL MAXELL

Chairman Grassley, Ranking Member Baucus, and members of the committee, thank you for providing me the opportunity to speak before you today. My name is Bill Maxwell and I currently serve in Washington as Director of International Trade Policy and Business Development for the Hewlett-Packard Company. I am here to discuss how the United Sates can improve security in the Middle East and globally by fostering greater economic opportunities in the area, and how free trade and other market-based economic incentives can serve as the foundational pillars for achieving a more stable and prosperous Middle East.

Several examples of countries having undergone transitions to freemarket economies since the 1970's, including, Spain, Taiwan and South Korea, demonstrate the power of industry and commerce to facilitate social, political and regional stability. In each of the aforementioned cases, political reform was not imposed on autocratic systems from the outside, but rather, it was grown from the inside—largely by a rising middle class that demanded social and political rights. Moreover, in each case, the lure of participating in a regional trading block, in the case of Spain and the European Community—or the benefits derived from already participating in such a block, as in the case of Taiwan and South Korea with APEC—Asia Pacific Economic Cooperation—provided a powerful impetus for reform. Perhaps it would be useful to think in terms of encouraging the creation of a similar organization in the Middle East—the Middle East Economic Cooperation—MEEC.

The creation of a common Arab market could yield similar dividends to the nations of the Middle East. Taken as a whole, the 22 Arab-speaking nations, having a population of more than 200 million, represents a region of great potential, both in terms of consumer demand and human capital. However, while population is expected to grow at five percent a year, gross domestic product growth is projected to remain at three to four percent, which means that absent some economic shift, it will be difficult to reduce current levels of unemployment, which run as high as 20 percent.

This demographic challenge has led many Arab leaders to acknowledge that part of the solution must be attracting new business and foreign investment to the Middle East. However, this is precisely where much of the problem arises. Rather than one unified market, the Arab-speaking world today is 22 separate markets, each with its own rules, regulations, barriers to investment and trade restrictions; all of which lead to a striking lack of regional cooperation. During the 1990's, less than seven percent of Middle East trade came from other Middle Eastern countries. Contrast that with Europe, where more than two-thirds of all trade is among countries in Europe; or Asia, where 30 percent of trade originates within Asia.

The lack of unification and cooperation among Middle Eastern countries has also put the region at a competitive disadvantage in the global economy. For companies like Hewlett-Packard, which operates in 178 nations around the world, it is less problematic and more cost-efficient to conduct business in regions defined by cooperation, such as the European Union or Asia Pacific Economic Cooperation. Such trade areas offer more hospitable investment climates, lower transaction costs, less restrictive barriers to entry, higher standards of transparency and more access to capital. Historical comparisons support this assertion.

In the 1950's, the per capita income level of Egypt and Korea were virtually equal. Today, Egypt's per capita income level is less than one-fifth of South Korea's. Similarly, Saudi Arabia's per capita gross domestic product was at one time higher than Taiwan's, but now is only half of Taiwan's output. To put these figures in perspective, the combined gross domestic product of all 22 Arab-speaking nations is less than the gross domestic product of Spain.

The Middle East's lack of integration for many historical reasons has also led to an imbalance between the wealth of certain nations and the availability of human resources. For instance, countries like Kuwait have great financial resources, but have limited human resources; whereas countries like Jordan have an abundance of capable and available human resources, but high levels of unemployment. These problems and inequities can easily be solved through integrated economic cooperation among the countries.

Integrating the 22 Arab-speaking nations of the Middle East into one common market is not without obstacles, including inevitable trade disputes and sovereignty concerns. However, the process of overcoming the challenges will, in the end, yield long-term benefits. Creating a more stable climate to spur entrepreneurship and attract investment will encourage Arab nations to confront issues of transparency and rule of law that are basic for creating a middle class. As many Arab leaders know, this is not about solutions being imposed from the outside—this is an issue of fundamental self-interest.

The reason companies like Hewlett-Packard are so committed to the Middle East today is because we believe in the vast promise of the region. As Carly Fiorina, HP CEO said in a recent speech, "HP is privileged to do our part . . . [in fostering the economic development of the area]. HP has made a commitment to be an asset as well as a partner as the future of the Middle East takes shape. We are proud today to be the largest IT Company operating in the Middle East, working from Saudi Arabia to Egypt, Jordon to UAE to use IT to empower more people than ever before."

As Senator Baucus said in his statement accompanying the submission of the Senate bill 1121—the Middle East Trade and Engagement Act of 2003--, historically, the Middle East has played an important role in global trade. Economics and history prove that as markets open, businesses grow; and as businesses grow, jobs are created, both in the regions of investment as well as investing nations. Thus, Hewlett-Packard sees the economic growth in the Middle East as a means to revitalize and strengthen ties both between the countries of the region, as well as the Middle East and United States.

In this context, on behalf of Hewlett-Packard, please allow to me express our company's support S. 1121 as introduced by Senator Baucus and Senator McCain. This bill promotes the notion that free trade and other market-based economic incentives are fundamental to achieving stability and prosperity in the Middle East.

RESPONSES TO QUESTIONS FROM SENATOR GRASSLEY

Question 1. You mentioned that a growing entrepreneurial climate in the Middle East will encourage countries in the region to seek greater transparency and to better recognize the importance of the rule of law. I imagine that most business people in the region understand this link.

But does the average person on the street realize that liberalized trade could lead to positive changes in the operation of governments in the Middle East?

Answer. You asked if the average person on the street understands the connection between a liberalized trading system and the prospect of good governance. I'm afraid there is no ready answer to this question. Our expectation is that the expansion of economic opportunity and growth that is afforded by the liberalization of trade will contribute to creating a stronger, stable middle class in the Middle East. That, in turn, will ultimately lead to the demand for greater transparency and a fuller recognition of the importance of the rule of law. It is not expected that this will be a smooth road but it is believed that the journey is worth taking.

Question 2. Hewlett-Packard is an information technology company, so I imagine that the protection of intellectual property is of key interest to Hewlett-Packard.

Given your knowledge of the Middle East, what is the experience of U.S. information technology companies with regard to intellectual property protection in the region?

Answer. Although there have been some challenges with respect to the protection of HP's intellectual property (IP) rights in the Middle East, thus far, it is not a widespread problem for the company. IP rights clauses are usually not problematic in contract negotiations. Rather, customers and suppliers generally accept them as set out in the contract by HP and they appreciate the fact that HP is concerned about IP rights.

Moreover, leaving aside Sharia Law, most legal systems in the Middle East are inherited to one extent or another from the British or French legal systems and provide for some degree of IP protection. The level of sophistication of these laws and their adaptability to stand up to current technologies is just now being explored. At this point, HP would have no issue trying to enforce IP rights in Middle Eastern countries where enforcement mechanisms exist if the need arises.

Finally, to the extent that HP has experienced difficulty, the challenge has generally involved convincing the authorities (police and prosecutors) to take counterfeiting as a serious issue and thereby enforce existing laws. However, even in such instances, HP has had good success, specifically in two focus countries (Egypt and Saudi Arabia) and attributes this to the quality of our investigators as well as having provided detailed training and support to authorities. This experience leads us to believe that the remedy to problems associated with IP protection is solid training and support of the authorities.

RESPONSES TO QUESTIONS FROM SENATOR BAUCUS

Question 1. The cornerstone of the Administration's trade policy in the Middle East is to negotiate FTAs with countries that are ready for a close economic relationship with the United States. Yet there are many countries that are not ready to take this step.

In your opinion, what can U.S. trade policy do in the short term to help these countries? Do you believe a trade preference program like the one Senators Baucus and McCain are advocating can play a useful role?

Answer. HP believes that a trade preference program, as outlined in the Baucus-McCain bill, would enable Middle Eastern countries to build closer economic relationships with the United States. The program would reward nations moving towards effective and responsible governance. Furthermore, the bill is consonant with our view that free trade and other market-based economic incentives are foundational pillars for achieving stability and prosperity in this very important region.

Question 2. If the Baucus-McCain bill were to become law, what would be its impact on companies like Hewlett-Packard? Would you increase your investment in the region?

Answer. Through its investments in the region, HP has already committed itself to being an asset and a partner in bringing prosperity to the people of the Middle East. Accordingly, HP is the largest information technology company operating in the area. The Baucus-McCain bill promises to enhance the conditions for making sound business decisions. As a result, in can only deepen HP's commitment to the region. We would expect that implementation of the provisions of the Baucus-McCain bill would encourage other companies to consider increasing their investments as well.

PREPARED STATEMENT OF HON. JOHN MCCAIN

Chairman Grassley, Senator Baucus, members of the Committee, thank you for the opportunity to testify before you today regarding U.S. economic and trade policy in the Middle East.

I wish to congratulate the Committee on its many trade-related successes this session. The many actions taken on trade policy since passage of the Trade Act of 2002 are to be commended—from the expedited consideration and approval of Free Trade Agreements (FTAs) with Chile and Singapore last year, to the consideration, perhaps in the not too distant future, of the recently concluded negotiations with Australia and Morocco.

In addition, the benefits available to eligible nations covered under the African Growth and Opportunity Act are due to be extended and possibly expanded. I would encourage efforts to do so expeditiously.

The United States is steadily regaining its leadership role on trade despite some counterproductive protectionist actions; however, we are feeling the after effects of those actions and support for free trade is no longer as robust and vocal as in recent memory.

Mr. Chairman, with your leadership, and that of Senator Baucus, I believe it possible to generate the support necessary to continue to approve strong trade deals that not only benefit the U.S. and promote market liberalization and transparency with our trading partners, but also provide them incentives to bring about political and social reform, when necessary.

Such a necessity exists in the greater Middle East. Tom Friedman has written that "many Arab economies are dominated by state oil revenues and state companies, with private enterprise very weak. Therefore, holding onto or being close to power are the only pathways to wealth. Control power, control wealth." Breaking the link between political power and wealth by creating a larger private sector independent of political control is an essential component of our efforts to help build democracy in the Middle East.

As we have witnessed in Bahrain—with whom we are in the final FTA negotiating stages—there is a willingness to begin this separation as evidenced by laws now on the books. But perhaps the more critical step will be the execution of those laws. We must remain vigilant on this issue to ensure those laws are enforced so our own financial services sector and others will be able to operate in a truly transparent and open market.

A key question for American policy is how to encourage such long-overdue political, economic, and social change in the Arab world. I believe we must expand our range of economic, cultural, and political tools to help give the people of the greater Middle East a stake and a voice in how they are ruled, with greater levels of democracy and prosperity serving as an antidote to the hatred whose malignancy was brought home to Americans on September 11, 2001. Trade preferences that help build prosperity in the Arab and Muslim worlds independently of state power can help advance our political objective of more representative, accountable, and transparent rule.

We have successfully pursued trade preference programs with the nations in sub-Saharan Africa, the Andean region, and the Caribbean basin, with tangible results. Would anyone argue today that the greater Middle East is less important?

The bill that Senator Baucus and I introduced would establish a baseline of trade as an incentive to those countries that do not engage in activities that undermine our national security or foreign policy interests, and support a peaceful resolution of the Israeli-Palestinian conflict, among other things.

This bill is designed to provide a reliable and even-handed approach toward improving relations with the Middle East through greater economic interdependence. It is not a panacea developed to solve overnight all of the problems that exist in relations between the U.S. and the nations of the greater Middle East. We need to send a clear signal to the region that we are serious about finding peaceful solutions to the fires that have been fanned over the years in part because of closed markets.

Engaging the region on this level will help spur increased investment and trade which can lead to a reduction in the risks posed by the severely restricted economic system under which a number of nations in the area operate. Reaching that goal would be no small achievement given the likelihood of tremendous population growth and an average unemployment rate in the region hovering around 22 percent—an obvious recipe for disaster.

In an era when our trade negotiators expressly pursue trade agreements to advance broader foreign policy interests, liberalizing trade with key partners in the Middle East, Turkey, and South Asia should be a strategic priority of the United States.

We all understand the critical need to engage the region and promote stabilizing reforms. I support the President's vision and believe that extending preferences to eligible countries compliments that vision by providing immediate, tangible benefits.

Mr. Chairman, again, thank you for this opportunity to testify.

Communications

Statement of Catherine Novelli, Assistant U.S. Trade Representative

Chairman Grassley, Senator Baucus, and Members of the Committee, on behalf of Deputy U.S. Trade Representative Peter Allgeier, we appreciate the opportunity to submit testimony today on the President's Middle East Free Trade Area initiative and the progress the Administration has made to date.

The Administration's trade agenda is a fundamental part of the President's broader efforts to advance reform in the Middle East. In May 2003, President Bush announced our goal of creating a U.S.-Middle East Free Trade Area by 2013. It is one element of a comprehensive approach that addresses the economic, social and political challenges facing the region and U.S. interests in the area. Our trade strategy complements our efforts in these areas and is designed to bring real, concrete change predicated on internally generated economic reform and the positive role that market based, trade liberalizing policies can play in promoting economic growth.

The strategy recognizes the differing levels of development across the region, the historical and political sensitivities faced by governments, and the reality that reform processes must be driven from within. Our goal is to assist nations that are ready to embrace economic change and the rule of law, integrate them into the global trading system, and help bring their economies into the modern era.

Creating the Middle East Free Trade Area (or MEFTA) will not occur quickly and we will most likely need the full decade that the President has given us. The depth of economic change we are seeking to promote is profound and will take time. Most importantly, to be successful it must be introduced at a pace that is sustainable for the leaders and populations in the region. We are committed for the long haul, through a step-by-step approach that will help nations build free, dynamic economies and raise standards of living for the people of the region.

The Challenge

There is no question that the region as a whole is in desperate need of significant structural economic reform. According to the United Nations, the Middle East attracted just 0.7 percent of global foreign direct investment throughout the 1990s. Exports from the region—over 70 percent of which are accounted for by oil and oil-related products—grew at 1.5 percent per year over the same period, far below a global average growth rate of 6 percent. On a per capita basis, exports are significantly lower today than 20 years ago.

U.S. trade with the region reflects the Middle East's isolated role in the global economy. The United States imports almost twice as much from Hong Kong as it draws in non-oil goods and farm products from the 22 members of the Arab League and Afghanistan combined.

This economic isolation has contributed to high levels of unemployment and poverty in the region. According to the World Bank, about 25 percent of people in the region live on less than $2 per day. The UN reports that Arab countries have the world's lowest percentage of people who use the Internet or have access to a computer.

In response to this challenge, the Administration created the U.S.-Middle East Free Trade Area—a region-wide commitment to open trade with the United States and, equally important, to liberalize trade among the nations of the Middle East.

There are different levels of development, preparation, interest, and capability on the part of countries in the Middle East and North Africa to make and implement serious economic reforms. Most importantly, the political will to embrace economic reform varies across the region. Our challenge is to encourage those countries that are lacking in political will and help them recognize the benefits the liberalized trade and more open and transparent markets can bring. Jordan, as the first Arab nation with a FTA is a prime example of the kinds of trade policies we are encouraging. Jordan's commitment to free trade and economic reform has produced multiple benefits including:

- Free trade with the United States has increased Jordan's exports to the U.S. from $16 million in 1998 to a projected $600 million in 2003. U.S. exports to Jordan have increased 14% between 2000 and 2002, especially notable given the decline of U.S. exports by 6% to the Middle East region as whole during the same period. The United States is now Jordan's top trade partner.
- Jordan's non-textile exports to the United States have risen to $100 million and there has been a major increase in diversification into such areas as stone and marble, jewelry, machinery and food products.
- The Jordanian Government reports that over 30,000 jobs have been created as a result of expanded trade with the U.S.
- The Jordanian Government also tells us that increasing numbers of businesses and organizations are choosing to locate in Jordan, as firms seek a safe, competitive, pro-business base from which to serve region.
  - This trend is reflected in growing foreign direct investment in Jordan, which rose from $627 million in 1995 to $2.4 billion, or 26% of gross domestic product, in 2002.

Jordan's overall trade figures attest to its increased competitiveness. Jordan's exports to the rest of the world increased 97 percent between 1998 and 2002 (from $1.2 billion to $2.3 billion), outpacing the 68 percent growth for the Middle East as a whole.

Countries have seen what the U.S.-Jordan FTA has meant for the Jordanian economy and its ability to generate jobs and wealth over the last several years. Leaders in the region also see their peers making the choice to reform and do not want to be left behind. First Jordan, now Morocco and soon Bahrain have put the region on notice that change is happening, and that if countries do not want to be left behind, then they too will need to begin the reform process.

The Middle East Free Trade Area (MEFTA)

The MEFTA framework has seven components. First, the United States will actively support WTO membership for those peaceful countries in the region that seek it. We are working with Saudi Arabia, Lebanon, Algeria, and Yemen on their accession process. We are also assisting countries that are already WTO members to gain full advantage of open global markets and help them implement commitments. We want to assist the full integration of the nations of the Middle East within the global trading system, and WTO membership provides the basic building blocs for deeper bilateral engagements with the United States.

Second, the United States will employ the Generalized System of Preferences program that Congress restored in the Trade Act of 2002 to increase U.S. trade ties with the Middle East to help provide short-term benefits. GSP provides duty-free entry to the U.S. market for some 3500 products for seven countries and the West Bank in the Middle East. In 2002, Americans bought over $278 million worth of products from the region under this program—including Egyptian furniture, Omani jewelry, and Lebanese olive oil. Like the Baucus/ McCain Bill, we see trade preference programs playing an important role in providing short-term benefits. For this reason, we are providing new resources to work with Middle Eastern businesses on GSP opportunities, applications for more products, and marketing to U.S. investors as GSP countries. We continue to believe, however, that seeking to enhance reciprocal trade with the Middle East and North Africa is the most effective strategy for engendering economic growth and reform in the region.

Third, the United States has negotiated Trade and Investment Framework Agreements, or TIFAs—which establish a work program to expand trade and resolve outstanding disputes—and we are deepening those agreements already in place with Egypt, Tunisia, and Algeria. Other countries are interested and three new agreements have been signed since the President's initiative was announced with two more pending. TIFAs are an important process in developing the experience, institutions, and rules that will make a country ready and capable of negotiating an FTA with the U.S. TIFAs encourage private sector participation through business councils that drive trade agendas and help us address the specific concerns of business. Our emphasis in these Council discussions is on producing concrete policy and business results.

Bahrain offers a good example of how a TIFA can create momentum for liberalization that can lead to an FTA. Bahrain has joined the WTO Information Technology Agreement, committing it to zero tariffs in computer, telecommunications and related products, provided an open environment for electronic commerce, taken initial steps to join and implement the World Intellectual Property Organization (WIPO)

Internet treaties, and pledged to treat agricultural biotechnology fairly. Bahrain has also liberalized its telecommunications market and passed legislation for transparent government procurement and labor rights. These gains, in turn, boosted public and business support for the U.S.-Bahrain FTA in both countries and prepared Bahrain in a short period of time (TIFA discussions lasted approximately a year and a half) for the higher standards embodied in a FTA. Countries see the TIFA as a valuable means of engaging with the U.S. in a vigorous economic dialog, but not under the pressure of a negotiating environment. In turn, under the MEFTA, countries understand that these discussions are stepping-stones to an FTA.

In Egypt, the TIFA process has supported passage and implementation of a new IPR law and assisted Egypt in acceding to WTO telecommunications agreements. We hope our TIFA with Egypt will encourage the government to continue its efforts to make Egypt a more hospitable location for investors, open its markets, overhaul a costly and counterproductive customs system and establish a reliable and transparent economic rule of law.

Fourth, the United States will offer as appropriate, to negotiate Bilateral Investment Treaties, or BITS, which establish common rules for investment. A BIT with the United States can help attract capital and new businesses. By agreeing to treat foreign investors fairly and offer legal protection equal to that available for domestic investors, a country signals that it offers a safe place to do business. By incorporating international business rules and norms in domestic practice, these treaties also lay the groundwork for comprehensive FTAs.

Fifth, the United States will negotiate comprehensive free trade agreements—which remove all barriers to trade and set high standards across all sectors—with the aim of expanding the bilateral FTAs into "subregional" FTAs by mooring other interested and qualified countries in the safe harbors of existing free trade agreements.

Over the course of the decade, North African countries might be connected to the Morocco FTA as they achieve a critical mass of reforms. Gulf States could join the Bahrain FTA when they are interested and prepared.

By working with Congress to bring new signatories into existing FTAs, we can help promote trade among the nations of the Middle East—a region that suffers the lowest internal trade rates in the world. For example, "cumulation clauses" in bilateral FTAs—which allow our FTA partners to produce and export in concert with their neighbors—would help spur intra-regional trade and integration. Development of region-wide customs rules would further help build regional, and global, trade linkages.

Sixth, the U.S. Middle East trade strategy pictures the eventual melding of these sub-regional FTAs into an historic regional Middle East Free Trade Area. A mutual commitment to high standards and the elimination of tariffs and other barriers to trade among the countries of the Middle East would provide an engine for economic growth and increase momentum for internal economic reform.

The seventh and final element of our trade strategy is the provision of financial and technical aid to help countries develop the capacity to take part in negotiations, implement trade agreements, and build the legal, financial and entrepreneurial infrastructure to partake in the benefits of open markets. The Middle East Partnership Initiative will help target more funding from various U.S. Government agencies and encourage partnerships with private organizations and businesses that support development. That initiative is also aimed at increasing educational opportunities, strengthening civil society and the rule of law, and supporting small businesses. The Partnership for Financial Excellence will help improve and modernize financial markets in the region so that financing for trade expansion and business development is made available to those eager to take advantage of freer trade, create jobs, and build more stable societies.

Results So Far

This strategy has produced a level of excitement and interest in economic reform in a region that in the past has not made economics its priority. In the short time since the President announced the MEFTA in May 2003, the Administration, in close cooperation with Congress, has been active in implementing the initiative.

Our strategy of engaging with countries at their level of development, with access to the U.S. market based on reciprocity and adoption of high standards for trade and investment rules is working. Key to our progress has been the pull of an FTA with the U.S., and what it represents in terms of market access, and high standards for such key elements of economic reform as intellectual property, transparency and anti-corruption, and services liberalization, among other areas.

FTA negotiations with Morocco concluded earlier this month, and we are well advanced in our FTA negotiations with Bahrain. These are high quality agreements that reflect these countries' leadership's commitment to economic reform. The announcement of our FTA negotiations with Bahrain has had a salutary effect on the region. Countries who have never before expressed an interest in discussing concrete economics and trade policies with us are now actively engaging. In July 2003, we signed a TIFA with Saudi Arabia. In October 2003 we held our first TIFA Council meeting with Tunisia. In February of this year we signed TIFAs with Kuwait and Yemen, and next week we are signing TIFAs with Qatar and the UAE. At the beginning of this month, the President granted GSP privileges to Algeria.

What the rapid pace of the developments just enumerated reflects is the qualitative change in attitudes that has griped the region. Saudi Arabia's WTO accession, which had been moribund for years, has been energized. An increasing number of countries in the region have expressed their strong interest in concluding FTAs with the United States.

Linking access to the U.S. market to reciprocal access and high-bar obligations is essential to changing how economics and business are done in the region. This strategy has allowed us to meet our foreign colleagues as partners, and provides ballast for ambitious, comprehensive economic reform along with reciprocal trade benefits to the U.S. Through our various agreements, dialogs and efforts, we are establishing a long-term economic relationship and a base from which to grow lasting benefits for U.S. and Middle Eastern workers, farmers and citizens.

Again, thank you for the opportunity to share with you the Administration's efforts on trade in the Middle East and North Africa. Congress' support for the Middle East Free Trade Initiative is deeply appreciated. The Administration looks forward to continued close cooperation with Congress on this issue.